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Causes of Demand for International Bribery

Edwin C. Moore Jr

Abstract

Corruption and bribery are not new to business. Bribes have been paid throughout recorded history. A large part of corruption includes bribe giving. Bribe giving, in the context of this paper, entails the payment giving or promising something of value to a government official to give favorable preference to the bribe giver. Although there has been some debate concerning whether or not bribery causes an economic drag on the economies of nations most evidence supports the contention that it is an economic drag. Bribery requires two parties the giver of the bribe, supply, and the receiver of the bribe, demand. Legislation and international agreements are designed to curb bribery are primarily directed at supply. The purpose of this paper is to identify, through a literature review, some of the demand determinates of bribery. From the literature four demand determinates have been identified; three are strong independent variables and one, political freedom, is less strong depending on its definition. The dimension of culture encompasses four components which were identified by Hofstede: Power distance, collectivism, masculinity, and uncertainty avoidance. The evidence indicates that to combat corruption and bribery all of the independent variables must be addressed. The most difficult variable to change is culture. A culture that supports bribery and corruption may continue to support bribery even if the economic and social variables are positively addressed. Since culture is imbedded and reinforced by a

culture that variable may take a long time to change. The findings suggest that since culture plays a large part, as a demand determinate of bribery, in the reduction of bribe taking a generic approach to reducing bribery may not be effective. A regional approach to studying the demand determinates of bribery may be more effective in identifying localized demand determinates and the most effective means to combat bribery on a regional scale.

Introduction

Corruption and bribery are not new to the world of business. Business people have been using gifts for many years to get favorable treatment from officials. In the early days of capitalism, when the Church saw profits as usury, a mortal sin, one man found a way around the problem. The first real European banker, Cosmo Medici, feared eternal damnation for his business activities. Medici had a meeting with the Pope and made a deal that the Pope agreed to. Medici would donate part of his fortune to the Church and in return he would be forgiven of the sin of usury (Means, 2001). During the Reign of Louis XVI in France, the class structure of the Ancien Régime allowed for massive corruption. In many ways the corruption in France was a prelude to the corruption in many developing nations today. Corruption slowed France's economic growth at a time when much of Europe was experiencing economic expansion. The structure of the Ancien Régime placed the decision power in the hands of a few. The few decision makers had little, if any, concern for the masses. Debt service accounted for 62% of collected tax revenue which was mostly paid by the people who could least afford it. Most tax revenue went directly to the various nobles and officials. In short, a few people exerted much power over the masses. Such concentrated power fueled corruption and stopped the economic growth of France (Kennedy, 2005). Today corruption tends to be most prevalent in undeveloped, developing, and transitional economies (Corruption Perception Index 2004, 2004).

A large part of corruption constitutes bribery. Corruption is an action of individuals or groups to take advantage of public office for private gain (Bahmani-Oskooee & Nasir, 2002). Economic corruption refers to a public official who views his/her office as a private business (Genaux, 2004). The supply of bribery would be the bribe giver, and the receiving party would create the demand side of the equation. The Foreign Corrupt Practices Act (FCPA) defines bribery as giving money or something of value to a government agent to do a favor for a brib-

er at the expense of the principle/principles (Goelzer, 1998). An agent would be a representative of the government, whether elected or appointed. The principles would be the people, residents, or beneficiaries of the government. The agent has the responsibility of acting in the best interest of the principles. A payment to the principles is not a bribe; only a payment directly to an agent is a bribe (James, Jr., 2002).

According to the FCPA, it is illegal for an officer, director, or agent of a United States company or a company traded on United States financial markets to offer, make a promise, or authorize any money, gift promise, or authorize giving anything of value to certain people or groups. These individuals or groups would be agents of foreign governments. In short the FCPA prohibits the payment of a bribe to any government official or political interest in order to influence their actions or influence (Goelzer, 1998). It is clear that the FCPA directs its attention toward the supply side of the bribery issue.

It appears from the literature, Heineman and Heiman (2006) and Sung (2005) much of the research carried out on bribery and corruption is directed at the demand-pull hypothesis; however, much action is directed at the supply-push hypothesis. One of the difficulties that occur when countries impose strict laws on domestic firms competing for business off shore is that it hurts a domestic firm's ability to compete. It is estimated that American companies have lost 400 major contracts due to bribers given by competitors to foreign government officials (Sung, 2005). The Organization for Economic Co-operation and Development (OECD) has developed guidelines to attack both sides of the equation. On the demand side the OECD suggests a strong ethical structure supported by an ethics infrastructure (Bertok, 1999). Although some research indicates a preference for focusing on the supply side of corruption, (Sung, 2005) such research is hampered by a very small data set. In the case of Sung's research there were only 19 countries with available data concerning the supply of bribes.

It appears that although national laws are effective, if enforced, in stopping bribery by domestic companies and employees, they pose two operational problems. The first problem is they cannot easily be forced on other countries to stop demand. And the second problem is national laws may impact the competitiveness of domestic companies in foreign markets that demand bribes. The question that this paper will attempt to answer, through a literature review, is: What are the causes of demand for bribery and what actions can be taken to reduce demand? The first section will discuss what bribery and corruption are and their negative effects on developing economies. The second section will be a literature review of the demand for bribery and the factors that cause demand for bribery to be present in an economy. The third section will discuss some possible solutions to reduce the demand for bribes within a political/economic system.

Literature Review

Issues in Combating Corruption and Bribery

Since bribery and corruption take many forms the terms are often difficult to define or separate (Shahabuddin, 2002). For the purposes of this paper the definition previously discussed will be used. One difficulty that is encountered when discussing bribery is grease. Grease payments are accepted by the FCPA as an accepted practice to expedite a normal and routine governmental duty. The official routine duties include: issuing permits, issuing licenses, processing paperwork, mail service, scheduling inspections, providing utilities, or other routine actions within the scope of a government agent (Goelzer, 1998). Grease pay-

ment are small amounts of money, very similar to a tip, paid to low level government operative to facilitate or expedite the government operatives normal activities (Paini, Swingen, & Rodgers, 2002). Since a certain amount of grease is allowed by the FCPA and international conventions, only explicit bribery will be considered in this research.

Bribery may take two forms it can be either top down or bottom up. Top down corruption includes high level bribe taking in an attempt for high level government officials to gain high rewards and a portion is shared with underlings as hush money. Bottom up bribery is often called petty corruption and involves numerous small payments to low level employees who pass some of the gains to their superiors as rent (Waller & Gardner, 2002).

Corruption always has to do with power (Bliss & Di Tella, 1997). Power, at all levels, is the ability of one party to control the behavior of the other. Either the act of giving or withholding something of value to a dependant party can be used to control the behavior of the dependant party (Robbins, 2000). It would appear that power would exist in the hands of a bribe giver and a bribe taker. Therefore both those who supply and those who demand hold some level of power over the other. When viewed in the classical supply and demand curve of economics one could place the level of power on the vertical axis and the amount of the bribe on the horizontal axis and equilibrium, or the bribe amount, would occur at equilibrium, where supply equals demand.

By further developing the discussion in economic terms the only way to reduce the level of bribery is to reduce either the level of supply or demand or maybe both. The major assumption that will be made in this paper is that power is derived by social, political, economic, or cultural factors. A secondary assumption, shared by the OECD, is that corruption and bribery can be reduced by reducing both supply and demand (Bertok, 1999). The OECD's efforts to address the demand for corruption are based on an assumption of a systemic failure and management failures. The OECD is attempting to develop a public sector ethic of better legislative action, stronger public institutions, law enforcement, adequate controls, oversight, and transparency (Bertok, 1999). Many researchers see a more basic cause for demand. Some such as Husted (1999) and You and Khagram (2005) are concerned with wealth and income distribution as causes of demand for bribery. Husted (1999) also discusses the impacts of government size and Hofstede's four cultural variables as being sources of demand. Other authors, who will be introduced in the remainder of this paper used similar determinates and added to them. O'Higgins (2006) and Dell (2004) view extractive industries as being major causes of both supply and Demand for corruption and bribery. Others such as Sanyal and Samanta (2004) and Sanyal (2005) have researched the cultural and economic determinates of corruption and add economic freedom to the list.

Diagnosis and Treatments of Bribery

A recent article by Mungui-Pippidi (2006) discusses some very preliminary work in the diagnosis and treatment of corruption. The author proposes that government and laws cannot solve corruption within corrupt countries. The reason government cannot solve the problem is because by definition government is the problem. Mungui-Pippidi also raises the point that although corruption can be identified, each nation must be looked at from an individual perspective. Such a conclusion runs counter to the findings of Sung (2005) who found actions taken through laws to reduce bribery would be effective. It also becomes evident

that a diagnosis and cure for corruption must be made through qualitative as well as quantitative analysis (Mungui-Pippidi, 2006). The various factors that will be discussed as demand side determinates of bribery fit the criteria of concerns that are not just controlled by government but also are both quantitative and qualitative in nature. GDP and income levels as well as the GINI index are all quantitative. Other variables such as the level of economic freedom, and even the Corruption Perception Index (CPI) are qualitative.

Determinates of Demand Income inequality

The first specific determinate that has been identified is income inequity. Since power is a basic requirement for corruption and bribery (Bliss & Di Tella, 1997) power can be achieved from income inequalities. Economies can become trapped in a cycle of poverty and corruption. Government actions in themselves can be a determinate of general welfare. Government actions may also tend to support the policies preferred by the rich and often add to the decreasing welfare of the poor (Jong-song & Khagram, 2005). Some insight to the issue of income disparity and the willingness to take a bribe can be found in a 1989 study conducted by Goel and Rich. This study looked at the relationship the change of getting caught and punished for accepting a bribe, income disparity between the public and private sectors, and unemployment. The study was based on United States government employees at the federal, state, and local levels. What Goel and Rich found was that there was a relationship between lower income levels of government workers as compared to private sector employees and the willingness of public sector employees to accept a bribe (Goel & Rich, 1989). Although Goel and Rich used samples from the United States their work has supported on an international level.

A very broad study was conducted on international corruption by Brian Husted, Husted (1999). One of the variables Husted considered was the impact of changes in the GINI index as a predictor of corruption. To study this variable a simple hypothesis was proposed "The greater the inequality in the distribution of income, the higher the level of corruption in a country." The author used the GINI to measure income equality and the CPI to measure corruption. The findings were significant at the $P < .01$ confidence level that income inequalities were related to an increase in the level of corruption.

A more recent study on income inequity and corruption was published in February of 2005. This study done by You and Khagram (2005) was a comparative study of income inequality and corruption indexes from Transparency International, the World Bank, and Risk Services. The authors used the GINI Index to gauge the level of income disparities in the subject countries. The researchers used four test hypotheses. The three hypotheses that are relevant for this paper are: 1. greater income inequality is associated with higher levels of corruption, 2. perceptions of the extent and norms for acceptability of corruption are higher in more corrupt countries, 3. higher levels of corruption are associated with higher levels of inequality (You & Khagram, 2005).

What You and Khagram (2005) found built on Goel and Rich (1989). They found that corruption was directly correlated with income inequality. The research implied that corruption was related to income inequalities within nations. They also found support for the argument that corruption and income inequality would, in fact, lead to a general level of acceptance of corruption and the income inequality, and corruption would continue (You & Khagram, 2005).

Economic freedom

Closely linked to income inequality is Economic Freedom. As pointed out by You and Khagram (2005), there is an apparent link between poverty and corruption. There is also a linkage to economic freedom and corruption (Eiras, 2003). The level of economic freedom is composed of several factors that include: trade, monetary policy, wages and prices, government intervention, and the size of the informal economy (Nwabuzor, 2005). Economic freedom is often thwarted by government policies. These policies are directed toward the imposition of strict economic constraints. The economic constraints create a loss of economic freedom and allows for increased corruption. The increasing level of corruption damages the faith of the people in a government in which structures and economic capacities are eroded. The continued erosion may even threaten the legitimacy of the government itself (Nwabuzor, 2005).

Sanyal and Samanta (2004) suggested two propositions germane to the economic freedom and corruption. The first proposition was that economic factors that support market forces, limited government, good public finances, and rule based systems are less likely to foster corrupt practices. The second proposition was that changing economic policies that make the economy more open and less closed will cause a decline in bribe taking over time. The authors used two time periods 1996 and 2001 to study 54 countries. The CPI was used to measure corruption and the Economic Freedom Index (EFI), developed by the Heritage Foundation was used to measure economic freedom. Countries are ranked from 1-5 with one being the most free and five the least open. The results showed strong support for the stated propositions. High EFIs were strong indicators of low CPI scores. In other words reduced economic freedom will indicate higher levels of corruption and bribe taking (Sanyal & Samanta, 2004). What is interesting about this research is it limited itself to the demand side of bribery. From the study conducted by Sanyal and Samanta (2004), it appears there is evidence that economic freedom has an impact on the demand for bribes in developing countries.

Political freedom

From the prior discussion both income inequality and a lack of economic freedom have been shown as being potential sources for the demand for bribes. Evidence has also been presented that bribery can cause political instability. Researchers have compared the effects of political and economic freedom and corruption (Ali & Isse 2003; Goel & Nelson 2005). Although one may draw the conclusion that political freedom may affect the level of corruption that may not be the case. Ali and Isse (2003) supported the later findings of Sanyal and Samanta (2004) in that economic freedom was and indicator of corruption. They also found that political freedom had a negative correlation to corruption but it was not direct. What they found was that political freedom had an impact on economic freedom and economic freedom had a direct influence on corruption. A composite measure of political and economic freedom may be a better predictor of the level of corruption.

Goel and Nelson (2005) used a different definition of political freedom and used a more general measure of political freedom which included freedom of the press, freedom of religion, open opposition, free elections and other soft variables. The authors studied 63 nations some were very corrupt while others relatively uncorrupt. The study investigated the impacts of both economic and political freedom. What was found was that by

using a more general measure of political freedom there was an inverse relationship between both economic freedom and political freedom on corruption in a country. The findings of both studies would support the contention put forth that the form of government is not a sole indicator of corruption. Even a democratic nation can be very corrupt without proper institutions, laws, and enforcement (Mungui-Pippidi, 2006)

Additional research has added government size to the possible predictors of corruption. Government size, in this case, is government's share of the GDP (Husted, 1999). In this study a simple hypothesis was put forth: "The larger the government's share of GDP, the higher the level of corruption in the government". As is the case with most research reviewed the CPI was used to measure corruption. The size of government was determined by World Bank data. 36 countries were included in the sample. The findings were significant supporting the hypothesis that as government increased its share of GDP corruption would increase. This finding was significant at the level $P < .01$ (Husted, 1999). It would appear that government's effect on corruption would depend on how it is defined. It would also appear that the impact of government on corruption would be not direct but indirectly through its influence on other variables.

Cultural variables

Cultural variables are also considered as determinates of demand for corruption and Bribery (Beets, 2005; Husted, 1999; Park, 2003; Sanyal & Samanta, 2004). While Park, Husted, and Sanyal and Samanta used Hofstede's cultural dimensions, in whole or in part, Beets used economic and demographic indicators. Beets (2005) used 12 economic and demographic indicators for his cultural variables. What was found was that of the 12 only five were significant at the $P < .001$. The significant factors were: the percentage of the population living in rural areas, percentage of adults employed or seeking employment, household size, and life expectancy at birth, economic aid received. Low corruption levels were found with high employment, longer life expectancy, and lower fertility rates and High levels of aid donation indicated low levels of corruption while high levels of received aid indicated high levels of corruption.

Husted's wide ranging 1999 study also brought culture into the discussion. Previous a previous study of Nigerian and United States students found that culture did affect how students viewed acts of bribery and extortion (Tsalikis & Nwachukwu, 1991). What is interesting here is the authors compared citizens of a very corrupt nation, Nigeria, and a relatively uncorrupt nation, The United States. The CPI for Nigeria is 1.6 placing it third from the bottom of the national rankings as very corrupt. The United States, on the other hand, is 7.5 out of a possible 10 and placed at 17th place on the list published by Transparency International (Corruption Perception Index 2004, 2004). Husted's research used four of Hofstede's five cultural dimensions. The dimensions used were: power distance, individualism, collectivism, and masculinity-femininity Confucian dynamism was left out since it appears that attributes at both poles could simultaneously reduce and increase corrupt behaviors. Four hypotheses were introduced to see if there was a relationship of: power distance and corruption, more collectivism and corruption, greater masculinity and higher levels of corruption, and finally higher uncertainty avoidance would lead to more corruption (Husted, 1999).

Husted's research demonstrated that increased power distance, high masculinity, high uncertainty avoidance, and uncertainty avoidance would all be indicative of higher levels of corruption. The most corrupt nations would share all four char-

acteristics. The author implies in his conclusions that corruption will not end easily since a nation cannot command economic growth or change a culture by edict. It also indicates that culture is a strong predictor and cause of corruption (Husted, 1999).

Beginning in 2003 a series of articles considered the effect of culture on corruption levels in nations. The first was written in the fall of 2003. The research considered multiple determinants of corruption. Along with national income, income inequality, and several other variables culture was considered. As was the case with Husted (1999) this study utilized Hofstede's cultural dimensions and used the same four employed by Husted in 1999. As in Husted's research this research used 4 specific hypotheses: the higher the power distance the higher the corruption level would be in a country, the more collective a culture the higher the level of corruption in a country, the more masculine a culture is the higher the level of corruption in a country, finally the higher the degree of uncertainty avoidance in a culture the higher the level of corruption in that country. Data sources were the CPI for the level of corruption and Hofstede's cultural indices were used to measure cultural variables. Because data, across the research, was only available 37 countries the total sample was 37. The research confirmed Husted's 1999 finding that culture was a major factor in the corruption level in a country. In this case, however, the two strongest indicators were power distance and masculinity (Park, 2003).

Following Park, Sanyal and Samanta (2004a, 2004b) and Sanyal (2005) studied the causes of corruption. Just as in the previously discussed research several indices were identified including economic, political and cultural factors. The first paper concerned bribe giving countries and bribe taking countries. The only available data for bribe giving comes from Transparency International's Bribe Payers Index. The data for bribe taking comes from the CPI. Unfortunately the Bribe Payers index only covers 19 countries and most are developed economies. They found countries that were bribe givers were also inclined to be bribe takers. In addition they measured Hofstede's cultural variables against bribe giving and bribe taking levels and supported cultural factors as being determinates for bribery and corruption. Especially strong correlations were uncertainty avoidance and power distance (Sanyal & Samanta, 2004a).

Sanyal (2005) used a sample of 47 countries that were represented on the CPI and also had corresponding economic and cultural data available. This research used Hofstede's cultural variables of: power distance, individualism, masculinity, and uncertainty avoidance. The economic factors included: per capita income (PPP), amount of foreign trade, and income distribution. The findings showed significant cultural relationships to CPI appeared for power distance and masculinity. Economic relationships existed for per capita income and income distribution, or income equality or inequality.

Considerations in Reducing the Demand for Corruption

From the research presented thus far it would appear that both economic and cultural factors have a strong influence on the level of corruption in a country. Although many other sub-factors have been identified the general cultural and economic factors are well documented. The question now turns to what can be done to curb corruption. Assuming that laws made by government will not solve the problem since those who make the laws are often the beneficiaries of corruption (Bahmani-Oskooee & Nasir, 2002). It has been demonstrated that governments that have had a sustained growth rate are nations that encourage

honesty and discourage corruption (Ali & Isse, 2003). It has also been demonstrated that government may not be able solve the corruption problem in corrupt countries since, by definition, government is part of the problem (Mungui-Pippidi, 2006). Legal controls have a limit to their effectiveness since they must not only exist but they must also be investigated, prosecuted and the punishment must be carried out. Whether they are effective will depend on the political regime of a country (Bertok, 1999). Since it appears that, from the previously discussed literature, national laws may only be partially effective that leaves two alternatives. Alternative one is through the use of trade agreements and Non-Governmental Organizations (NGOs). Although they can create a platform for transparency and models for conduct they cannot control the activities of sovereign nations.

Forces enabling corruption

As pointed out in a recent article in *Foreign Affairs* (Heinemann & Heiman, 2006) four primary forces perpetuate corruption: money, greed, power, and institutional weakness. Along with enforcement and prevention two other elements must be included in an attempt to curb corruption. The first element is state building. State building, according to the authors includes institutions designed to create a society based on laws enabling an environment that allows for transparency, accountability, as well as a legal, economic, political foundation. The final piece of the equation is cultural change. That cultural change requires the development of norms and values that reinforce anti-corruption efforts. The pressure will need to come from below. The leaders have no reason to change unless their leadership is questioned and their power threatened.

Actions to Reduce the Demand for Corruption

The efforts to reduce corruption must come from the supply and demand side. Research has shown that there is equilibrium for corruption. Simply making corruption more costly will lower the level of corruption but will also make it more lucrative for those who engage in corrupt practices. What must be shifted to the left are both the supply and the demand for corruption. A shift in either curve must be a non-price shift. One common factor that will shift either curve is expectations. From the demand side, and that is the focus for the conclusion of this paper, it appears that economic conditions and cultural norms and beliefs must be changed. From an economic standpoint the biggest factor is economic freedom. From economic freedom will flow a higher per capita income and with it will be less income inequality. As demonstrated by Mungui-Pippidi (2006) governments have no desire to see change since it is the people who run the government who are gaining the most benefit from corrupt activities. The implications are clear that the political structure must be directed at creating good legal systems, education, and a concern for developing the economy (Ali & Isse, 2003).

From the standpoint of NGOs it is important to realize that organizations such as Transparency International, Freedom House, and other groups that monitor transparency and accountability are a valuable asset in the reduction of corruption the role they play is monitoring and making corruption known. Other NGOs such as the World Bank, IMF, and aid giving organizations can limit aid to countries that exhibit corrupt practices. MNCs can also play a role in reducing the supply of briber to corrupt countries. Regional Organizations such as the Coun-

cil of Europe, the Organization of American State, and the G-8 are promoting member countries to stop the supply and aid in reducing the demand for corruption and Bribery. Ultimately the battle against corruption begins in the home nation (Heinemann & Heiman, 2006).

At the national level economic, socio/political and educational changes must be made. Many of the changes will need to have a cultural impact. The culture of bribery will be the most difficult to change. Sanyal & Samantra (2004b) conclude that developed economies are more transparent and have freer and more open economies. They conclude that openness and economic freedom lead to reductions in the level of bribery in a country. Other research finding concluded that legalistic means in themselves would not curb bribery; in fact, cultural factors may significantly inhibit the reduction of bribery.

Conclusions and Further Research

Conclusions

Much of the reviewed research points to a multi-factor attack on the sources of demand for bribery. It also would appear that one of the biggest stumbling blocks to reducing corruption and bribery are the cultural characteristics of a country. Multiple sources such as economic, political, and cultural variables impact the level of demand for corruption in a country. Not only do various factors need to be examined but the internal and external environment must be considered. Not only does reform require internal changes but it must be supported and in some cases encouraged by external organizations and forces. The biggest problem encountered when attempting to reduce corruption and bribery is the cultural shifts that discourage bribe taking. Culture is embedded in a society. Economic and political changes can be made relatively quickly through policy changes and economic development. On the other hand since culture is part of the fabric of society it is more difficult to change. Culture is made up of spiritual as well as family and social values and beliefs. Although economic and political attributes may change the culture may still support corruption and bribery.

Future Research

Further research could consider a study of two regions, such as Latin America and the old Soviet Block Nations of Eastern Europe. Such a study could compare economic, political, and cultural factors of each of those regions and attempt to identify similarities and dissimilarities between those regions. Since multiple factors are involved in creating the demand for bribes it is possible that different countries and regions may require different treatments due to the effects of different variables. A study of two regions would allow a comparison of environmental factors and explore if the demand determinates are the same or different in each region.

While much research has been done on the variables that are involved in the supply and demand for bribes, little research has been carried out concerning the variables in regional groups of countries. A research stream directed at countries that may share similarities in the demand variables would add to the understanding of demand causes in various national groups. Such an understanding would aid in the development of policies and actions that can more effectively curb bribery and corruption on a regional scale.

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Author

Moore, Edwin C. Jr. South University, West Palm Beach, Florida.