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**WHAT ARE CAUSES AND CONSEQUENCES  
OF CORRUPTION IN MONGOLIA?****Б.Ариун-Эрдэнэ****Introduction**

Over the last several years, the issue of corruption has been attracting an increasing attention from both academics and policymakers. US Vice President Al Gore addressed that "Corruption ...is a serious crime with devastating consequences" in the first Global Forum on Fighting Corruption (GFFC) in 1999. World Bank (WB) addresses that corruption is a major factor impeding development. WB President James D. Wolfensohn said, "Corruption hampers economic growth, burdens the poor disproportionately, and undermines the effectiveness of investment and aid" at the fourth GFFC in 2005. Moreover, US president Bush sent a message, "...Every country is capable of fighting corruption, and the United States stands by nations who embrace transparency, promote the rule of law, and implement responsible economic policies" to the fourth GFFC.

Corruption is a phenomenon existing everywhere around the world in both developed and developing countries. Nevertheless, some countries are damaged from it more than the others depending on its origins, its extent, and efforts fighting against it. In transition countries, a transformation from command economies to market economies has created massive opportunities for the appropriation of rents (Mauro 1998: 11). Seen through democratic governance lens, corruption cannot co-exist with economic growth. As poverty and inequality are exacerbated by this phenomenon, problems escalate within the least-developed countries context (UNDP 2006: 69).



Mongolia has coped with double transition – from an authoritarian state to a democracy, and as well as from centrally planned to a market economy. During the transition period, Mongolia has made notable progresses in private sector

development and institution building process (ADB 2005: 5). However, like other transition countries, Mongolia has faced governance problems, including apparently increasing level of corruption. Over the past ten years, corruption in Mongolia has been increasing prevalently. According to WB indicator measuring corruption, Mongolia's placement had been worsened from 60<sup>th</sup> percentile among all countries in 1996 to 40<sup>th</sup> percentile in 2005.

I aim to provide a better understanding of the degree to which corruption exists in Mongolia, what are causes and consequences of it, and how Mongolians are fighting against corruption. In the following part, literature review related to the issue of determining causes and consequences of corruption and suggesting anti-corruption strategies and policies is provided. Then, I explore several definitions for and classifications of corruption provided by international organizations, and determine causes and consequences of corruption by summing up literatures particularly for transition countries. The next part provides a survey of corruption in Mongolia based on international perception and outcomes of surveys conducted in recent years. Particularly, I draw attention to anti-corruption efforts by the government of Mongolia and civil society. Since all materials used here are secondary sources, comparative or qualitative analysis technique is used in this paper.

#### Part I. Literature Review

With an increasing attention of the world in damaging effects of corruption, the studies on corruption are rising. A number of researchers and various international and domestic organizations are working in a field of determining causes of corruption and its effects on the economy and society, and designing and recommending anti-corruption policies and strategies. Consequently, numerous theoretical and empirical works have been done over time. This part presents a review of studies related to determination of corruption, identification of causes and consequences, and prevention of it particularly focusing on transition countries.

To understand determinants and effects of corruption is important for policy makers, as well as for public. Mauro (1998) listed the number of possible causes and consequences of corruption. By his definition, consequences of corruption are lower rate of investment, hence hindrance to economic growth, misallocation of talent, ineffectiveness of aid flows, loss of tax revenues, adverse budgetary consequences, lower quality of infrastructure and public

services, and distortion of the composition of government expenditure. He conducted a regression analysis on the relationship between corruption and the components of government expenditure and found a negative and significant relationship between corruption and education expenditure. Since educational attainment is an important determinant of economic growth, from the empirical result, it can be concluded that corruption retards growth.

Gray and Kaufmann (1998) considered "goods" that can be "purchased" from a politician or bureaucrat by corruption. They are government contracts, government benefits, public revenues, time savings and regulatory avoidance, and influencing outcomes of the legal and regulatory process. Consequently, they clarified economic costs of corruption as increase in transaction costs and uncertainty in the economy, inefficient economic outcomes as a result of impediment to investment and economic growth, misallocation of talent, and distortion of sectoral priorities and technology choices, and vulnerability in the state's legitimacy. When the incidence of corruption becomes systematically, the detection and punishment for it will become difficult and unattainable, and incentives for corruption increase further. They concluded that "...in sum, corruption is a symptom of fundamental economic, political, and institutional causes. ... The major emphasis must be put on prevention – that is, on reforming economic policies, institutions, and incentives (Gray and Kaufmann, 1998: 10)".

Corruption significantly impedes economic growth and shrinks production possibility frontier. Husain (1999) examined the detrimental effects of corruption in developing countries. Along with his evaluation using the Business International indices of corruption, a one-standard-deviation improvement in corruption index affects investment to rise by five percent of the GDP. He concluded that corruption diverts resources to the rich, and, hence, the lower classes are hardly hit by loss of infrastructure and excessive bribes.

Leite and Weidmann (1999) established the major determinants of corruption and evaluated its dependency by constructing corruption as a function of those factors. Using a simple model, they illustrated that the extent of corruption depends on natural resource abundance, government policies, and the concentration of bureaucratic power. In accordance with their investigation, institution building tends to be more effective in less developed countries in combating corruption while stricter enforcement is predicted to be more effective in developed countries.

In their paper, Broadman and Recanatini (2000) explored the relative roles of different market institutions in corruption with an empirical study. As indicated by the investigation, entry barriers, an effective legal system, and well-developed and competitive infrastructure service providers play significant roles in curtailing corruption. In other words, well-established market institutions with clear and transparent rules and healthy environment reduce the incentives



for corruption. They suggested that in order to reduce the incentives for corruption, policy makers should pay an utmost attention on reforms that foster building and development of effective market institutions.

In 2000, economic and social consequences of corruption are determined for transition countries in the study, *"Anti-Corruption in Transition: A Contribution to the Policy Debate"*, prepared by the WB. It defines the origins of corruption in transition countries as institutional legacies, economic legacies, transition paths, the redistribution of assets, and the role of foreign investment and assistance. Subsequently, the consequences of corruption are derived from experiences of transition countries such as lowering investment and growth, increases in poverty and inequality, erosion of the quality of public services, and lower credibility of the state. In the end, they suggested several approaches to combat corruption and provide a guideline to design anti-corruption strategies. This volume is the first study that examines the economic, political, and historical factors underlying the persistence of corruption in transition countries and contributes to the policy debate on developing practical strategies for combating corruption.

Hodess (2004) addressed problems of the regulation of political finance; the disclosure of money flows in politics and the enforcement of political finance laws, and vote buying in the context of political corruption. He highlighted that political corruption is an obstacle to transparency in public life. As his conclusion, in transition and developing countries, "...political corruption threatens the very viability of democracy, as it makes the newer institutions of democracy vulnerable (Hodess, 2004: 11)".

In order to identify problems and examine outcomes, fighting against corruption requires measurement of corruption itself. Kaufmann et al. (2005) addressed main issues of measuring corruption in the form of seven myths and their realities. In accordance with the study, corruption can be measured by gathering the informed views of relevant stakeholder, by tracking countries' institutional features, and by careful audits of specific projects. Furthermore, corruption can be measured at the aggregate and disaggregate levels. The main recommendation of the work is that to use a wide variety of different measures of corruption will improve reliance on it since any individual approaches has imperfections.

Fritz (2005) examined democratization and corruption issue in Mongolia. He determined the sources of corruption based on the World Governance Survey in Mongolia and underlined the anti-corruption efforts. According to his examination, in order to fight against corruption, important steps are first, to

give more attention on the implementation of formal rules<sup>1</sup>, second, to increase an access to reliable information, and third, to strengthen civil society. As his conclusion, while Mongolia has challenged in basic democratic structures, corruption now becomes a serious problem due to institutional and capacity constraints.

Anderson and Gray (2006) examined trends in corruption in transition countries over the years of 2002-2005 and influencing factors on those trends based on the findings of cross-country surveys of enterprises conducted by the WB and the European Bank for Reconstruction and Development (EBRD). The survey data shows that the firms, which are new, private, and domestically owned, pay more in bribery than that owned by foreigners. Throughout the paper, they accentuated the importance of efficient economic policies and institutions in controlling of corruption. Along with the analysis, broad indicators of corruption by international organizations have declined in these years, and the trend is continuing. They concluded that the success in reduction of corruption strongly related to the appropriate design and determined implementation of reforms in policies and institutions. Since it is a study based on the enterprises' survey, this represents only a perspective on the state capture by firms in those countries.

## Part II. Theoretical Underpinnings

### Definition for corruption

Generally, corruption is defined as the "abuse of public office for private gain (Kaufmann, 2005: 82)". It is a form of behavior that deviates from ethics, morality, tradition, and law. Here are several other common definitions provided by international organizations or on global documents in which<sup>2</sup>:

- Corruption is behavior on the part of officials in the public sector, whether politicians or civil servants, in whom they improperly and unlawfully enrich themselves, or those close to them, by the misuse of the public power entrusted to them. This would include embezzlement of funds, theft of corporate or public property as well as corrupt practices such as bribery, extortion or influence peddling.

#### *Transparency International (TI) (TI, 1996: 1)*

- ...corruption is an abuse of (public) power for private gain that hampers the public interest. ...corrupt entails a confusion of the private with the public sphere or an illicit exchange between the two spheres. In essence, corrupt

<sup>1</sup> Rules for preventing and dealing with corruption are widely regarded as inadequate and not implemented as well while Anti-Corruption Law was adopted in 1996 and a national program to fight corruption was adopted by parliament in July 2002.

<sup>2</sup> Source: <http://www.anticorruption.info>



practices involve public officials acting in the best interest of private concerns (their own or those of others) regardless of, or against, the public interest.

*United Nations (UN) Manual on Anti-Corruption Policy, (UN, 2001: 7)*

- Corruption involves behavior on the part of officials in the public and private sectors, in which they improperly and unlawfully enrich themselves and/or those close to them, or induce others to do so, by misusing the position in which they are placed.

*The role of the World Bank, (WB, 1997: 8)*

- The promise, offering or giving to a public official, directly or indirectly, of an undue advantage, for the official himself or herself or another person or entity, in order that the official act or refrain from acting in the exercise of his or her official duties;

The solicitation or acceptance by a public official, directly or indirectly, of an undue advantage, for the official himself or herself or another person or entity, in order that the official act or refrain from acting in the exercise of his or her official duties.

*Article 8 of the Convention against Transnational Organized Crime (UN, 2000: 6)*

- In broad terms, corruption is the abuse of public office for private gain. It encompasses unilateral abuses by government officials such as embezzlement and nepotism, as well as abuses linking public and private actors such as bribery, extortion, influence peddling, and fraud. Corruption arises in both political and bureaucratic offices and can be petty or grand, organized or unorganized.

*A Handbook on Fighting Corruption by the Centre for Democracy and Governance (USAID, 1999: 5)*

- Corruption is principally a governance issue – a failure of institutions and a lack of capacity to manage society by means of a framework of social, judicial, political and economic checks and balances... From an institutional perspective, corruption arises when public official have wide authority, little accountability and perverse incentives, or when their accountability responds to informal rather than formal forms of regulation...

*Anti-Corruption: Practice Note (UNDP, 2004: 2)*

#### Types and classifications of corruption

There are many types of corruption. It encompasses bribery, fraud, extortion, embezzlement, and nepotism. According to the *"Handbook on Fighting*

*Corruption"*, criminal activities such as drug trafficking, money laundering, identity theft, white-collar crime, and prostitution are also considered as forms of corruption.

**Bribery:** an offer of money or favors such as inside information, gifts, entertainment, a job, a company shares etc. to influence a public official. It may be given to a public servant (directly), or to another person or entity (indirectly).

**Fraud:** a criminal deception to obtain a benefit or gain unjust advantage. Basically, it means cheating the government or public organizations through deceit.

**Extortion:** Unlawfully and intentionally gaining some advantage from another person or entity by placing illegitimate pressure. This coercion can be under the threat of physical harm, violence or restraint and may even be a threat that a third party will suffer injury.

**Embezzlement:** Theft of money or other property entrusted with authority and control over these valuable resources.

**Nepotism:** The provision of services or resources, or favoritism shown by public officials to relatives, party affiliation, tribe, sect, and other preferential groups.

Furthermore, there are several classifications of corruption: Administrative and Political corruption, Grand and Petty corruption, and Organized and Disorganized corruption.

**Administrative Corruption:** Corruption by individuals, groups or firms in the private sector to influence the implementation of laws and regulations. Some sources called it as business corruption<sup>3</sup> or bureaucratic corruption (USAID, 1999: 5).

**Political Corruption:** Corruption that influences the formulation or content of laws, regulations, and policies. The other source underlines that this type of corruption usually associated with the electoral process<sup>4</sup>.

**Petty Corruption:** Practiced on a smaller scale. This involves relatively smaller amounts of money and typically more junior officials. Petty corruption is defined as the use of public office for private benefit in the course of delivering a public service. The direct victim of this abuse of power is the citizen.

**Grand Corruption:** The most dangerous and covert type of corruption. It involves substantial amounts of money and usually high-level officials. Grand corruption is considered to be seriously since policy making, its design and implementation are compromised by corrupt practices. It occurs at financial, political and administrative centers of power or at elite level.

<sup>3</sup> [http://www.anticorruption.info/types\\_class.htm](http://www.anticorruption.info/types_class.htm). Business corruption determined here is somewhat similar to administrative corruption. They claim that this type of corruption is often not regarded as a crime, rather as a means to accelerate business processes.

<sup>4</sup> [http://www.anticorruption.info/types\\_class.htm](http://www.anticorruption.info/types_class.htm)



Corruption is also classified as organized or systematic corruption and disorganized or chaotic corruption.

**Organized corruption:** A well-organized or hierarchical system in which there are clear idea of whom to bribe, how much should be offered, and confidence that they will receive the desired property or service in return.

**Chaotic corruption:** A disorganized or independent system where there is no clarity regarding whom to bribe and how much payment should be offered. In this case, there exists uncertainty or no guarantee that the favor will be delivered and no coordination between the recipients of benefits, with the result.

However, all these distinctions have no value since there is no form of corruption is better or worse than another.

#### Causes of corruption

In recent years, many studies have presented causes and consequences of corruption conceptually and empirically. Responding to the obstacles to the development posed by corruption requires an understanding of its causes. As investigated in the literature review, causes and costs of corruption are broadly defined by Mauro (1997), Gray and Kaufmann (1998), Broadman and Recanatini (2000), and especially by the WB for transition countries in 2000. I summarized causes of corruption on account of these works as follows:

**Government intervention** – it comprises trade restrictions, government subsidies, licenses for specific activities and for certain properties, price controls etc.

**Incentives for economic gain** – that refer to natural resource endowments, redistribution of assets (privatization), monopoly rents, monetary benefits (for example, tax evasion), and low wages in the civil service,

**The role of Foreign Direct Investment and Assistance** – that would be considered as a problem mostly for developing countries and for transition countries as well.

One specific cause particularly for transition countries is that

**Transition path** – this involves weak political accountability, progress of political and economic reforms, low level of transparency, limited civil participation etc.

#### Consequences of corruption

Corruption is one of the key development challenges for less developed countries and for transition countries as well (UNDP, 2006: 65). It poses serious consequences on the economy and society. I combined consequences of corruption in three areas – economic, social, and institutional – on the basis of literature review as following:

#### **Economic costs** – that embrace

- low level of investment further retards economic growth through increase in transaction costs and uncertainty, and distortion in sectoral priorities and technology choices,
- adverse fiscal consequences by reduction in tax collection through tax evasion and raise in government expenditure or distortion in the composition of government expenditure,
- loss of productivity with regard to misallocation of talent for rent-seeking activities,
- ineffectiveness of aid flows through the diversion of funds, for example, aid may help support unproductive and wasteful government expenditures or may be allocated to ineffective or redundant sectors of the economy,
- low quality of infrastructure and public services by reducing or delaying funding,
- increase in underground economic activity (informal sector).

#### **Social costs** – that encompass

- growing poverty level for the reason that corruption undermines social safety nets and reduces the quality of public services that poor suffers more,
- expansion in inequality with high levels corruption and state capture (it diverts resources from the poor to the rich, raising the Gini coefficient (Husein, 1999: 11)), for example, bribes paid by small enterprises in their annual revenue is greater than that do by large firms<sup>5</sup>.

#### **Institutional consequences** – that involve

- destruction in the state's legitimacy with insecure property and contract rights,
- erosion of trust in the state institutions or reduction in credibility of the government,
- suspension in democracy by distorting electoral process, altering the rule of

<sup>5</sup> From the data compiled by BEEPS



law, and creating bureaucratic predicament as a consequence of these political instability will rise.

### Part III. Analysis of Corruption in Mongolia

Corruption is not easy to measure since those engaged in corruption intend to conceal it. However, as stated in Kaufmann et al. (2005), it can be measured by gathering the informed views of relevant stakeholders, by tracking countries' institutional features, and by careful audits of specific projects. Furthermore, corruption can be measured in aggregate and also disaggregate levels. With an increasing attention from the government of Mongolia, international organizations, and public, several studies and surveys have been conducted in Mongolia in order to measure it. In this section, I will examine corruption in Mongolia based on international perceptions and related surveys carried out by international organizations and domestic institutes as well. Furthermore, I will review here anti-corruption efforts by the government of Mongolia and civil society.

#### International perception

More than a decade into a simultaneous political and economic transition, Mongolia has been engaged in a process of defining the basic rules and institutions to govern the market economy and society. During the transition period, Mongolia has made notable progresses in democracy, private sector development, and civil liberty. Nonetheless, Mongolia, like other transition countries, is experiencing problems of poor governance; including apparently rising levels of corruption.

Two major international indices for corruption are provided by the TI<sup>6</sup> and the WB. In this section, I investigated international perception for corruption in Mongolia by comparing indices with that for several countries that have received same rankings or have same transition characteristics. I also compared indicators of democracy, dimensions of governance, and per capita income of selected countries.

According to the Corruption Perception Index (CPI)<sup>7</sup> by the TI, Mongolia is ranked 99 out of 163 countries in 2006 in which the score is 2.8 same as that for Dominican Republic, Georgia, Mozambique, and Ukraine. The new ranking showed that Mongolia slipped down by 14 places from its 2005 ranking of 85 where the score was 3.0 which were same for Dominican Republic and Romania. Table 1 shows several measures of democracy, political

<sup>6</sup> Transparency International is the global civil society organization leading in a fight against corruption.

<sup>7</sup> The CPI is a composite index, making use of surveys of business people and assessments by country analysts. The score ranges between 10 (highly clean) and 0 (highly corrupt).

liberalization, and corruption, comparing indices for Mongolia and those for selected countries.

Table III.1 Indices of Polity, Freedom, and Corruption for selected countries

Countries	Polity IV, 2003		Index of Economic Freedom, 2006			Freedom in the World, 2006			Global Corruption Report			
	Polity Index	Political Regime	Score	Rank	Category	Civil Liberty	Political Right	Status	CPI, 2005	Ranking, 2005	CPI, 2006	Ranking, 2006
Mongolia	10	Full Democracy	2.83	60	Mostly free	2	2	Free	3.0	85	2.8	99
Dominican Republic	8	Partial Democracy	3.39	116	Mostly Unfree	2	2	Free	3.0	85	2.8	99
Georgia	5	Partial Democracy	2.98	68	Mostly free	3	3*	Partly free	2.3	130	2.8	99
Mozambique	6	Partial Democracy	3.35	113	Mostly Unfree	3	4	Partly free	2.8	97	2.8	99
Ukraine	7	Partial Democracy	3.24	99	Mostly Unfree	3*	2*	Free	2.6	107	2.8	99
Romania <sup>8</sup>	8	Partial Democracy	3.19	92	Mostly Unfree	2*	2	Free	3.0	85	3.1	84
Hungary <sup>9</sup>	10	Full Democracy	2.44	40	Mostly Free	1	1	Free	5.0	40	5.2	41
Slovenia <sup>10</sup>	10	Full Democracy	2.41	38	Mostly Free	1	1	Free	6.1	31	6.4	28
Russia <sup>11</sup>	7	Partial Democracy	3.50	122	Mostly Unfree	6	5	Not free	2.4	126	2.5	121
Uzbekistan <sup>12</sup>	-9	Autocracy	3.91	144	Mostly Unfree	7	7*	Not free	2.2	137	2.1	151
Kazakhstan <sup>13</sup>	-6	Autocracy	3.35	113	Mostly Unfree	6	5	Not free	2.6	107	2.6	111

#### Sources:

Column 1: Polity Index (Polity IV), based on a scale of -10 to 10, strongly autocratic to strongly democratic

Column 2: Regime Type Assessment, based on Polity IV score

Column 3-5: Index of Economic Freedom and rankings, Heritage Foundation. Its scaling is 1 to 5 which is free to repressed

Column 6: Civil Liberties Index, Freedom House. Scale is 1 to 7, most to least civil liberties

Column 7: Political Rights Index, Freedom House. Scale is 1 to 7, most to least political rights

Column 8: Assessment of Freedom, based on combined political rights and civil liberties, Freedom House

Column 9-12: Corruption Perception Index and rankings, TI. Scale for CPI is 0 to 10, high to low corruption

<sup>8</sup> As classification by Freedom House, one of the Balkans countries which are prospective reformers

<sup>9</sup> Hungary is selected from new EU members that are considered as most prominent and successful reformers among transition countries in order to compare performance of Mongolia with that of successful reformer

<sup>10</sup> Same as for Hungary

<sup>11</sup> According to WB publication on ACT, Russia is considered as a problematic country in transition process and as well as in institutional development which is most prominent response to corruption.

<sup>12</sup> Uzbekistan has a completely opposed political regime compared to that of Mongolia while they are same transition countries and most often compared.

<sup>13</sup> Same as for Uzbekistan



From the table, for two countries, Dominican Republic and Mozambique, that received same ranking of 99 on the CPI in 2006, the rankings were worsened whilst for the other two, Georgia and Ukraine, it was improved. Georgia and Ukraine, transition countries, received the ranking of 99 through improvement in their rankings and scores as well but Mongolia ranked in 99 by worsening its score in 2005-2006.

In 2006, Romania's ranking on the CPI increased by one place, at the same time that for Mongolia declined significantly, though their rankings were identical in previous year.

While the corruption score of Mongolia is relatively low compared to that of Russia with significant natural resources and Uzbekistan and Kazakhstan, Central Asian countries, to which Mongolia is most often compared, the difference is not too much in which only 0.1 to 0.3 percentage points.

For Polity Index, Mongolia is a full democratic country similar to Hungary and Slovenia, the leading reformers. But corruption index is much better for those countries than that for Mongolia. In contrast, rankings of Uzbekistan and Kazakhstan in 2006 with autocratic political regime are far from that for Hungary and Slovenia, full democratic countries.

Moreover, Mongolia is regarded as a mostly free country in accordance with economic freedom (similar Georgia, Hungary and Slovenia), and is considered as a respectful country for political rights and civil liberty (like Dominican Republic, Hungary, Romania, Slovenia, and Ukraine). Among the countries with better economic freedom, Mongolia and Georgia have same rankings on the CPI whereas Hungary and Slovenia get much better perception. The countries that considered not free in terms of political and civil rights have received low scores on the CPI compared to other countries that considered free or partly free. Russia, Uzbekistan, and Kazakhstan are included in this area.

The other indicator measuring corruption is Control of Corruption (CC), one of dimensions of governance indicator<sup>14</sup> provided by the WB since 1996. I displayed here indices of dimensions of governance and GDP per capita for selected countries used in previous comparison. Mongolia's score on CC fell down from 0.41 to -0.55 in ten years, and this places Mongolia in the 40<sup>th</sup> percentile among all countries in 2005, down from the 60<sup>th</sup> percentile in 1996. Corruption worsened for all selected countries at different levels over the period of 1996-2005 along with the index, except a significant improvement in Georgia and little progresses in Russia and Ukraine. Especially, for Mongolia,

<sup>14</sup> These are aggregate indicators developed by Kaufmann, Kraay, and Zoido-Lobaton first in 1996. They are issued on annual basis since 2002 covering 213 countries and drawn from 31 separate databases constructed by 25 organizations.

the decline in index is the highest, which is 0.96 percentage points, among those countries.

From the table, Mongolia received lower scores in terms of government effectiveness, regulatory quality, the rule of law, and control of corruption in comparison with voice and accountability and political stability. Among those the score on control of corruption is the worst one. The score on CC of Mongolia is close to that of Georgia while Mongolia has almost half of GDP per capita in comparison with Georgia. It shows that even as per capita income is very different, corruption is same prevalent in those countries. Other scores on dimensions of governance of Georgia are much worse than that of Mongolia.

Mongolia is considered as a politically stable country with regard to the highest score on political stability among selected countries, except Slovenia. This means that Mongolia is a country out of domestic violence and terrorism. Unfortunately, control of corruption in Mongolia is much worse compared to Slovenia.

Table III.2 Dimensions of Governance and GDP per capita for selected countries

Countries	World Bank Governance Survey, 2005								GDP per capita,	
	Control of Corruption			Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Atlas method (US dollars)	PPP (international)
	Score, 2005	Score, 2004	Score, 1996							
Mongolia	-0.55	-0.52	0.41	0.36	0.92	-0.35	-0.32	-0.26	690	2190
Dominican Republic	-0.66	-0.53	-0.34	0.20	0.05	-0.41	-0.27	-0.66	2370	7150
Georgia	-0.57	-0.88	-1.12	-0.27	-0.80	-0.47	-0.54	-0.82	1350	3270
Mozambique	-0.68	-0.81	-0.54	-0.06	0.04	-0.34	-0.60	-0.72	310	1270
Ukraine	-0.63	-0.96	-0.79	-0.26	-0.39	-0.42	-0.26	-0.60	1520	6720
Romania	-0.23	-0.29	-0.18	0.36	0.03	-0.03	0.17	-0.29	3830	8940
Hungary	0.63	0.63	0.70	1.10	0.79	0.79	1.11	0.70	10030	16940
Slovenia	0.88	1.00	1.15	1.08	0.94	0.99	0.86	0.79	17350	22160
Russia	-0.74	-0.71	-0.78	-0.85	-1.07	-0.45	-0.29	-0.84	4460	10640
Kazakhstan	-0.94	-1.16	-0.90	-1.19	0.03	-0.71	-0.47	-0.79	2930	7730
Uzbekistan	-1.07	-1.16	-1.05	-1.76	-1.91	-1.20	-1.71	-1.31	510	2020

Sources:

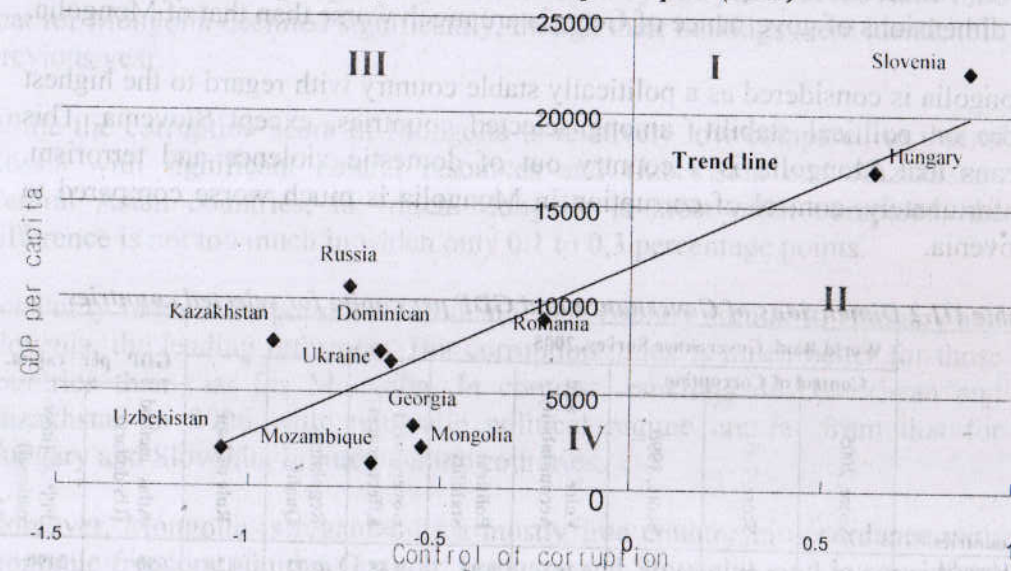
Column 1-9: Governance dimensions, Kaufmann, Kraay, and Mastruzzi, 2005. The score is ranking from -2.5 to 2.5, poor to good.

Column 10-11: GDP per capita in different methodologies, World Development Indicators



Among the selected countries, Hungary and Slovenia (leading reformers in terms of economic and also institutional transition) have controlled corruption in somewhat level since their scores are the best. In addition, per capita GDP in those countries are the highest amongst chosen countries. Following figure shows that the relationship between the index of control of corruption and per capita GDP in these countries.

**Figure III.1 Control of corruption and GDP per capita (PPP)**



From a trend line in the figure, per capita GDP increases with regard to an improvement in control of corruption. This is consistent with the main results or conclusions of theoretical and empirical studies discussed before. Along with y axis and the trend line, I divided an area into four sections.

Only Slovenia from selected countries falls in a first section with a high income and good control of corruption. Hungary drops in the second section in which corruption is controlled well whereas with a lower income. Most of selected countries drop in third and fourth sections that are with a high income though corruption is weakly controlled and with a low income and a poor control of corruption respectively. Particularly, Mongolia falls in a worst section with Georgia, Romania, and Mozambique and also deviation from the trend line for Mongolia is a highest in this area. It shows that corruption should be considered seriously in Mongolia.

#### Types, causes, and consequences of corruption in Mongolia

As mentioned before, several surveys have been conducted in order to determine types, origins, and costs of corruption in Mongolia in recent years. The following sentences adopted from survey reports show that corruption

became a prevalent phenomenon that consequently hinders country's development and damages democratic values.

"Corruption became reality in Mongolia and causes great damage to the development of the country, to democratic values, and to reform process" (Zorig Foundation (ZF), 2002: 1),

"Corruption is increasingly prevalent in Mongolia and the stakes are getting larger as economic growth makes more resources available" (USAID, 2005: 2),

"...corruption has become widespread phenomenon, which embraces every sphere of Mongolian society..." (Mongolian Chamber of Commerce and Industry, 2000: 22),

"Many recent governance concerns, including corruption, are associated with recent quick growth and the opportunities it offers for misuse of the governance structure." (ADB, 2005: 5), and

"The most crucial issues Mongolia is facing now are unemployment, corruption and poverty, said 75% of respondents of a survey made by the AF and Sant Maral center" (Open Society Forum news, 2006)

I hereby combine results of six surveys conducted in Mongolia between 1999 and 2005 in terms of types, causes, and consequences of corruption. Then, a list of most corrupted institutions of Mongolia is derived by collaborating results of these surveys.

From findings of these surveys, corruption became a major problem in business sector and at household level as well. For example, 31.5% of respondents of a business sector survey responded that the most leading factor embedding the creation of a sound business environment is corruption whereas 31.1% thought poor administration and 27.7% considered financial constraints. Corruption is cited as a second principal problem affecting Mongolia after unemployment and ahead of poverty in a household level survey. The other surveys conducted by international organizations also pointed out cautiously that corruption is on the increase in Mongolia. Especially political or "grand" level corruption should be concerned critically since it influences the formulation or content of laws, regulations, and policies.

Causes of corruption in Mongolia are classified into four areas that defined in the theoretical part of the paper as following:

#### Government intervention

- Licenses for mineral exploration – Currently, the government of Mongolia has imposed licenses for exploration and mining of mineral resources.



- Land privatization and permission for construction land – Especially, to get a permission in a business district and residential area is most difficult.
- Import, excise, and income (corporate) taxes – The government of Mongolia has imposed 5 percent tax for all import goods, and up to 80 percent excise tax on specific products such as alcohol, beer, car, and gasoline etc. Corporate tax has two levels: 10 percent (up to 400 million tugrik which almost equals US\$400000) and 30 percent (over 400 million tugrik). Value added tax is equal to 15 percent of value of imported and traded goods. However, it is not too high compared to other transition countries, for example, in Bulgaria-20%, Romania-19%, Poland 22%, Russia-18% etc.

#### *Incentives for economic gain*

- Natural resource endowments – Mongolia has over 6000 mineral deposits of 80 different minerals have been discovered. Only 160 of the 400 deposits that surveyed in detail have been developed or for production, or are now being developed. Thus, the remaining 240 deposits are might be considered as incentives for economic gain for administrators or government staffs.
- Tax evasion – It occurs mostly in business sector. Moreover, individuals who import goods are also attempting to avoid taxes. Main problem here is that people have seen that tax evasion as a source to generate an extra income. Also, there is no efficient institutional mechanism to investigate tax evasion.
- Redistribution of assets – While most of small and medium enterprises were privatized by voucher privatization, privatization of high-valued properties such as state-owned banks, big enterprises, airline and railway companies etc. are still not privatized. Public think that somebody's (politicians or businessmen) influence exists in delaying privatization.
- Low wages in the civil service – In quantitatively, an average wage of government officials is less than 50 percent of an average wage in private sector. I think that it is one of major causes of bureaucratic corruption in administration and public service sectors such as local administration, hospitals, educational organizations etc.

#### *The role of FDI and Assistance*

- Misappropriation of foreign aid – Like other developing and transition countries, Mongolia has received a significant amount of money from international organizations and donor countries for investment in

infrastructure, poverty reduction, and solving other socio-economic problems. However, inadequate quality of investment and unavailability of information about the usage and distribution of assistance money to the public are common phenomena in Mongolia. The government of Mongolia is still not accountable for reporting this kind of information to the public.

#### *Transition path*

Transition path is a most significant cause of corruption in Mongolia with regard to a large scale institutional and economic changes have created a massive opportunities for rent-seeking activities. Misunderstandings of newly established governance structure, free-rider problems related to state properties, imperfections in institution building, and weak enforcement of law are common features in transition countries, and Mongolia as well. Hence, I investigate following interrelated institutional and ethical causes of corruption.

- Weak political accountability
- Lack of access to information
- Lack of transparency
- Limited public participation
- Imperfect law and weak enforcement
- No political will to combat corruption
- Unprofessional bureaucracy caused by politicization in administration
- Unfair judicial system

Amongst these causes, I think that unfair judicial system, imperfect law and weak law enforcement, and no political will to combat corruption are roots of flourishing corruption in Mongolia. Protection of property rights and contract enforcement are inadequate and not implemented at all due to deficiencies and contradictions in laws and unfair judicial system. In Mongolia, contract enforcement through judiciary system takes on average 314 days with 26 stages by spending 22.6% of contract value. For example, case studies show that people who have not relatives or friends in judicial system have started to hire "gangsters" in order to enforce their contracts instead of appealing to judges. They said that this approach can save time and can solve problems regarding to contract enforcement without transaction cost. (Khashchuluun et al., 2006: 78).

Moreover, the other major cause is no political will to fight against corruption. A significant number of members of parliament and cabinet seem to view the holding of decision-making positions as a mean to access



state resources and power for private gain<sup>15</sup>. As a result, transparency and accountability are almost evaporating. In addition, the courts and the media are not free from political and economic pressures. Demands for investigation and justice from public are unattended due to lack of access to information. All these transitional problems affect on "flourishing" corruption in Mongolia.

The Table III.3a presents a list of most corrupted institutions in Mongolia. Here, I show that a percent of respondents who answered that a regarding institution is most corrupted in each survey except "Assessment of corruption in Mongolia" which is a secondary source analysis. In the table, x mark indicates institutions that underlined as most corrupted institutions in the study, "Assessment of corruption in Mongolia".

**Table III.3a Most corrupted institutions**

	Courts	Customs	Prosecutor office	Police	Tax office	Land authorities	Local administration
"Comparison of 1999 and 2002 Mongolian Public Perception Anti-Corruption Surveys" 2003	86.5 <sup>16</sup>	89	80.7	90.7		82.1	72.7
"Monitoring of the implementation of the Government's Anti-Corruption Program in Mongolia and the role of the Open Society in Fighting Corruption" 2004	79	79.1	76.9	70.9	67.6	66.8	63.6
"Assessment of Corruption in Mongolia" 2005	X <sup>17</sup>	X	X	X	-	X	X
"Mongolia Corruption Benchmarking Survey" March 2006	5.8	10.9		21.7	9.3		35.3
"Mongolia: Trends on Corruption Attitudes" September 2006	7	9.6		22.7	8.3		34.1

<sup>15</sup> After 2004 election, the number of businessmen in parliament was increased drastically from 10 percent to almost 50 percent.

<sup>16</sup> This shows that a percent of respondents who answered that a regarding institution is most corrupted.

<sup>17</sup> The study had not conducted a survey. It was done based on the secondary sources and interviews. Therefore I illustrate most corrupted institutions underlined in the study using x mark.

From the table, unfortunately, law enforcement organizations such as courts, prosecutor offices and police lead the list of most corrupted institutions. Instead of changing this situation corruption problem cannot be solved at all. Following, customs, tax offices, and land authorities are regarded as most corrupted. This outcome principally relates to causes that are government intervention in the economy and incentives of individuals or companies to generate extra monetary income by avoiding taxes.

The Table III.3b shows that political corruption which is considered to be most harmful to development and democracy is widespread in Mongolia. More than 60 percent of respondents, on average, think that political parties, ministries and government agencies, and parliament are most corrupted institutions. As aforementioned, this situation will affect negatively on economic development and democracy of a country by influencing a formulation and content of laws, regulations, and policies. Moreover, transparency and accountability will be worsened further since politicians and elites want to conceal their illegal or disagreeable activities. Increasing political corruption affects negatively on resource allocation since this type of corruption involves greater amounts of money. Furthermore, it sets the tone and example for administrative corruption.

**Table III.3b Most corrupted institutions (continues)**

	Political parties	Ministries and Government agencies	Parliament	Hospitals	Educational organizations	Banks
"Comparison of 1999 and 2002 Mongolian Public Perception Anti-Corruption Surveys" 2003	61.9	70.0	67.1	87	83.2	78.2
"Monitoring of the implementation of the Government's Anti-Corruption Program in Mongolia and the role of the Open Society in Fighting Corruption" 2004	63.7	56.3	56.4	52.0	51.7	54.8
"Assessment of Corruption in Mongolia" 2005	X	X	X	-	-	X
"Mongolia Corruption Benchmarking Survey" March 2006				38.4	29.1	
"Mongolia: Trends on Corruption Attitudes" September 2006				37.6	39.3	

According to the household level surveys that are last two in the list, local administration, hospitals, and educational organizations are considered as most corrupted institutions. More than 30 percent of people paid for doctors,



teachers, and public officials among the people who encountered corruption cases during the survey period. I think this outcome is related to a characteristic that ordinary people more often communicate with these organizations rather than others.

To measure consequences or costs of corruption in quantitatively is difficult since the direct victims can not be determined and not only monetary costs also non-monetary costs should be counted. Even though, based on results of surveys in Mongolia, I investigated following consequences which are consistent with theory.

- Tax avoidance that reduces government revenue, consequently, adversely affects on implementations of policies with regard to reduction and distortion in government expenditure and reduces government effectiveness to solve other socio-economic problems.
- Loss of trust in the state that leads to weak enforcement of laws and regulations furthermore raises political instability.
- Soil for organized crime that would be a root of instability and life insecure
- Violation of basic human rights which are access to basic health service and education etc. Consequently, poverty and inequality will increase because of unequal public services. Moreover participating in decision-making process that affects one's life will become disparate due to distortion in electoral process.
- Increase in inequality and poverty since it generates monetary damage for all those engaged in corruption, especially for the poor.
- Low economic development caused by low level of investment due to an increase in transaction cost and uncertainty.
- Deterioration in democracy initiated by violation of human rights, distortion in electoral process, and alteration of the rule of law etc

#### Anti-corruption efforts

The government of Mongolia started anti-corruption actions by approving a first "Anti-corruption law" in 1996. However, this law was not implemented at all due to its imperfection and no political will to enforce it.

In July 2002, the government of Mongolia passed the National Program for Combating Corruption (NPCC). The program calls for a two-phase implementation. The first phase ended on July 1, 2005 and focused mainly on awareness raising. With support by international organizations, Mongolia has achieved some short-term goals of the first phase, particularly, in the area of accelerating public administration reforms. For example, the law on management and finance of public sector was passed by the parliament in 2004. Implementation of a legal and policy framework remains the greatest challenge for the government of Mongolia. A second phase, from 2006 to 2010, is

running now. However, the program has some shortcomings. It should be revised to ensure that it incorporates the provisions of international conventions that Mongolia agreed to implement.

The government of Mongolia ratified the United Nations Convention against Corruption (UNCAC) in October 2005 that is an important step forward in creating legal environment and institutional arrangement to prevent and combat corruption. The UNCAC calls for numerous initiatives that require adapting Mongolian legislation to the requirements of the convention and strengthening control mechanisms.

On July 6, 2006, the government of Mongolia approved the "Anti-corruption law", which came into force on November 1. The law calls for the proposed independent anti-corruption body to embark on a three-pronged approach to combat against corruption which are a) implementing government-wide policies and procedures to prevent corruption, b) investigating and prosecuting acts of corruption when they occur, and c) engaging in activities to educate the citizens and public officials in order to prevent corruption.

In December 2006, a parliament of Mongolia approved a director of new anti-corruption body through an appointment by a president. The formation of new anti-corruption body is a significant step in fighting corruption though it is early to say about activities of this organization. Moreover, 77 percent of respondents of the survey on public perception anti-corruption in Mongolia held the opinion that it is necessary to set up an independent agency to combat corruption.

Civil society initiatives in a field of combating against corruption are increasing in recent years. Approximately fifty civil society organizations are pushing the issue and most of them are located in Ulaanbaatar. They are involved in transparency, accountability, access to information issues, electoral and judicial reforms, and other topics directly related to fighting corruption. Here is a list of civil society organizations that are working actively in this field by conducting surveys and implementing educational programs to the citizens and public officials.

- Globe international – works in an area of freedom of information, media for transparent governance and enhancing participation of the poorest
- The Liberty Center – is acting in field of training administrative courts, raising awareness on how to contest the government.
- The Open Society Forum – works to support active engagement of citizens and civil society in civic life, facilitate broad public access to policy relevant information resources, and encourage improved policy research and analysis.



- Sant Maral – is a board member of TI-chapter in formation. Therefore, it is a main corruption survey institution in the country. This organization conducted surveys on “Public perception of the judicial system in Mongolia” in 2001, 2003, and 2005 and “Trends in corruption attitudes” in collaboration with AF in 2006.
- The Zorig Foundation – has been working to spread democratic values, to strengthen human rights, freedom and social justice, to respect and promote pluralism, and to improve the system of transparency and accountability of the state and government to the public. The foundation conducted a survey under a project on “Monitoring of the implementation of the Government’s Anti-Corruption Program in Mongolia and the role of the Open Society in Fighting Corruption” in 2002.

### Conclusion

This paper focused on deriving a current situation of corruption in Mongolia in terms of types, causes, and consequences of it. Both international perceptions and survey results show that corruption is on the increase in Mongolia, and point out that political (or elite) corruption, which comprises greater amount of money and harms economic growth and democratic values, should be concerned more seriously. Moreover, since law enforcement organizations such as courts, police, and prosecutor offices are involved in corruption severely, laws, regulations, and contracts cannot be implemented properly at all and the property right seems to be not protected. The new anti-corruption law still can not influence on the current situation without resolving those problem initially. While generally government intervention, natural resource endowments, privatization, and low wages in the civil service sector are origins of corruption, the lack of a transparent and accountable political system, no political will to combat corruption, lack of access to information, and unfair judicial system create a fertile ground for both political and bureaucratic corruption in Mongolia.

There are some successes in freedom and political regime. However, these achievements in democracy might be intimidated from a wide spread of corruption at both elite and administrative levels. Whilst the government of Mongolia has attempted to combat corruption, the achievements and results are not adequate due to lack of transparency and accountability in administrative level. Civil society organizations should play a more active and strong role in fighting corruption by enhancing citizen’s participation, improving access to information, and raising awareness against corruption. Finally, to change or

affect morals or ethics of the citizens and public officials would be most effective way to prevent corruption since an average Mongolian believes that

they cannot receive desired or entitled services or outcomes without paying bribes to relevant officials. In addition, to raise political will to combat corruption is a most vital condition in fighting corruption in Mongolia.

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