ANTITRUST AND COMPETITION CORPORATE GOVERNANCE NEWS

We Need More Research on Corporate Corruption

BY ARMANDO CASTRO, NELSON PHILLIPS *November 5, 2020*

Image by erhui1979, via Getty Images

The last decade has seen a continuous drumbeat of revelations of corporate corruption and the current economic crisis is sure to reveal many more. But most studies of corruption have focused on government. A new study integrates research on corporate corruption and identifies areas urgently requiring more attention.

Corporate corruption remains an unsolved problem with the potential to erode trust in business and interfere with the proper functioning of competitive markets. Over the last few years, corruption has been uncovered at a veritable who's who of the corporate elite including Airbus, Goldman Sachs, McKinsey, Novartis, Siemens, and Rolls Royce. By all indications, we have made little progress in understanding how to prevent corporate corruption before it happens and made only moderate progress on detecting it when it is occurring.

We expect further significant scandals to arise soon due to the effects of the Covid-19 pandemic and the resulting economic crisis. As Warren Buffet famously observed in his 2001 Chairman's letter to Berkshire Hathaway shareholders, "you only find out who is swimming naked when the tide goes out." Good economic times cover up a multitude of business sins, including helping corrupt managers conceal their nefarious activities. Consider how recessions and economic slowdowns such as the 2008 financial crisis led to the uncovering of the Madoff investment scandal. Indeed, many of the largest corporate corruption scandals of the past 20 years—for example, Enron and WorldCom—emerged in or immediately following economic downturns.

Yet, in media reports and even in academic research, corruption in government is much more prevalent. In fact, a 2017 report by the European Commission showed that "37 percent of EU businesses consider corruption to be a problem for them when doing business."

According to the World Bank, "moving business from a country with a low level of corruption to a country with medium or high levels of corruption has been found to be equivalent to a 20 percent tax on foreign business." Yet what is usually less mentioned is that many immoral companies quite often admit to having used corrupt strategies. A 2014 survey of businesses by the European Commission found that 60 percent agree with the statement that bribery and the use of connections is often the easiest way to obtain certain public services. So in reality, corruption is much more complex than it's commonly portrayed.

In a recent paper, we explore the existing academic research on corruption in business and argue that corporate corruption—which we define as "the misuse of formal power by a corporate representative for personal and/or organization benefit"—deserves to be recognized as a distinct type of corruption and further researched.

We review the existing literature in management and adjacent literature to identify four key perspectives on corporate corruption that span levels of analysis, deploy different methodologies, and draw on different theoretical foundations: 1) corruption as rational action; 2) corruption as institutionalized practice; 3) corruption as cultural norm; and 4) corruption as moral failure.

To date, there has been little recognition that scholars working in these different areas are engaged in the same enterprise and a few conversations between these different perspectives have occurred. We argue that business school researchers, with their deep knowledge of corporations, are uniquely positioned to develop an improved understanding of corporate corruption to better guide regulators, business executives, and others in thinking about how to better deal with corporate corruption. So it is critical to begin these conversations to achieve a comprehensive understanding of corporate corruption

This is not, of course, to say that there has not been extensive research on corruption. In fact, existing research on corruption has provided a range of thinking about its causes and how to prevent it. At the same time, the existing work has focused almost exclusively on corruption in government. Much of this government corruption research focused either in a firm facilitating corrupt activity, providing improper incentives of some kind to a government official, or an official "straddling" the boundary between government and the private sector to benefit in some way. Yet little attention has been paid to the corporate partners in these types of corruption.

Furthermore, significant instances of corruption occur within and between firms, both large and small. So focusing on corruption in corporations is an essential perspective to complement the work on corruption in government and understand corruption in general.

Therefore, focusing *on corporate corruption* is particularly important as, while both government and corporate corruption involve people in positions of power abusing their authority, the contexts in which the abuse occurs are fundamentally different.

Government bureaucracies differ from companies in terms of culture, incentives, governance, and logic, making the opportunities for corruption, the decision to be corrupt, and the practicalities of acting corruptly, radically different. Unlike governments, firms face competitive pressures that can affect the likelihood of executives engaging in corruption. The impression, whether true or not, that competitors are engaging in corrupt behavior can lead to pressure to follow suit in order to maintain the firm's competitive position. Intense competition leads firms to search for any advantage that might help them beat their competitors and can make corruption more likely.

> **"Significant instances of corruption occur within and between firms, both large and small. So focusing on corruption in corporations is an essential perspective to complement the work on corruption in government and understand corruption in general."**

Recognizing that corporate corruption is a phenomenon that deserves attention also reveals new and important questions that should be further researched. First, while entrepreneurship may create wealth, jobs, and provide new products and services that improve everyday life, this is far from being universally the case. In many parts of the world, not only are many entrepreneurs corrupt, but entrepreneurship is often highly corrosive of the institutions that support fair and regulated markets.

Focusing on corporate corruption raises several important questions about entrepreneurship: Why do some entrepreneurs engage in corruption? Why do some entrepreneurs identify opportunities that involve corruption while other entrepreneurs in the same context do not? Understanding more about how to create legitimate businesses in corrupt contexts is another area that deserves attention from researchers. If new ventures engaging in corrupt business are identified, it is important to reform the business in a way that preserves jobs and revenues and relationship building but also eliminates corruption. But how should the government, or other actors, respond? What levers exist to move a business into less corrupt activities?

Second, a focus on corporate corruption raises questions around innovation. Innovation can happen in startups as well as established firms and it is generally believed that corruption negatively affects both types of firms. This would be the case since corruption might allows firms to sell new substandard goods and avoid health and safety and labor laws. Yet some scholars have argued that actually corporate corruption, "greasing the wheels", might have a positive effect on efficiency of the delivery of innovation as whole, helping to overcome bureaucratic obstacles. This counterintuitive finding highlights the need for more research on the nexus between innovation and corporate corruption to understand the different impacts of corporate corruption on innovation. Research can further explore how adopting questionable, immoral, and illegal tactics (e.g., erecting entry barriers to deter competitors, avoiding labor taxes, or relaxing safety standards and sidestepping regulations) affects innovators in these markets.

Third, there are many questions about corporate corruption and digital transformation that have received little attention. From a corporate corruption perspective, new digital technologies are a two-edged sword. On the one hand, a key step in addressing corporate corruption is the development of better anti-corruption technologies. Emerging digital technologies such as blockchain and AI can be applied to expose and prevent corrupt practices and discussions of digital transformation in the corporate world have huge ramifications for the ability to reduce corporate corruption. At the same time, these same technologies can just as easily facilitate corporate corruption. Blockchain, particularly cryptocurrencies, can just as easily hide transactions as make them transparent and an understanding of the implications of these technologies for corporate corruption and good corporate governance remains under-developed. Therefore, this area offers a fertile avenue for research.

In summary, given the extremely negative impact of corporate corruption on businesses, investors, and government, this is a *grand challenge* where researchers of all kinds can have a significant and immediate impact on society. While it has parallels with corruption in government, corruption in corporations has significant differences due to the special nature of the firm, and applying solutions developed to deal with corruption in government risks failure. We hope that our work helps advance this critically needed research program.

Related Posts:

1. The SEC's Shareholder Voting Reform Runs Counter to Attempts at Democratizing Corporate America
2. Should Whistleblower Reward Laws be Capped?
3. Government Regulation is the Pro-Market Solution

TAGS *Corporate Governance* *Corruption* *economists* *regulatory capture* *research*

Previous article
Social Media Companies Survived Election Day. More Tests Loom.

Next article
Uber and Lyft in Driving Seat to Remake US Labour Laws

LATEST NEWS

The Useful Distraction of Section 230

Institution Man: How Corporations Came to Dominate the US Economy