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## Corruption as an Assurance Problem

Philip M. Nichols

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# **CORRUPTION AS AN ASSURANCE PROBLEM**

PHILIP M. NICHOLS\*

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INTRODUCTION

Corruption is the use or abuse of public office for private gain.<sup>1</sup> Although particular definitions of corruption may be different, its conceptualization appears to be universal, and corruption is universally condemned.<sup>2</sup> Corruption was condemned in the past just

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1. This definition is drawn from Joseph Nye, who defines corruption as “behavior which deviates from the formal duties of a public role because of private-regarding (personal, close family, private clique) pecuniary or status gains; or violates rules against the exercise of certain types of private-regarding influence.” J. S. Nye, *Corruption and Political Development: A Cost-Benefit Analysis*, 61 AM. POL. SCI. REV. 417, 419 (1967); see Thomas F. Burke, *The Concept of Corruption in Campaign Finance Law*, 14 CONST. COMMENT. 127, 129 n.9 (1997) (citing Nye’s definition); Claire Moore Dickerson, *Political Corruption: Free-Flowing Opportunism*, 14 CONN. J. INT’L L. 393, 396 (1999) (same); cf. Saladin Al-Jurf, *Citizens, National Governments, and International Financial Institutions: Changing Conceptions of Development in the 1990s*, 9 TRANSNAT’L L. & CONTEMP. PROBS. 193, 196 (1999) (stating that the World Bank’s definition of corruption is “[t]he abuse of public office for private gain”); David H. Bayley, *The Effects of Corruption in a Developing Nation*, 19 W. POL. Q. 719, 720 (1966) (Corruption is the “misuse of authority as a result of considerations of personal gain, which need not be monetary.”); Philip B. Heymann, *Democracy and Corruption*, 20 FORDHAM INT’L L.J. 323, 325 (1996) (describing “[c]orruption, as secretly receiving private benefits to affect a decision that is supposed to be made in the interests of others and uninfluenced by private gain. . .”).

2. See Ibrahim F.I. Shihata, *Corruption—A General Review With an Emphasis on the Role of the World Bank*, 15 DICK. J. INT’L L. 451, 453 (1997) (relating that “[s]ocieties may differ in their views as to what constitutes corruption, although the concept finds universal manifestations.”).

as it is condemned now.<sup>3</sup> Corruption is condemned by monotheists,<sup>4</sup> pantheists,<sup>5</sup> and other religious schools of thought.<sup>6</sup>

Despite such approbation, corruption continues to exist and presents a serious obstacle to change in emerging economies. Corruption imposes tremendous costs in the form of parallel institutions<sup>7</sup> and diminished foreign investment.<sup>8</sup> Corruption degrades bureaucratic decision-making and popular support for change.<sup>9</sup> Corruption, therefore, is squarely in the sights of those who wish to effectuate positive changes in emerging economies.<sup>10</sup>

Most people perceive corruption as a failure of institutional controls over bureaucrats or a failure of the legal system that controls

3. See THE CODE OF HAMMURABI (Robert F. Harper trans., 1904) (making the taking of bribes illegal like the Egyptian Edict of Harmab). "If a man (in a case) bear witness for grain or money (as a bribe), he shall himself bear the penalty imposed in that case." *Id.* § 4.

4. See The Meaning of the Holy QUR'AN, 2:188 ('Abdullah Yusuf 'Ali trans., amana publications 8th ed. 1996) (warning not to "eat up your property among yourselves for vanities, nor use it as bait for the judges, with intent that ye may eat up wrongfully and knowingly a little of (other) people's property"); see also *id.* 28:77 (stating that "Allah loves not those who do mischief").

5. See UPENDRA THAKUR, CORRUPTION IN ANCIENT INDIA 14 (1979) (explaining that "a perusal of the Sm ti works makes it clear that the earlier Sm ti writers prescribe a much more drastic punishment for the bribe seeker [than for the bribe giver], who finds a graphic mention in one of the early inscriptions").

6. See U. Dhammaratana, *The Social Philosophy of Buddhism*, in THE SOCIAL PHILOSOPHY OF BUDDHISM 1, 17-18 (Samdhong Rinpoche ed., 1972) (noting that "[s]ila [morality] as practiced by the Buddha may be said to be the widest [moral principle] in scope. . . . The second moral precept of refraining from taking what is not given . . . involves abstinence from all deceptive practices such as bribery that lead to social disintegration.").

7. See discussion *infra* Part I.A (detailing the costs of the creation of parallel institutions and noting attempts at various types of parallel institutions through history).

8. See discussion *infra* Part I.B (citing empirical evidence that corruption negatively decreases foreign investment).

9. See discussion *infra* Part I.D, I.E (arguing that because people lose faith in corrupt institutions, there is little incentive or possibility for social or economic growth).

10. See Martin Wolf, *Corruption in the Spotlight*, FIN. TIMES, Sept. 16, 1997, at 23 (stating that it "is difficult to think of a significant international organization not looking at corruption.").

the behavior of bribe payers.<sup>11</sup> In essence, these views treat corruption as a conglomeration of discrete failures, which in the aggregate constitute a phenomenon. While such a description of corruption undoubtedly does reflect some aspects of corruption, a differing description may provide fresh insights—and new approaches to addressing corruption.<sup>12</sup>

This paper suggests that corruption presents an assurance problem.<sup>13</sup> An assurance problem exists when all actors are better off if they adhere to at least the same minimal standard, but are second best off if, in the event that there are defectors, they join the defectors rather than continue to adhere to the standards, and are worst off if there are defectors but they do not join those defectors. Actors faced with an assurance problem, therefore, must choose between cooperating in hopes of accruing the greatest benefit or defecting as a defensive measure.<sup>14</sup> The standard solution for an assurance problem is to impose penal sanctions on defectors, but that solution is not possible in endemically corrupt systems.<sup>15</sup> Thus, this paper explores a proposal by the Panamanian group, Asociación Panameña de Ejecutivos de Empresa (“APEDE”), which offers a viable solution to assurance problems.<sup>16</sup>

In order to demonstrate that corruption is an assurance problem, this paper discusses the fact that corrupt relationships are neither

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11. See Padideh Ala'i, *The Legacy of Geographical Morality and Colonialism: A Historical Assessment of the Current Crusade Against Corruption*, 33 VAND. J. TRANSNAT'L L. 877, 906-07 (2000) (discussing changes in the manner in which legal regimes and legal scholars perceive corruption).

12. See Robert S. Lieken, *Controlling the Global Corruption Epidemic*, FOREIGN POL'Y, Winter 1996-97, at 55, 68 (suggesting that controlling corruption will require a multiplicity of techniques and approaches).

13. See discussion *infra* Part III (defining the assurance problem as consistent with game theory wherein survival and success depend on whether actors defect from a group of participants).

14. See *infra* notes 82-84 and accompanying text (discussing the prisoners' dilemma and the problems with assurance).

15. See *infra* notes 91-94 and accompanying text (noting that sanctions often do not work in corrupt systems because all institutions, including those that would sanction, are thoroughly corrupt).

16. See discussion *infra* Part V.C (describing APEDE and its mission to promote ethical conduct among businesses in Panama).

desired nor optimal,<sup>17</sup> but that corruption does confer a short-term advantage on parties in endemically corrupt systems.<sup>18</sup> In order to underscore the significance of this issue, however, this paper starts with a discussion of the effect of corruption on emerging economies.<sup>19</sup> Just as perniciously, corruption degrades societies and erodes support for change.

## I. CORRUPTION AFFECTS EMERGING ECONOMIES

Corruption affects any polity in a negative manner, but its effects are particularly acute in emerging economies.<sup>20</sup> Indeed, positive change and economic growth cannot occur in endemically corrupt polities.<sup>21</sup> Corruption fosters the creation of expensive parallel institutions, which siphon resources away from other uses.<sup>22</sup> Corruption decreases foreign investment and distorts decision-making by bureaucrats.<sup>23</sup>

### A. PARALLEL INSTITUTIONS

One of the most burdensome and yet least quantified burdens corruption imposes on emerging or developing economies is the cost of maintaining parallel institutions. Parallel institutions are institutions created alongside “official” or extant institutions to

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17. See discussion *infra* Part II (illustrating that while corruption may confer some short-term benefits by facilitating the formation of certain political relationships, a deeper analysis shows that corrupt actors actually degrade these relationships over time).

18. See *id.* (arguing that certain actors benefit particularly from corruption, when other participating actors are not corrupt).

19. See discussion *infra* Part I.B (observing that corruption discourages foreign investment, which is vital to the success of emerging economies).

20. See *id.* (describing the ways that corruption hurts emerging economies, for example, because governments cannot spend necessary funds on other areas).

21. See discussion *infra* Part I.E (detailing that corrupt institutions do not support a climate for growth).

22. See *id.* (noting that economies cannot grow economically when institutions are endemically corrupt).

23. See discussion *infra* Part I.B (noting that foreign investment inevitably decreases where there are indicators of rampant corruption).

perform essentially the same functions as the official institutions.<sup>24</sup> The state can create parallel institutions, for example, when an existing official institution cannot service the needs of all people in need of that institution.<sup>25</sup> More often, however, parallel institutions are a reaction to a failure in the state, either because the state uses its institutions as a means of repressing people, or because the state actively denies access to its institutions to groups of people.<sup>26</sup>

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24. See M. Michael Rosenberg & Jack Jedwab, *Institutional Completeness, Ethnic Organizational Style and the Role of the State: The Jewish, Italian and Greek Communities of Montreal*, 29 CANADIAN REV. SOC. & ANTHROPOLOGY 265, 67 (1992) (noting that parallel institutions impede participation in official institutions or provide an alternative to official institutions); see also Richard Janda, *Something Wicked That Way Went: Law and the Habit of Communism*, 41 MCGILL L.J. 253, 266 (1995) (describing the creation of parallel institutions in Central and Eastern Europe that, in many cases, surpassed the official state institutions). "The parallel culture consisted of myriad artistic, political and philosophical expressions symbolized by figures such as Lech Walesa and Vaclav Havel and by events such as the 1956 Hungarian uprising. Parallel institutions were formed—parallel unions, parallel universities, parallel publishing houses, and to some extent even a parallel economy." *Id.* at 266.

25. The Virginia Military Institute ("VMI") provides a convoluted and ultimately unsuccessful example. See *United States v. Virginia*, 766 F. Supp. 1407, 1415 (W.D. Va. 1991) (holding VMI's policy of excluding women to serve an important state educational objective, and finding that the only means of obtaining the objective was to exclude women, and therefore holding that VMI's policy was within the bounds of the Fourteenth Amendment's Equal Protection Clause), *vacated & remanded*, 976 F.2d 890, 899-900 (4th Cir. 1992) (ordering the state to admit women to VMI, set up a parallel institution for women, or discontinue state sponsorship of VMI in order to comply with the requirements of equal protection), *enforced*, 852 F. Supp. 471 (W.D. Va. 1994), *aff'd*, 44 F.3d 1229 (4th Cir. 1995), *rev'd*, 518 U.S. 515 (1996) (holding that equal protection guarantees preclude the state from excluding women from VMI's unique educational opportunities, and finding that the creation of a parallel program for women at a nearby women's college was insufficient to meet the equal protection standard); see William Henry Hurd, *Gone With the Wind? VMI's Loss and the Future of Single-Sex Public Education*, 4 DUKE J. GENDER L. & POL'Y 27 (1997) (discussing the case). Parallel institutions can also be created among states. See Jennifer Schultz, *The GATT/WTO Committee on Trade and the Environment – Toward Environmental Reform*, 89 AM. J. INT'L L. 423, 438 (1995) (discussing a proposal among states "to create a parallel institution to the GATT to handle the environmental aspects of the trade and environment interface").

26. See Tomiko Brown-Nagin, *Toward a Pragmatic Understanding of Status-Consciousness: The Case of Deregulated Education*, 50 DUKE L.J. 753, 845 (2000) (discussing the creation of "freedom schools in the United States in the 1960s," which were "experimental educational academies designed 'to fill an intellectual and creative vacuum' in the lives of African-American youth left by inadequate

Privately created courts provide a striking example of parallel institutions. In the past, for example, rabbinical courts provided Jewish communities with viable, albeit extralegal, alternatives to the corrupt courts of the Ottoman Empire or the brutal courts of the Nazis.<sup>27</sup>

Corrupt institutions engender the creation of parallel institutions because corrupt institutions are dysfunctional.<sup>28</sup> They are dysfunctional for a variety of reasons, including the fact that they work in ways other than the ways they were designed to function and in fact often work to the detriment of those they are intended to serve.<sup>29</sup> They are especially dysfunctional because people do not trust

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public schooling"); see also Jeffrey S. Morton, *The Legality of NATO's Intervention in Yugoslavia in 1999: Implications for the Progressive Development of International Law*, 9 ILSA J. INT'L & COMP. L. 75, 77 (2002) (describing parallel institutions created by repressed Albanians in Kosovo); Hansjorg Strohmeyer, *Collapse and Reconstruction of a Judicial System: The United Nations Missions in Kosovo and East Timor*, 95 AM. J. INT'L L. 46 (2001) (discussing the creation of parallel institutions by repressed populations in Yugoslavia and Indonesia). Institutions that are not part of the state but that are part of the fabric of society might also be copied under similar pressures; the institutions of legal scholarship provide an example. See Linda S. Greene, *From Tokenism to Emancipatory Politics: The Conferences and Meetings of Law Professors of Color*, 5 MICH. J. RACE & L. 161, 182-83 (1999) (discussing the creation of parallel institutions such as conferences and academic proceedings among legal scholars of color who felt that they were excluded from mainstream institutions); Harry G. Prince, *A Parallel Community—People of Color Legal Scholarship Conferences and the Advancement of Legal Education*, 20 B.C. THIRD WORLD L.J. 1, 3 (2000) (discussing the creation of parallel institutions among legal scholars of color in the United States and noting that the echoes of those parallel institutions continue to provide "a supportive community for the many teachers who still find themselves as the only teacher of color at their home institutions").

27. See 4 MENACHEM ELON, *JEWISH LAW* 1592-97 (B. Auerbach trans., 1994) (describing rabbinical courts created by Jewish communities as an alternative to the corrupt courts of the Ottoman empire). See generally IRVING ROSENBAUM, *THE HOLOCAUST AND HALAKHAH* (1976) (describing the emergence of networks of religious schools and authorities that interpreted Jewish laws under the Holocaust).

28. See Bernard Black & Reinier Kraakman, *A Self-Enforcing Model of Corporate Law*, 109 HARV. L. REV. 1911, 1915 (1996) (describing corruption as dysfunctional); Angel Ricardo Oquendo, *Corruption and Legitimation Crises in Latin America*, 14 CONN. J. INT'L L. 475, 488 (1999) ("Moreover, it is precisely the culture of corruption that, to a significant extent, renders them dysfunctional and illegitimate.").

29. See discussion *infra* Part I.C (discussing poor decisionmaking caused by corruption and obfuscation caused by corruption).



them and will not use them if it is possible not to do so.<sup>30</sup> In the face of corrupt institutions, therefore, people create parallel institutions.<sup>31</sup> Karen Halverson provides a striking example of the creation of private court-like institutions when state courts are corrupt:

Criminal groups in Russia function to enforce legal rules and resolve economic disputes. One of the ironies of Russian organized crime is that criminal groups have long governed themselves according to internal criminal "laws." Those who rule the criminal world are known as "thieves-in-law" [*vory v zakone*], and they resolve disputes between criminals (or between businesses protected by them) through a procedure known as a "sorting out" [*razborka*]. As one Russian described the *razborka* procedure, it may involve powerful bankers appointing a "barely literate," retired ex-convict to resolve a dispute according to the traditional rules followed in the criminal world. Although often violent, a *razborka* may resemble a western-style negotiation session where each side brings its attorney and the parties follow the Russian Code of Civil Procedure. The prevalence of the *razborka* indicates that extralegal institutions of dispute resolution are perceived by some Russians to be

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30. See Susan Rose-Ackerman, *The Political Economy of Corruption*, in CORRUPTION AND THE GLOBAL ECONOMY 31, 44 (Kimberly Ann Elliott ed., 1997) (discussing the disengagement of people from state institutions based upon their mistrust for corrupt institutions); James M. Cooper, *Access to Justice*, 30 CAL. W. INT'L L.J. 429, 431 (2000) (discussing the withdrawal of Latin Americans from the judicial system because of corruption); Jerold S. Kayden, *Market-Based and Regulatory Approaches: A Comparative Discussion of Environmental and Land Use Techniques in the United States*, 19 B.C. ENVTL. AFF. L. REV. 565, 573 (1992) (asking "why should some individuals observe the law when others can pay to elude it? If the rule of law isn't the rule of law, can anarchy be far behind?"); Herbert H. Werlin, *The Consequences of Corruption: the Ghanaian Experience*, 88 POL. SCI. Q. 71, 79 (1973) (noting that "the effect of corruption is to generate an atmosphere of mistrust which pervades all levels of administration").

31. See Ariel Porat, *Enforcing Contracts in Dysfunctional Legal Systems: The Close Relationship Between Public and Private Orders: A Reply to McMillan and Woodruff*, 98 MICH. L. REV. 2459, 2478 (2000) ("Hence, if legal systems are dysfunctional due to the corruption of the judges, we may expect all forms of the private order to emerge: relational contracts, arbitration, business networks, trade associations, and social networks."); see also Mark Galeotti, *Criminal Russia: The Traditions behind the Headlines*, 44 HISTORY TODAY, Aug. 1994, at 12 (explaining that informal loan arrangements, often at high premiums, are parallel institutions that reflect state banks); Manash Ranjan Gupta & Sarbajit Chaudhuri, *Formal Credit, Corruption and the Informal Credit Market in Agriculture: A Theoretical Analysis*, 64 ECONOMICA 331, 340-41 (1997) (noting that when farmers have to bribe officials to get loans, they go to loan sharks).

superior to the state, thus reinforcing the perceived ineffectiveness of the judiciary in Russia.<sup>32</sup>

Institutions are not free.<sup>33</sup> Indeed, emerging economies often spend a disproportionate percentage of their available wealth on maintaining basic institutions.<sup>34</sup> Countries that operate two or more sets of institutions for the same task spend even more.<sup>35</sup> This inefficiency could seriously impede development and has an obvious negative affect on the quality of life.<sup>36</sup> Every unit of money expended

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32. Karen Halverson, *Resolving Economic Disputes in Russia's Market Economy*, 18 MICH. J. INT'L L. 59, 99-100 (1996) (noting that corruption is endemic in courts in the former countries of the former Soviet Union); see also Cynthia Alkon, *The Cookie Cutter Syndrome: Legal Reform Assistance Under Post Communist Democratization Programs*, 2002 J. DISP. RESOL. 327, 328 (pointing out that corruption and inefficiency continue to plague post-communist legal systems).

33. See Marina Ottaway & Theresa Chung, *Toward a New Paradigm*, 10 J. DEMOCRACY 99, 99 (1999) (stating that institutions are expensive, and questioning whether some developing countries can afford the institutions that support democracy); Montrose M. Wolf, *The Development of the Teaching-Family Model*, 30 J. APPLIED BEHAVIOR ANALYSIS 381, 381-82 (1997) (comparing the costs of different models of institutions). Three of the least populated states in the United States provide examples of the high costs of institutions. See Department Totals—Operating Budget: Alaska Court System (2003) (reporting that in fiscal year 2002 the Alaskan court system spent \$52,740,700), available at [http://www.gov.state.ak.us/omb/04\\_OMB/budget/ACS/04DeptTotals\\_ACS.pdf](http://www.gov.state.ak.us/omb/04_OMB/budget/ACS/04DeptTotals_ACS.pdf) (last visited Oct. 31, 2004); Iowa Judicial Branch, Budget (2003) (reporting that the operating budget for the Iowa court system for the 2002-2003 fiscal year was \$113 million), available at <http://www.judicial.state.ia.us/courtadmin/budrev.asp> (last visited Oct. 31, 2004); Maine Judicial Branch, *The State of the Judiciary: A Report to the Joint Convention of the First Regular Session of the 121st Legislature* (2003) (indicating that the operating budget for the Maine court system was \$54 million), available at <http://www.courts.state.me.us/mainecourts/supreme/speeches/State%20of%20Judiciary%202-10.htm> (last visited Oct. 31, 2004).

34. See WORLD BANK, *THE STATE IN A CHANGING WORLD* 13-14 (1997) (observing that economies with strong institutional capabilities tend to grow faster).

35. See *id.* (noting that reformers can start to improve institutional capabilities by strengthening central agencies and introducing more transparency).

36. See Maria Dakolias, *A Strategy for Judicial Reform: The Experience in Latin America*, 36 VA. J. INT'L L. 167, 185-86 (1995) (noting the negative effect that money spent to work around corrupt courts has on the ability to develop other institutions in Latin America); see also Thomas E. Plank, *The Essential Elements of Judicial Independence and the Essence of Pre-Soviet Russia*, 5 WM. & MARY

operating a second, unofficial court system, for example, is a unit of money not expended on health care, on creating business infrastructure, or on other critical needs.<sup>37</sup>

Corruption causes people to disengage from the state and to create parallel sets of institutions. Although it has not been studied by developmental economists, the cost of these parallel institutions may have the most deleterious effect on economic and social development.

## B. CORRUPTION DECREASES INVESTMENT INTO EMERGING ECONOMIES

Corruption decreases foreign investment.<sup>38</sup> The most well-known empirical work demonstrating this effect is that of Paolo Mauro, which found a “negative association between corruption and investment, as well as growth, [that] is significant in both a statistical and an economic sense.”<sup>39</sup> Edgardo Campos and others find that while the negative effect is lessened if a corrupt government is predictable, there is still a negative effect.<sup>40</sup>

Orthodox economic theory teaches that lower investment rates lead to lower rates of economic growth.<sup>41</sup> Development theorists

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BILL OF RTS. J. 1, 3 n.3 (1996) (explaining that outside parties' influence on court decisions can hinder the development of a market economy).

37. See, e.g., Edgardo Buscaglia & Maria Dakolias, *An Analysis of the Causes of Corruption in the Judiciary*, 30 LAW & POL'Y INT'L BUS. 95, 111-12 (1999) (stating that money spent on alternative community-based institutions in Peru caused “a loss in the country's productive capabilities due to the high transaction costs of access to public services”).

38. See J. Edgardo Campos et al., *The Impact of Corruption on Investment: Predictability Matters*, 27 WORLD DEV. 1059, 1065 (1999) (recognizing that the emerging consensus among academics and scholars is that corruption impedes growth and investment).

39. Paolo Mauro, *Corruption and Growth*, 110 Q.J. ECON. 681, 705 (1995) (finding that a measurable decrease in corruption in a country would increase its investment-to-gross domestic product ratio by almost four percent and the annual growth of its gross domestic product per capita by almost half a percent).

40. See J. Edgardo Campos et al., *supra* note 38, at 1065 (commenting that corruption regimes that are more predictable have a less negative impact on investment than those that are less predictable).

41. Philip M. Nichols, *Outlawing Transnational Bribery Through the World*

argue that foreign investment is critical either to finance technological innovation or to absorb excess labor capacity.<sup>42</sup> Whatever the theory, empirical observation illustrates that corruption and the concomitant lower levels of foreign investment are directly related to low rates of growth.<sup>43</sup> In turn, low rates of growth are directly related to deteriorating social conditions and standards of living.<sup>44</sup>

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*Trade Organization*, 28 LAW & POL'Y INT'L BUS. 305, 348 (1997) (explaining that a study supported by orthodox economic theory has found that corruption lowers private investment, thereby reducing economic growth).

42. Most empirical studies suggest a positive relationship between foreign investment and economic growth. See Ray Barrell & Nigel Pain, *Foreign Direct Investment, Technological Change, and Economic Growth Within Europe*, 107 ECON. J. 1770, 1770 (1997) (commenting that foreign direct investments play vital roles in the acceleration of technological change and economic growth of European countries); see also Glenn Firebaugh, *Growth Effects of Foreign and Domestic Investment*, 98 AM. J. SOC. 105, 105 (1992) (finding that there is a beneficial relationship between foreign investment and growth). The evidence, however, is not completely unambiguous, and the point is debated. See Amitava Krishna Dutt, *The Pattern of Direct Foreign Investment and Economic Growth*, 25 WORLD DEV. 1925, 1925 (1997) (providing that different patterns of foreign investment affect growth in host countries differently); Jeffrey Kentor, *The Long-Term Effects of Foreign Investment Dependence on Economic Growth, 1940-1990*, 103 AM. J. SOC. 1024, 1025 (1998) (describing that there is a "contentious" debate between those who believe that dependence of a national economy on foreign investment promotes economic growth and those who believe that it causes underdevelopment).

43. See Mauro, *supra* note 39, at 700-01 (finding a negative relationship between corruption and economic growth, as well as institutional efficiency and economic growth); see also Andrei Shleifer & Robert W. Vishny, *Corruption*, 108 Q.J. ECON. 599, 611-15 (1993) (stating that corruption has a distortionary effect that is greater than heavy taxation because of the added imperative of secrecy); SHANG-JIN WEI, WHY IS CORRUPTION SO MUCH MORE TAXING THAN TAX? ARBITRARINESS KILLS 1, 2 (NBER, Working Paper No. W6255, Nov. 1997) (finding empirically that corruption severely distorts economies).

44. See Tord Kjellstrom et al., *Current and Future Determinants of Adult Ill-Health*, in THE HEALTH OF ADULTS IN THE DEVELOPING WORLD 209, 211-13 (Richard G.A. Feachem et al. eds., 1992) (discussing that there is a relationship between economic development and ill health and concluding that improved health requires a decrease in poverty); Morris D. Morris, Book Review, 39 ECON. DEV. & SOC. CHANGE 667, 668-69 (1991) ("Although cautions occasionally are noted, there is general acceptance of the correlation between declining economic growth rates and deteriorating social conditions.").

### C. CORRUPTION DISTORTS BUREAUCRATIC DECISION-MAKING IN EMERGING ECONOMIES

Corruption distorts decision-making in two profound ways: by distorting the parameters within which decisions are made, and by distorting the pool of decisionmakers.

Corruption, especially bribery, often involves economic decisions.<sup>45</sup> In a rational market system, decisions about which good or service to purchase are made on the basis of price and quality.<sup>46</sup> On the other hand, rather than purchasing a good or service based on the price and quality, a corrupt decisionmaker makes a decision on the basis of the size and quality of a bribe.<sup>47</sup> Results of such decision-making dot the developing world in the form of bridges built where there are no roads, buildings that easily collapse during earthquakes, and other poorly-conceived and wasteful products.<sup>48</sup>

Corruption also distorts the pool of bureaucrats who make decisions.<sup>49</sup> Capable and honest persons tend to avoid corrupt bureaucracies.<sup>50</sup> In his classic empirical study of corruption in the

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45. See Mark B. Bader & Bill Shaw, *Amendment of the Foreign Corrupt Practices Act*, 15 N.Y.U. J. INT'L L. & POL. 627, 627-29 (1983) (noting that bribery is often used to influence economic decisions).

46. See *id.* at 627 (explaining that a fundamental tenet of free market systems is that economic transactions should be based solely upon the price and quality of a product and the service provided by the seller).

47. See *id.* (maintaining that corporate bribery of foreign officials distorts the relationship between price and quality, thereby affecting the stability of overseas and domestic business).

48. See Philip M. Nichols, *The Myth of Anti-bribery Laws as Transnational Intrusion*, 33 CORNELL INT'L L.J. 627, 627-28 (2000) (providing examples of corruption-driven projects, including disasters involving man-made constructions in countries such as Turkey and South Korea where builders pay bribes rather than meeting local business codes). Corrupt bureaucrats also divert resources to hide illicit activity, which compounds the distortionary effect of their already-poor decisions. *Id.*; see also M.S. Alam, *A Theory of Limits on Corruption and Some Applications*, 48 KYKLOS: INT'L REV. FOR SOC. SCI. 419, 431 (1995) (noting that resources are diverted and wasted to hide illicit activities).

49. See Omotunde E.G. Johnson, *An Economic Analysis of Corrupt Government, With Special Application to Less Developed Countries*, 28 KYKLOS: INT'L REV. FOR SOC. SCI. 47, 56 (1975) (explaining that government officials, as civil servants, are a segment of society who have an incentive and ability to aid in the collection of corrupt revenue in return for a share of the proceeds).

50. See *id.* at 57 (observing that capable and honest persons avoid government

Irrigation Department of a state in southern India, Robert Wade found that corrupt senior officials sold government posts to junior officials who desired those positions because such positions allowed them to extract bribes, thus perpetuating the entry of dishonest and incapable persons into—and the exclusion of honest decisionmakers from—bureaucratic service.<sup>51</sup> While it is possible to find honest bureaucrats even in endemically corrupt systems,<sup>52</sup> the ill effect of corruption on the composition of critical decisionmakers in emerging economies is beyond peradventure.

#### D. CORRUPTION CORRODES SOCIAL INSTITUTIONS AND UNDERMINES SUPPORT FOR REFORM

Corruption delegitimizes governments and undermines support for change, particularly market-oriented change.<sup>53</sup> Susan Rose-Ackerman powerfully summarizes the social affects of corruption and its detrimental effect on the legitimacy of governments: “Citizens may come to believe that the government is simply for sale to the highest bidder. Corruption undermines claims that the government is substituting democratic values for decisions based on ability to pay. It can lead to coups by un-democratic leaders.”<sup>54</sup>

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work for moral reasons when corruption is pervasive); Vito Tanzi, *Corruption, Governmental Activities, and Markets*, FIN. & DEV., Dec. 1995, at 26 (suggesting that people will seek jobs that pay good bribes rather than jobs for which they are qualified); Francisco E. Thoumi, *Some Implications of the Growth of the Underground Economy in Columbia*, 29 J. INTERAM. STUD. & WORLD AFF. 35, 44 (1987) (asserting that over time, an honest individual in a corrupt system adapts and becomes more dishonest).

51. See Robert Wade, *The Market for Public Office: Why the Indian State Is Not Better at Development*, 13 WORLD DEV. 467, 474-80 (1985) (describing the sale of offices in a south Indian state).

52. The vast majority of bureaucrats that the author has encountered in his own fieldwork have been honest.

53. See Karl M. Meessen, *Fighting Corruption Across the Border*, 18 FORDHAM INT'L L.J. 1647, 1647 (1995) (“Corruption both in government and private business has no little role in discrediting freshly installed democratic procedures and freshly installed free market systems.”).

54. Rose-Ackerman, *supra* note 30, at 44; see also Nancy Zucker Boswell, *Combating Corruption: Focus on Latin America*, 3 SW. J. L. & TRADE AM. 179, 184 (1996) (“Perhaps the greatest casualty of . . . corruption has been the erosion of public trust in public institutions and leaders, the foundation of democracy.”); A.W. Cragg, *Business, Globalization, and the Logic and Ethics of Corruption*, 53

There are two effects that are particularly acute in emerging economies. The first is that popular support for reform erodes, and the absence of that support can seriously undermine the possibility of positive change.<sup>55</sup> The other effect is harder to quantify, but has far more of a human face: corruption contributes to miserable social conditions.<sup>56</sup> As Martin Davies forcefully put it, "we delude ourselves if we think bribery to be purely economic conduct incapable of leading to fear, cruelty, and humiliation."<sup>57</sup>

### E. CORRUPTION PREVENTS DEVELOPMENT

Corruption clearly impedes or prevents positive change in emerging economies by distorting, by denying or diverting resources, and by degrading social support.<sup>58</sup> Corruption is detrimental on a macro scale; it is also not the optimal relationship to enter into on a micro scale.

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INT'L J. 643, 654 (1998) (noting that respect for law and legal institutions is a "casualty" of bribery); Werlin, *supra* note 30, at 79 ("the effect of corruption is to generate an atmosphere of distrust which pervades all levels of administration"). Again, this point is borne out by recent, empirical findings of fact rather than theoretical speculation. See John Brademas & Fritz Heimann, *Tackling International Corruption: No Longer Taboo*, FOREIGN AFF., Sept.-Oct. 1998, at 17-18 (describing damage done by bribery scandals to governments in Brazil, Colombia, Ecuador, India, Indonesia, Italy, Japan, Mexico, NATO, Pakistan, South Korea, Venezuela, and Zaire).

55. See Cheryl W. Gray & William W. Jarosz, *Law and the Regulation of Foreign Direct Investment: The Experience from Central and Eastern Europe*, 33 COLUM. J. TRANSNAT. L. 1, 27 (1995) ("charges of bribery and corruption can easily erode popular support for economic reform in general, and foreign investment in particular"); see also Kevin Done, *High Level of Bribes Harms Rate of Growth*, FIN. TIMES, June 28, 1996, at 4 (reporting that, as indicated in a World Bank development report, the public's perception of widespread corruption in many transition countries is one of the most significant barriers to market reforms in such emerging economies).

56. See Martin Davies, *Just (Don't) Do It: Ethics and International Trade*, 21 MELBOURNE U. L. REV. 601, 614 (1997) (explaining that, however commonplace it might be in practice, most cultures regard bribery as unethical conduct).

57. *Id.*

58. See discussion *infra* Part I (describing the economic and social effect of corruption on society).

## II. CORRUPT RELATIONSHIPS ARE NOT DESIRABLE

Corruption does, in some respects, facilitate relationships in the sense that two or more parties transact with one another.<sup>59</sup> Indeed, in the post-colonial period of the 1960s, some scholars did suggest that corruption enhanced development by creating an avenue by which foreign investors could enter a developing country.<sup>60</sup> Nathaniel Leff was at that time the most vocal advocate of the “speed money” argument,<sup>61</sup> although Samuel Huntington has since become better known.<sup>62</sup> Huntington argued that

Corruption may be one way of surmounting traditional laws or bureaucratic regulations which hamper economic expansion. In the United States, during the 1870s and 1880s, corruption of state legislatures and city councils by railroad, utility, and industrial corporations undoubtedly speeded the growth of the American economy . . . . A society which is relatively uncorrupt—a traditional society for instance where traditional norms are still powerful—may find a certain amount of corruption a welcome lubricant easing the path to modernization. A developed traditional society may be improved—or at least modernized—by a little corruption.<sup>63</sup>

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59. See Bryan W. Husted, *Honor Among Thieves: A Transaction-Cost Interpretation of Corruption in Third World Countries*, 4 BUS. ETHICS Q. 17, 18-19 (1994) (stating that corruption can be conceived of as the transferal of a service between the bribe donor and the bribe recipient and generally describing corruption in transactional terms). This statement is not meant to imply that these relationships are beneficial; any positive statement about corruption is in danger of being seized upon by scholars desperate for an argument to skewer. See, e.g. Dickerson, *supra* note 1, at 397 n.17 (misquoting the author of this article as suggesting that corruption is beneficial).

60. See Shihata, *supra* note 2, at 454 (describing—and disagreeing with—pro-corruption arguments in the literature, including capital formation, predictability in government relationships, and “efficient” escape from burdensome regulations).

61. See Nathaniel H. Leff, *Economic Development Through Bureaucratic Corruption*, AM. BEHAVIORAL SCIENTIST, Nov. 1964, at 10, 10-11 (stating that bribes are speed money that allow productive businesses to bypass recalcitrant bureaucracies).

62. See SAMUEL P. HUNTINGTON, *POLITICAL ORDER IN CHANGING SOCIETIES* 59-71 (1968) (arguing that bribery can speed up economic development); see also Bayley, *supra* note 1, at 719 (arguing, in 1966, that bribery is a step in economic development).

63. HUNTINGTON, *supra* note 62, at 68-69.



Time has proven these scholars wrong, and a more sophisticated understanding of corruption helps to explain why. The speed money argument relies on a static analysis of benefits: the cost directly attributable to a transaction is subtracted from the benefit directly accruing from a transaction.<sup>64</sup> Static analysis is no longer considered an accurate measure of the effects of corruption.<sup>65</sup> Instead, a dynamic analysis that considers the damage done to a system over a period of time is considered more accurate, and does not favor the use of corruption as a development tool.<sup>66</sup>

Corruption may actually inhibit the creation of new relationships. Occasional examples of bravado and hubris aside (as well as apocryphal stories that usually turn out to be third or fourth-hand), corrupt actors generally hide their activities and discovery of their conduct can expose actors to heavy costs.<sup>67</sup> Corrupt relationships are, therefore, generally created only among those who already have

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64. See Husted, *supra* note 59, at 18-19 (opining that corruption is a transaction between parties).

65. See Steven R. Salbu, *Battling Global Corruption in the New Millennium*, 31 LAW & POL'Y INT'L BUS. 47, 49 (1999) ("The once-popular 'functionalist' view of bribery, under which corruption purportedly yields benefits of allocative efficiency and optimal capital formation, retains little favor among today's academics.").

66. See THE WORLD BANK, *HELPING COUNTRIES COMBAT CORRUPTION: THE ROLE OF THE WORLD BANK* 14-15 (1997) (stating that by using a dynamic analysis, what appears to be a short-term gain can be shown to impose tremendous costs in the long run); Buscaglia *supra* note 37, at 112 (noting that "present corruption decreases future productivity, thereby reducing dynamic efficiency"); Shihata, *supra* note 2, at 454-55 (positing that the consensus among scholars is that the long-term damage done by corruption far outweighs any immediate benefits). Salim Rashid's research illustrates how static and dynamic analyses of corruption might lead to different conclusions. See Salim Rashid, *Public Utilities in Egalitarian LDC's: The Role of Bribery in Achieving Pareto Efficiency*, 34 KYKLOS: INT'L REV. FOR SOC. SCI. 448, 448-55 (1981). Rashid studied bribes paid to obtain telephone service in India: his original premise was that the payment of differently sized bribes would help to differentiate customers in a system that otherwise was completely egalitarian, and thus bribes would allow for Pareto optimalization. *Id.* Rashid found that while this may have been the case at first, over time, bureaucrats came to expect bribes and also created inefficiencies in order to extract more and larger bribes; rather than contributing to Pareto optimality, bribery degraded the system. *Id.*

67. See FRITZ F. HEIMANN, *SHOULD FOREIGN BRIBERY BE A CRIME* 7 (1994).

some reason to trust one another.<sup>68</sup> Corruption also creates barriers to relationships by allowing corrupt actors to buy monopolies from the state.<sup>69</sup>

Relationships formed through corruption are generally more burdensome to actors than legitimate relationships.<sup>70</sup> Far from cutting through red tape, corrupt relationships actually consume more time and are more costly to maintain. Corrupt relationships bear a risk of discovery and punishment, as well as the monetary cost of maintaining secrecy.<sup>71</sup> Corrupt relationships are not enforceable in public institutions, and therefore must be enforced through more costly means. Corrupt relationships also corrode the internal culture of a bribe-paying company.<sup>72</sup>

The myth that “corruption is how business is done” or that “corruption is acceptable” in some systems<sup>73</sup> does not stand up to close scrutiny.<sup>74</sup> Certainly, corruption has become endemic in some

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68. See Alam, *supra* note 48, at 449 (stating that bribe-taking officials limit entry to those whom they trust).

69. See Frederick M. Abbott, *Foundation-Building for Western Hemispheric Integration*, 17 NW. J. INT'L L. & BUS. 900, 914 (1996-97) (“Governmental corruption and non-transparency are likely to benefit inefficient local operators over efficient multinational operators.”); Franklin A. Gevurtz, *Commercial Bribery and the Sherman Act: The Case for Per Se Illegality*, 42 U. MIAMI L. REV. 365, 390-91 (1987) (noting that inefficiencies are created when firms bribe to create monopolies); Herbert Hovenkamp, *Antitrust's Protected Classes*, 88 MICH. L. REV. 1, 16 (1989) (providing examples of how bribes are used to obtain or retain monopolies). The author of this article notes that he has spoken with many businesspeople who purchased a monopoly through a bribe, only to find that the same monopoly was sold to other bribe payers, or whose monopoly was later revoked in favor of a later payer of a better-quality bribe.

70. See Alam, *supra* note 48, at 449 (describing how bribery may create costs when bureaucrats hold back information and resources in order to extract larger bribes).

71. See Schlieffer & Vishny, *supra* note 43, at 600 (noting that there are costs imposed by the “imperative of secrecy”).

72. See Cragg, *supra* note 54, at 653 (noting that the payment of bribes creates an environment in which employees think that it is appropriate to put their own interests ahead of those of the company).

73. See H. Lowell Brown, *The Extraterritorial Reach of the U.S. Government's Campaign Against International Bribery*, 22 HASTINGS INT'L & COMP. L. REV. 407, 473 n.248 (1999) (asserting that corruption is a way of life in some cultures).

74. See David Hess & Thomas W. Dunfee, *Fighting Corruption: A Principled*

systems,<sup>75</sup> but even in those systems, endemic corruption seems to be an aberration when examined longitudinally.<sup>76</sup> Moreover, not one study indicates that corruption is accepted in any society.<sup>77</sup>

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*Approach; The C2 Principles (Combating Corruption)*, 33 CORNELL INT'L L.J. 593, 611-16 (2000) (discussing and dismissing the anecdotal but persistent belief that corruption is ethically-justified); *see also* JOHN T. NOONAN, JR., BRIBES 702-03 (1984) (dismissing the myth of corruption's justifiability as an example of cultural arrogance with the argument that "[i]t is often the Westerner with ethnocentric prejudice who supposes that a modern Asian or African society does not regard the act of bribery as shameful in the way that Westerners regard it.").

75. *See* Moisés Naim, *The Corruption Eruption*, 11 BROWN J. WORLD AFF. 245 (1995) (stating that the incidence of corruption worldwide has exploded); *see also* Konyin Ajayi, *On the Trail of a Spectre—Destabilisation of Developing and Transitional Economies: A Case Study of Corruption in Nigeria*, 15 DICK. J. INT'L L. 545, 545 (1997) (noting that the recent "astronomical" increase in the level of corruption in most parts of the world is alarming); Maria Dakolias & Kim Thachuk, *Attacking Corruption in the Judiciary: A Critical Process in Judicial Reform*, 18 WIS. INT'L L.J. 353, 357 (2000) (reiterating Moisés Naim's observations regarding an "eruption" in the incidence of corruption); David A. Gantz, *Globalizing Sanctions Against Foreign Bribery: The Emergence of a New International Legal Consensus*, 18 NW. J. INT'L L. & BUS. 457, 463 (1998) (noting that globally, corruption remains "disturbingly common"); James P. Wesberry, Jr., *International Financial Institutions Face the Corruption Eruption: If the IFIs Put Their Muscle and Money Where Their Mouth Is, the Corruption Eruption May Be Capped*, 18 NW. J. INT'L L. & BUS. 498, 499-500 & n.1 (1998) (noting that, over the last fifty years, corruption has become "pervasive").

76. As one corruption expert notes,

The incidence of grand corruption has increased tremendously during the last decade. What used to concern a relatively small number of people working in a relatively small number of countries has now become a major South-wide problem. . . . [By] general consensus, there has been a tremendous deterioration in the last ten years, with grand corruption becoming the general rule, rather than the exception, in major government-influenced contracts in the South.

GEORGE MOODY-STUART, *THE GOOD BUSINESS GUIDE TO BRIBERY: GRAND CORRUPTION IN THIRD WORLD DEVELOPMENT* 2-3 (1994); *see also* Ajayi, *supra* note 75, at 545 (emphasizing the recent large-scale increase in levels of corruption).

77. Fritz Heimann notes,

[t]hat bribes have to be paid secretly everywhere, and that officials receiving bribes have to resign in disgrace if the bribe is disclosed, makes clear that bribery violates the moral standards of the South and the East, just as it does in the West. . . . There is no country in the world where bribery is either legally or morally acceptable.

Heimann, *supra* note 67, at 7; *see also* RICHARD T. DE GEORGE, *COMPETING WITH*

A growing amount of empirical evidence suggests that even endemically corrupt societies abhor corruption.<sup>78</sup> In an early study on Sierra Leone, Sahr John Kpundeh found that while corruption in Sierra Leone was endemic, those who lived there nevertheless considered corruption harmful and supported anticorruption regimes.<sup>79</sup> Robert Mattes and Cherrel Africa found a similar rejection of corruption in South Africa.<sup>80</sup> The author of this paper, along with George Siedel and Matt Kasden, has conducted fieldwork in Mongolia and Bulgaria, and found that students reject corruption.<sup>81</sup> The author's fieldwork in Kazakhstan found that citizens of that country reject corruption.<sup>82</sup>

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INTEGRITY IN INTERNATIONAL BUSINESS 104 (1993) ("In no country in the world do high government officials openly practice and publicly justify the acceptance of large sums of money for preferential treatment.").

78. See Daniel Y. Jun, *Bribery Among the Korean Elite: Putting an End to a Cultural Ritual and Restoring Honor*, 29 VAND. J. TRANSNAT'L L. 1071, 1085 (1996) (drawing an important distinction between a practice that occurs in a culture and a practice that is accepted in a culture by noting that although bribery has become very prevalent in Korean, it is still not accepted morally).

79. See SAHR JOHN KPUNDEH, *POLITICS AND CORRUPTION IN AFRICA: A CASE STUDY OF SIERRA LEONE* 161-66, 172 (1995) (showing that in interviews of three hundred persons representing all areas of the country and all social strata, 83.8% of interviewees stated that a new government should put a high priority on combating corruption). Interestingly, public distaste extended to such acts as public officials using their influence to have relatives admitted to college. *Id.* at 173.

80. See Robert Mattes & Cherrel Africa, *Corruption—The Attitudinal Component: Tracking Public Perceptions of Official Corruption in South Africa, 1995-1998*, at 1-4 (Oct. 12, 1999) (setting forth data showing that 46% of South Africans feel that most, if not all, public officials are involved in corruption, and that public concern about corruption is on an upward curve), available at [http://www.transparency.org/iacc/9th\\_iacc/papers/day2/ws1/d2ws1\\_caficarmattes.html](http://www.transparency.org/iacc/9th_iacc/papers/day2/ws1/d2ws1_caficarmattes.html) (last visited Oct. 31, 2004).

81. See Philip M. Nichols, George J. Siedel, & Matthew Kasdin, *Corruption as a Pan-Cultural Phenomenon: An Empirical Study In Countries at Opposite Ends of the Former Soviet Empire*, 39 TEX. INT'L L.J. 215, 231 (2004) (noting that among survey respondents, almost half of Bulgarians and over one-third of Mongolians ranked corruption as the most serious social problem on the survey list).

82. See Philip M. Nichols, *The Fit Between Changes to the International Corruption Regime and Indigenous Perceptions of Corruption in Kazakhstan*, 22 U. PA. J. INT'L ECON. L. 863, 927 (2001) (stating that 96% of survey respondents indicated that fighting corruption should be a high government priority). The author has also conducted fieldwork studies in Belize, Senegal, and France, none

In short, corruption not only corrodes a society in general, it also imposes burdens on those who are involved in corrupt relationships. A corrupt relationship is sometimes better than no relationship at all, but it is not the type of relationship that a rational actor would voluntarily choose.<sup>83</sup>

### III. CORRUPTION PRESENTS AN ASSURANCE PROBLEM

Corruption imposes generalized costs, and a corrupt relationship is rarely optimal. Nonetheless, corruption can confer a short-term benefit on an actor, and maintaining high standards when others are corrupt could prove fatal to an actor.<sup>84</sup> Corruption, therefore, presents actors with a dilemma often referred to as an assurance problem.<sup>85</sup>

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of which have been published, but all of which indicated that societies in those countries reject corruption.

83. See THOMAS DONALDSON & THOMAS DUNFEE, *TIES THAT BIND: A SOCIAL CONTRACTS APPROACH TO BUSINESS ETHICS* 226 (1999) (concluding—pursuant to extensive discussions of bribery with Indian businesspersons in India—that while most admitted to having paid bribes, all expressed outrage and disgust at the practice).

84. See *supra* Part II.

85. Amartya Sen developed the concept of the assurance problem in the 1960s. See Amartya K. Sen, *Isolation, Assurance and the Social Rate of Discount*, 81 Q.J. ECON. 112, 114 (1967) (building upon the problem of the prisoners' dilemma to establish the concept of the assurance problem); see also Lee Anne Fennell, *Beyond Exit and Voice: User Participation in the Production of Local Public Goods*, 80 TEX. L. REV. 1, 40 n.135 (2001) (crediting Amartya Sen with formulating the assurance problem). The assurance problem has been used to explain the behavior of the United States and Europe in negotiating and signing the anti-bribery conventions, using game theory to examine the behavior of nations rather than individual actors. See Kenneth W. Abbott and Duncan Snidal, *Values and Interests: International Legalization in the Fight Against Corruption*, 31 J. LEGAL STUD. 141, 164 (2002) (describing the assurance problem faced by countries that want to curtail transnational bribery, but could be placed at a competitive disadvantage if they comply and other countries defect). One such attempt at curtailing transnational bribery is the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, Dec. 18, 1997, S. Treaty Doc. No. 105-43, 37 I.L.M. 1 (1998) (entered into force Feb. 15, 1999) [hereinafter "OECD Convention"]. This Convention requires OECD Convention members to criminalize transnational bribery. *Id.*; see also Hess & Dunfee, *supra* note 74, at 602 ("The most significant advancement in the fight against corruption and the strongest demonstration of its

Corruption confers a short-term benefit over legitimate actors because corruption distorts the decision-making process.<sup>86</sup> According to traditional neo-classical economic theory, a decisionmaker makes a decision based on the price and fit of a good or service.<sup>87</sup> A rational producer, therefore, uses resources to lower the price of a product and to enhance its quality.<sup>88</sup> In a corrupt system, on the other hand, the price or quality of the product is irrelevant.<sup>89</sup> The decisionmaker bases the decision instead on the size and quality of the bribe.<sup>90</sup> A rational, albeit corrupt, producer, therefore, uses its resources to increase the size of the bribe and improve the quality of the bribe rather than quality of the product.<sup>91</sup> Assuming that resources are finite and that producers initially have roughly equal access to those resources, a producer who uses even a portion of its resources legitimately will not be able to create a bribe of the same size or

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universal condemnation is the [OECD Convention]"); Nii Lante Wallace-Bruce, *Corruption and Competitiveness in Global Business—The Dawn of a New Era*, 24 MELBOURNE U. L.R. 349, 368 (2000) ("Perhaps the most significant step in the efforts to combat corruption in global business was taken on 17 December 1997 in Paris, when members of the OECD signed the [OECD Convention]."); Jong Bum Kim, *Korean Implementation of the OECD Bribery Convention: Implications for Global Efforts to Fight Corruption*, 17 UCLA PAC. BASIN L.J. 245, 254 (2000) ("the OECD Bribery Convention has built the most significant multilateral instrument in the fight against bribery and corruption").

86. See discussion *infra* Part I (analyzing the long-term damage of corruption to a state's economy and infrastructure).

87. See THE WORLD BANK, *supra* note 66 and accompanying text (describing the importance of the price and quality of goods or services in a rational economy).

88. See *id.* (presenting alternative reforms that may help economic growth).

89. See *infra* note 71 and accompanying text (describing how hiding illicit activities leads to a waste of resources).

90. See Heimann, *supra* note 67, at 7 (explaining that a high-quality bribe is a bribe that a corrupt bureaucrat can use without fear of discovery or punishment, and that "bribes everywhere have to be paid in secret").

91. See M. Shahid Alam, *Anatomy of Corruption: An Approach to the Political Economy of Underdevelopment*, 48 AM. J. ECON. & SOC. 441, 448-52 (1989) (indicating that manufacturers and providers have little incentive to produce high-quality, low cost goods and services, and instead are rewarded when they divert money from production to the payment of bribes; see also Stanley Sporkin, *The Worldwide Banning of Schmiergeld: A Look at the Foreign Corrupt Practices Act on its Twentieth Birthday*, 18 NW. J. INT'L L. & BUS. 269, 280 (1998) (noting that corruption often results in low-quality construction).

quality as a producer who dedicates all of its resources to creating a good bribe.

Corruption degrades systems and societies and, in the long-run, imposes heavy costs on all actors.<sup>92</sup> All actors are better off if a system operates without corruption. Few people accept corruption, and it is conceivable that most actors would prefer not to engage in corrupt acts. Nonetheless, corruption can confer a short-term benefit, and if one actor engages in corruption, then in the short run that actor has a significant advantage over those who do not.<sup>93</sup> Corruption, therefore, presents a paradigmatic assurance problem.

The assurance problem is most often described with the descriptors of game theory.<sup>94</sup> As such, it can be contrasted with the far better-known prisoners' dilemma game. In a prisoners' dilemma situation, an actor is best off if he or she defects while everyone else complies and is next best off if everyone complies.<sup>95</sup> In an assurance

92. See discussion *infra* Part II (explaining that it is more difficult and inefficient to maintain a corrupt relationship than a legitimate relationship).

93. See *infra* note 97 and accompanying text (discussing the example of the stag hunt, where the defector experiences a short-term gain and compliant individuals experience a total loss).

94. See Duncan Snidal, *Coordination versus Prisoners' Dilemma: Implications for International Cooperation and Regimes*, 79 AM. POL. SCI. REV. 923, 924-25 (1985) (explaining that basic solutions for game models such as the prisoners' dilemma may display divergent ramifications for the institutionalization, stability, and adaptability of regimes and for the role of hegemony in the international system). See generally ROBERT O. KEOHANE, *AFTER HEGEMONY: COOPERATION AND DISCORD IN THE WORLD POLITICAL ECONOMY* (1984); ARTHUR A. STEIN, *WHY NATIONS COOPERATE: CIRCUMSTANCE AND CHOICE IN INTERNATIONAL RELATIONS* (1990); Kenneth A. Oye, *Explaining Cooperation under Anarchy: Hypotheses and Strategies*, in *COOPERATION UNDER ANARCHY* (Kenneth A. Oye ed., 1986).

95. See Steven Kuhn, *Prisoner's Dilemma*, THE STANFORD ENCYCLOPEDIA OF PHILOSOPHY (Edward N. Zalta ed., 2003), available at <http://plato.stanford.edu/archives/fall2003/entries/prisoner-dilemma> (last visited Oct. 31, 2004). In a prisoners' dilemma game, players are each offered a set of choices about whether to defect from the group or not; if one player defects and no others do, then that player is best off and the other players are worst off, however, if no player defects, then the players are next best off, and if all of the players defect then they suffer more than if none of the players had defected. *Id.* The prisoners' dilemma game is a tool that "illustrates a conflict between individual and group rationality. A group whose members pursue rational self-interest may all end up worse off than a group whose members act contrary to rational self-

problem, on the other hand, all actors will be best off if all actors coordinate their behavior, but in the event that there are defectors, those who defect are better off than those who do not defect.<sup>96</sup>

The assurance problem is often illustrated through games similar to the prisoners' dilemma game. One of the more common is the stag hunt game, based on a scenario created by Jean Jacques Rousseau.<sup>97</sup> A group of hunters can successfully hunt and kill a stag, which they will share, if they coordinate their efforts.<sup>98</sup> Alternatively, they could defect and hunt a rabbit, which is a smaller animal but which an individual hunter could probably kill by himself.<sup>99</sup> The hunters who continue to hunt a stag after others have defected will not be successful and will have nothing.<sup>100</sup> The dilemma faced by an individual hunter is that if she does her job for the group she will get a large portion of meat—if every other hunter does his or her job as well; but if she does her job for the group and someone else defects, she will not only get nothing but will also have passed up an opportunity to get a medium portion by not defecting herself.<sup>101</sup> An

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interest." *Id.* at 1.

96. See Aaron-Andrew P. Bruhl, *Public Reason as a Public Good*, 4 J.L. SOC'Y 217, 259-60 (2003) (explaining that the difference between the prisoners' dilemma and the assurance game is that in the assurance game, the payoff the individual receives when other individuals cooperate is greater than that in the prisoners' dilemma); see also Daphna Lewinsohn-Zamir, *The "Conservation Game": The Possibility of Voluntary Cooperation in Preserving Buildings of Cultural Importance*, 20 HARV. J. L. & PUB. POL'Y 733, 736 (1997) (noting that in those circumstances in which prospects of voluntary cooperation are high are better modeled by a cooperative assurance game, and where prospects of cooperation are low, a game even more competitive than a prisoners' dilemma game is an appropriate model).

97. See Jean Jacques Rousseau, *Discourse on the Origin of Inequality*, in THE ESSENTIAL ROUSSEAU (Lowell Bair trans., Meridian Books 2d ed. 1983) (setting forth the parable of the stag hunt, in which several hunters agree to cooperate to catch a stag; when one hunter defects from the group in order to catch a small rabbit, the group fails to capture the large stag).

98. *Id.*

99. *Id.*

100. *Id.*

101. See GameTheory.net, *Assurance Game*, Game Theory Dictionary (noting that "assurance game" is also a generic name for the stag hunt), available at <http://www.gametheory.net/Dictionary/Games/AssuranceGame.html> (last visited Oct. 31, 2004).



economic actor in a potentially corrupt system faces a similar dilemma. If she behaves appropriately and everyone else does, as well, she will join the others in reaping a large reward; but if others defect and she does not join them, their small gain will surpass hers and she may starve.

Mathematicians can calculate elegant solutions to hypothetical games.<sup>102</sup> These solutions obviously have little application in the real world, because both the vastly greater number of actors in real life<sup>103</sup> and the vastly greater complexity of real life cannot be replicated in a game.<sup>104</sup> Nonetheless, the insights gained through game theory are of use to persons constructing real social structures, and although a mathematically calculated solution may have little application, the general concept of a solution may be valuable. Unfortunately, the most obvious solution probably will not work.

#### IV. PUNITIVE LEGAL SANCTIONS DO NOT SOLVE A CORRUPTION ASSURANCE PROBLEM

Punitive sanctions for defection have long been perceived as the solution to an assurance problem.<sup>105</sup> Robert Axelrod showed that

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102. See John C. Harsanyi, *Advances in Understanding Rational Behavior*, in RATIONAL CHOICE 82, 94-96 (Jon Elster ed., 1986).

103. See Susan Block-Lieb, *Congress' Temptation to Defect: A Political and Economic Theory of Legislative Resolutions to Financial Common Pool Problems*, 39 ARIZ. L. REV. 801, 817-18 (1997) (illustrating that the difficulty and cost of monitoring and punishing a game increases with the number of actors involved); see also Carlisle Ford Runge, *Institutions and the Free Rider: The Assurance Problem in Collective Action*, 46 J. POL. 154, 169-70 (1984) (explaining that the larger the group of actors, the lower both the probability of contribution by others and the assurance with which such estimates are held become).

104. See Bruhl, *supra* note 96, at 259 (noting that in real life, situations are in fact more complex and uncertain than in hypothetical collective action problems); Robert C. Ellickson, *Bringing Culture and Human Frailty to Rational Actors: A Critique of Classical Law and Economics*, 65 CHI.-KENT L. REV. 23, 23 (1989) (discussing the limitations of assumptions and noting that a richer model for positive analysis may look to psychology and sociology to obtain a more accurate picture of social influences on human behavior).

105. See William A. Edmundson, *Social Meaning, Compliance Conditions, and Law's Claim to Authority*, 15 CAN. J. L. & JURIS. 51, 55 (2002) (stating that legal sanctions transform compliance into a moral mandate). See generally Margot Priest, *The Privatization of Regulation: Five Models of Self-Regulation*, 29

retaliation, which he labeled “tit-for-tat,” would lead to coordinated behavior and the accrual of the maximal benefit for all.<sup>106</sup> While sanctions can be imposed through a variety of sources, the most common is criminal law. Indeed, John Rawls famously found “no need even for the penal law except insofar as the assurance problem [makes] it necessary.”<sup>107</sup>

In the case of an endemically corrupt system, however, criminal sanctions often do not constitute a viable means of ensuring compliance with minimal standards of behavior.<sup>108</sup> The reasons for this are fairly obvious: non-enforcement of enforcement standards can be purchased through a corrupt relationship.<sup>109</sup> As Hiram

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OTTAWA L. REV. 233, 238 (1997-98) (noting that sanctions may be applied to noncompliant actors in solving assurance problems).

106. See ROBERT AXELROD, *THE EVOLUTION OF COOPERATION* 36-39 (2d ed. 1989) (discussing the preservation of coordination through the threat of sanction for defection); Robert Axelrod, *The Emergence of Cooperation among Egoists*, 75 AM. POL. SCI. REV. 306, 308 (1981) (analogizing sanctions in coordination games to regulatory actions designed to prevent collusion).

107. JOHN RAWLS, *A THEORY OF JUSTICE* 315 (2d ed. 1971). Rawls questioned the general need for criminal law in a just society because just society’s motives would be duly regulated by a sense of justice. *Id.*; see also David Crump, *Game Theory, Legislation, and the Multiple Meanings of Equality*, 38 HARV. J. ON LEGIS. 331, 408 (2001) (discussing Rawls’ arguments in the context of game theory and the assurance problem).

108. See WORLD BANK, *supra* note 34, at 13 (noting that official enforcement bodies in corrupt states are themselves susceptible to corruption); O. Lee Reed, *Law, the Rule of Law, and Property: A Foundation for the Private Market and Business Study*, 38 AM. BUS. L.J. 441, 467-68 (2001) (“Other problems have been caused by widespread corruption and an inadequate enforcement process to implement laws, underscoring the need for a developed legal system to interpret and enforce rules and to settle disputes over owned resources.”); Stephen J. Toope, *Legal and Judicial Reform through Development Assistance: Some Lessons*, 48 MCGILL L.J. 357, 375 (2003) (stating that enforcement of corruption laws is impossible if enforcers are corrupt); Celeste Boeri, Note, *How to Solve Argentina’s Debt Crisis: Will the IMF’s Plan Work?*, 4 CHI. J. INT’L L. 245, 250-51 (2003) (“Dependence on [a] legally enforced strategy is likely to be ineffective.”).

109. See Tarik Abdel-Monem, *Foreign Nationals in the United States Witness Security Program: A Remedy for Every Wrong?*, 40 AM. CRIM. L. REV. 1235, 1244 (2003) (“In a number of nations, formal institutions are undermined by corruption, violence, or other factors that counteract efforts of law enforcement authorities.”); Robert W. Gordon, *A New Role for Lawyers?: The Corporate Counselor After Enron*, 35 CONN. L. REV. 1185, 1185 (2003) (criticizing politicians who attempt to abolish, weaken, or cripple regulations dealing with corruption); Neal Kumar Katyal, *Conspiracy Theory*, 112 YALE L.J. 1307, 1379 n. 266 (2003) (noting that

Chodosh summarizes: "Vague ethical norms, a poorly regulated and fragmented body of legal professionals, weak monitoring capacity, corrupted review systems, and ineffectual prosecution and enforcement substantially sustain systemic impunity for illicit practices."<sup>110</sup> Daryl Levinson goes further, cautioning that weak enforcement agencies confronted with powerful corrupt actors not only will refuse to enforce rules, but also will become even more corrupt themselves.<sup>111</sup>

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corruption impedes the enforcement of rules by state entities); Daniel Richman, *Prosecutors and Their Agents, Agents and Their Prosecutors*, 103 COLUM. L. REV. 749, 825 (2003) (describing the difficulty of pursuing cases of corruption against enforcement agencies). Examples of such degradation can be found throughout the world. See, e.g., Jane Goodall, *The Evolving Legal Status of Chimpanzees*, 9 ANIMAL L. 1, 90 (2003) (describing the non-enforcement of conservation laws due to corrupt officials' integral involvement in both illicit activity and the enforcement of rules against the illicit activity); Jeremiah E. Goulka, *A New Strategy for Human Rights Protection: Learning from Narcotics Trafficking in Mexico*, 9 CARDOZO J. INT'L & COMP. L. 231, 239 (2001) ("Political corruption is the core of the problem. It pervades the entire system, keeping the dysfunctional system oiled, maintaining and protecting the 'standards' of police and judicial perversion. The government has become, in many areas, so corrupt as to make the Rule of Law a comic impossibility."); Nathanael Heasley et al., *Impunity in Guatemala: The State's Failure to Provide Justice in the Massacre Cases*, 16 AM. U. INT'L L. REV. 1115, 1154 (2001) (finding that massacre cases against government officials are not prosecuted in Guatemala because of corruption); Steven E. Hendrix, *Innovation in Criminal Procedure in Latin America: Guatemala's Conversion to the Adversarial System*, 5 SW. J.L. & TRADE AM. 365, 369 (1998) (stating that although there are basic laws against corruption, there is a lack of enforcement and compliance); Randall Peerenboom, *Seek Truth From Facts: An Empirical Study of Enforcement of Arbitral Awards in the PRC*, 49 AM. J. COMP. L. 249, 303-05 (2001) (finding empirically that corruption impedes enforcement of arbitral awards in China); Boeri, *supra* note 108, at 251 (discussing how rampant political corruption in Argentina hampers implementation of reforms). Indeed, in the United States prosecution of local corruption cases was given to federal agencies in part as a response to the impossibility of using corrupt institutions to impose legal sanctions on corrupt actors. *Id.* See also George D. Brown, *New Federalism's Unanswered Question: Who Should Prosecute State and Local Officials for Political Corruption?*, 60 WASH & LEE L. REV. 417 (2003); Charles Ruff, *Federal Prosecution of Local Corruption: A Case Study in the Making of Law Enforcement Policy*, 65 GEO. L.J. 1171 (1977).

110. Hiram E. Chodosh, *Emergence from the Dilemmas of Justice Reform*, 38 TEX. INT'L L.J. 587, 601 (2003); see also *The Experts Roundtable: A Hemispheric Approach to Combating Corruption*, 15 AM. U. INT'L L. REV. 759, 786 (2000) ("despite a plethora of laws, corruption persists because of inadequate enforcement and impunity").

111. See Daryl J. Levinson, *Collective Sanctions*, 56 STAN. L. REV. 345, 390-91

When state institutions fail, the actors must turn to other means of ensuring compliance. APEDE represents an organization capable of doing so.<sup>112</sup>

## V. A CERTIFICATION SOLUTION TO THE ASSURANCE PROBLEM

Panama in general and APEDE in particular illustrate that corruption is sometimes best understood as an assurance problem, and also provide a solution to the problem that is independent of criminal law.<sup>113</sup> Corruption almost certainly exists in Panama, and APEDE's members, who are prominent businesspeople, are among those best poised to reap the short-term gains of corrupt relationships. Nonetheless, APEDE's members recognize that corruption imposes tremendous costs both on themselves and on their country, and are actively seeking means to establish and enforce standard behavior among all members.<sup>114</sup>

### A. PANAMA

Approximately three million people live in Panama—an area roughly the size of South Carolina or the Czech Republic located at the juncture of Central America and South America.<sup>115</sup> Panama's service sector is the primary driver of its economy, accounting for

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(2003) (noting that a corrupt group may even conspire to overthrow or undermine the sanctioning body); see also Bruce L. Benson, *Corruption in Law Enforcement: One Consequence of 'The Tragedy of the Commons' Arising with Public Allocation Processes*, 8 INT'L REV. L. & ECON. 73 (1988) (discussing the corruption of entities charged with enforcing corruption standards).

112. See discussion *infra* Part 5.3 (introducing APEDE's activities).

113. See *id.* (addressing APEDE's non-governmental status and methods for combating corruption).

114. See *id.* (describing APEDE's mission to develop free enterprise in Panama).

115. See CENTRAL INTELLIGENCE AGENCY, THE WORLD FACTBOOK 2004 (2004) [hereinafter CIA WORLD FACTBOOK] (noting that Panama's total area measures 78,200 square kilometers), available at <http://www.cia.gov/cia/publications/factbook/geos/pm.html> (last visited Oct. 31 2004).

around three-fourths of Panama's gross domestic product.<sup>116</sup> Panama's government, installed after the United States invaded Panama to overthrow its military dictatorship, consists of a constitutional democracy with a President, a unicameral Asamblea Legislativa, and a Corte Suprema de Justicia.<sup>117</sup>

Panama is a vibrant and economically active polity that possesses control over arguably the most important waterway in the world—the Panama Canal.<sup>118</sup> Panamanians should enjoy tremendous success, yet a great deal of evidence indicates that corruption is a serious problem in Panama.

### B. CORRUPTION IN PANAMA

There are five reasons, ranging from Panama's colonial past to current perceptions, to believe that corruption is an issue in Panama. The first reason stems from its colonial history. Although people inhabited Panama<sup>119</sup> before Rodrigo Bastidas "discovered" Panama in 1501, or Cristóbal Colón built a settlement in 1503,<sup>120</sup> the present situation in Panama's may be a product of its colonial roots. Panama

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116. See *id.* (estimating that Panama's GDP in 2003 was 18.62 billion dollars, which ranked 109th in the world, or \$6300 per capita, which was 108th in the world).

117. See *id.* (detailing that members are elected for five-year terms to 78 legislative seats available for five year terms, and nine justices appointed to ten year terms); see also Mark Andrew Sherman, Comment, *An Inquiry Regarding the International and Domestic Legal Problems Presented in United States v. Noriega*, 20 U. MIAMI INTER-AM. L. REV. 393, 400 (noting that Noriega problematized the 1984 election that installed officials following the U.S. invasion of Panama).

118. See CIA WORLD FACTBOOK, *supra* note 119 (including the canal in the service sector, which accounts for three fourths of Panama's GDP).

119. See SAILA DUMMAD IGUANABIGINIA, LA MIGRACIÓN DE LOS KUNAS HACIA LA COSTA ATLÁNTICA: SEGÚN LA HISTORIA ORAL KUNA (Atilio Martínez ed., 1999) (discussing the Kuna people of pre-Columbian Panama).

120. See CHARLES LOFTUS GRANT ANDERSON, OLD PANAMA AND CASTILLA DEL ORO: A NARRATIVE HISTORY OF THE DISCOVERY, CONQUEST, AND SETTLEMENT BY THE SPAINARDS OF PANAMA, DARIEN, VERAGUA, SANTO DOMINGO, SANTA MARTA, CARTAGENA, NICARAGUA, AND PERU 85-116 (1911) (compiling a collection of first hand accounts of the first Spanish interactions with what is now Panama, including the fourth journey of Cristóbal Colón—whose anglicized name is Christopher Columbus—in which he founded the first Spanish settlements on the territory).

was a Spanish colony from 1538 until Simon Bolivar liberated it in 1821.<sup>121</sup> Once freed from Spanish rule, Panama continued to be associated with what is now Colombia until it achieved its independence from Colombia in 1903.<sup>122</sup> That Panama was a colony for so long supports an inference of corruption.<sup>123</sup>

Secondly, Panamanian independence coincided with the United States' interest in the possibility—and later with the realization—of a canal across the isthmus; indeed, some argue that the United States' interest greatly helped Panama achieve independence.<sup>124</sup> For most of

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121. See CHRISTOPHER WARD, *IMPERIAL PANAMA: COMMERCE AND CONFLICT IN ISTHMIAN AMERICA, 1550-1800* 46-7 (1993) (describing Spanish imperialism as being particularly heavy-handed); see also *infra* note 123 and accompanying text (tracing corruption's origin in many countries, including Panama, to colonial rule and noting that post-colonial states are marred by corruption and authoritarian rule).

122. See generally THE UNITED STATES DISCOVERS PANAMA: THE WRITINGS OF SOLDIERS, SCHOLARS, SCIENTISTS, AND SCOUNDRELS, 1850-1905 (Michael LaRosa & Germán R. Mejía eds., 2004) (compiling a collection of first-hand reports of this portion of Panama's history).

123. See Francis N. Botchway, *Good Governance: The Old, the New, the Principles, and the Elements*, 13 FLA. J. INT'L L. 159, 169 n.44 (2001) (attributing corruption in Latin American to its Spanish colonial heritage); Thomas J. Moyer, *Mediation as a Catalyst for Judicial Reform in Latin America*, 18 OHIO ST. J. ON DISP. RESOL. 619, 642 (2003) (emphasizing that corruption in Latin America became an everyday occurrence during colonial times under Spanish rule); see also Grady Jessup, *Symbiotic Relations: Clinical Methodology—Fostering New Paradigms in African Legal Education*, 8 CLINICAL L. REV. 377, 381 (2002) ("indigenous legal systems were largely ignored or corrupted by European colonizers"); Carmen G. Gonzalez, *Beyond Eco-Imperialism: An Environmental Justice Critique of Free Trade*, 78 DENV. U. L. REV. 979, 980 n.5 (2001) (noting that colonially trained administrators are generally perceived to be corrupt); John McFarlane, *Corruption and the Financial Sector: The Strategic Impact*, 19 DICK. J. INT'L L. 47, 50 (2000) (listing colonialism as a cause of corruption in Asia); cf. El-Obaid Ahmed El-Obaid & Kwadwo Appiagyei-Atua, *Human Rights in Africa—A New Perspective on Linking the Past to the Present*, 41 MCGILL L.J. 819, 822 (1996) (describing how post-colonialism has been marked by corruption and authoritarianism).

124. See OVIDIO DIAZ ESPINO, *HOW WALL STREET CREATED A NATION: J.P. MORGAN, TEDDY ROOSEVELT, AND THE PANAMA CANAL* 157-63 (2001) (discussing the involvement of Roosevelt and J.P. Morgan in Panama's liberation from Columbia). Espino's argument, of course, discounts the contributions of so many Panamanians whose serious commitment to the independence of their country was probably the most significant contributor to Panama's independence. *Id.*

the early years of its independence, Panama and the United States were inextricably intertwined in a hegemonic relationship in which the United States controlled and at the same time protected those in power in Panama.<sup>125</sup> Again, the control exerted over Panama by the United States is a reason to infer corruption.<sup>126</sup>

A third reason to infer corruption is that an authoritarian regime appeared in Panama once the United States relinquished its control. For many years, military generals actually ruled Panama, even on those occasions when an elected president sat in office.<sup>127</sup> The last of Panama's military dictators was Manuel Noriega, who for many years worked closely with and even for the United States, but who in the end was finally removed from office with the assistance of a U.S.

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125. See MICHAEL L. CONNIFF, *PANAMA AND THE UNITED STATES: THE FORCED ALLIANCE* 19-20 (2001) (exemplifying the enormity of U.S. influence over Panama in its discussion of the Hay-Bunau-Varilla Treaty that gave canal rights to the U.S. "in perpetuity"); see also JOHN LINDSAY-POLAND, *EMPERORS IN THE JUNGLE: THE HIDDEN HISTORY OF THE U.S. IN PANAMA* 7 (2003) (stating that the United States "was the guarantor of Panama's separation from Columbia," and therefore held enormous power in Panama).

126. See Henry J. Richardson, III, *U.S. Hegemony, Race, and Oil in Deciding United Nations Security Council Resolution 1441 on Iraq*, 17 TEMP. INT'L & COMP. L.J. 27, 40 (2003) ("Predictably, the hegemon will move to corrupt the community's system of law by using its power to lift its actions beyond adverse adjudication, to bar enforcement of the law against its inevitable wrongs, and to demand and construct or impose pseudo-legal rationales and strategies that shield its objectives by attempting to credibly justify its drive for community control."); see also Chantal Thomas, *International Debt Forgiveness and Global Poverty Reduction*, 27 FORDHAM URB. L.J. 1711, 1714 (2000) (noting that during the Cold War, the United States was willing to support corrupt regimes in exchange for those regimes' support).

127. See CARLOS GUEVARA MANN, *PANAMANIAN MILITARISM: A HISTORICAL INTERPRETATION* 195 (1996) (lamenting that although civilian attorneys control Panama's security force, aspects of militarism are still present); ROBERT C. HARDING II, *MILITARY FOUNDATIONS OF PANAMANIAN POLITICS* 32-35 (2001) (recounting how the military's emergence in Panamanian politics created illegitimacy in civilian politics). See generally Steve C. Ropp, *Explaining the Long-Term Maintenance of a Military Regime: Panama Before the U.S. Invasion*, 44 WORLD POL. 210 (1992) (advancing both new and existing theories to account for Panama's corrupt military history).

invasion of Panama.<sup>128</sup> There is little doubt that Noriega's regime was very corrupt:

From the early 1970s to 1989, Noriega secured progressively greater dominion over state military and civilian institutions in Panama, first as his nation's chief of military intelligence and later as commander of the Panamanian Defense Forces. In the early 1980s, Noriega's position of authority brought him into contact with a group of drug traffickers from the Medellin area of Colombia (the 'Medellin Cartel'). Various Medellin Cartel operatives met with Noriega's associates and, later, with Noriega personally, regarding the Medellin Cartel's desire to ship cocaine through Panama to the United States. Eventually, Noriega and the Medellin Cartel reached the first of a series of illicit agreements. Thereafter, from 1982 through 1985, with Noriega's assistance, the Medellin Cartel transported significant quantities of cocaine through Panama to the United States. It also utilized its relationship with Noriega to move ether for cocaine processing and substantial cash proceeds from drug sales from the United States to or through Panama.<sup>129</sup>

It is also fairly clear that Noriega's regime actively pushed corruption from the top down. As Michael Fowler and Julie BuncK argue, "[u]nder the regime of General Manuel Noriega, official corruption in Panama assumed a somewhat different guise, directed by the country's leadership."<sup>130</sup> Authoritarian regimes tend to produce corrupt societies and systems, and Noriega's regime in

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128. See generally JOHN DINGES, *OUR MAN IN PANAMA* (1990) (detailing the United States and Noriega's intimate, three-decade-long relationship that ultimately ended in failure in 1989 when the United States invaded Panama).

129. *United States v. Noriega*, 117 F.3d 1206, 1210 (11th Cir. 1997); see Michael A. McKenzie, Recent Development, *Treaty Enforcement in U.S. Courts—United States v. Noriega*, 808 F. Supp. 791 (S.D. Fla. 1992), 34 HARV. INT'L L.J. 596 (1993) (discussing many cases and questions generated by the United States' capture and criminal prosecution of Manuel Noriega); Recent Case, *Separation of Powers—Head-of-State Immunity—Eleventh Circuit Holds That the Executive Branch's Capture of Noriega Exempts Him from Head-of-State Immunity—United States v. Noriega*, 117 F.3d 1206 (11th Cir. 1997), 111 HARV. L. REV. 849 (1998) (reviewing the Eleventh Circuit's holding in *United States v. Noriega* and arguing that the Noriega court should have adopted a default no-immunity rule, rather than a default immunity rule, which gave the judiciary excessive foreign policy power).

130. Michael Ross Fowler & Julie Marie BuncK, *Narcotics Trafficking, Central American Prisons, and the Law*, 25 SUFFOLK TRANSNAT'L L. REV. 433, 469 (2002).



particular lent itself to oppression and corruption.<sup>131</sup> Panama still experiences echoes of the corruption engendered during its periods of authoritarian rule.<sup>132</sup>

The fourth issue that allows for inference of corruption in Panama is that the country has been a center for money laundering and a hub for drug transshipments. As recently as a decade ago, Silvano Paternostro described Panama as a country in "chaos" because of narcotics trafficking and money laundering.<sup>133</sup> Many organizations have lauded the Panamanian government and its citizens for extraordinary diligence in eliminating these practices, but all observers recognize that they once existed in Panama.<sup>134</sup>

131. See Eytan Gilboa, *The Panama Invasion Revisited: Lessons for the use of Force in the Post Cold War Era*, 110 POL. SCI. Q. 539, 540 (1995) (listing various corrupt activities in which Noriega involved himself, such as drug trafficking, arms sales, and money laundering, not to mention his systematic violation of treaties with the U.S. and harassment of U.S. forces).

132. See Delissa A. Ridgway & Mariya A. Talib, *Globalization and Development - Free Trade, Foreign Aid, Investment and the Rule of Law*, 33 CAL. W. INT'L L.J. 325, 343 (2003) (stating that although there is no longer a dictator in Panama, its politics are still riddled with corruption, and noting that democracy is rarely the result of the United States' efforts to forcibly remove dictators from power).

133. See Silvana Paternostro, *Panama: Casablanca Without Heroes*, 10 WORLD POL'Y J. 53, 53-58 (1993) (writing that despite the United States' initial urgency to investigate drug trafficking and money laundering, four years after the 1989 invasion, drugs continued to be run through Panama daily).

134. See BUREAU FOR INTERNATIONAL NARCOTICS AND LAW ENFORCEMENT AFFAIRS, U.S. DEP'T OF STATE, INTERNATIONAL NARCOTICS CONTROL STRATEGY REPORT (2002) (identifying Panama as a center for money laundering and drug transshipment but emphasizing that Panama has undertaken several measures to curb these behaviors), available at <http://www.state.gov/g/inl/rls/nrcrpt/2001/rpt/8487.htm> (last visited Oct. 31, 2004); see also Jaime Ospina-Velasco, *Strengths and Hurdles in the Struggle Against Asset Laundering and the Repression of Financial Crime: The Colombian Perspective*, 13 FLA. J. INT'L L. 96, 104 (2000) (noting that the Latin Federation of Banks, a federation of national banking associations, adopted the Declaration of Principles and Actions of the Latin American System Against Asset Laundering in Panama City to support Inter-American efforts to curb money laundering). Compare FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING, ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT, REVIEW TO IDENTIFY NON-COOPERATIVE COUNTRIES OR TERRITORIES: INCREASING THE WORLDWIDE EFFECTIVENESS OF ANTI-MONEY LAUNDERING MEASURES 8 (2000) (identifying Panama as a center for money laundering, but noting that the government is committed to combating that practice), available at

Panama's drug trafficking and money laundering problems are notable because many people closely associate these activities with corruption.<sup>135</sup>

Fifth, those who work with or observe Panama perceive a great deal of corruption. Transparency International's Corruption Perceptions Index is the most authoritative measure of perceived corruption in a country.<sup>136</sup> The Corruption Perceptions Index correlates different sources of information as to how much perceived corruption exists in a country, assigns a score to a country, and then ranks the scored countries against one another.<sup>137</sup> With a score of ten indicating no perceived corruption and a score of zero indicating

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[http://www1.oecd.org/fatf/pdf/ncct2000\\_en.pdf](http://www1.oecd.org/fatf/pdf/ncct2000_en.pdf) (last visited Oct. 31, 2004), with FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING, ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT, REVIEW TO IDENTIFY NON-COOPERATIVE COUNTRIES OR TERRITORIES: INCREASING THE WORLDWIDE EFFECTIVENESS OF ANTI-MONEY LAUNDERING MEASURES 9-10 (2001) (delisting Panama and describing Panamanian efforts to implement an anti-money laundering program), available at [http://www1.oecd.org/fatf/pdf/NCCT2001\\_en.pdf](http://www1.oecd.org/fatf/pdf/NCCT2001_en.pdf) (last visited Oct. 31, 2004).

135. See Janet Reno, Remarks, 40 ST. LOUIS U. L.J. 1009, 1009 (1996) (proclaiming that all countries have long suffered from drug trafficking and the money laundering and corruption that results from this practice, and urging the judiciary to take steps to address this problem); Nora M. Rubin, *A Convergence of 1996 and 1997 Global Efforts to Curb Corruption and Bribery in International Business Transactions: The Legal Implications of the OECD Recommendations and Convention for the United States, Germany, and Switzerland*, 14 AM. U. INT'L L. REV. 257, 269-70 (1998) (arguing that technology allows those in the drug trade to use their profits as "potent corruption tools").

136. See Alejandro Posadas, *Combating Corruption Under International Law*, 10 DUKE J. COMP. & INT'L L. 345, 404-05 (2000) (describing Transparency International, which is comprised of a group of former World Bank executives, as one of the most promising developments in the anti-corruption field); Wesberry, *supra* note 61, at 500 n.7 (1998) (stating that Transparency International is the "best known global NGO" because of its Corruption Perception Index).

137. See John Graf Lambsdorff, *Corruption in Comparative Perception*, in ECONOMICS OF CORRUPTION 81, 87-97 (Arvind K. Jain ed., 1998) (explaining the corruption perception index at length); see also Posadas, *supra* note 136, at 405-07 (describing the activities of Transparency International).

nothing but corruption, Panama's score of 3.7 in 2004<sup>138</sup> indicates that observers perceive a great deal of corruption in Panama.

### C. APEDE

APEDE is a group comprised of Panamanian business leaders.<sup>139</sup> Although the state recognizes APEDE, the organization remains aggressively independent of the state and is a completely private sector civil enterprise.<sup>140</sup> APEDE's core mission includes "monitoring and strengthening the development of free enterprise, one of the pillars of any free society."<sup>141</sup> To accomplish this mission, APEDE undertakes activities such as educating businesses, creating linkages among businesspersons, and lobbying for appropriate laws.<sup>142</sup> APEDE also states that its fundamental tasks include combating corruption and promoting ethical conduct among Panamanian businesses.<sup>143</sup>

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138. See Transparency International, *Corruption Perception Index 2004* (Oct. 20, 2004) (explaining that the Corruption Perception Index is a good tool for measuring perceived corruption, but noting that a greater number of sources results in greater reliability as to a country's ranking; Transparency International requires a country to have at least three surveys, and Panama had seven), available at <http://www.transparency.org/cpi/2004/cpi2004.en.html#cpi2004> (last visited Oct. 31, 2004).

139. See Asociación Panameña de Ejecutivos de Empresa, *¿Qué es APEDE?* (reporting that Panama's business community widely accepts APEDE and values its efforts to promote economic development in Panama), available at <http://www.apede.org/apede/index.html#01> (last visited Oct. 31, 2004).

140. See ENRIQUE ARTURO DE OBARRIO, PANAMÁ: HACIA UNA SOCIEDAD CADA VEZ MÁS INTEGRAL—LA VISIÓN Y MISIÓN DE LA APEDE 1 (2003) (describing the stated mandate of APEDE).

141. *¿Qué es APEDE?*, *supra* note 139 (elaborating that APEDE achieves its mission through initiatives such as the Conferencia Anual de Ejecutivos de Empresa, which focuses on issues ranging from poverty reduction to the administration of justice and economic development, or the Law on Transparency, which scrutinizes the public administration and advocates for accountability).

142. See *id.* (stating that its activities also include promoting equal opportunity, education, urban development, and business training).

143. See *id.* (explaining that "APEDE's Ethics and Civic Affairs Commission is leading the business sector in the fight against corruption."); see also DE OBARRIO, *supra* note 140, at 1 (stating that the primary goal of APEDE is to promote transparency in government and ethical conduct in private companies).

APEDE's involvement is interesting for at least two reasons. The first is that business is a vastly underappreciated resource in combating corruption. Throughout the world, from the Clean Hands movement in Poland to the Development Coalition in South Africa, businesses are acting to curb corruption.<sup>144</sup> Indeed, private individuals and businesses initially funded Transparency International, the driver of much global activity with respect to corruption.<sup>145</sup> Businesses constitute a potent adversary to systemic corruption because they are funded, organized, and habituated to achieving discrete goals.

The second reason why APEDE's involvement is interesting is that it underscores the fact that corruption can be described as an assurance problem. APEDE clearly recognizes that corrupt relationships are not optimal, and also clearly recognizes that defection from minimal standards of behavior could be perceived as a necessary defense mechanism by which actors hope to hedge against other defectors. Indeed, APEDE explicitly recognizes private sector parties acting in an ethical fashion as the most probable means of effectuating changes in the government sector.<sup>146</sup>

APEDE has initiated educational programs on corruption, and is working with the government to create laws on transparency and accountability.<sup>147</sup> Among the most intriguing of APEDE's ideas, however, is the proposal that the organization certify companies based upon how they make decisions regarding potentially corrupt situations.

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144. See Carolyn Hotchkiss, *The Sleeping Dog Stirs: New Signs of Life in Efforts to End Corruption in International Business*, 17 J. PUB. POL'Y & MKTG 108, 111 (noting that developing countries are attempting to combat corruption and that business leaders globally have witnessed the negative effect of corruption on profit margins and are publicly calling for it to end).

145. See TI History, Transparency International, 2004 (detailing the involvement of businessmen in the creation of Transparency International and early funding from private foundations such as the Ford Foundation), available at [http://www.transparency.org/about\\_ti/history.html](http://www.transparency.org/about_ti/history.html) (last visited Oct. 31, 2004).

146. DE OBARRIO, *supra* note 140, at 4.

147. See *infra* note 139 and accompanying text (incorporating education into APEDE's plan to combat corruption).

## VI. A CERTIFICATION PROCESS FOR DECISIONS ABOUT CORRUPTION

### A. THE INTERNATIONAL STANDARDS ORGANIZATION

The idea of certifying decision-making processes is not novel. Two of the best-known sets of privately created standards deal with decision-making processes rather than with the actual makeup of goods or services. The International Standards Organization's *ISO 9000* group of standards concerns quality management processes,<sup>148</sup> while its *ISO 14000* group concerns environmental management processes.<sup>149</sup> The International Standards Organization is instructive in contemplating a certification process for decisions about corruption because they create "generic management system standards."<sup>150</sup> By "generic," the organization means "the same standards can be applied to any organization, large or small, whatever its product—including whether its 'product' is actually a service—in any sector of activity."<sup>151</sup> By "management system," the organization means "what the organization does to manage its processes, or activities in order that the products or services that it produces meet the objectives it has set itself."<sup>152</sup> By "management system standards," the organization means "a model to follow in setting up and operating the management system. Experts in the field

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148. See Lisa C. Thompson & William J. Thompson, *The ISO 9000 Quality Standards: Will They Constitute a Technical Barrier to Free Trade under the NAFTA and the WTO?*, 14 ARIZ. J. INT'L & COMP. L. 155 (1997) (discussing *ISO 9000*'s quality management processes and their impact on trade).

149. See Paula C. Murray, *Inching toward Environmental Regulatory Reform—ISO 14000: Much Ado about Nothing or a Reinvention Tool?*, 37 AM. BUS. L.J. 35, 38 (1999) (touting *ISO 14000* as "as perfect tool to foster evolutionary environmental policy reform"); Paula C. Murray, *The International Environmental Management Standard, ISO14000: A Non-Tariff Barrier or a Step to an Emerging Global Environmental Policy*, 18 U. PA. J. INT'L ECON. L. 577 (1997) (noting an increasing awareness of the need for environmental protection on a global scale and, at the same time, a recognition that international trade liberalization policies may be at odds with environmental protection).

150. International Standards Organization, *Generic Management Systems Standards*, available at [http://www.iso.org/iso/en/iso9000-14000/basics/general/basics\\_3.html](http://www.iso.org/iso/en/iso9000-14000/basics/general/basics_3.html) (last visited Oct. 31, 2004).

151. *Id.*

152. *Id.*

have reached a consensus that this model is built on “state of the art practices.”<sup>153</sup>

Businesses that wish to receive certification go through an auditing process.<sup>154</sup> In the audit, an auditor examines each stage of decision-making and of effectuating decisions against a template of internationally-accepted best practices. If needed, the auditor suggests processes designed to improve decision-making to meet those best practices. When the processes under scrutiny conform with international standards, then the auditor issues a written assurance to that effect. The business may, if it chooses, ask the auditor to register that assurance in a central registry.<sup>155</sup>

The advantage to a business of this certification is fourfold. First, decision-making processes may be improved.<sup>156</sup> More effective management processes are obviously to any business’s advantage.<sup>157</sup> The second, third and fourth advantages are less obvious, but far greater in scope.

The second advantage is that certification adds reputational value. This is particularly true with respect to the environmental management system group of standards. Much of the public in many of the world’s regions are quite sensitive to the environmental behavior of a supplier.<sup>158</sup> *ISO 14000* certification signals to that

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153. *Id.*

154. See Murray, *supra* note 149, at 69 (discussing *ISO 14000*’s role in certifying firms through audits of business practices); see also Paulette L. Stenzel, *Can the ISO 14000 Series Environmental Management Standards Provide a Viable Alternative to Government Regulation?*, 37 AM. BUS. L.J. 237, 240-41 (2000) (providing a background of the ISO and ISO standards for implementation).

155. See Donald A. Carr & William L. Thomas, *Devising a Compliance Strategy Under the ISO 14000 International Environmental Management Standards*, 15 PACE ENVTL. L. REV. 85, 88 (1997) (explaining the integral role of compliance auditing *ISO 14000* audit and registration process).

156. See Stenzel, *supra* note 154, at 273-74 (discussing costs savings companies have attributed to improved decision-making following an ISO audit).

157. See Linz Audain, *Judicial Careers, Judicial Selection, and an Agency Cost Model of the Judicial Function*, 42 AM. U.L. REV. 115, 134 n.103 (1992) (noting that effective business managers create conditions that enable firms to profit for long durations).

158. See Philip M. Nichols, *Trade Without Values*, 90 NW. U. L. REV. 658, 672-79 (1996) (discussing the deeply-held environmental values of many consumers).

public that a given firm makes environmental decisions in an appropriate manner.<sup>159</sup>

Third, certification makes a business's product or service cheaper by reducing the transaction costs involved in investigating that business.<sup>160</sup> Potential buyers, particularly those contemplating long-term or multiple-repeat arrangements, must investigate many aspects of a potential supplier, including the supplier's quality assurance processes.<sup>161</sup> Such investigations can be particularly expensive when businesses are physically distant from one another or when one of the businesses is in a remote location.<sup>162</sup> Given the choice between suppliers that appear equal in every other way, a rational buyer will choose the supplier that will be cheaper to investigate. *ISO 9000* certification significantly reduces the cost of investigation because someone else has completed a substantial part of the investigation of the business that has received certification has already been done.

Finally, conforming to internationally-accepted standards lowers the risk that a business will be found legally liable for its behaviors (although, of course, conformity does not entirely eliminate that risk).<sup>163</sup> This is particularly pertinent to environmental management standards, because environmental laws change a great deal and generally become more expansive.

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159. See Samuel N. Lind, *Eco-Labels and International Trade Law: Avoiding Trade Violations While Regulating the Environment*, 8 INT'L LEGAL PERSP. 113, 149-50 (1996) (discussing the value of *ISO 14000* certification as a signal of environmentally responsible behavior).

160. See Richard W. Painter, *Toward a Market for Lawyer Disclosure Services: In Search of Optimal Whistleblowing Rules*, 63 GEO. WASH. L. REV. 221, 268 (1995) (observing how positive signaling to regulators reduces the immense costs of compliance).

161. See *id.* at 269 (discussing the tremendous transaction costs that the need for due diligence imposes).

162. See Richard L. Bohanon & William C. Plouffe, Jr., *Mongolian Bankruptcy Law: A Comparative Analysis with the American Bankruptcy System*, 7 TULSA J. COMP. & INT'L L. 1 (1995) (making exactly this point using Mongolia as an example).

163. See Stenzel, *supra* note 149, at 274-75 (discussing legal implications).

## B. STANDARDS FOR DECISIONS THAT MAY INVOLVE CORRUPTION

Business ethicists have long realized the need to provide a decision-making framework for individuals in a business who are confronted with morally complex situations.<sup>164</sup> In the absence of such a framework, decisionmakers can become confused, can make contradictory decisions, or decisions that they will later regret.<sup>165</sup> A situation that may involve corruption presents the same dangers, would benefit from *prior* thought and guidance.

The certification process APEDE envisions would provide this guidance and would also accrue all the advantages obtained through the certification process. The certification process would also mitigate the assurance problem presented by corruption.<sup>166</sup>

APEDE proposes a code that gives life to a fairly simple standard: when confronted with a complex moral situation, act in the way that would be considered most appropriate if all of the facts were made universally public.<sup>167</sup> This simple standard is especially applicable to situations where corruption may be an issue, as corruption is generally hidden and carried out in secret.<sup>168</sup> In order to be certified,

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164. See Keneth Goodpaster, *Some Avenues for Ethical Analysis in General Management*, HARV. BUS. SCH. CASES No. 9-383-007, 1 (1982) (discussing the need for frameworks to guide decisionmakers in morally ambiguous situations).

165. A story often used by business ethicists to demonstrate these tendencies is Bowen McCoy's *The Parable of the Sadhu*. HARV. BUS. REV., May-June, at 54 (1997). The author of this story was a senior executive at the banking firm of Morgan Stanley who spent a six month leave trekking in the Himalayas. *Id.* During one particularly strenuous trek, in which the party had to reach and cross an ice-covered pass at 18,000 feet, McCoy's party found an "almost naked, barefoot body of an Indian holy man—a Sadhu" who was experiencing hypothermia. *Id.* at 55. The party was not prepared to make decisions that required balancing the life of a stranger against the completion of their goal. *Id.* at 57. After a great deal of internal agitation, the party made the Sadhu comfortable and then left him; the decision distracted the entire party. *Id.* at 55-56. Moreover, Bowen does not know whether the Sadhu lived or died, and the decision still troubles him. *Id.* at 56. Bowen, and others, argue that the party would have been better off if it had prepared a process for making decisions about morally complex situations. *Id.* at 57-58; see also James R. Elkins, *Lawyer Ethics: A Pedagogical Mosaic*, 14 ND J. L. ETHICS & PUB POL'Y 117, 142-45 (2000) (discussing the parable of the Sadhu at length).

166. See Lind, *supra* note 159 and accompanying text (highlighting the value of the certification process).

167. See DE OBARRIO, *supra* note 140, at 5.

168. See Heimann, *supra* note 67 and accompanying text (noting that because



an independent auditor would have to find a process for training each person who makes decisions for a business in both the content and use of the code.

A code, though laudatory, is not by itself sufficient. Certification should also examine decision-making processes and impose at least three structural requirements. First, decisions that are at risk of involving corruption must be approved by multiple and distinct parties. Second, managers must make all decisions in a transparent fashion so that observers can assign responsibility to an accountable party. Finally, an enterprise must account for all of its funds in a manner that precludes the creation of slush funds that could be used to finance bribes.<sup>169</sup>

Upon binding itself to an appropriate code, meaningful training in that code, a decision-making process that spreads out authority but focuses accountability and responsibility, and a financial accounting process that prevents the creation of secret funds, a business could be certified and that certification registered.<sup>170</sup> Companies could agree that they would only conduct business with other certified companies, and the government could require that companies who wish to conduct business with the government be certified. Foreign parties might also require certification of their Panamanian business partners.<sup>171</sup> In these ways, certification would become a critical attribute for conducting business.

Each of the four benefits that arise from the International Standards Organization certification process would accrue to businesses adhering to this certification model.<sup>172</sup> First, clearer direction and training in dealing with complex situations improves management, and improved management inures to the benefit of a

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corrupt actors generally hide their activities, the discovery of their conduct leads to increased costs).

169. Cf. David A. Gantz, *A Post-Uruguay Round Introduction to International Trade Law in the United States*, 12 ARIZ. J. INT'L & COMP. L. 7, 177 (1995) (stating that the impetus behind many U.S. anticorruption laws is the elimination of slush funds that could be used to hide corrupt payments).

170. See discussion *infra* Part VI.A (elaborating on the certification process).

171. See discussion *infra* Part V.B (discussing corruption in Panama).

172. See discussion *infra* Part VI (describing ISO's group of standards).

business. Corruption presents a complex situation that the code would help actors navigate.<sup>173</sup>

Second, certification also would confer reputational benefits. A majority of people condemn corruption.<sup>174</sup> Most people also perceive corrupt relationships to be harmful.<sup>175</sup> Certification is a signal that a particular business does not engage in this form of conduct.

Third, certification also makes a good or service cheaper, particularly for foreign buyers. In addition to the general distaste that most businesses have for corrupt relationships, an increasing number of jurisdictions criminalize transnational bribery, and thus an increasing number of businesses are required to investigate possible corrupt relationships among those with whom they might conduct business.<sup>176</sup> A meaningful certification process would signal to these foreign entities that they could safely conduct business with a certified business without the transaction costs that would otherwise be associated with entering into a business partnership.

Finally, certification would also mitigate the risk of future legal liability. Actors in emerging economies face two challenges that increase the risk of future liability. The first is that, by definition, the laws and regulations in emerging economies undergo a great deal of change.<sup>177</sup> The second is that as societies emerge from endemically corrupt regimes, it is quite possible that they will impose liability retroactively on the businesses with which those regimes entered into corrupt relationships.<sup>178</sup>

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173. See Salbu, *supra* note 65, at 49 (discussing the moral and legal complexity of corruption).

174. See *supra* note 4 and accompanying text (highlighting the major religions' rejection of corruption).

175. See *supra* note 3 and accompanying text (providing a historical context of the condemnation of corruption).

176. See OECD Convention, *supra* note 85 (requiring OECD members to criminalize transnational bribery); see also Eric Stein, *International Integration and Democracy: No Love at First Sight*, 95 AM. J. INT'L L. 489, 495 (2001) (stating that the OECD "represents 85 percent of world trade and 90 percent of world foreign investment").

177. See Philip M. Nichols, *A Legal Theory of Emerging Economies*, 39 VA. J. INT'L L. 229, 231-32 (1999) (noting that the most salient aspect of emerging economies is change).

178. The difficulties experienced by businesses in Indonesia who had been

Most importantly, a certification process addresses the assurance problem that corruption presents. Corrupt relationships are not optimal, and most actors would prefer to avoid them, but might not be able to do so without assurances that other actors are behaving in accordance.<sup>179</sup> A certification process provides such an assurance.<sup>180</sup> First, a very clear standard is established for conduct by all actors. Second, the conduct of actors is monitored. Third, defection is penalized, not by dysfunctional state institutions, but instead by a diffuse marketplace.

## CONCLUSION

Corruption is a serious impediment to positive change in emerging economies. As such, it merits the attention given to it by both policymakers and scholars. Too often, however, that scrutiny analyzes corruption as simply a failure of enforcement, and does not take into account the choices facing an actor in an endemically corrupt setting.<sup>181</sup>

A more textured understanding of corruption reveals that corruption often presents an assurance problem.<sup>182</sup> Actors do not want to enter into corrupt relationships and they understand that both

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associated with Suharto during that corrupt regime's reign serve as a warning of possible retribution in other countries. See Dave Lindorff, *Stark Lessons from Indonesia*, GLOBAL FIN., Aug. 1998, at 5 ("hundreds of major international contracts" are under review). Retroactive liability is not an unknown concept; in the United States the Comprehensive Environmental Reclamation and Cleanup Liability Act imposes retroactive liability for acts that may have been legal at the time they occurred but which contributed to environmental degradation. See Bruce Howard, *A New Appreciation for Retroactive Liability In CERCLA: An Appreciation of the Synergy Between Common and Statutory Law*, 42 ST. LOUIS L.J. 847, 847 (1998) (observing that retroactive liability is not an unknown concept, and that the doctrine of retroactive liability is seriously flawed).

179. See *supra* Part VI.A (explaining how certification encourages anti-corruption compliance).

180. See *supra* notes 158-165 and accompanying text (outlining the numerous benefits of certification).

181. See discussion *infra* Part II (noting that the complexity of corruption requires many differing solutions).

182. See discussion *infra* Part III (suggesting that corruption is an assurance problem).

they and their society are better off if they do not.<sup>183</sup> In the absence, however, of assurances that their competitors are not acting corruptly, actors who behave honestly risk losing everything.<sup>184</sup> Unfortunately, the usual solution to an assurance problem—penal law—does not work in endemically corrupt systems.<sup>185</sup>

The certification process suggested by APEDE solves the assurance problem.<sup>186</sup> Businesses are assured that other actors are complying, and know that those who do not will be punished by the marketplace. Certification also confers other benefits that make it attractive.

Certification alone will not eradicate corruption. It does, however, constitute an important component in the bundle of structures that will, and it highlights a better understanding of an ancient but still too little-understood phenomenon.

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183. See Jun, *supra* note 78, at 1085 (noting that although corruption may be a prevalent practice in Korea, it is not a morally acceptable practice).

184. See Rousseau, *supra* note 97 and accompanying text (stating that, consistent with the underlying rationale of the stag hunt, actors who coordinate their actions will be best off, but when there are defectors, those who do not defect risk losing everything).

185. See WORLD BANK, *supra* note 34, at 13 (highlighting the problems associated with corruption within official enforcement bodies in endemically corrupt systems).

186. See discussion *infra* Part V (describing the process that APEDE uses in attempting to solve assurance problems).