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Policy Briefing Note: Drafting Executive Regulations to Fight Corruption
Drafting Implementing Regulations for International Anti-Corruption Conventions: A Summary

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Introduction

For over 10 years, organisations such as the Organisation for Economic Co-operation and Development (OECD), the Council of Europe (CoE), and the United Nations (UN), have been intensively helping developing countries adopt legal measures to fight corruption. However, such work has sometimes had less than desired impacts on reducing corruption. The UN, OECD and CoE conventions against corruption have been under-effective because these conventions, while being ratified by national parliaments, are not being implemented in executive agencies most prone to corruption – particularly the traffic police, security services, customs, and tax inspection. This short article seeks to provide practical guidance (inspired by the academic and practitioner literature on the subject) for the advisors of executive agencies (particularly working in Central and Eastern Europe) who are looking to help implement international conventions in their agencies. Figure 1(a) and (b) show the various legal provisions which may be adopted in order to help strengthen transition economies’ fight against corruption and maps the various arguments made in the original paper which this article summarises.

The Cause of Corruption

Corruption is caused by regulations which prevent economic actors from engaging in activity which they would prefer to engage in. These regulations cause rationing and other types of economic distortions which led to the creation of rents. These rents provide a “pool of resources” which can be used to pay civil servants (who are supposed to be enforcing particular regulations) either to do their job or not to do their job. While more regulations on civil servants can sometimes reduce corruption (particularly when these regulations help increase productive over-sight or reduce secrecy), regulations often cause economic harm. Regulations require resources (and thus tax revenue) in order to be enforced and they can cause demoralization. While slapping regulations on civil servants is an almost visceral response to corruption, such an approach can – and often does – cost more than it benefits the civil service.

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economic distortions create black markets and incentives to break law

contract test intention and act for a corruption offence

criminal liability test deciding which party has regular habits of collecting bribes and which party had a clear, present and distressing need to pay a bribe

respondeat politicae dismissal if any staff involved in corruption

civil law standard and fines civil servants can be sanctioned for failing to prevent the appearance of engaging in bribery

corruption

poor anti-corruption regulation raising taxes, vexes civil servants and prevents optimal performance

optimal detection effort balances rising costs of shared liability and lower benefits from avoiding more corruption

complicity test tests probability of scienter and harms from corrupt act

civil servants can be sanctioned for failing to prevent the appearance of engaging in bribery

Figure 1a: Increasing risk of losing a share of rents

respondeat superior

“pool” of rents

complicity

administrative liability

criminal system malfunction

low risk of detection

Figure 1b: Decreasing expected pay-off through fines

performance-based budgeting giving law enforcement agencies resources proportional to their effectiveness.

dampening effect reducing compensation proportionally in order to prevent “shake downs”

marginal benefit principle allocate bounty to individual or agency who can best fight corruption

recover assets from foreign countries

empowering managers and administrative tribunals assigning jurisdiction over a case of suspected corruption to the agency who can most cheaply process the case.

internalising the externality reward to whistle-blower should exceed individual costs and strike a fair balance between rewarding stool-pigeon and providing welfare to harmed third-parties.

negligence fines companies pay fines based on probability of participation in corruption.

Figure 1c: Legal Solutions to Corruption

first best: removing distortions

second best: spreading liability over more actors, dissuading corruption

third best: “mopping up” rents through optimal fines.

fourth best: providing anti-corruption self-financing mechanisms

companies pay fines based on probability of participation in corruption.

increases corruption money used to pay negligence fines

decreases corrosion acts as financial deterrent to paying bribes

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In developing countries, bribes are often confused with gifts. A two-part test can help civil servants (and the internal as well as external prosecutors who must decide between bribes and gifts) understand the difference between bribes and gifts. A “payment” (a bottle of cognac or a box of chocolates) is not corrupt consideration if the gift does not coincide with the delivery of a service which the public service user has a right; and if the civil servant could not anticipate ex-ante (before delivering the service) that the gift would be rendered. If both these tests succeed, the “payment” is unlinked with possible corrupt service delivery. Naturally, a fixed rule against accepting any gifts may be easier to implement and cases where one part of the test fails would require special consideration. These issues are discussed in-depth in the full article.

Corruption often remains unprosecuted because in many cases, prosecutors can not tell the difference between the initiator and the passive participant. Clearly, justice demands that the passive or unwilling party should receive a lighter (or no) punishment for engaging in corruption. In order to help assign responsibility, a test can be applied which helps identify which party held the criminal intent. Namely, liability for corruption should fall more heavily on the party which has regularly established methods of engaging in corruption and liability should fall more lightly on the party which had a “clear, present and distressing” need to perform on the corrupt contract.

Corruption must occur because civil servants’ bosses (or superiors) exercise insufficient oversight over their subordinates. Thus, transferring additional liability for corruption through a public sector version of respondeat superior may both increase the superior’s incentives to engage in oversight and reduce the profitability of corruption (particularly in cases where the superior may be involved). Such respondeat superior can be seen a risk-transferring mechanism – assigning liability in a way to encourage oversight.

In the developing world, corruption is sometimes tied to political clientalism (and the proceeds from corruption are sometimes used to finance political campaigns). A form of respondeat politicae may reduce the incentives to collect bribes for use in the political process. Under respondeat politicae, the politician would be legally required to resign from office if any funds used to fund the candidate’s campaign resulted from bribery or corruption. The political equivalent of respondeat superior in an administrative context, the politician would answer for the corruption of his or her campaign staff.

Both respondeat superior and respondeat politicae point to expanding the legal definition of complicity in corruption offenses. In many corruption cases, colleagues of the corrupt official either passively participate or at least have scienter (guilty knowledge). Most legal traditions define for both delicts and crimes “inchoate offences.” In the case of corruption, such inchoate offences – particularly conspiracy in or aiding and abetting corruption – should clearly place liability on civil servants who know about – or who are likely to know about – their colleagues’ corruption.

Making Government a Good Neighbour: Applying a More Stringent Duty of Care Standard to the Public Sector

In theory, government arises from a social contract made between free individuals. Such a social contract imposes on government (and its employees) the positive obligation to protect
citizen rights and promote their interests. Governments, as organisations, incur risks too large for private individuals (or even particular representatives of the current administration) -- in contract to corporations in which liability vicariously passes to directors or their appointed representatives. Government, by constitution, must exercise a duty of care in its administration above and beyond the good neighborliness of other organisations.

Toward its own civil servants, the government agency has a positive obligation to ensure civil servants do not have incentives to engage in corruption. If a civil servant engages in corruption because of strong incentives provided by his or her department, the government (as an organisation) should clearly found liable for contributory negligence. Because government agencies are created to assume public risks and because of the compelling nature of government's duty of care, the burden of proof should be reversed – such that contributory negligence of a government department should be an effective defense against charges of corruption and the agency’s superiors must show (to a civil law standard) that the agency afforded a reasonable level of protection to its civil servants.

Toward public service users, government agencies also have the duty of care. Clearly, civil servants who solicit bribes commit two legal infraction – the personal infraction committed by the civil servant (acting *ultra vires*) and the professional infraction (as the civil servant follows the incentives and implied terms of his or her service contract). While managerial, administrative, civil or criminal proceedings can be filed against the civil servant, *his or her department should also bear responsibility (morally if not legally) in cases where public service users must pay bribes.* As will be discussed later, damages paid by the government should be equal to the social harm engendered by the corruption of its staff.

Civil servants have the duty to report cases of suspected corruption, given their duty to rescue the public service user. Clearly, failure to report cases of suspected corruption make the civil servant with *scienter* complicit in the corruption offence. If the civil servant is likely to have known about the corruption of his or her peers, that civil servant should be prosecutable under a civil law standard (as applied in an administrative or civil law context).

Because government agency managers both have a duty of care and bear responsibility for possible corruption under *respondeat superior*, they should be allowed to engage in *integrity probes* of their staff. Such integrity probes may involve placing a nominated individual in contact with randomly sampled civil servants from the manager's department in order to measure the frequency by which agency staff solicit bribes. Because such probes are so new, the goal of such probes (as a “smoking out” exercise as opposed to as a measurement exercise of the magnitude of corruption) is often unclear as is the legal basis for such probes.

Despite pleas that these probes are illegal or unconstitutional, in many countries these probes can be designed in ways which *avoid entrapment* and do not violate privacy (and indeed may protect privacy better than the panoply of other checks already in place). Such probes may not fall afoul of entrapment if such probes are used only to collect data on the incidence of bribery, if civil servants consent to these probes (to the extent they are statutorily allowed) and temptation is not added to the probe exercise.

**Paying for Anti-Corruption**

Public budgets in developing countries are often too small to fund large scale anti-corruption work – requiring some anti-corruption work to be *self-financing*. Allowing law enforcement
agencies to keep (or claim from the budget) a proportion of the value of corruption they successfully detect and prosecute can both provide incentives to fight corruption and tie anti-corruption effort to the amount of corruption affecting the agency. Such payments also allocate resources to the individual or agency which can best fight corruption. While some countries have had good experiences using such a scheme (for example letting the Agency sell off cars seized from criminals), too strong ties between crime detection and budgetary allocations can lead to “shake downs” and more inspections than economically, socially or legally desirable. However, rewards to department and civil servants (in the form of promotion prospects or perquisites paid by many developing country governments such as social housing or subsidies on public services) can be dampened to reduce the incentive to shake-down public service users.

*Qui tam* rewards can also help finance anti-corruption work as well as provide positive incentives to prevent corruption (instead of the negative incentives attendant with extending liability for corruption offenses as described earlier). The phrase *qui tam* derives from *qui tam pro domino rege quam pro se ipso in hoc parte sequitur*, meaning he who sues for the king as well as for himself. *Qui tam* provisions allow individuals to sue an individual who harms the State and claim a share of the damages paid by the offender. In a corruption context, *qui tam* rewards certainly include lost revenue (from under-valuation of customs or tax declarations) and – depending on the liberality of the legal tradition – may even include damages for restricts in trade, harm to third-parties and the cost of enforcement.

The optimal *qui tam* reward will balance the need to reward the whistle-blower with the need to compensate victims and fund future anti-corruption work. Figure 2(a) shows the economic value of harms from corruption as lying on a line. Clearly bribes paid represent harms -- either as money unwillingly paid (in the case of coercion) or as losses in inefficiency (as preferential treatment is given to a less efficient producer, intermediary or less needy consumer). However, corruption indirectly harms a number of third parties – companies which compete with the briber, consumers vying for public services (which may be rationed). Corruption can also increase prices, thereby decreases real wages and/or returns on capital. These social harms are also represented on a line in Figure 2(a) as social harms.

Any *qui tam* award which is above the cost of investigating and exposing corruption results in gains to number of parties. Figure 2(b) illustrates the case in which the reward level is less than the bribe paid. The extra money is returned to the government or original victim and third-parties gain from being rescued from the damages concomitant with the corrupt act. Figure 2(c) shows the case where the whistle-blower is paid more than the value of the bribe – internalizing the gain to third-parties which his or her whistle-blowing activity has engendered. The government would still have an incentive to compensate the whistle-blower for this amount because the society overall still benefits. In this example, the malfeasor either internalizes part of the negative externality (or damage) which his corrupt act has caused by paying more than he or collected in bribes; or society compensates the whistle-blower from the general budget. However, Figure 2(d) shows the harms of offering too high a reward. For rewards which exceed the value of all harms imposed on society, the whistle-blower searches for ways of obtaining these rewards (instead of engaging in other productive activity) and government forgoes spending on other socially beneficial activities in order to pay the whistle-blower. The optimal reward clearly balanced the need to provide the maximum incentives (reward) to the whistle-blower with the need to use these resources on other productive anti-corruption activities.
Who Should Investigate Corruption? Where Should the Case be Heard?

Heavy reliance on the criminalisation of corruption offences is not practical in corruption-ridden public administrations. Four jurisdictional levels can be defined for investigating and prosecuting corruption offences (as shown in Figure 3).

**Managerial:** The suspected civil servant’s manager receives a complaint and hears preliminary evidence. The manager imposes remedial disciplinary measures (such as written sanction); being convinced of guilt on a civil evidentiary standard. Managers can reasonable handle minor offences where the civil servant is probably acting individually, probably has no repeated offences and the offence involves a small amount of money.

**Administrative:** The suspected civil servant appears in front of a dedicated tribunal (such as one in Internal Security/Affairs or in an administrative court). The administrative instance has expanded powers of investigation (including ability to subpoena witnesses and documents) and prosecution (ability to impose fines and fire). Administrative jurisdiction should be reserved for cases of possible collusion between multiple suspects, where a more senior officer is involved, or when the manager is not-competent to adjudicate. The administrative instance may also hear appeals of managerial sentences.

**Civil:** The suspect may be called to compensate victims of corruption for damages. Civil procedure is well-defined and applies a more lenient burden of proof than that required for a criminal case. As discussed previously, the government agency should be eligible to act as a plaintiff or defendant in civil cases.
**Criminal:** Used when evidence against a suspect is likely to convince a judge or jury that the civil servant engaged in corruption “beyond a reasonable doubt.” Penalties under criminal liability are often rather severe (large fines, jail time). International organisations promote criminalisation because of expected deterrence effect of criminal sanctions (though the extent of such deterrence remains to be empirically proved!)

The investigation of corruption offences should be done by the individual or organisation with the **lowest marginal cost** and highest marginal benefit of conducting the investigation and/or prosecution. Any Internal Security department or Anti-Corruption Agency in a corruption-prone government will have a docket of corruption cases. The cases in this docket can be sorted by the probable amount of funds involved in the particular corruption case (accepting that very few cases have enough *prima facie* evidence to ascertain with certainty the amount of bribes collected by corrupt officials). The investigators can subsequently prosecute those high value cases (or cases which cause the greatest amount of economic distortion to commerce). Balanced against the gains of prosecuting these cases are the costs of prosecution. The extra marginal hour the investigator spends collecting evidence will have different impacts for different cases. Again, the docket of cases can be sorted based on the expected likelihood of collecting strong enough evidence to convince a judge or jury of the suspect's guilt. Clearly, in some cases, handing over cases to the police for criminal prosecution very expensive and the expected quality of evidence collected by the Internal Security department of the Agency involved is at least at good as that collected by the prosecutor's office.

Corruption increasingly crosses national borders. In one recent case, Turkish nationals smuggled American goods through Ukraine, Poland and finally into Germany -- bribing officials in each transit country. Because of the fundamental legal principle that the same case can not be tied in more than one place and that judgment is a *res judicata*, the issue of *forum selection* comes to the fore. Because of the differing quality of various legal systems, the highest quality courts should be used -- using a legal standards of the jurisdiction decided by the judge in that court.

Should British bank regulators and courts accept rulings from Nigerian courts about the guilt of Nigerian citizens with accounts in the UK (for example)? As corruption -- and the proceeds from corruption -- increasingly crosses national borders, national courts and executive agencies need to decide on the extent to which they will accept the judgments of foreign government bodies. *Under the United Nations Convention Against Corruption*, countries who receive requests for the restitution of gains from corruption can apply four standards -- foreign jurisdiction (accepting foreign requests), translated judgment (retrying the case by receiving country's legal standards), joint judgment (participating in the foreign investigation and trial), and no foreign jurisdiction. The choice of which standard to apply depends on the reliability of the foreign court and the costs/benefits of applying each standard.

Restituted funds in corruption cases can be awarded to a number of parties; and the choice of beneficiary should be governed by both concerns for efficiency and equity. Allocating part of these funds to the *law enforcement agency* helps provide salary, material and moral incentives to continue investigating international corruption cases. Awards to the *victims of corruption* (or the plaintiffs in a lawsuit) encourage victim activism against corruption and justly ties compensation to actual harm. Providing damages to *groups of individuals indirectly harmed* by the corruption case -- through a class-action suit for example -- helps remedy social harms caused corruption and ties benefits to social harms (a desirable feature from a public policy
Helping to Enforce the OECD Anti-Bribery Convention

The OECD Convention criminalizes the payment of bribes by businessmen from OECD member countries to foreign officials anywhere in the world. Yet, the relative lack of successful prosecutions under the Convention suggests that a criminal standard (requiring guilt beyond a reasonable doubt) as well as the problems of international investigation may be hindering the successful application of the Convention. The Convention can be amended in order to help promote enforcement without significantly reducing liberties or hindering trade. Organisational liability -- incurred by the corporation independently of its directors -- can be established for corruption offenses. Such a civil (rather than criminal) liability would be incurred when: a) representatives of the company could reasonably anticipate that a company representative could have incentives to engage in corruption and, b) when the company can not provide documentation definitively refuting allegations of corruption. Effectively, such a provision reverses the burden of proof on corporations as legal persons (but not for its directors and members as "real" persons). The reversal of the burden of proof is justified by the stronger duty of care which should be required of corporations and the lower costs of obtaining the evidence needed to disprove allegations of corruption.

Organisational liability for corporations whose employees are suspected of engaging in corruption can pave the way of "negligence fines" which dissuade corruption and provide finance for anti-corruption work. Such "negligence fines" (targeted at companies which can not show that they are not engaged in corruption) encourage companies to spend more on self-monitoring. For too low levels of fines, companies have the incentives to benefit from corruption and pay these low fines. Fines which are set too high choke-off commerce, as businesses spend large amounts of money on protecting themselves against allegations of corruption. The optimal fine balances these two effects; while also providing finance for future anti-corruption work (particularly qui tam rewards for whistle-blowing).

Conclusions

International anti-corruption conventions are forcing signatory countries to impose more regulations on their administrations and spend taxpayer money on controls without providing means of financing these requirements. Yet, many non-regulatory legal solutions exist in order to help fight corruption. The best legal solutions remove the economic distortions which cause rents (and thus rent-seeking behaviour) in the first place. The second-best legal remedies -- such as expanding the liability for corruption through punishment for complicity, respondeat superior, respondeat politicae, and applying a more stringent duty of care -- help spread liability over more people; making corruption more expensive to participants in corrupt transactions. The third-best legal remedies "mop-up" the rents from corruption by rewarding whistle-blowers, investigators, and other law enforcers -- while providing the socially welfare maximising compensation to victims of corruption from these rents. The fourth-best remedies make anti-corruption work self-financing; providing incentives for more individuals to fight corruption instead of actively participating in it.