

# Corruption sometimes fosters regulatory compliance, new study shows

May 7 2013

---

(Phys.org) —Inspired by a personal experience, a University of Arkansas economist examined the relationship between corruption and regulatory compliance – on both a theoretical and empirical level – and found, surprisingly, that corruption in some circumstances actually fosters regulatory compliance.

"What I found was that whenever public agents who control monitoring are paid a fixed wage – and that point is critical – an increase in corruption may actually foster regulatory compliance," said Fabio Mendez, associate professor of economics in the Sam M. Walton College of Business. "How is this possible? It happens because the prospects of obtaining a bribe drive corrupt public officials – whether it's a [police officer](#) or a food inspector or a tax regulator – to monitor firms with greater intensity. That is, if those agents think they could make a little extra money, they'll work harder, and when firms – or people, for that matter – are monitored with greater intensity, they find it optimal to comply with regulations."

Mendez, who studies corruption in general, conceived the idea for this study while on vacation with his wife outside the United States. Driving to a beach, he saw a policeman – presumably paid a fixed wage – napping in a patrol car. Confident that he would not get pulled over, Mendez sped up and exceeded the speed limit after passing the patrol car. Later, while returning from the beach, Mendez exceeded the speed limit again and was stopped by a different officer, who, after much explanation about how difficult it would be for Mendez to resolve the

matter, essentially asked for a bribe.

It occurred to Mendez later that under circumstances such as this, [private individuals](#) might be more motivated to comply with laws and regulations if they knew they would have to deal with a corrupt official.

Which is counter to the prevailing assumption about corruption. It is generally assumed that corruption – in government and business – discourages or erodes regulatory compliance. In other words, if citizens know that their government officials accept bribes, then it is more likely that those citizens will feel justified or comfortable disobeying laws and regulations. In fact, many legal and economic studies overwhelmingly support this notion – that regulatory compliance decreases in the presence of corruption. But Mendez's study showed this isn't always the case.

His findings were the same on both a theoretical and empirical basis. Mendez first developed a theoretical model upon which compliance might increase under corrupt conditions. In the model, public officials monitored the actions of private firms that must adhere to government regulations. Firms chose whether to comply with the regulations depending on the monitoring rate they faced and the incidence of corrupt officials. And, depending on the existing level of regulatory compliance, public officials chose the degree of monitoring effort and their willingness to accept bribes. The model merely showed that it was possible for corruption to foster compliance.

In the empirical study, Mendez used firm-level data from the World Bank's Business Environment and Enterprise Performance Survey, which includes information about 4,100 private firms in 26 "transition" countries. Primarily Eastern European, transition countries are those that are changing from a centrally planned economy to a free market economy. The survey examines interactions between the firms and the

state regulatory agencies that monitor them. It contains detailed information regarding bribes paid to government officials and the purposes for which they were paid. Specifically, Mendez focused on compliance with regulations requiring firms to pay sales tax and the bribes these firms paid to avoid paying the taxes. At the firm and industry level, the data corroborated the theoretical findings and showed that corruption was positively correlated with compliance.

"I guess you could say 'encourages' or 'promotes' compliance, rather than fosters," Mendez said, "but I don't want to give the impression that corruption is a good thing. This study simply shows that it is possible under certain conditions for [corruption](#) to increase compliance, and I think the findings are important because they might compel organizations to evaluate how they pay employees."

Mendez's study was published in *Public Choice*, a research journal that explores the intersection of economics and political science.

Provided by University of Arkansas

Citation: Corruption sometimes fosters regulatory compliance, new study shows (2013, May 7) retrieved 10 July 2024 from <https://phys.org/news/2013-05-corruption-fosters-regulatory-compliance.html>

This document is subject to copyright. Apart from any fair dealing for the purpose of private study or research, no part may be reproduced without the written permission. The content is provided for information purposes only.