

Final article:

Lindgreen, A. (2004), "Corruption and unethical behavior: report on a Danish code", *Journal of Business Ethics*, Vol. 51, No. 1, pp. 31-39. (ISSN 0167-4544)

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Corruption and Unethical Behavior: Report on a Danish Code

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ABSTRACT

Corruption is defined as private individuals or enterprises who misuse public resources for private power and/or political gains. They do so through abusing public officials whose behavior deviates from the formal government rules of conduct. Ethical behavior is defined as individuals or enterprises adhering to a non-corrupt work or business practice. A review of the academic literature is conducted drawing on perspectives from the political, economic, and anthropological sciences, and experiences with a Danish program are reported on. This program identifies five different actions for dealing with corruption: (1) no action; (2) withdrawals from markets; (3) decentralized decision-making process; (4) establishment of an anti-corruption code; and (5) mutual commitment through integrity pact. The following aspects of ethical behavior should be regulated through an anti-corruption code: the company *vis-à-vis* political parties; gifts and entertainment expenses; political campaign contributions; and policy against small-scale corruption. Directions for future research are considered including the role of international organizations and multinational companies in fighting corruption and fostering ethical behavior; the role of countries and their governments; and management systems.

KEYWORDS. Corruption, code, Denmark, ethical behavior, guidelines, unethical behavior.

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INTRODUCTION

With a worldwide cost of bribes estimated to some \$80 billion a year (Ferrell, Fraedrich, and Ferrell 2002), corruption and unethical behavior have become the latest buzzwords. For example, the objectives in corporate citizenship are not only to be productive and profitable but also to work within the legal framework and to follow socially established moral standards (Carroll 1979, 1998; Laufer 1996; Maignan and Ferrell 1998; Pinkston and Carroll 1994). Indeed, believing that responsible management is inextricably linked to corporate survival, some observers suggest that corporate citizenship activities really ought to be viewed as the entry ticket to doing business (Altman 1998).

Guidelines are needed, however. Consider for example *The Economist* that recently has focused on the widespread prevalence of corruption; the sheer number of reported cases indicate that at least not all companies follow socially established moral standards. One case of corruption is the \$14 million looting in the wake of the privatization of Mozambique's largest bank, BCM (*The Economist* 23 November 2002). Another case is the disappearance of \$4.3 billion from state coffers in the past five years in Angola, an amount that equals about a tenth of the country's GDP (*The*

Economist 26 October 2002). For the African continent as a whole the African Union has estimated that the costs of corruption are almost \$150 billion a year (*The Economist* 21 September 2002).

Whilst common in Africa it should be realized that corruption is not confined to this continent, as corruption does not disappear with the modernization of countries, it simply takes on a new form (Girling 1997). Spectacular cases of corruption from the corporate world have thus besieged the United States during the past 12 months including Andersen Consulting, Enron, WorldCom, and Xerox (*The Economist* 6 July 2002). Europe has also suffered from the perils of corruption. For example, Germany has witnessed numerous scandals involving companies, public officials, and politicians, and it is claimed that corruption has now become the norm in German waste disposal, building, property, and pharmaceuticals (*The Economist* 6 April 2002), while in Italy eight former prime minister and some 5,000 businessmen and politicians have been charged with corruption (*The Economist* 16 February 2002).

The exposure of corruption not only highlights the negative effects of corruption and unethical behavior but also brings to the fore the role that international companies play in supporting and upholding the system of corruption (*The Economist* 21 September 2002). When caught red-handed some companies explain that they were not aware that they had done something illegal, or they claim that the only way to do business in a corrupt market is to play the game. If this is true it would seem that in order to assist companies there is an acute need for guidelines. Andvig and Fjeldstad (2001) note that one of the major difficulties in researching corruption and unethical

behavior has been the lack of empirical data, and the purpose of this paper is, therefore, to add to the relatively limited body on corruption and unethical behavior.

Organization of the Paper

After defining corruption we address how, if at all, it is possible to avoid corruption and unethical behavior in the business world. We achieve this by building upon the research studies from the Confederation of Danish Industries and the Norwegian Institute of International Affairs. To this end we first conduct a review of the academic literature on corruption drawing on perspectives from the political, anthropological, and economic sciences before we report on a code that the Confederation of Danish Industries has developed to aid its members. This code has been put together using knowledge from country specialists and international business people. We finish the paper by considering managerial and research implications and outlining future research.

THEORETICAL BACKGROUND

Corruption takes place on the national scene and the international scene, in the public sector and the private sector, and between these two sectors. One must realize that "[corruption] is a complex and multifaceted phenomenon with multiple causes and effects, as it takes on various forms and functions in different contexts" (Andvig and Fjeldstad 2001: p. 7). The literature has traditionally distinguished between different kinds of corruption: bribes including kickbacks, gratuities, commercial arrangements, baksheesh, sweeteners, pay-offs, and speed or grease money; embezzlement and straddling; fraud; extortion, blackmailing, protection or security money, under-the-

table fees, and gifts; and favoritism and nepotism (e.g., Amundsen 1999; Andvig and Fjeldstad 2001; Ferrell, Fraedrich, and Ferrell 2002; Poole-Robb and Bailey 2002). For the public sector a distinction is also commonly made between political corruption (Moody-Stuart 1997) and bureaucratic corruption (Andvig and Fjeldstad 2001). An interesting distinction also has been made between economic corruption, which entails an exchange of cash or material goods, and social corruption, which includes clientelism, nepotism, as well as ethnic and other favoritism (Médard 1998, as referenced in Andvig and Fjeldstad 2001).

Although narrow definitions risk ignoring parts of the problem most authors understand corruption as private individuals or enterprises misusing public resources for private power and/or political gains through abusing public officials whose behavior deviates from the formal government rules of conduct (see, for example, Heidenheimer, Johnston, and LeVine 1989; Huntington 1968; Khan 1996; Nye 1967; Poole-Robb and Bailey 2002). In a similar vein, 'ethical behavior' can conveniently be defined as adhering to a non-corrupt business practice.

Perspectives on Corruption

We will consider three perspectives on corruption in the following: the political perspective, the economic perspective, and the anthropological perspective.

The political perspective on corruption argues that the state is needed in order to ensure economic development, and that our understanding of corruption therefore must take into account a country's political system (Hope 2000; Johnston 1997). The

general belief is that corruption can be avoided only if a country is democratic, which is achieved through the strengthening of democratic institutions, civic society, and general public sector reforms (Andvig and Fjeldstad 2001; Doig and Theobald 2000; Friedrich 1989; Hope 2000; Treisman 2000). However, the argument has also been put forward that democratic countries run the risk of increasing the opportunities for officials becoming involved in corruption (Diamond and Plattner 1993; Quah 1999). In the case of non-democratic countries the control over politics and economies is key: for example, the Chilean military dictatorship exercised a centralized power that permitted it to keep corruption in the country at a low level.

The economic perspective has long been predominant in the research on corruption. This literature stream believes that the level of corruption decreases with economic development because it otherwise would lead to inefficient and unpredictable transactions (Shleifer and Vishny 1993) and/or social stigma (Ekpo 1979). Moreover, much research has found that the existence of political rights and democracy decreases the risk of corruption, especially if political rights and democracy have been around for a long time (Diamond and Plattner 1993; Treisman 2000). It has also been argued that federalism leads to corruption (e.g., Wunsch and Olowu 1990), but that this is not the case for decentralization due to local social pressure (e.g., Goldsmith 1999); there is support for the opposite view, too, though (Fjeldstad and Semboja 2000; Prud'homme 1995; Treisman 2000). Findings on the relationship between public sector salaries and recruitment policies on the one hand and corruption on the other hand are not conclusive, and the same holds true for a possible relationship between international openness and trade on the one hand and corruption on the other hand.

Lastly, the anthropological perspective on corruption contends that corruption is a function of culture and that it is essential to examine how individuals evaluate social practices. One case in point is the African countries where corruption is part of traditional social practices (Bratton and van de Walle 1994; Chabal and Daloz 1999; de Sardan 1996; Médard 1998). Another case in point is that corruption appears to be less frequent in countries with Protestant traditions, histories of British rule, more developed economies, and (probably) higher imports (Treisman 2000). It is therefore not an easy task to judge whether activities are corrupt or not, as this will depend on the cultural view one has on corruption (Andvig and Fjeldstad 2001; Williams 1999). One difficult-to-evaluate example is the practice of *guanxi* in China, which is doing business through personal relationships (Arias 1998; Yang 1989, 1994).

METHODOLOGY

Until the mid-1990s, research on corruption and unethical behavior was not considered to be serious because of the numerous problems of analyzing the data (Andvig and Fjeldstad 2001). We chose to investigate the experiences from one particular country that consistently has been among highest-scoring countries in the Corruption Perception Index surveys (Transparency International 2002): Denmark. Whilst corruption in Denmark is limited, Danish companies are becoming international and, indeed, global in their orientation and so they are frequently faced with corrupt markets. The question then is: what do these companies decide to do? We first examined what has appeared in the Danish business press on corruption and unethical behavior before we considered the code that the Confederation of Danish

Industries has developed. 250 companies participated in a questionnaire survey in 2000; all the companies are members of the confederation and export to, or have established production facilities in, the so-called transit economies in the Baltic region. We therefore realize that our discussion deals only with the experiences of a small number of companies in Denmark.

FINDINGS

In 2002-2003, *Dagbladet Børsen*, the leading business daily in Denmark, ran an editorial campaign on corruption and unethical behaviour. The newspaper's investigative journalists documented how Danish companies, when they do business abroad, frequently face corruption and how this results in increased costs, risky investments, and/or loss of contracts. For example, a survey in 2000 of 250 Danish companies with business activities in the Baltic region revealed that 30 per cent of the companies believed the problem of corruption is overshadowing most other problems. South America and the Middle East are also markets perceived to be troublesome (Olsen 2002b, 2002c). In the following we will first consider that part of the Danish penal code that deals with corruption before we move on to examine the guidelines that the Confederation of Danish Industries have written up to help their members avoid corruption.

The Danish Penal Code

The Danish penal code's provisions concerning corruption have recently been changed in accordance with the conventions that the European Union, the Organization for

Economic Co-operation and Development, and the Council of Europe have introduced since 1996 in their fight against corruption (Confederation of Danish Industries 2001). However, these changes to legislation did not clarify the situation in Denmark: whilst expenses incurred because of corruption previously were tax deductible, corruption is now punishable with up to three years imprisonment regardless of where the act has taken place. But corruption is not the same across different countries, and this means that what is considered as corruption in one country might not be viewed as corruption in another country. This is important because according to Danish legislation a lawsuit can only be brought about if the act is punishable in Denmark and in the country where it took place. It thus becomes key whether a country has signed up to the Organization for Economic Co-operation and Development because this organization limits its convention to active bribes, whereas the European Union and the Council of Europe both operate with active and passive bribes (for active and passive, see shortly). These two organizations also distinguish between small-scale and large-scale corruption depending where in the hierarchy corruption takes place because the consequences of large-scale corruption are more severe in terms of the economic growth, resource allocation, and democratic accountability, and it involves the favoritism of non-competitive companies. Lastly, the Danish legislation differentiates between the public and private sector. For both sectors, however, the legislation covers natural persons such as employees, as well as legal persons including the management team and agents (Confederation of Danish Industries 2001; Olsen 2002b).

For the public sector a crime of active corruption has been committed when a person gives, promises, or offers a present, or other form of advantage, to somebody who is

in Danish, foreign, or international public service or commission in order to persuade this person to do, or refrain from doing, what should rightfully have been done; whilst accepting a bribe constitutes a crime of passive corruption (Danish Penal Code §122). The following should be noticed. An act of corruption has taken place even though a public servant has only been promised a gift, but not actually (yet) received it. The bribe must be unjustified, which means that it is necessary to consider the state of things in the country where the bribe is paid and the reason behind offering the bribe before a judgment can be made. If a company has not held out the prospect of something to a person then it is not against the law that this person gets a small gift after the business activity is over. The bribe does not necessarily need to be given to a person with decision power – it still constitutes bribery although the present is for this person's wife or friends. Lastly, if the person is paid to take actions, or refrain from taking actions that he should have rightfully done it constitutes bribery. The law also affects a private company if it carries out activities for the public (Confederation of Danish Industries 2001).

For the private sector a crime of corruption has been committed when a person receives, demands, or accepts presents or any other advantages, or when a person gives, promises, or offers such a present or advantage (Danish Penal Code §299, number 2). The same considerations apply here as for the public sector. However, the crime is punishable up to 18 months in prison only, and a number of countries outside Europe have no legislation against corruption in the private sector (Confederation of Danish Industries 2001).

It can be difficult for companies to explain to their employees what corruption is, as this is dependent upon the country. For example, Ferrell, Fraedrich, and Ferrell (2002) note that decision rules often are vague or in conflict making it difficult to say which decision is the correct one. Some companies argue that corruption is just another way of doing business, as evidenced in the following text: "If Danish businesses want to export to Middle Eastern countries they will have to pay so that things run smoothly - otherwise they can forget about it" (Christian Bruun, manager with Kuwait Danish Dairy Co., as referenced in Olsen 2002c). In general, a company's liberty of action will be dependent on the size of the company's economic activities and the amount of the company's available resources such as legal assistance, negotiations with public authorities, etc. Small companies are more likely to do business with a corrupt partner than larger companies, *ceteris paribus*, as a closed business deal easily can decide whether or not the company continues to stay in business. This is why Transparency International distinguishes between small- and larger-sized companies (Transparency International 2001).

It is because of the above mentioned difficulties and/or misunderstandings that the Confederation of Danish Industries decided to gather information from a range of their member companies, which have experienced corruption in one way or another, so as to identify possible actions for preventing corruption and unethical behavior.

Anti-corruption Actions

The Confederation of Danish Industries identified five different actions: (1) no action; (2) Odysseus action – withdrawals from markets; (3) decentralized decision-making

process; (4) establishment of an anti-corruption code; and (5) mutual commitment through integrity pact (Confederation of Danish Industries 2001). Each of these actions is examined in the following.

No action: At times, it would seem entirely reasonable not to have a drawn-up action at all. This is, for example, the case when companies enter corrupt markets only seldom, or when small companies have much less negotiation power than their bigger counterparts. Moreover, the consequences could be serious of making an anti-corruption action public if, for example, the company does not succeed in following this action effectively: the public would then be likely to attack the company for its lack of role-model behavior. One of this action's main drawbacks is that employees or agents could easily break the penal code inadvertently since they have not been made aware what constitutes corruption.

Odysseus action – withdrawals from markets: This action takes its name from the *Odyssey* where Odysseus tied himself up in order to avoid the temptations of the sirens. In a similar fashion a company could argue that the only real way to avoid demands for bribes is to stay away from corrupt markets. Evidence from the World Bank suggests a negative relationship between the degree of corruption and the amount of foreign investment meaning that companies tend not to do business in corrupt markets: for example, investment levels in Eastern European and Central Asian countries with high levels of corruption were six per cent lower on average than in countries with medium levels of corruption (World Bank 2002).

Decentralized decision-making process: Some multi-national corporations let the national subsidiaries decide whether or not an anti-corruption action is warranted. Although it would seem logical to adapt to regional differences the problem is that according to Danish legislation the parent company will be held legal accountable if it can be demonstrated it has turned a blind eye to the activities of its subsidiaries.

Establishment of an anti-corruption code: Other companies reach the decision that an anti-corruption code should be written up. Among the fundamentals of such a code are to explain employees how to behave in corrupt markets; to protect the company and its employees; and to build transparent procedures that can be checked so that mistakes and corruption are avoided.

Mutual commitment through integrity pact: Through this action the public authorities and competing companies set up an integrity pact the principle of which is that all parties refrain from engaging in corruption. In order to reduce the likeness that corruption takes place the pact also establishes a set of procedures that seek to increase transparency, protect wholesale purchasing against corruption, and forbid corrupt activities of agents through written agreements, as well as mete out sanctions if one party nevertheless breaks the pact. The value of an integrity pact increases the more companies sign up for it – ideally, all companies in a given sector should participate, and the possible sanctions must be credible.

In summary, companies should know that although it may seem tempting to pay for easing business this is "the thin end of the wedge, as it results in increased vulnerability to extortion, and if corrupt [governmental or municipal] authorities are

revealed the company, which had fallen victim to these authorities, may go down as well" (Jarl Frijs-Madsen, head of office with the Danish Embassy in Warszawa, as referenced in Olsen 2002a: p. 13). Because of changes in legislation it is now necessary that bribes be financed out of funds that are kept secret and this makes it difficult for the company to control its flow of money, which in turn makes it easier for the employees to cheat the company (Confederation of Danish Industries 2001).

Ethical Behavior

Four aspects of ethical behavior are regulated through an anti-corruption code (Confederation of Danish Industries 2001). These are (1) the company *vis-à-vis* third parties such as agents, customers, and suppliers; (2) gifts and entertainment expenses; (3) political campaign contributions; and (4) the company's policy against small-scale corruption.

The company vis-à-vis third parties such as agents, customers, and suppliers: The company must identify clearly who is covered by the code, as well as the extent to which these parties are liable and what the sanctions for breaking the code are. The use of agents (and suppliers) can be especially problematic since these may be used to operate in a corrupt market and find this the normal way of doing business. If there is a need for agents a company should scrutinize an agent's reputation beforehand; keep up-to-date lists with names of the agents that the company has employed in the past, and what their experiences have been; and require the agent to comply with the company's policy, which also means that a contract is cancelled if the agent behaves

in an unethical behavior. In questions of dispute a good piece of advice is to seek the help of a legal adviser in the particular region.

Gifts and entertainment expenses: In most countries it is common to invite a business partner out for dinner, or to offer him a gift. But with the difficulty of distinguishing between courtesy and corruption it becomes necessary with a set of guidelines. Gifts and entertainment expenses should not be against the receiving company's policy or the country's penal code. It should also be the case that the company, which receives gifts and entertainment, can give something back gifts and entertainment of equal value. Moreover, gifts and entertainment expenses should not be extravagant. With regard to business partners a gift should never be a sum of money, be given in secret, or offered at the time of a quotation or contract negotiation. With regard to gifts from business partners a gift should never be accepted if the purpose is to influence the direction of negotiations. Also, the monetary value of a gift should not exceed an amount that has been laid out in the company's policy.

Political campaign contributions: Before contributing to a political party a company must decide whether it is prudent or not. Some companies believe it is better to refrain from such contributions, as it could make the companies prone for criticism; other companies support all political parties in the parliament. If a company should decide for campaign contributions these should ideally take place through the headquarters to make sure that the anti-corruption policy is adhered to.

The company's policy against small-scale corruption: Whilst the Danish penal code generally does not distinguish between small- and large-scale corruption, some

foreign organizations like the Organization for Economic Co-operation and Development do operate with such distinctions arguing that it otherwise would be impossible to engage in business activities. There are cases where the Danish penal code would not consider it criminal to offer a bribe, for example if a person's security is threatened or if this is standard procedure for maintaining normal relationships. In all instances it is paramount that the bribe be documented in the company's records, and that the relevant manager be informed about the episode.

DISCUSSION AND CONCLUSIONS

Murray (1997) writes that corruption distorts decision-making in favor of those who can afford to pay and that it further enriches these people; that it leads to a sub-optimal resource allocation, especially in international aid programs, and that it frequently results in some programs that are unnecessary luxurious; and that it leads to the employment of people and organizations who are not competent of doing the job. It is hoped that the preceding discussion of the guidelines developed by the Confederation of Danish Industries helps in providing suggestions on how to fight corruption, which is condemned by almost everyone as being universally shameful, a sell-out to the rich, a betrayal of trust, and a violation of a divine paradigm (Noonan 1984).

When faced with a corrupt market, companies are in a typical prisoner's dilemma, as they must decide whether to pay a bribe or not: if they do not cough up with the money they risk losing a contract to a less-honest competitor, but if they accept that corruption is part of doing business they break the law and could become even more

vulnerable to extortion in the future. The optimum situation is, of course, if all companies refuse to engage in corrupt activities (Confederation of Danish Industries 2001).

A company's anti-corruption policy should not be just another document; rather it must be referred to on a regular basis. The document also has to be embraced by the management team, and employees must see that it pays off career wise to live by the rules (Ferrell, Fraedrich, and Ferrell 2002). For example, a person should not be promoted on the grounds of achieved sales alone – it is also important to know how these sales were realized. Although top management is key the involvement of lower-ranked managers, sales people, and people closer to the different regional markets is important, too, as these people will have valuable local information about corruption. Employees within the sales and purchasing departments, together with agents, are probably the ones who are most likely to be confronted with corruption, and special attention must therefore be given to these groups. Preferably, external auditors, who can also audit the company's economic activities, should evaluate the anti-corruption policy.

Research Implications

Pope (1997) argues that in order to fight corruption it is necessary to support public programs, government reorganization, law enforcement, and public awareness, as well as to change attitude at all levels. With corruption continuing to take on new forms when countries develop and modernize, this is a never-ending fight (Girling 1997). One direction for future research would be to examine the roles of international

organizations and multinational companies *vis-à-vis* the fight against corruption and unethical behavior.

The role of governments in the fight against corruption should be examined. For example, across Latin America one problem has been parliamentary immunity, but things are starting to change. Brazil's Congress has recently expelled members who faced corruption charges, and in Nicaragua president Bolanos made corruption an issue in his election campaign (*The Economist* 24 August 2002).

Research could also look at different management systems. For example, the problems of bribes related to public contracts in Germany are partly due to lack of openness, and because of this the federal interior ministry has recently drafted a freedom-of-information bill that covers local authority contracts and the government has plans for a national blacklist of companies paying bribes (*The Economist* 6 April 2002). Upgrades in management systems such as the appointment of foreigners as board members could dramatically improve the corporate image of previous tainted companies; this is what Lukoil, Russia's largest oil company, did in its attempt of catching up with Yukos, the most westernized oil company in Russia. International reports must also meet international accounting standards (*The Economist* 29 June 2002); in this respect the Sarbanes-Oxley act has reformed accounting practices in the United States (*The Economist* 8 February 2003).

It is also interesting to investigate why big investors traditionally have shown little inclination to criticize companies or to vote against corporate management at shareholder meetings although executives have undermined corporate governance.

Some reasons have been suggested as to why institutions decide to keep quiet: they do not want to damage the share prices; they pursue short-term momentum strategies; and they invest money on behalf of these companies and risk being dumped (*The Economist* 2 November 2002).

Lastly, although all members of the Organization for Economic Co-operation and Development have undertaken to introduce legislation dealing with corruption, progress in this area has been slow. Future research might therefore look into the implications, if any, of recent anti-corruption legislation (Givskov 2002).

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