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Political decentralization and corruption: Evidence from around the world ☆

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ABSTRACT

How does political decentralization affect the frequency and costliness of bribe extraction by corrupt officials? Previous empirical studies, using subjective indexes of perceived corruption and mostly fiscal indicators of decentralization, have suggested conflicting conclusions. In search of more precise findings, we combine and explore two new data sources—an original cross-national data set on particular types of decentralization and the results of a firm level survey conducted in 80 countries about firms' concrete experiences with bribery. In countries with a larger number of government or administrative tiers and (given local revenues) a larger number of local public employees, reported bribery was more frequent. When local—or central—governments received a larger share of GDP in revenue, bribery was less frequent. Overall, the results suggest the danger of uncoordinated rent-seeking as government structures become more complex.

1. Introduction

How does political decentralization affect the frequency and the costliness of corrupt bribe extraction by officials? Theories suggest conflicting conclusions. On one hand, by bringing officials “closer to the people” or encouraging competition among governments for mobile resources, decentralization might increase government accountability and discipline. On the other hand, decentralization could impede coordination and exacerbate incentives for officials at different levels to “overgraze” the common bribe base. More generally, one might expect a variety of effects associated with different types of decentralization to operate simultaneously, pulling in many directions, with different strength in different contexts.

A number of scholars have sought to answer this question empirically by looking for relationships between measures of political or fiscal decentralization and cross-national indexes of perceived corruption derived from surveys of risk analysts, businessmen and citizens. In particular, scholars have examined perceived corruption ratings produced by Transparency International (TI), the World Bank (WB), and the business consultancy Political Risk Services, which publishes the International Country Risk Guide (ICRG). The findings of these studies have been mixed and sometimes mutually contradictory.

Focusing on fiscal decentralization, Huther and Shah (1998), De Mello and Barenstein (2001), Fisman and Gatti (2002), and Arikan (2004) all report that a larger subnational share of public expenditures (as measured in the IMF's *Government Finance Statistics*) was associated with lower perceived corruption using the TI, ICRG, or WB indexes. Enikolopov and Zhuravskaya (2007) do not report an unconditional effect, but find that a larger subnational revenue share is associated with lower perceived corruption (using WB, but not TI, data) in developing countries with older political parties (and vice versa); a larger subnational revenue share in developing countries where there are few parties in government is associated with lower corruption (on both WB and TI measures) (and vice versa). Looking at political rather than fiscal indicators, Goldsmith (1999), Treisman (2000), and Kunicová and Rose-Ackerman (2005) all found that federal

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structure was associated with higher perceived corruption. However, in a more recent review of the empirical literature, Treisman (2007) suggested that neither the (negative) expenditure decentralization effect nor the (positive) federalism effect was robust. The fiscal decentralization effect was weakened by controlling for national religious traditions, and the federal effect disappeared as the number of countries in the sample increased. Treisman (2002) and Arikan (2004) explored whether smaller local units were associated with less corruption because of more intense interjurisdictional competition, but obtained inconclusive results. Finally, examining the effect of the vertical structure of states, Treisman (2002) found that a larger number of administrative or governmental tiers correlated with higher perceived corruption, but whether subnational governments were appointed or elected did not have a clear effect.

In this paper, we advance and improve upon this literature in three ways. First, our analysis exploits an original cross-national data set on different varieties of decentralization, compiled from more than 480 sources. This allows us to design indicators of particular types of decentralization to match the underlying logic of specific arguments. We look for relationships between reported experience with corruption and: (i) the number of tiers of government or administration in the country (see Section 3.1), (ii) the average land area of lowest tier units (see Section 3.2), (iii) several proxies for the extent of subnational political decisionmaking (see Section 3.2 and others), (iv) an indicator for whether lower tier units have elected executives (see Section 3.3), (v) a measure of subnational tax revenues as a share of GDP (see Section 3.4), and (vi) an estimate of the share of subnational government personnel in total civilian government personnel (see Section 3.5).

Second, most previous studies have used perceived corruption indexes that rely on the aggregated perceptions of businessmen or country experts, many of whom may have formed impressions—perhaps subconsciously—based on common press depictions of countries or conventional notions about what institutions or cultures are conducive to corruption. More recently, a second type of data has become available: survey responses of businessmen and citizens in particular countries about their own (or close associates') concrete experiences with corrupt officials. In a recent study, Treisman (2007) showed that, for developing countries, the perceived corruption indexes were relatively weakly correlated with experience-based indicators. Among countries rated as highly corrupt on the subjective indexes of TI, WB, and the ICRG, there is great variation in the level of reported experience with corruption. For instance, on the World Bank perceived corruption index, Argentina and Macedonia were both rated about equally corrupt in 2000: they were ranked 103 and 114 respectively out of 185 countries. But respondents from these two countries gave dramatically different answers when surveyed by the United Nations Interregional Crime and Justice Research Institute (UNICRI) in the late 1990s about their own personal experience with bribery. When asked whether during the previous year “any government official, for instance a customs officer, police officer or inspector” had asked or expected them to pay a bribe for his services, respondents in Argentina were three and a half times as likely as the Macedonian respondents to say yes. While Argentina had the second highest frequency of reported demands for bribes (second only to Indonesia), Macedonia was only 24th in the list of 49 countries, about even with South Africa and the Czech Republic. Perhaps of greater concern, a number of factors commonly believed to affect corruption (democracy, press freedom, oil rents, even the percentage of women in government) do an excellent job explaining the cross-national variation in the subjective corruption indexes (R-squareds approaching .90). But the same factors are mostly uncorrelated with the frequency or scale of self-reported experiences with corruption once one controls for income. One cannot help wondering if the businessmen and experts whose perceptions are being tapped might be inferring corruption levels from its hypothesized causes.

In this study, we explore the results of an experience-based survey of business managers conducted in 80 countries. The World Business Environment Survey interviewed managers from more than 9000 firms in 1999–2000. We focus on two questions. Respondents were asked: “Is it common for firms in your line of business to have to pay some irregular ‘additional payments’ to get things done?” and “On average, what percent of total annual sales do firms like yours typically pay in unofficial payments/gifts to public officials?” The first question provides an indicator of the frequency of bribery, while the second aims to estimate its scale. The relationship between the proportion of respondents that said irregular payments were expected “always”, “mostly”, or “frequently”, and the World Bank's subjective index of perceived corruption for the year 2000 are graphed in Fig. 1. It is interesting to note that while businessmen in France and Brazil gave very similar responses to this question (about 27% saying bribes were expected “always”, “mostly”, or “frequently”), France is rated as among the least corrupt countries on the World Bank's index, while Brazil is perceived to have much higher corruption. Of course, no approach is completely without problems; it is possible that questions that focus more closely on managers' direct experience with corruption might not be answered with complete frankness for fear of some kind of self-incrimination. However, we believe this danger is less serious than the danger that bias will creep into the assessments of “experts” and foreign businessmen because of inconsistencies in media coverage. (As a robustness check, we compare our results to those obtained using the traditional perceived corruption data.)

Third, besides permitting us to focus on experience-based rather than subjective indicators of corruption, the WBES makes it possible to control better for individual characteristics of survey respondents (which vary systematically across countries). Specifically, we can control for the size, ownership structure, investment level, and level of exports of firms in analyzing their managers' responses on corruption.

In the next section, we briefly introduce the decentralization data used in the paper. We review common arguments about the consequences of decentralization for governance in Section 3, and in Section 4 discuss the corruption data and controls. We then look for evidence of the hypothesized effects in the WBES. In Section 5 we present empirical results and discuss robustness tests. Section 6 discusses the findings and concludes.

2. A new data set on governance in multi-level states

Previous work has often used measures of fiscal decentralization or simple dummies for federal structure to proxy for various other types or dimensions of political and administrative decentralization. The data set introduced here permits a more fine-