WHY IS CORRUPTION A PROBLEM OF THE STATE?

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Abstract:
Economic theories of the last decades provide analytical framework within which we can explain institutional conditions for corruption. Specialists making economic policy recommendations to resolve this problem use several approaches, the most dominant of which are rent seeking and agency theories. In this paper, I explain economic policy recommendations that stem out of both approaches. I argue that scholars suggesting these recommendations within these two frameworks do not understand each other because of different assumptions they make. More specifically, I show that two sets of policy recommendations presented here are based on the particular system of property rights assumed within each theory. In this example, I show why corruption is a problem of the state rather than the market.

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1. Introduction

Quite often, we can meet people, who think corruption is the problem of modern society. Such people usually point out the seriousness of corruption, which seems to them like a problem of morality disintegrating society from the inside. They may mean corruption degenerate society. Such people quite often complain against corruption but they are not able to find its essence and therefore they are not able to identify the way of its elimination.

If we look at the Czech Republic before 1989, we could find services (i.e. personal services or craft services) being sold on the underground markets. People were finding these kinds of services very useful even though they were officially forbidden. They were aware they were breaking the law, but they did not care. In those times, some people considered these activities as corruption. Today it is legal to offer such services to our neighbours. We can find hundreds of workers providing personal services or artisanship doing practically the same activity by just using their privately owned means. Now, hardly anyone says that they are corrupt.

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The moral point of view does not provide practical meaning for corruption. That is why the public is confused about what corruption really is. However, the aim of the paper is not to define morality and classify actions as moral versus immoral, but to provide deductive economic analysis of corruption based on methodological individualism. Positive economic theory can provide a sophisticated analytical framework within which we can look for the solutions for the problem of corruption. Moreover, there exists more than one theory, within which the problem of corruption is solved.

When a citizen bribes a public official to ensure himself a special treatment and quality public services, one would usually say he corrupts the official. When a customer pays a higher price for a service, which brings him better satisfaction because of its exclusiveness, economists would say he enters the market to exchange. If there is no essential difference, it is reasonable to solve the question why the first example is usually considered as corruption and the second is not.

This paper reveals seemingly different theoretical approaches for solving the phenomenon of corruption. The first one is the approach of Gary Becker and George Stigler as the proponents of agency theory. The second one is the approach of Gordon Tullock as the proponent of rent seeking. In this paper, I will attempt to explain the institutional assumptions of these different approaches so that we recognize the advantages or the disadvantages of their economic policy recommendations. In the first section, I will show the Chicago recommendation and I will analyse its explicit and implicit characteristics. Section two is dedicated to explaining and analysing public choice recommendations, which are based on an unjustified critique of Chicago economist’s recommendations. Due to the fact that principal agent is the problem per se, we can think about both approaches in the context of institutional theory. From this point of view, I present in Section three a comparative institutional analysis to explain that Tullock’s critique is not valid. His arguments against suggested market solution are not acceptable because of the different institutional framework, which he assumed in his critique. Consequently, I argue that it is not Becker’s and Stigler’s recommendations that are criticized by Tullock, but the state that provides space for the existence of worldwide corruption.

2. Corruption in the Light of Agency Theory

Most of works focusing on corruption differentiate themselves by their definition of corruption. Nevertheless, we can find several essays that use bribery as the typical example of corrupt action (i.e. Shleifer, Vishney, 1993). For a simple comparison of different approaches, it would be useful to understand corruption just as bribery. Bribery is voluntary exchange between economic agents, where a bribe is the price paid by an agent buying a particular service provided by another particular agent. This is a wider example of an economic activity, which I will analyse and specify in this section.

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1 For example, Pavol Frič (1999) thinks that corruption is the consequence of corruption climate, which is mix of formal institutions and moral attitudes of society. See Frič, 1999, p. 73 – 115.
Gary Becker and George Stigler (1975) also define corruption as bribery but they go further. According to the agency theory (see Demsetz, Alchian; 1972; Padilla, 2002) they understand bribery as a mutually profitable contract:

“The expectation of mutually profitable contracts between repetitive violators (in this case agents breaking law) and enforcers (public officials) is part of the logic behind the widely held view that prostitution or the regular sale of consumer goods cannot be successfully prohibited.”

In other words, the example explains that repetitive contract between the enforcer of the law and the violator guarantees that the entrepreneur smooths the running of his incremental business, which is officially forbidden. A public official, in this case a police officer, sells to an entrepreneur protection against the sanction of the law for a bribe. If the entrepreneurial act was not profitable, it would be probably not worthy for him to pay for the protection of his business. Thus, profitability from illegal economic activities motivates the enforcer and the entrepreneur to cooperate and mutually gain. The public official gains bribes and the unlawful entrepreneur saves himself from sanction.

In the light of above example, there is nothing too complicated in the relationship between the violator and the enforcer; it is just a simple analogy of a standard contractual relationship. The economic problem of corruption is probably on a different side. When we speak about corruption, we typically assume the existence of another very important explicit or implicit contractual relationship, which is between agent and principal. In the case of bribery, we do not suppose only one contract between two agents — enforcer and violator, but also a contract between enforcer and his principal.

The principal is the person whose welfare, usually measured in monetary terms, is affected by the action of the agent. According to our example of bribery, the agent (enforcer) fulfilling the terms of contract concluded with a briber (violator of law) is simultaneously supposed to act according to the terms of the explicit or implicit contract concluded with the principal — the third party. If the principal, in this case the state, does not wish the agent to provide services for bribes, i.e. to sell the protection against the public law, we meet the problem that agency theories try to solve. Jensen and Meckling (1976) define such agency relationship precisely:

“We define agency relationship as a contract under which one or more person (the principal/s) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. If both parties to the relationship are utility maximizers, there is a good reason to believe that the agent will not always act in the best interest of the principal.”

The key problem of bribery is behind the implicit assumption that the principal does not wish the agent, with whom he is in a contractual relationship, to take bribes. Bribery

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2 Becker, Stigler, 1975, p. 4.
3 Jensen, Meckling, 1975, p. 5.
is not in the principal’s interest. Thus, the policy recommendation comes out from the principal’s effort to set an arrangement of contractual terms or rules developing a system of incentives forcing the agent not to take rewards for providing services that the principal does not wish to sell. This is the key point of following economic policy recommendation resolving problem of bribery. Hence, a contractual relationship between an enforcer and a violator is not an economic problem connected with corruption. An economic problem connected with corruption is the principal’s effort to make some kinds of contracts among agents and others prohibited. The principal, in this case the state, is the one who does not want the enforcer to be rewarded for prohibited services (protection against its interest) and then tries to force the enforcer not to sell them. That is why most of the economic recommendations solve corruption from the principal’s point of view.

**Becker’s and Stigler’s Recommendations**

Becker and Stigler (1975) presented two sets of economic policy recommendations. In this subsection, I will clarify their first recommendation to explain the incentives, which are supposed to force agent not to take bribes.

The first proposal is based on punishing the agent who does not respect the rules set in the contract:

“The first proposal concerns punishment of enforcers for taking bribes or other acts of misfeasance or nonfeasance. We assume that enforcers discovered committing such acts are simply dismissed.”

In other words, they assume the state, which is monopolistic supplier of the law, to take care about respect to the law. The state is supposed to dismiss every enforcer who takes bribes for not doing his job, enforcing law by forbidding every illegal action.

To cancel the employment contract is commonplace way how to punish the agent for not fulfilling the terms of the contract. Even though there may be different sanctions, the essential purpose of which is to cause the agent bearing some cost of breaking the deal. When an agent is caught acting illegally, he is dismissed thus he loses future gains from doing his job, which is salary, pension, using the company vehicle or prestige of the bureau. An agent making decision about action he wants to perform he is considering future gains and loses, hence if a principal wants an agent not to take bribes he has to arrange the terms of contract in order to raise the agent’s future loss, which should be higher than the loss of the opportunity of bribe.

Nevertheless, the detection of bribery and the consequent cancelling of the contract are not costly only for an agent. More importantly, it causes the costs to a principal who attempts to prevent himself against future losing of his welfare. That is why principal seeks to avoid costs of monitoring and detection of the agent’s malfeasance and he considers making the agent more “loyal”. To help the principal in this effort B. and S. explains sophisticated mathematical model that copy not original assertion, which is

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4 Becker, Stigler, 1975, p. 6.
raising the salaries. Raising the salaries in accordance with written essentially means raising opportunity costs of bribery.

“The fundamental answer is to raise the salaries of enforcer above what they could get elsewhere.”

The second B.’s and S.’s suggestion stems out of the assumption that previous recommendation is targeted to principal, which is the state. They present several arguments why the state cannot effectively avoid providing public services, such as law enforcement, without corruption even though it raises salaries of its agents (law enforcers). Therefore, they found another solution, which will be completely explained in the third section.

3. Corruption in the Light of Rent Seeking

“The problem of corruption is real, and it is connected with rent seeking.”

Rent seeking theory contains a relatively wide-ranging of specific economic activities directed to obtain a monopoly position on the market in order to gain the monopolistic rent. Such activity may be legal (i.e. lobbying) and still absorb resources in unproductive way. Nevertheless, unproductiveness of rent seeking comes out of the assumption that wasted resources are spent on the creating or maintaining monopolies (Krueger 1974, Tullock, 1998). For instance, an entrepreneur bribing the enforcer of the law achieves a monopolistic rent. This results from his privileged position on the illegal market because all other entrepreneurs are forbidden to run a competing business by the enforcer. Such understanding of corrupt action may raise the question if there is any economic reason to prevent potential competitors to bribe the enforcer. In other words, there may be asked if it is reasonable to prevent anybody bribing the public officials to gain position on the illegal market.

In this section, I will clarify the Tulock’s arguments against legalization of bribery by the state. He tries to show why is reasonable to fight corruption instead of its legalization.

Tullock’s Recommendations

Arguments against the legalization of bribery stem out of the idea that legalized bribery virtually means that citizens are allowed to pay prices to public officials in order to buy the public law (government privileges), which brings them such benefits or rents.

If one assumes that it is permitted to purchase congressional votes, then the legalization of bribery is established. This implies the institutionalization of bidding for administrative monopolies, which would be pushed ahead by elected congressional representatives. In general, it means that democratic representatives of the state would

5 Becker, Stigler, 1975, p. 6.
6 Tullock, 1996, p. 6.
be paid from the pockets of private citizens, big enterprises and whoever interested in adaptation of formal institutional conditions in the country. In such situation there would be given space for market demand for the congressional votes allocated by the market mechanism but also there would be great profits on the congressman side, because of his monopoly position in setting the rules.

“Think of the libertine prince who sells policies in this way and spends the money entirely on his luxury consumption. The citizens would be moved into the most efficient possible conformation of their economy, but the profit would go entirely to the prince.”

The example of “libertarian prince” illustrates powerful leader, who sets and enforces the law and who may sell his political power and secure every administrative monopoly position he wants. According to this example, it may be asked if there would be any supply of governmental privileges at all. If the prince were not powerful enough to secure the privileges he sells, nobody would probably buy his services. If the prince were powerful enough to secure privileges there would not exist any incentive that forces him to sell it. It may not be worthwhile to sell political power of the prince when he may take whatever he wants just by his power. However, if we suppose that it is worthwhile for the prince to join a mutually profitable exchange, the question is if he is subordinate to any constraints that would make him observe the contract and force him not to use power against his potential customers.

The important assumption of previous argumentation is that the rules, which the corrupted agent violates, should be enforced by the state or its agents. Thus, the state sets together with the agents all other conditions of contracts. For example, the state as the principal may choose who will be his agent (employee) and who will be fired. The state may also sell the privileges to be its employee. As Tullock (1996) stresses, we can find historical cases when the European governments were selling such governmental positions. The British government sold army officers commissions (i.e. “Honorable Arthur Wellsley became a colonel on his sixth day in the army. Without this head start he would have never become a Field Marshall in time to command at Waterloo.” Tullock, 1996, p. 12). This system worked well and European rulers had no reason to change it. Reforms were initiated in 19th century just thanks to criticism of prices of sold commissions since then system started to be price controlled. However, history supports the advantages of monetary incentives theoretical explanation of its function is obvious.

The key circumstance of the proposal is the marketability of governmental jobs. Thus, governmental employee who bought himself the privilege to perform his function and who reaches the monopoly rent is allowed to sell or leave his position whenever or to whomever he wants. Hence, if there is in the contract the term that deprives the agent of his privilege to be a governmental employee without reimbursement of the price he has invested when he violates his duties, he is motivated to perform well. When he breaks the contract, he loses his future profit from selling the position. In other words, he bears the opportunity cost of future incremental trade.

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7 Tullock, 1996, p. 11.
This has the same logic that Becker and Stigler suggest in the case of the first raising of the salaries recommendation. The salaries or other occupational advantages are as well agent’s future profits as the gains from future selling the rent providing privilege. When the agent breaks the terms of contract and the principal knows it, he bears the costs in form of losing future gains form performance his job. Mises (1996) argues that every individual decision is the choice between alternative actions. Since an agent chooses between alternative of taking the bribes and he risks loosing the job (future salaries or profit from future selling the privilege) he balances psychic future costs and revenues. If the monetary profit from the realization of one of these alternatives is higher, then an agent is likely to choose it. Therefore, if the opportunity costs of the agent’s performance of his official duties are higher (lesser) than opportunity cost of taking the bribes, the agent probably chooses taking the bribe (perform his duties).

Becker (1968) even argues that if choosing the forbidden alternative is riskier, there is a higher probability that an agent chooses not taking bribes. Hence, even though salaries maybe high or governmental employment privileges may be in great demand, it does not necessarily mean that bribery will be eliminated because it still depends on the efficiency of the monitoring system. Tullock certainly agrees with this assertion when he writes: “This argument for purchase and possession of government jobs can be fairly good one if there is a good supervision process.”

4. Comparative Institutional Analysis

In this section, I will show another proposal by Becker and Stigler, which Tullock does not understand and incorrectly interprets as selling governmental privileges. For evidence: “They [Becker and Stigler] pointed out… that simply selling governmental privileges in auction would put the privileges in the most efficient hands.” I will use a comparative institutional analysis to show the main contribution of the second free competition recommendation, and consequently, argue that the point of misunderstanding results from different underlying property rights systems assumed in their theories.

4.1 Free Competition Recommendation

The second free market suggestion stems out of the assumption that previous recommendation is targeted to principal, which is the state. Now, it must be clear that while we think about “selling privileges,” we must think about the state as the principal also. It should be also clear that previous recommendations might be logical and functional only when the monitoring system works “well”. Otherwise, the probability of agent’s disclosure is high enough. That is why, the function of the monitoring system is essential, because it guarantees that system of incentives set in the contract works.

For instance, if the state knew about bribery between their enforcers and violators of the law, it may raise the salaries of the enforcers but it is not certain that such step

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8 Tullock, 1996, p. 12.
9 Tullock, 1996, p. 9.
eliminates corruption. When the enforcer feels comfortable with his position and he is not afraid of dismiss he may take high salary and bribes also. In the case that there is nobody who would watch the enforcer’s performance, there is no guarantee that the enforcer is not corrupted even when it is forbidden by the contract. Even though the principal tries to minimize the monitoring costs he must spent any in order to make agent feel uncertain, because in the reality principal cannot be perfectly informed about an agent’s interests. Typical examples of such action are haphazard controls.

It is certainly not the problem for the state to raise the monitoring costs in order to make its agents uncertain about their positions. Nevertheless, in such case the raising salaries proposal loses its sense, because the state does not have to pay its agents if it spent enough resources to monitor them. For example, it may hire more enforcers to watch their colleagues. However, Benson (1988, p. 149) argues that the monitoring system of the state is never sufficient because bureaucrats monitoring subordinate bureaucrats feel loyal to their colleagues. This brings us to the question of what is meant by saying that the monitoring system works effectively or “well”.

“Although the compensation structure we have developed could eliminate malfeasance, it would not automatically result in optimal enforcement. No guidance is provided to optimal number of enforcers (or more generally to the optimal total expenditure on enforcement)… Moreover, considerable resources may be spent by the state in detecting malfeasance, by enforcers in hiding it, and more generally, by the state and enforcers in protecting their own interest.”

In other words, Chicago economists point out, along with Demsetz’s (1968) arguments, that the state as the principal never knows the optimal number of its agents (enforcers). That in general means, the state is not able to optimize expenditures spent on the production of public services (law enforcement). Furthermore, the state does not effectively monitor activities of its employees that do not correspond with its goals, because, also as Benson (1988) argues, it is not sufficiently monitored by its citizens in pursuing value-maximizing allocation of resources.

The fact is that the state faces problems arising from of the impossibility of economic calculation in a system of public ownership. As Misses (1990) shows, in a system of public ownership do not exist incentives to optimize the expenditures spent on production of public services as well as incentives motivating public officials to optimize the costs spent on the monitoring of the agents. Since the state is the only owner of the means of production, it cannot calculate profit and losses. Because of the

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10 Becker, Stigler, 1975, p. 13.
11 Benson points out that the citizen’s cost of spending on monitoring public officials are relatively high in comparison with benefits he may reach by the identification and prosecution of corrupted official. High opportunity costs of monitoring in combination with bureaucratic secrecy motivate the citizen to be a free rider. Monitoring public officials is the duty of watch organizations or media, which are paid again by their donors or consumers of advertisement considering benefits from their investments. Public officials are relatively free in comparison with the market in pursuing corrupt discretionary policy because of the higher opportunity cost of monitoring public officials. See Benson, 1988, pp. 147 – 148.
absence of private ownership, there is no exchange and consequently no monetary price. That is why the state cannot assess the monetary value of its production and agent’s decisions.

Mises (1949) goes further and compares different economic organizations framed by different underlying property-rights systems. While the enterprise where monetary calculation creates monetary incentives is called market organization, the public enterprises where is monetary calculation impossible because of the lack of exchange based on the private property is called bureaucratic organization. Banfield (1974) as well compares business and governmental organizations and as well stresses that without the profit-and-loss mechanism the public officials cannot easily sanction and reward agent’s decisions and consequently create the system of incentives, which would motivate agents to pursue value-maximizing allocation of resources.

“In a business organization, the principal’s interest consists of one-or of very few-objectives the parameters of which—for example, a satisfactory level of profit and beyond that the maximization of emoluments (including staff and expenses) to managers—are easily ascertained. The goods and services produced by the (business) organization can generally be brought under the measuring rod of money and can be distributed via market competition, thus reducing, and to some extent eliminating, the need to exercise discretion. If over time the revenues of the firm do not cover its costs, it must go out of business”\textsuperscript{12}

Kirzner (1985) argues that the absence of monetary calculation in bureaucratic organizations restrains competitive entrepreneurial activities because it lacks the essential incentive in the form of the pure entrepreneurial profit, which motivates the entrepreneur to discover the value maximizing opportunity nearing the market to equilibrium. Therefore, even if the state tries to eliminate corruption by means of raising the monitoring costs it cannot guarantee the value maximizing allocation of resources because it lacks monetary calculation based on market prices, which hold, as Hayek (1945) argues, irreplaceable informational function.

Following the above logic, Becker and Stigler suggest a solution, which would be leading to the efficient monitoring system and is the logical result of their argumentation and our analysis of their arguments. “A highly promising method of compensating enforcers (agents) is suggested by the market in private transaction….\textsuperscript{12}” (Becker and Stigler, 1975, p. 13) In other words, the recommendation means if the bribe is just a market price for the demanded profitable service, it is reasonable to think about letting agents sell these demanded services and compensate them by “bribes” (market prices) instead of salaries. More precisely, in the case of the state being the principal, Becker and Stigler ask if we are aware of the difficulties of the state’s monitoring system. Why we do not think about loosing the contract with the state and as the result, we allow the agents to take “bribes” (market prices) for their demanded services. In the words of Austrian scholars, this advice simply says that it is reasonable to let the bureaucratic

\textsuperscript{12} Banfield, 1974, p. 591.
agent calculate his own gains in form of “bribes” and make him entrepreneur bringing the market to equilibrium.

Now, I would like to stress again that this proposal does not mean selling monopoly privileges as Tullock (1996) explains. The proposal is based on free market competition where private agents provide enforcement of law. So the state does not form the conditions of the contract with the enforcer – there is no third party. The evidence is that Becker’s and Stigler’s assertion: “Free competition among enforcement firms may seem strange… But society does not pretend to be able do designate who the bakers should be – this is left to personal attitudes and taste. Why should enforcers of law be chosen differently? Let anyone who wishes to enter the trade, innovate and prosper or fail.” (Becker and Stigler, 1975, p. 12). Nevertheless, a question may be raised whether there is no third party, no principal in form of the state, who monitors or creates incentives forcing the enforcer to do his job as his clients expect. The answer is free competition, which means, as Kirzner (1997) explains, free entry to the market in order to seek entrepreneurial profit.

4.2 Competition as a Monitoring System

A constitutional economy considers democratic elections as exchange among citizens and politicians (see Buchanan, Tullock, 1962, Chapter 18). In democratic elections, self-interested politicians sell their political power for reelection. They try to follow wishes of interest groups in order to gain political capital.

When we follow this logic, we can say that politicians have to satisfy demand by their political decision-making to be successful (see Rothbard, 2004, Chapter 2). Political parties compete for their voters’ favour in elections and that may be considered as desirable, because in such view, political competition force politicians not act against citizen’s interest. Therefore, democratic elections are supposed to make political representatives to be uncertain about their position and in this way force them to act according the interest of their principals – citizens.

In this subsection, I argue that political competition does not compensate free market competition, which is usually supposed to ensure that the customer (principal) gets the service he wants and makes the agent (entrepreneur) uncertain about his position on the market. First, let’s take a look at problems related to competition inside bureaucratic management.

Shleifer and Vishney (1993) appreciate the meaning of competition too. They try to implement the competitive process into the bureaucratic or governmental organization.

“Our industrial perspective suggests that the best arrangement to reduce corruption without theft is to produce competition between bureaucrats in the provision of government goods, which will drive bribes down the zero.”

In Shleifer’s and Vishney’s views, corruption “without theft” results from the bureaucrat’s ability to restrict the quantity of public goods sold. In this way, bureaucrats may by the discretionary decision-making affect prices of public goods. They charge

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13 Shleifer, Vishney, 1993, p. 610.
bribes for public goods they sell. For instance, bureaucrats selling licenses for official price x are able to charge bribe b figured in the final price, which is x plus b. Shleifer and Vishney suppose that if a bureaucratic organization constituted enough similar bureaux we can eliminate bribery by their rivalry. According to this example, we can eliminate b (bribe) down to zero by their competition.

Again, Demsetz (1968) convincingly demonstrates that the number of rivals on the partial market does not determine the degree of its competitiveness. He argues we cannot find a relevant theory that would present knowledge about an optimal number of rivals, because transaction costs may play a significant role in determination of competitiveness of the market (Demsetz, 1982). Kirzner (1976) explains, as was said above, that there is only one criterion by which we are able to judge the competitiveness of the market. Only when the market is completely free to entry (there are minimum legal transaction costs preventing the entrepreneur from running the business, or there are no artificial barriers) we may proclaim that the market is competitive.

However, even though the state finds a given number of bureaux as “competition”, it cannot perfectly know the level of the bribes and it does not even know if the public authority (its agent) is corrupt until it effectively monitors the bureaucratic agents. Thus again, the state can spend a public budget completely on monitoring or on endless duplications of bureaux. In the opposite extreme, if the level of bribes is known without monitoring, the state does not have to fight corruption at all, because it can just set the price as the sum of the x and b or increase supply of public good sold.

It would probably be unwise to accept the notion that subordinate agents will report the level of their illegal incomes to their monitor agent. That is why competition between duplicate bureaux is supposed to force the corrupt agent to sell licenses for a minimum price. But, it should be asked what would motivate the agent to lower his price. Again, the answer is the profit incentive. Only if the agent was the owner of goods he sells and therefore is the receiver of profit for a higher quantity of goods, he would be likely motivated to enter the competitive process. That is why I have to remind the reader that in the system of public ownership, bureaucrats are neither owners nor entrepreneurs, they do not receive profit from their activities, but remuneration. Because of the lack of profit incentives in bureaucratic organization, bureaucrats are subject to rules and budget. They are interested in the budget and the rules of the bureau.14

More importantly, even political competition of political parties could not be considered as market competition. The main reason is that it is not competition for profit but for votes. Thus, public laws, which are established by the political process are not supposed to be modified in private contractual exchange but only through political decisions made by citizens and consequently by their representative’s political decisions. Therefore, however a contractual relationship between a public official and its customers is mutually profitable it does not necessary mean that such contract is desirable by citizens, who have privately owned constitutional right to vote for modifying or forbidding such exchange. Every citizen have the same property right...

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14 Niskanen presents a model of bureaucratic equilibrium. He argues that each bureaucrat appointed directly by the elected executive seeks to maximize a utility function made up of perquisites of the office, public reputation, power, patronage, output of the bureau, ease of making changes, and ease of managing the bureau. Generally, bureaucrats seek to maximize budget. See Niskanen, 1868.
(Alchian, Demsetz, 1973) to decide in elections if the exchange is in his interest or not, even though he does not wish to realize any exchange at all. Thus, when the price in the form of a bribe is established in governmental organization it may be considered as corruption whenever citizens think so. Mutually profitable exchange may be in the interest of the customers, but it is never supposed to be in the interest of a public official or a politician if, especially during elections, it does not correspond with the “common interest” of voters. The problem of corruption in governmental organization arises from the assumption that public officials are supposed to push ahead “common interest” of all citizens instead of individual interests of their immediate customers.

A democratic voting system has another specific quality. It virtually provides to every citizen a very specific privilege to choose his favorite politician in elections. The rule “one vote for one citizen” gives to every citizen a very specific property right to exercise political power. This kind of artificial property is not convertible; it could be used just in time of elections. It is practically worthless in “day-to-day” economic activities, because it cannot be consumed or exchanged for higher values. These circumstances give to politicians a relatively certain position about the future of their industry. The very specific character of votes, which are useful only in time of elections, guaranties to politicians that there has to be always demand for their services established by elections. Moreover, in the case, that the great part of citizens will decide not to use their rights to vote, the politicians of the particular country are in a better position, because they have to go along with interest of the smaller group of citizens in order to be elected. In the market, the politician would be in an opposite situation. If the customers do not wish to buy the politician’s services, he would fail to gain the profit and he would be forced to leave the market. In the extreme, if there were no demand for political services in the market at all, the whole industry would disappear. According to the logic of a democratic voting system, even though ninety nine per cent of voters will not vote, one percent will still give to the winning politician the same power to sell monopoly positions to his voters or interest groups for reelection.

The problem of Gordon Tullock’s argument does not arise from the undesirability of value maximizing allocation of political power, but from the relative certainty of elected politicians in pursuing their conflicting individual interests. The democratic voting system cannot sufficiently compensate a competitive voting system of monetary prices. Politician’s ability to act against citizen’s interest results from the relatively certain position they possess in comparison with the uncertainty of the market competition process. In this way, a democratic state will always provide less strong incentives that would pursue their agents to avoid corruption. That is why the problem of corruption will prevail in governmental organization.

5. Conclusions

In the second section, I explained the economic problem of corruption in the example of bribery. Bribery is a profitable exchange, which is performed by one of the parties (the agent) that is responsible to perform on behalf of principal. Principal delegates some decision-making authority to the agent. It was shown that the problem of corruption comes out when the principal does not wish an agent to act in ways he may consider as corrupt. It was also shown that the principal is able to use the monetary
incentive in the form of a salary to motivate an agent not to take bribes. When the principal increases the salary in the case of an employment contract, an agent is likely to choose not to take bribes because he risks the future loss of his higher salary. He bears the opportunity cost of a potential dismissal.

In the third section, we analysed some suggestions that imply the principal is the state. The state may for example sell monopoly privileges for being its employee and in this way motivate an agent not to take bribes. It was argued that key circumstance of such economic measure is the marketability of sold privilege. Loosing future gain from selling the privilege in the case of agent’s disclosure motivates the agent to act in accordance with principal’s interest. It was also argued that this proposal of Gordon Tullock based on the criticism Becker’s and Stigler’s free competition proposal could be analysed in the same way as it is in case of raising salaries. Even though Tullock tries to criticize Becker and Stigler paradoxically, he supports their arguments. Moreover, they even agree that the function of the principal’s monitoring system is essential for function of monetary incentives.

The fourth section provides a comparative institutional analysis to explain the state’s difficulties with the monitoring system. The system of monitoring agents is essential for the function of every system of monetary incentives, because it makes an agent feel uncertain about his future gains. It is not reasonable to expect an agent to perform in the principal’s interest without being monitored, even though he takes a great salary. That is why the functional monitoring system is needed for every proposal using monetary incentives. But, the problem of the state results from its disability to connect effectively the monitoring system and the system of incentives because the state lacks monetary calculation. Monetary incentives forcing an agent to act in the principal’s interest lose their sense when the whole budget may be spent just on the monitoring system.

The democratic state is traditionally supposed to be an agent acting on behalf of its citizens. Democratic fluctuation of elected political parties is usually supposed to make political leaders feel uncertain about their privileged position and in this way force them to act in the interest of citizens. Nevertheless, such political competition cannot compensate the lack of free market competition, because bureaucratic agents are not supposed to participate in the essential monetary incentive of market organization, which is profit, but in the common wishes of all citizens. As the result of the lack of monetary calculation, free competition is not only practicable in bureaucratic organization but free competition also provides more incentives for pursuing actions in the interest of customers than a democratic voting system, which is supposed to provide incentives for pursuing actions in interest of citizens. This answers the question why is corruption a problem of the state.

Recent discussions rotate around the following assertion by Becker and Stigler:

“…new economic approach to political behavior… …asks why certain industries and not others become regulated or have tariffs imposed on imports or why income transfers take the form and direction they do, in contrast to asking which industries should be regulated or have tariffs, or what transfer should be made.”

15 Becker, Stigler, 1974, p. 1
If we are prepared to abandon normative economic analysis, eventually such question has to arise. Boettke (2005) stresses that if the conflicting interests, which certainly corruption represents, are solved through institutional arrangement, we should not be concerned about the “right” institutional framework. Instead, we should examine alternative market self-enforcing institutional conditions. Austrian economists in this way argue against presumptions based on protective governmental organization of public choice theories, such as the theory of public goods, monopoly and market failure. They hold on the predatory nature of the state that Tullock emphasize too in his understanding of monopoly and rent-seeking and the consequent arguments against legalizing corruption. In my view, Austrians provide some progressive insight into behavioural and institutional economic analysis.

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