

# Building Integrity and Reducing Corruption in Defence

A Compendium of Best Practices



# CONTENTS

<b>Part I Introduction</b> .....	<b>1</b>
Chapter 1 The Corruption Curse.....	3
<b>Chapter 2 A Strategic Approach to Building Integrity and Reducing Corruption in Defence</b> ... 13	<b>13</b>
Chapter 3 NATO and the Evolution of the Building Integrity Initiative.....	22
Chapter 4 National Approaches in Support of Building Integrity and Reducing Corruption in Defence.....	31
<b>Part II Corruption Risks and Vulnerabilities in Defence</b> .....	<b>41</b>
Chapter 5 Personnel Policies.....	43
Chapter 6 Defence Budgeting and Financial Management.....	57
Chapter 7 Defence Procurement.....	72
Chapter 8 Offset Arrangements.....	86
Chapter 9 Opportunities and Risks with Outsourcing, Privatization and Public-Private Partnerships in Defence.....	99
Chapter 10 Utilisation of Surplus Equipment and Infrastructure.....	112
Chapter 11 The Involvement of Defence Personnel and Assets in Economic Activities.....	124
Chapter 12 Integrity Issues Related to Military Operations.....	135
Chapter 13 Combating Defence-related Corruption in Countries with Unresolved Territorial Disputes or Frozen Conflicts.....	148
<b>Part III Building Integrity and Reducing the Corruption Potential in Defence Establishments</b> .....	<b>163</b>
Chapter 14 The Importance of Integrity Building.....	165
Chapter 15 Regulatory Frameworks.....	172
Chapter 16 The Human in the Loop.....	193
Chapter 17 The Role of Government.....	205
Chapter 18 The Role of Parliaments and Audit Offices.....	222
Chapter 19 The Role of Ombudsperson Institutions.....	234
Chapter 20 The Defence Industry as an Ally in Reducing Corruption.....	250
Chapter 21 The Role of Civil Society and the Media.....	261

Chapter 22 The Role of International Organisations.....	281
<b>Part IV Implementing Integrity Building Programmes.....</b>	<b>297</b>
Chapter 23 Making Change Happen .....	299
Chapter 24 Cultural Awareness in Implementing Integrity Building Programmes.....	312
Annex 1: Selected Resources .....	323
Annex 2: TI International Defence and Security Programme .....	327
Annex 3: Abbreviations .....	329

## Chapter 2

# A Strategic Approach to Building Integrity and Reducing Corruption in Defence

The crippling costs of corruption, discussed in chapter 1, can be reduced significantly through the application of proven principles, mechanisms and practices of good governance. Governments have a wide spectrum of choices in their efforts to minimize corruption. These can be distilled into three main categories:

- Building integrity;
- Increasing transparency; and
- Improving accountability.

A simple strategic framework offers an illustration and serves as a guide to shape government investments to counter corruption. This framework combines a philosophical view of corruption with an economic perspective. It couples views on ethics of the great German Enlightenment figure, Emmanuel Kant, with the utilitarian perspective attributed to the 19<sup>th</sup> century English philosopher, John Stuart Mill.

Mill's utilitarian perspective reappears in a contemporary economic model of crime developed by Nobel Prize winner Gary Becker entitled *Crime and Punishment: An Economic Approach*.<sup>1</sup> The theory of rational crime proposed by Becker requires that we place ourselves in the shoes of a public employee, bureaucrat or elected government official. According to Becker, any individual with an opportunity to be corrupt evaluates the potential (marginal) benefits of their actions against the expected (marginal) costs if detected and punished. Becker conjectures "... individuals become criminals because of the financial and other rewards from crime compared to legal work, taking account of the likelihood of apprehension and conviction, and the severity of punishment."<sup>2</sup> His framework was later extended to include the ethical costs of crime.<sup>3</sup>

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<sup>1</sup> Gary S. Becker, "Crime and Punishment: An Economic Approach," *Journal of Political Economy* 76 (1968): 169–217.

<sup>2</sup> *Ibid.*, 176.

<sup>3</sup> Michael K. Block and John M. Heineke, "A Labor Theoretic Analysis of the Criminal Choice," *The American Economic Review* 63:3 (1975): 314–25.

According to this approach, two major factors help deter the corruption of elected officials, civilian and military government employees, defence contractors and others in the defence sector. The first is a culturally determined ethical or “moral burden” – if individuals recognize corrupt actions as immoral and unethical, this deters corruption. The second major factor is the “Expected Punishment” – if individuals recognize their actions are illegal, and that they may be discovered and imprisoned, this deters corruption. From this perspective, when evaluating whether or not to engage in corrupt practices, individuals often implicitly consider two costs: 1) the ethical or moral burden of committing an illegal act; and 2) the probability of being arrested and punished. These costs are then compared to potential rewards.

Assuming diminishing marginal benefits of corrupt actions and increasing marginal costs (see Figure 2.1) an opportunistic official would be tempted to engage in corruption as long as their perceived marginal benefits exceed their expected marginal costs, up to the point where marginal benefits equal marginal costs. Aggregating individual returns over all those engaged in corruption offers a lower bound on the costs of corruption. The total costs of corruption must also capture damage to the moral fabric of society and distortions in the economy that raise the cost of public services and reduce overall economic growth. In this framework, the two ways to decrease corruption are to reduce perceived marginal benefits or to increase the expected marginal costs of engaging in corrupt behaviour.

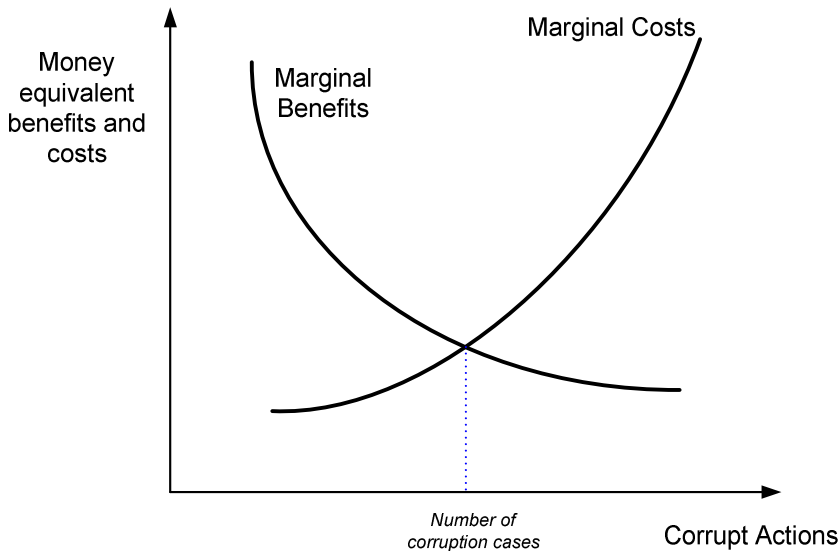


Figure 2.1: Expected Costs versus Potential Rewards from Corrupt Actions.

## Modifying the Expected Costs of Corrupt Behaviour

The expected costs for an individual considering an act of corruption include a moral component and the likelihood of being punished. But why should anyone care about being moral? Classical philosophers provide a range of answers:<sup>4</sup>

- Being true to one's own rational nature (Kant);
- Because one aspires to human fulfilment (Aristotle); or
- Because keeping one's contract with one's fellow citizens is necessary to prevent social chaos and warfare (Hobbes).

In Kant's conception, "the moral agent must have an exemplary character, one which recognizes the rational demands of duty upon him even when there are no external incentives or constraints to compel, constrain, or otherwise shape his behaviour."<sup>5</sup> Kant talks about "the Moral Law within" and "imperatives of duty." According to Kant, "we are to do our duty regardless of the consequences."<sup>6</sup> We are acting in a morally worthy fashion, and possess what Kant calls "a morally good will," only if we are "individuals who can be counted upon to do what we know we must and ought to do, even when there are no external forms of incentive or accountability in place."<sup>7</sup> In sum, we should not require external inducements or constraints to force us to behave morally.

In sharp contrast to Kantian ethics is the so-called "utilitarian" school of John Stuart Mill who recognizes that "... as fallible human beings we will not always be adequately motivated by... *moral* reasons for obeying the law."<sup>8</sup> Contemporary thinking about the historically-conditioned, cultural grounding of morality needs to be mixed with "social and political responsibilities to establish justice, equality, and... rule of law."<sup>9</sup>

On the one hand, *building integrity* supports the Kantian ethics view. Investing in ethics training, cultural awareness, formal and informal codes of conduct, reputation, ideals, core values, honour, etc. increases the "Moral Burden" of corrupt actions. On the other hand, *increasing transparency* and *improving accountability* reflect Mill's utilitarian perspective. For instance, utilitarians believe the guilty should be punished only if the punishment would serve some deterrent (or preventative) purpose. They

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<sup>4</sup> George Lucas and William Rubel, eds., *The Moral Foundations of Leadership* (Boston, MA: Pearson Education, 2004), 116.

<sup>5</sup> *Ibid.*, 184.

<sup>6</sup> *Ibid.*, 133.

<sup>7</sup> *Ibid.*, 161.

<sup>8</sup> *Ibid.*, 386.

<sup>9</sup> *Ibid.*, 159.

**Box 2.1. Emmanuel Kant and “the Moral Law within”: Lessons for Defence Officials**

The moral agent must have an exemplary character, one which recognizes the rational demands of duty upon him even when there are no external incentives or constraints to compel, constrain or otherwise shape his behaviour.

Defence officials and military officers are acting in a morally worthy fashion and possess a “morally good will” only if they are individuals that can be counted upon to do what they know they must and ought to do, even when there are no external forms of incentive or accountability in place.

consider not the punishment but the threat of punishment as most important and set the task “to find the right punishment that will serve as the optimum deterrent.”<sup>10</sup>

Policymakers can increase the threat of punishment in three ways:

1. By increasing the probability of detection;
2. By increasing the probability of conviction given detection; and
3. By increasing the severity of the punishment.

Each approach corresponds to a different component of law enforcement:

1. Systematic monitoring for violations of the law and identifying and arresting offenders (here transparency increases the probability of detection);
2. An independent court system to assess guilt (accountability increases the probability of prosecution given detection); and
3. A corrections system to administer punishment (here accountability provides for independent assessment of penalties given conviction, and the recovery of misappropriated assets).

Since law enforcement is costly, the optimal level of enforcement will likely minimize but not entirely eliminate corruption (see Figure 2.1 and Figure 2.2). Increasing transparency—investing in building defence institutions by implementing effective and efficient budgeting and accounting systems, systematic application of economic and decision tools, independent financial audits, monitoring and oversight, etc.—increases the probability that corrupt actions will be detected. Improving accountability—investing in judicial reforms such as the promotion of an independent judiciary, enforcing laws, rules and regulations, etc.—increases the probability an individual will be convicted if detected and influences the assessment of penalties.

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<sup>10</sup> Ibid., 149.

### Box 2.2. Utilitarian Theory on Rationality of Criminal Behaviour

Utilitarian theory predicts the likelihood an individual chooses to commit a crime will fall in response to an increase in either the probability or severity of punishment. Empirical work by Ehrlich (1973) demonstrates that increases in both the certainty and severity of imprisonment consistently have negative impacts on crime rates. Trumbull (1989) finds evidence that, for most crimes, certainty of imprisonment has a greater effect than severity of imprisonment. Block & Gerety (1995) find that prisoners are more easily deterred by increases in the probability of punishment (certainty) than its severity.

Collectively, these studies help explain Becker's (1968) observation that "a common generalization by persons with judicial experience is that a change in the probability has a greater effect on the number of offences than a change in the punishment." If these results apply more broadly, then strategic investments in defence institutions that increase transparency could generate powerful deterrent effects that reduce corruption in the defence sector.

*Sources:* Isaac Ehrlich, "Participation in Illegitimate Activities: A Theoretical and Empirical Investigation," *Journal of Political Economy* 81:3 (May–June 1973): 52–65; William N. Trumbull, "Estimations of the Economic Model of Crime Using Aggregate and Individual Level of Data," *Southern Economic Journal* 56 (1989): 423–39; Michael K. Block and Vernon E. Gerety, "Some Experimental Evidence on Differences between Student and Prisoner Reactions to Monetary Penalties and Risk," *Journal of Legal Studies* 22 (1995): 123–38.

## Modifying the Potential Rewards of Corrupt Behaviour

The potential reward from an act of corruption depends on the amount of resources that are under the control of the public official and the discretionary power s/he has, and is heavily influenced by the level of transparency and accountability.

The combination of high discretionary power (high marginal benefits of corruption) and low accountability (low expected costs) is considered among the most common causes of corruption.<sup>11</sup> Corruption risks increase dramatically in the absence of trans-

### Box 2.3. Expected Cost of Corruption

The expected cost to a public official, military officer or defence contractor of engaging in corrupt behaviour consists of two components:

$$\text{EXPECTED COST} = \text{MORAL BURDEN} + \text{EXPECTED PUNISHMENT}$$

Where:  $\text{EXPECTED PUNISHMENT} = (\text{Probability of Detection}) \times (\text{Probability of Conviction if Detected}) \times \text{Penalty}$

<sup>11</sup> Minxin Pei, "Government by Corruption," *Forbes* (January 26, 2009).



parency and when limited alternatives are available and officials are paid below market incomes. Alternatively, the discretionary power of defence officials is limited when the decision-making process is transparent, includes consistent and readily accessible decision criteria and measurable results, and there are multiple alternatives provided by open and fair competition (for example, in defence procurement). The potential for corrupt behaviour related to discretionary power would be further reduced if defence officials are held accountable in a systematic manner to superiors, parliamentary committees and auditors, not only for legality of procedures (financial audits) but also for objectively assessing alternative solutions (managerial audits). Efforts to reduce corruption can usefully be combined with an increased focus on the efficiency and effectiveness of public expenditures.

Finally, in order to benefit from corrupt activities, officials invest effort—and possibly money—to minimize detection. Increasing transparency and accountability increases the cost of such efforts and therefore contributes to lower corruption. It is also useful to recognise that individuals have different attitudes towards risk – some are risk seekers, while others are risk-averse. Greater risk aversion in opportunistic public officials would be associated with lower perceived marginal benefits and higher expected marginal costs of engaging in corrupt actions. Therefore, turning to Figure 2.2, highly risk averse individuals would be expected to participate in significantly lower levels of corrupt activity (at a point where their lower marginal benefit curve intersects their higher marginal cost curve).

## A Strategic Approach to Reduce Corruption

The strategic approach proposed in this compendium (illustrated in Figure 2.2) aims at reducing corruption in the defence sector by:

- Reducing perceived rewards of corrupt behaviour (reducing marginal benefits); and
- Increasing the expected costs (increasing marginal costs).

This is bound to lead to a change of behaviour of defence officials, resulting in lower numbers of cases of corruption and reduced cost of corruption to the public, as indicated in Figure 2.2.

This framework offers an approach to good governance with a special focus on integrity, transparency and accountability:

- Building integrity increases the *moral burden* of corrupt behaviour through professional codes of conduct, ethics training, education, cultural exchanges, etc. This also contributes to reducing any perceived benefits of corrupt activity.

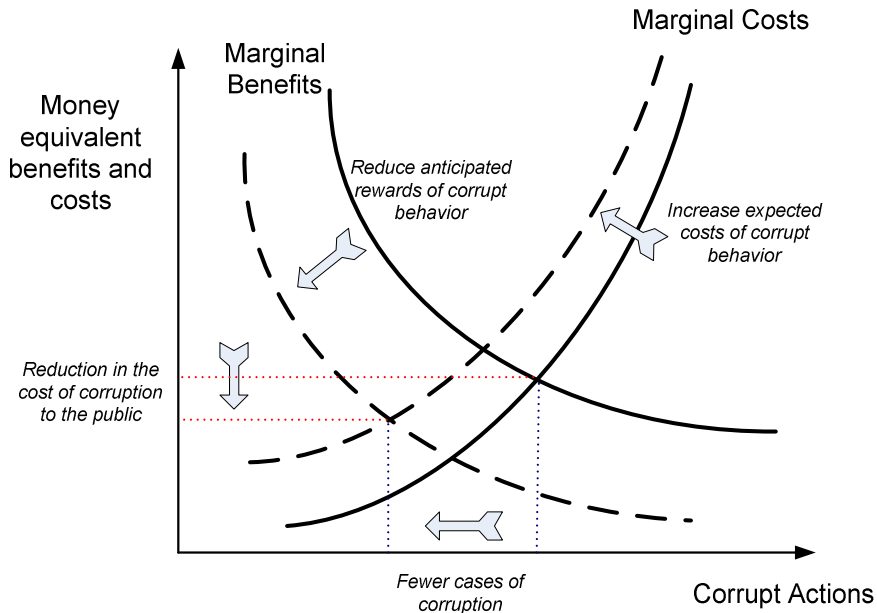


Figure 2.2: Foundations of the strategic approach to reducing defence corruption.

- Increasing transparency increases *expected punishment* by raising the probability of detection. This increases the expected costs of corrupt activity. Moreover, transparency of defence decision making, in combination with open and fair competition in appointments, career advancement, procurement of goods and services, etc., limits discretionary power and, hence, reduces the potential benefits of corruption. Defence institution building, in particular the explicit development of defence policy and strategy, planning, budgeting and resources management, is the main venue for increasing transparency, effectiveness and efficiency.
- Improving accountability through legislative and judicial reforms increases the *expected punishment* of corrupt behaviour by raising the probability of conviction if detected and the penalty if convicted. It increases the expected costs of corrupt behaviour and reduces the perceived net benefits of a corrupt act.

### Box 2.4. Empirical Evidence in Support of the Selected Approach

Setting the strategic approach to reducing corruption in defence in a good governance framework is based on solid empirical evidence. Since 1996, the Worldwide Governance Indicators project reports aggregate and individual governance indicators for 212 countries and territories over the period 1996–2008 for six dimensions of governance: voice and accountability; political stability and absence of violence; government effectiveness; regulatory quality; rule of law; and control of corruption.

The analysis of the time series for two of the newer NATO members—Bulgaria and Slovakia, which joined the alliance in 2004—reveals a strong correlation between governance and the level of corruption. As an example, Figure 2.3 presents the percentile ranking of the two countries along the dimensions of “government effectiveness” and “control of corruption.” Other data series also indicate dependence between corruption levels and other governance indicators: corruption is consistently lower when a country scores highly in regard to openness, accountability, effective government and rule of law.

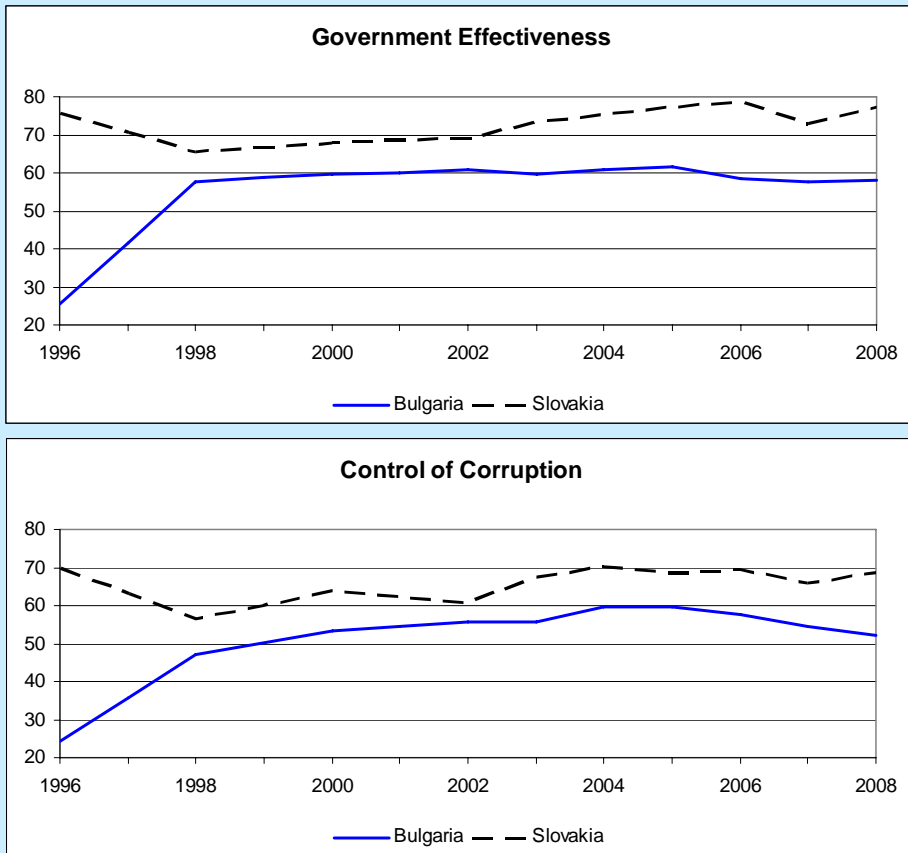


Figure 2.3: Correlation between Effective Government and Control of Corruption.

Given a country's limited defence resources, and the relative costs of building integrity, increasing transparency and improving accountability, the objective of each nation, as well as the NATO Alliance, should be to find an optimal mix of investments in integrity, transparency and accountability that minimizes corruption while preserving the efficiency and effectiveness of defence forces. This optimal mix will depend on a particular country's circumstances, costs and culture. What is considered optimal in one country may be very different in another. It must be recognized that the effectiveness of a country's investments in building integrity, increasing transparency and improving accountability partly depends on its history and can change over time.

Therefore, it is recommended that countries adopt a multi-year programmatic approach to integrity building initiatives that reduce the perceived benefits of corrupt actions and increase the expected costs. This approach can include regular assessments of institutional capabilities and responses to corruption that emphasize both the prevention and treatment of corrupt behaviour, including clear definitions and measures of success.

*Sources:* Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters VIII: Aggregate and Individual Governance Indicators, 1996-2008* (June 29, 2009), World Bank Policy Research Working Paper No. 4978; Ilin Stanev, "Daniel Kaufmann: Radical Transparency is the Best Solution for Reducing Corruption," *Capital* 29 (25 July 2009), 22–23.

## Recommendations

- Approach the problem of defence-related corruption strategically, aiming to reduce potential rewards of corrupt behaviour (reduce marginal benefits), while increasing the moral burden and the expected punishment (increase marginal costs).
- Reduce corruption through good governance, evaluating alternative approaches to deter corruption and to respond to corrupt behaviour.
- Adopt a multi-year programmatic approach to integrity building initiatives.
- Based on a country's costs and political realities, find the optimal mix of investments to build integrity, increase transparency and improve accountability that minimizes corruption risks, while preserving or increasing the efficiency and effectiveness of defence expenditures.
- Conduct regular assessments of institutional capabilities and responses to corruption and periodically review the optimality of the chosen mix of investments.