

Corrupt Reciprocity

Johann Graf Lambsdorff

“Perspectives on Global Issues” Volumn 2, Issue 1, Autumn 2007

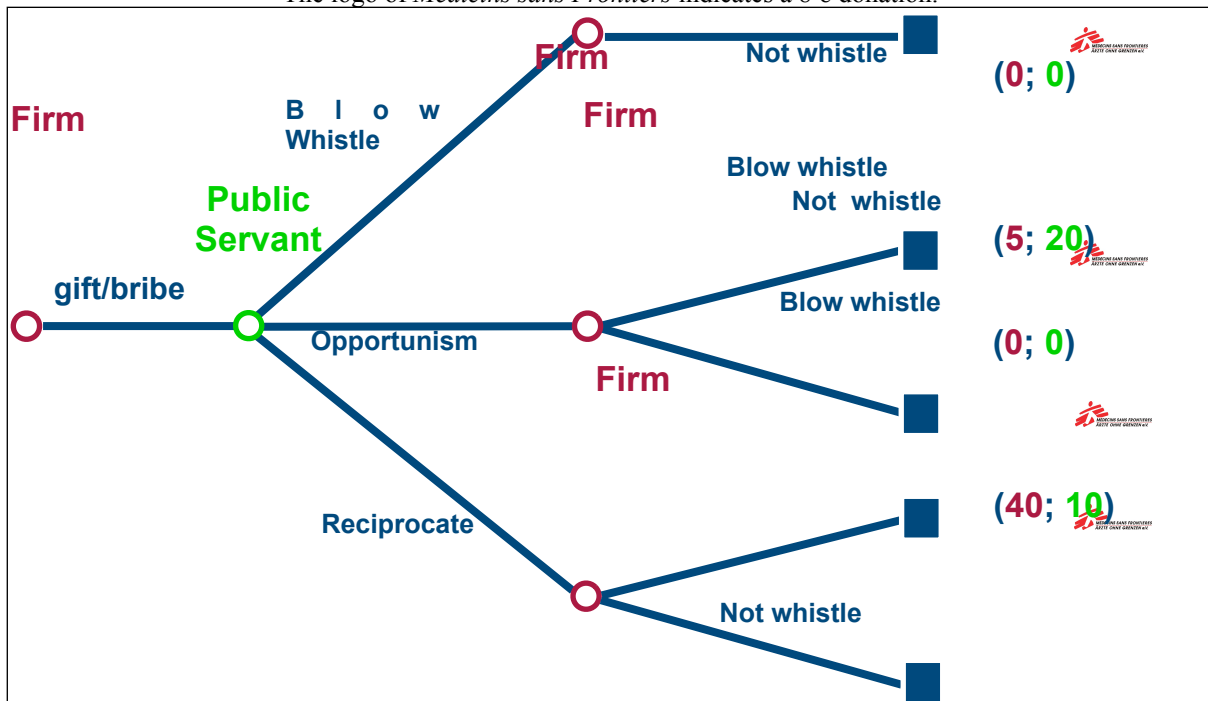
Corruption has been a feature of public institutions for centuries, yet only relatively recently has it been made the subject of sustained scientific analysis. In a recent publication, The Institutional Economics of Corruption and Reform,¹ I investigate how insights from institutional economics can be used to develop a better understanding of the institutions necessary to carry out corrupt transactions and those that are helpful in inhibiting them. One core point is that rather than being deterred by penalties, corrupt actors are more influenced by other factors such as the opportunism of their criminal counterparts and the danger of acquiring a reputation of unreliability. This suggests a novel strategy for fighting corruption - the "invisible foot" - whereby the unreliability of corrupt counterparts induces honesty and good governance even in the absence of good intentions.

Related to this approach we carried out an experimental investigation.² In the lecture halls, during introductory courses of economics at the universities of Clausthal and Passau, Germany, first year students were supposed to play a corruption game. (0; 2)

Figure 1: Corrupt Reciprocity – the Payoffs to Students

Numbers in parenthesis indicate payoffs in € (businessperson; public servant).

The logo of *Medicins sans Frontiers* indicates a 8 € donation.



¹ Lambsdorff, J. Graf. The Institutional Economics of Corruption and Reform. Cambridge: Cambridge University Press, 2007.

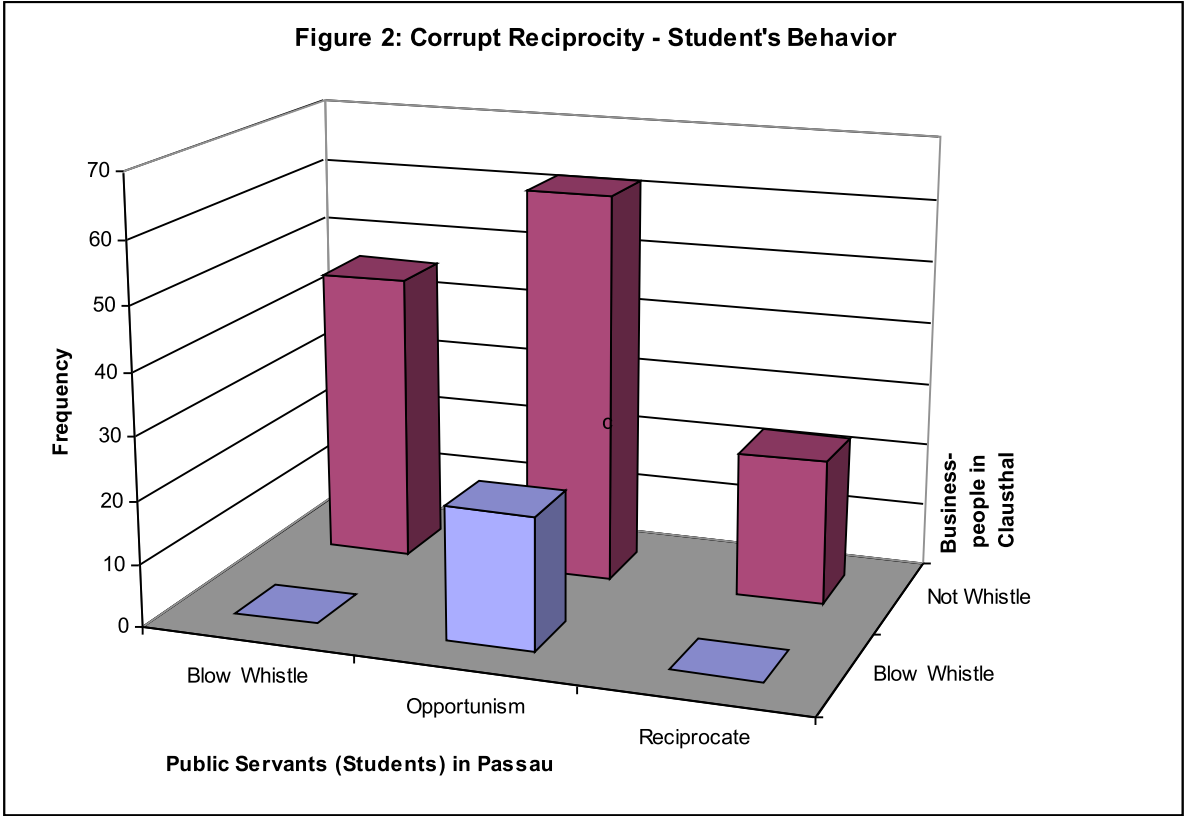
² See Lambsdorff, J. Graf and B. Frank. “Corrupt Reciprocity.” Discussion Paper of the Economics Faculty of Passau University. No. 51-07. August 2007.

Those in Passau obtained the role of public servants and chose between whistle-blowing, opportunism (that is, rejecting to provide the favor in spite of acceptance of a payment) and reciprocity by delivery (of a contract to an anonymous partner in Clausthal). Those from Clausthal acted as businesspeople who requested being awarded a contract albeit offering low quality work. They chose whether or not to blow the whistle at the end of the game.³

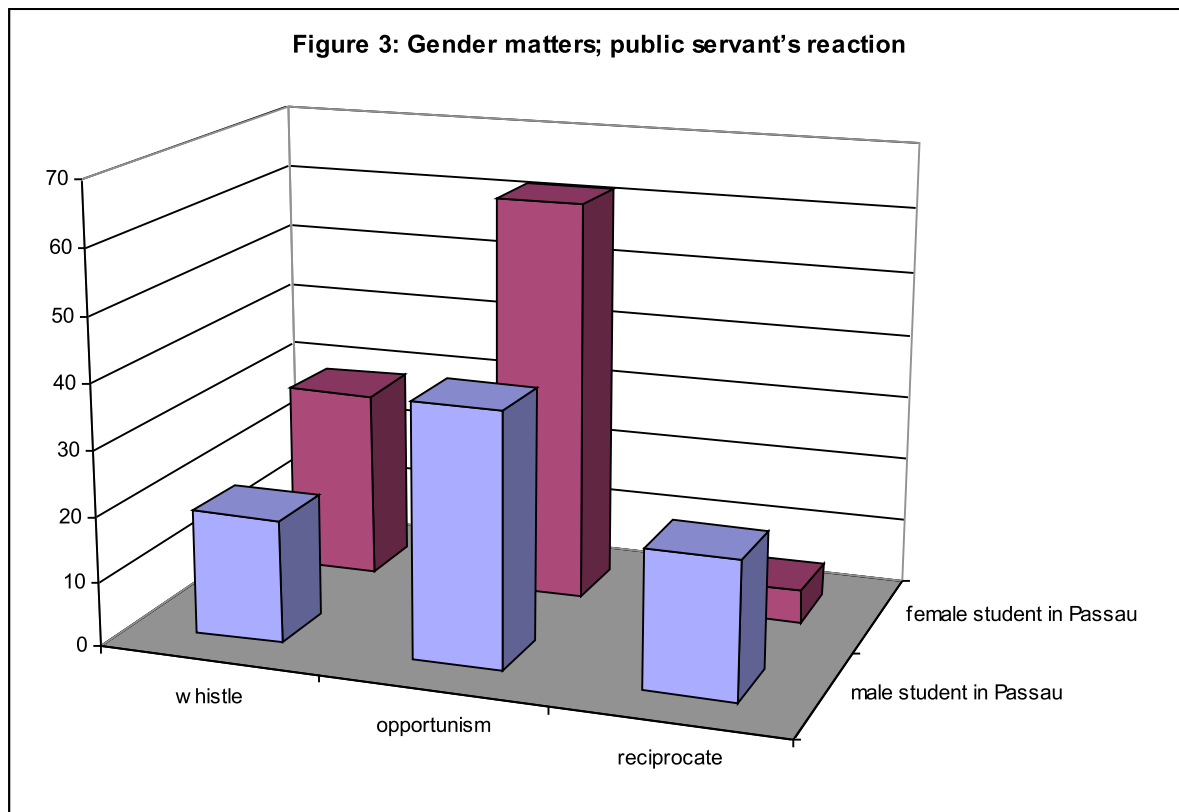
Altogether, 180 valid questionnaires were collected in the first round of the experiment. These were then sent to Passau University, where 176 students participated in an economics lecture. (Four forms from the 180 received from Clausthal were left over and filled out by the instructors). The completed forms were then sent back to Clausthal, where 152 of the valid 180 first round participants showed up to play round three. Afterwards, 25 forms (i.e., 50 participants) were randomly chosen, like in a lottery, and the selected participants could get their payments in € in Clausthal and Passau from a secretary in a separate room, their decisions remaining hidden from the other participants and from the experimenters.

All participants in Clausthal and in Passau were shown figure 1. Starting from an endowment of 25 €, the businessperson gives 20 € (as a gift or bribe) to the public servant, resulting in an initial endowment of 5 €. He or she would win a further 35 € as a profit from the contract in case of reciprocity and lose 5 € if someone blew the whistle. The public servant obtains a payoff of 20 € (gift or bribe) from the businessperson. He would have to pass on 10 € for arranging the awarding of the contract (reciprocity). Upfront whistle-blowing induces confiscation of the gift or bribe but a bonus of 2 €. If the contract were not given to the businessperson in Clausthal (either due to opportunism or whistle-blowing) no damage would be imposed on society. This is considered in our game by a 8 € donation to *Medecins sans Frontiers*.

³ A formal treatment of the game and resulting policy recommendations can be found in: Lambsdorff, J. Graf and M. Nell. "Fighting Corruption with Asymmetric Penalties and Leniency." CeGE-Discussion Paper No 59, February, University of Göttingen. 2007.



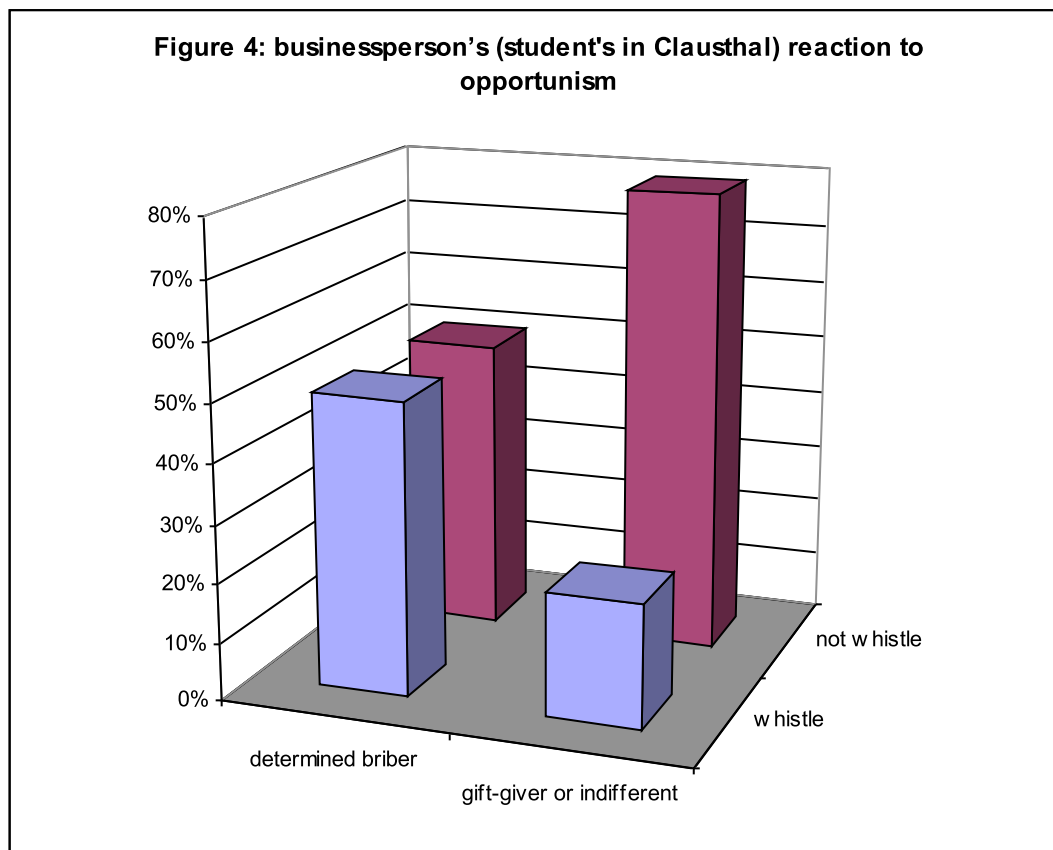
Forty-nine participants out of 176 in Passau preferred to blow the whistle upfront. As shown in figure 2, we observe a considerable amount of public servants reciprocating the bribe, although this goes along with a lower income. The apparent reason relates to 21 cases of whistle-blowing by businesspeople that were cheated by public servants. Also this behavior is a departure from income maximization, being motivated by the desire to take revenge for having been cheated by an opportunistic public servant (negative reciprocity). These cases reveal a risk of opportunism among public servants. Either this risk or positive reciprocity (“do good to those who did you good”) may thus motivate public servants to deliver the contract.



There were remarkable differences in gender, as revealed in figure 3. Women are markedly more likely to behave opportunistically and less likely (at a 1-percent error level) to reciprocate. There is a related finding at the University of Clausthal, where female students were significantly less likely to blow the whistle, that is, to retaliate after they were cheated by an opportunistic public servant.

Finally, students in Clausthal were at the outset asked whether they would prefer their payment to be called a “gift” or a “bribe”. Twenty-five questionnaires with a gift-wording and 25 with a bribe-wording were auctioned to students. Those with a lower willingness to pay were assigned a randomly chosen questionnaire. While some preferred the milder gift-wording, others expressed (also in written questionnaires) preference for a “clearer language”. As revealed in figure 4, students who preferred the bribe-wording were more willing to retaliate when they were cheated.

We thus observe two different approaches to bribe public servants. While transferring a "gift" is preferred because it appears less offensive and demanding, a bribe is chosen precisely for the opposite reason: it is more demanding and clearer that reciprocity is expected, including the threat to retaliate in case of opportunistic behavior. We found empirical evidence on these differences.



In July 2007 we played the game also at a summer school with 40 senior prosecutors and fraud investigators from various continents and found results that are much along the lines of those reported here. While the sample was rather small, also in discussion we detected similar patterns of reasoning, confirming our overall findings, confirming that the findings are of general validity beyond the calculus of sophomore students.

Corrupt transactions require trust among the criminal partners, particularly because the hidden agreements are not enforceable by courts. Women appear less capable or willing of establishing this trust among corrupt criminals. This is also corroborated by related empirical evidence that states the countries with more women in parliament and in the labor force are less affected by corruption.

Corrupt actors must be deterred from their criminal actions. But deterrence involves more than just the threat of legal sanctions. It encompasses also the risk of being cheated by one's counterpart and the threat of being exposed. This finding is at the heart of the game we played. There are numerous policy recommendations that build on this insight, elaborated in Lambsdorff (2007) and Lambsdorff and Nell (2007). 1) It is vital to improve incentives for the "good" whistleblowers (those who act upfront or after having completed a corrupt transaction), but to deter the "bad" whistleblowers (who threaten to retaliate after being cheated). 2) Penalizing public servants already for the taking of small gifts may backfire by forcing them to reciprocate. 3) Penalties should be imposed on all businesspeople, also those who were cheated by public servants. 4) Stronger involvement of women in team work can help shatter the trust among male dominated networks. 5) Public servants should receive

harsher penalties for reciprocating bribes, and businesspeople should be heavily fined for paying bribes.

The power of economic thinking started with the notion of the invisible hand. Competition substituted for benevolence by guiding self-seeking actors to serve the public. Individual morality lost relevance as a guiding principle for directing behavior in private markets. May this also be true for politics and administration? Can anticorruption flourish without good intentions? Will anticorruption come to a standstill if it focuses on moral sanctions, which may be detrimental to civil liberties? With respect to fighting corruption we may not have a mechanism as powerful as the invisible hand. If something comes close to it, it is the failure to make credible promises once actors are willing to take bribes. The risk of betrayal may operate like an invisible hand, making life hard for those who fail to commit to honesty. This principle can motivate even the self-seeking actors to abstain from corruption and reconcile civil liberties with good governance.