

Corruption and Primary Accumulation of Capital in Transitional Economies

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Abstract:

The corruption is a secondary phenomenon, because there are economic preconditions causing it. Unless the achievement of macroeconomic stability and the formation of the institutions appropriate to a market economy reach their logical ending, both of them may become the cause of corruption in the post-Communist transformation of the economy. In order to restrict corruption and establish the institution of private property, it is necessary to legalize the existing results of primary accumulation of capital, which will let it “act” in the public interest. Such an approach does not exclude the punishment of all the lawbreakers according to the law.

Keywords: corruption, macroeconomic stability, market institutions, primary accumulation of capital, transitional economy, post-Communist country

Corruption is one of the most pressing problems of modern society (Elliott, 1997, Klitgaard, 1998, Mauro, 1997, Rose-Ackerman, 1999, Tullock, 1996, Waller, Verdier, and Gardner, 2002). It has become a priority for consideration by International organizations and more generally among politicians and scientists. It should be mentioned that the scientific analysis of this problem is often of secondary importance and gives way to political approaches to ways of suppressing of corruption, not to mention proposals intended for populist effect.

It should be made clear from the very beginning what kind of event is the corruption from the economic point of view in post-Communist countries (Negru, and Ungurean, 2001, Papava, 2005, pp. 57-62). This will help in creation of an effective mechanism for its restriction.

Secondary Phenomenon

It should be mentioned that *corruption*, as such, is a *secondary phenomenon* and it will be practically impossible to elaborate an effective mechanism for its restriction without revealing the economic reasons causing it.

One terminological aspect should also be discussed. Namely, as general rule, in respect to corruption the word combination – “*to combat corruption*” – is used, what, in our opinion is *unacceptable in principle*, because there are economic preconditions causing corruption, the fight against which, *or against economy is just nonsense*. It is true that the various manifestations of corruption could be combated, which in a short period of time will have camouflage-type pseudo-effect, but actually nothing will be changed: the “main actors” of corruption will change, but the economic reasons causing corruption will remain untouched. At the same time, if we consider, that the full disappearance of corruption is impossible in principle, then, by taking into account the above, the right approach to the problem from a terminological point of view, will be the word combination “*the restriction of corruption.*”

Corruption in Transitional Economies

The nature of corruption in countries post-Communist with transitional economies differs from that of developed countries. This process itself is unique, as the corresponding economy is no longer a command one, but is not yet fully a market one either; and it is this that is directly reflected in the causes of corruption and its various manifestations.

In order to study the economic nature of corruption in post-Communist countries, it will be appropriate to remember that the process of transition to market consists of two mutually complementary sub-processes. The first is *the achievement of macroeconomic stability* and the second – *the formation of the institutions appropriate to a market economy*. Unless these sub-processes reach their logical ending, both of them may (and it is generally the case) become the cause of corruption in the post-Communist transformation of the economy.

If the macroeconomic stability of the country has not been achieved, which can be revealed in high rate of inflation and devaluation of the national currency and /or in considerable failure to collect the tax revenues, then this first of all, creates a possibility of “rapid” earning of dirty money.

In this case, the management of the State banking system and persons close to them, having access to the State credits, are given “legally unlimited” opportunity to become rich through rapid currency or commodity transactions, with the help and by means of devaluation of national currency and increases in prices.

Failure to collect revenues to finance the national budget is nothing else than directing them to the pockets of the tax collectors and their protectors and on the other hand incomplete budget creates the productive grounds for the authorities of the State Treasury, to give priority to those persons, who give a larger bribe, while financing the budgetary expenses, approved by the Law and in settlement with the budget. Low tax revenues are not able to ensure the relevant level of payment of the employees of the budgetary sector, and this is an objective reason for initiating corruption in respect of high officials.

Therefore, *post-Communist macroeconomic instability is quite a strong nourishing source for the corruption.*

As far as control of inflation, the achievement and maintenance of exchange rate stability is possible within a quite short period of time, this makes it possible not only to restrict, but also to practically eradicate corruption in this field. The IMF has a great experience of this and all those post-Communist countries, which have intensively cooperated with it, achieved the positive results in a short period of time.

It is far more difficult to establish perfect order in fiscal system. As proved by the international experience, there is practically no country in the world, where concealment of revenues does not take place with the aim of evading the payment of taxes. Tax evasion is the main element of illegal activities in any country with a developed market economy. In order to restrict corruption in this field it is necessary

for: continuous improvement to the administration of taxation and customs systems; the development of taxation and customs legislation relevant to this process; and practically continuous education of the public in taxation and customs matters.

As proved by the international experience, the reformation of fiscal system requires much more than one year. A longer period is needed for the second constitutive sub-process of post-Communist transformation of the economy – the establishment of the institutions appropriate to the market economy. At the same time, *the lack or imperfection and weakness of the part of such institutions create possibilities for corruption*. It should also be stressed that the creation of some institutions in a hasty way, for which, as a general rule, the direct copy of Western analogues is used, does not prove right in most cases, not to mention the obvious adverse effects revealed in some cases.

One of the relatively “harmless” examples of the above in the Republic of Georgia is the law on bankruptcy, which is practically a copy of the German legislative model, drafted with the help of German experts and then adopted by the Georgian Parliament. Despite the general approval of foreign experts the law was *still-born* from the very beginning, inasmuch as according to this law none of the *de facto* bankrupt enterprises was *de jure* bankrupt. After the improvement of this Law its possible enactment was halted for an undetermined period of time by the Law on Tax Arrears Restructuring, the draft of which was prepared with the help of World Bank experts and which expresses the nationally detrimental interests of the most anti-reformatory wing the industrial lobby of the Republic Georgia. It tries to demonize bankruptcy. Yet, it should be stressed, that prolongation of the operation of a bankrupt undertaking is equivalent to maintenance of bad management without any changes (something which destroys the development prospects of an undertaking). The Tax arrears restructuring procedure is of a corruptive nature for enterprises, because the preparation of the draft of the approval on restructuring, consideration of deadlines and other conditions in this draft is dependent upon a public official. Furthermore, the above mentioned lobby has been trying for years to introduce a mechanism for writing off the tax arrears, what will obviously be a step “forward” towards corruption in this field.

Primary Accumulation of Capital

In order to restrict corruption caused by the institutional vacuum, that is characteristic of the post-Communist economic transformation, *it is inevitable to choose that main institution*, without which the establishment of a market economy will be impossible: *the institution of private property*.

The difficult process of establishing the institution of private property in a post-Communist transformation is the main cause of corruption and thus differentiates itself from the reasons for corruption in Western Countries.

The creation of a liberal legal environment, necessary for the development of the entrepreneurship, is the basis for the reinforcement of the institution of private property. It is also necessary to place all of the entrepreneurs, both local and foreign ones, in equal conditions, in order for fair competition to be the only way of revealing the winner.

Primary accumulation of capital is taking place in the post-Communist countries. This process took place a long time ago in well-developed Western countries; without it transition to a market economy is impossible.

History does not show any example of carrying out the process of primary accumulation of capital with "*clean hands*" and *only legally*; usually, this process was based on the phenomenon, which today is considered as the corruption.

In the process of primary accumulation of capital, the use of mainly punitive measures with the purpose of restriction of the corruption will inevitably fail. The introduction of a rule that every official should prove that his property has been legally acquired (a breach of the principle of the "presumption of innocence"), and that in the absence of documentation of the origin of the property, its owner should be fined, or the property should be seized, etc. will finally result in returning of the process of primary accumulation of capital to its point of origin. Launching this process all over again will prolong the "life" of corruption. Besides, as a result of imposing the mentioned punitive measures a renewed process of primary accumulation of capital will be carried out in an even more disguised manner and accordingly will develop as a more hideous event.

The main way of transformation of newly accumulated capital into property terms in post-Communist countries is house-building, or creating other immovable property, from which many people are employed and get remuneration for their work, construction materials are bought, and gives employment to the workers of their enterprises etc. If only punitive measures are introduced, first of all the rate of bribery will be increased because of the increased possibility of disclosure (or risk-factor), and secondly – illegally gained money will not be transferred into property terms in these countries, but it will flow out abroad. In other words corruption will not be restricted, but its "main actors" will change and the society will be deprived of the indirect effect of primary accumulation of capital.

Final Remarks

In order to restrict corruption and establish the institution of private property, it is necessary to legalize the existing results of primary accumulation of capital, which will let it “act” in the public interest.

Such an approach does not exclude the punishment of all the lawbreakers according to the law, provided the constitutionally recognized, very important principle of “presumption of innocence” is not violated.

Measures for restricting corruption should be carried out in law enforcement agencies with particular care, and to this end institutional reforms should be carried out together with the financial stimulation of the officers. Otherwise, the agencies intended for the defense of order, may become the initiators of an extension of corruption or in a worse case even *institutions of political settlement* (the epoch of Stalin, when because of the well known events of 1937 many persons, who had different thinking, the whole army of innocent people were subjected to repression, was a bitter experience for all post-Soviet countries).

From this point of view, special care is needed in regard to the establishment of any *anti-corruptive institution*, or institution having special rights (namely the right of criminal prosecution and investigation) for combating corruption. In conditions of weakness in the institutional arrangement of the State, such an institution will become a shelter of corruption itself. Unfortunately there are many examples of this in the world practice. Only the creation of an institution with coordinating functions is acceptable, which at the same time will monitor the measures to be carried out for the purpose of the restriction of the corruption.

With a view to the restriction of corruption, it is very important to comply with the *principle of publicity*, which should ensure the provision of the society with maximum information regarding the current processes, in order to increase the efficiency of the measures to be carried out.

Corruption is a contagious disease, the whole society is more or less sick from it – the appropriator of collected taxes, the thief of the Treasury, or the ordinary citizen who does not pay for electricity consumed. Unfortunately, even *media could not avoid this disease*, when financially powerful clans (some of them of political in nature) can bribe them and dictate the kind of information to be publicly spread. This first of all is caused by existence of unorganized state institutions and by grave economic conditions in the country, when the press and the television have the difficulties to survive independently. But despite this, only the press and the television are efficient

instruments, which could be used for restricting corruption, through the State promotion of competition between them.

And finally, as corruption is a secondary phenomenon, the overcoming of poverty by means of economic growth should be the main object of the country. This itself will be the precondition for the restriction of the economic basis of corruption.

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