

Incentives for the private sector to refrain from corruption

Query:

“What are specific incentives or drivers for the private sector NOT to be corrupt? “

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Part 1: Introduction

The costs of corporate corruption to business and the state are high. In 2003, the office of the Comptroller of New York State issued a report stating that corporate corruption had cost the New York economy USD 2.9 billion and a cut in tax revenues of USD 1 billion. A Control Risk Group Report from 2006 shows that one in four UK companies lost business to corruption in the past 5 years. (See

http://www.transparency.org/content/download/10177/85676/file/controlrisks2006_corruption_survey.pdf)

In this U4 Expert Answer we set out reasons why companies and individuals should be motivated to carry out their business with integrity. We also present findings from a recent study on corporate social responsibility that interrogates the issue of what really makes companies act ethically.

Part 2: Incentives for Integrity at the Corporate Level

Practices that were once seen as an inevitable part of doing business in many parts of the world are becoming increasingly unacceptable. More stringent domestic laws and international conventions such as the 1999 OECD Anti-Bribery Convention and the United Nations Convention against Corruption (UNCAC) are compelling companies to develop new anti-bribery policies or to review existing ones. The high-profile corporate scandals of recent years have made companies increasingly aware that corrupt practices pose serious and costly risks to their reputation and sustainability. This understanding, coupled with growing public expectation of accountability and probity in the corporate sector, are putting added pressure on companies to articulate and live up to more ethical business practices.

Perhaps the most compelling reasons for companies to act ethically are those reasons which also make business sense. For example a company that demonstrates anti-bribery commitments with proven implementation can gain access to bidding lists of companies and public institutions which demand evidence of no-bribes policies. Under US sentencing

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guidelines “No-bribes” policies which are in place can, if indeed something does go wrong and companies are accused of bribe-giving or taking, lead to reduced sentences under blacklisting procedures. In addition, the existence of no-bribes policies allows companies to figure in Social Responsible Investment (SRI) indices, such as the FTSE4Good and Dow Jones Sustainability (DJSI), and to be recommended by ethical investment programmes. Overall, companies are aware that an ethical reputation will impact the company's long-term success because it results in fewer crises, an enhanced ability to attract excellent young staff and, in some cases, stronger acceptance by consumers.

Researchers at the Chr Michelsen Institute have analysed the effect of Corporate Social Responsibility programmes on business ethics (http://www.cmi.no/pdf/?file=/publications/2007/2_07_web.pdf) Part of their analysis looked at what responsibilities are profitable and in the interest of firms to pursue, and how firms can be given incentives to fulfil their other responsibilities. Their findings are notable:

“The claim often made by business executives, that CSR is profitable, is unsubstantiated. Empirical studies on the relationship between CSR and profitability, are inconclusive and largely uninformative due to severe methodological shortcomings. Nor is there a theoretical justification for the idea that CSR is generally good for profits. The implication is that many of the responsibilities assigned to corporations will not be pursued voluntarily, requiring the imposition of additional incentive mechanisms for firms.

The programme has focused on three areas of corporate incentives for CSR; organizational structure, market structure, and executive pay. A code of ethics is unlikely to have a significant and lasting effect on behaviour in an organization where misconduct is sufficiently engrained. An article published in the Journal of Socio-Economics, argues that norms are formed and reformed through the continued interaction of workers within firms, and interaction between firms. By implication, the structure of an organization affects the outcome in terms of norms. Changing widely accepted but unproductive norms may require substantial organizational change. The introduction of a code of ethics must in certain cases be accompanied by an organizational restructuring, to effectively reduce misconduct.

Executive pay can be fixed or performance-based. A final result established by the programme is that an introduction of performance-based pay decreases effort executives allocate to CSR under certain conditions. This is an important result, which suggests that there may be trade-offs between corporate governance reform, and corporate social responsibility, which is contrary to much of the received wisdom in this area.”

Part 2: Incentives for Integrity at the Personal Level

If there is a clear company commitment to containing corruption, staff will be able better to identify with the company's goals and resist engaging in corruption. Indeed, as indicated above, for senior staff the risk of criminal prosecution is lessened if the company has clear anti-corruption policies. A good company anti-corruption programme should also have a helpline and whistleblower function which will make staff feel more comfortable in dealing with dilemmas and being able to get advice or in extremis to blow the whistle.

Part 3: Further reading

OECD Guidelines for Multinational Enterprises

http://www.oecd.org/document/6/0,2340,en_2649_34889_36887622_1_1_1_1,00.html

[Business Anti-Corruption Portal](#) This portal supports small and medium sized enterprises (SMEs) in avoiding and fighting corruption and creating a better business environment.

TI's Business Principles.

http://www.transparency.org/global_priorities/private_sector/business_principles

The Business Principles provide a model for companies seeking to adopt a comprehensive anti-bribery programme. TI encourages companies to consider using the Business Principles as a starting point for developing their own anti-bribery programmes or as a benchmark for existing ones. To support the users of the Business Principles, TI has produced a suite of tools, including a comprehensive [Guidance Document](#) which provides additional background and practical information for those wishing to implement the Business Principles or review their own anti-bribery processes. The [TI Six Step Implementation Process](#) is a how-to guide for companies that are early on in the process of devising and implementing an anti-bribery programme. TI is also developing a Self-Evaluation Module to assist companies wishing to assess their anti-bribery performance.