

### 4.3. Corruption phenomenon: increasing threat for the economy

$$\text{Corruption} = \text{Monopoly} + \text{Discretion} - \text{Accounting}^1$$

The large-scale spread of corruption and shadow economy are phenomena characteristic to a country in transition. Since the beginning of '90s, in the Republic of Moldova these phenomena keep intensifying. As preconditions for that could be mentioned the weakness of the newly formed state and its structures, contradictions and lack of transparency of the legislation system, dismemberment of state, inefficiency of customs service, low wages of state employees. The large spread of this phenomenon represents a threat to the security of the state.

If by the beginning of '90s one of the biggest problems for the transition countries was shadow economy, and the main objective of the state policy in this domain was supposed to be the creation of conditions for the incorporation of shadow economy into the formal one, then during the last years the problem modified into a national tragedy for a series of countries – corruption. Corruption in many cases undertook the mechanisms, structures, and functions of the state.

If at the beginning of the decade the corruption in transition countries was in a big part as a brake to the economic development, creating obstacles for local producers and pushing out the potential foreign investors, then, actually it simply blocks the reforms in the country. Any amendment of the acting legislation does not have any positive expected effects due to the impact of corruption; the economy does not develop according to market rules, there are no competition and progress in utilizing the disposable resources, state debts grow spontaneously, pauperization of the society deepens, a decrease of population's credibility in the state and a creation of a conflict situation take place.

A simple **definition of corruption** can be formulated as follows: abuse of power for private gain by the state officials.

**Main forms of corruption** are: acceptance, soliciting or extortion of bribes, patronage, nepotism, theft of public goods, causing losses to the state, political corruption, etc.

**Bribes** – in order to obtain state contracts (choice of firms, terms and conditions for contracts), assure state guarantees for credits, obtain facilities, material and financial benefits, preferential support of patronaged enterprises, shading investigated violations, non-application or diminishing penalties, obtaining licenses, exclusive rights for economic activities, for speeding-up delivering documents, obtaining political positions, employment in state structures and prestigious positions.

**Thefts** – spontaneous privatization of public enterprises, equipment, financial sources, uncontrolled utilization of enterprise funds, obtaining credits without repayment, payment of wages to non-existent employees, etc.

**Political corruption** – violation of the election legislation, financing the electoral campaigns, solving parliamentary conflicts in illegal modalities, lobbying;

**Causes of corruption** can be economic, institutional, politic, social and moral:

- The *economic* ones include: unlivable budget, low wages for state employees, delays in payment of wages;

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<sup>1</sup> Governance and the Economy in Africa: Tools for Analysis and Reform of Corruption, IRIS, University of Maryland at College Park

- The *institutional* ones are: lack of real will to fight corruption, lack of strategy in this field, high level of discretion in the work of legal bodies, an inadequate accounting system, lack of transparency in the legal system, weak state policy generating rent-seeking, career promotion without real performance.
- *Political* causes include: transformation of fighting corruption into fighting political opponents, interest of some political groups in the economic and financial collapse of the state, thus willing to return to the old dictatorial system, import of corruption.
- *Social and moral* causes: demoralization of the society, ethical values erosion caused by the corruption amongst the top level employees, insufficient information of population, insufficient work of mass-media, public tolerance.

*Corruption can have a **strong impact on the economic, political, social and ecological security of the state.***

*Economic consequences* of corruption are:

- Growth of transactional costs, especially for economic activities in small business, diminishing competitiveness for goods and services;
- Discouragement of investments and innovational ideas;
- Growing costs and diminishing of public projects quality;
- Sliding of economy towards the underground sector;
- Unfairness, non-loyal competition by using state institutions as repressing tools, falsification of information regarding competitors, technical and industrial espionage, racketing, signing monopolistic agreements, etc.
- Fund embezzlement, diminishing economic efficacy;
- Macroeconomic instability, vulnerability of the country to economic crises.

*Social consequences:*

- Creation of additional tax burden;
- Strong negative impact on the vulnerable strata of the society, having no political influence vulnerable strata often have to face a heavier social pressure;
- Reduction of quality of goods and services;

*Consequences on the state political security:*

- Formation of an economic and political clan, which imposes to the society its wish, regardless to the needs of the society, and contributing to the huge growth of state indebtedness;
- Diminishing payments to the budget result in the failure of the small business supporting, social, educational, health and environment policies, as well as in unfair work retribution in the budget waged sphere;
- Paralysis of state institutions, affection of citizens' rights and constitutional guarantees, discredit of the state system, lack of respect towards the state on behalf of the population;
- Deterioration of economical and political security of the state.

*Environment consequences:* Deterioration of the environment due to the fact that the society is imputed interests of certain separate groups - immediate profits without redemption of environmental losses.

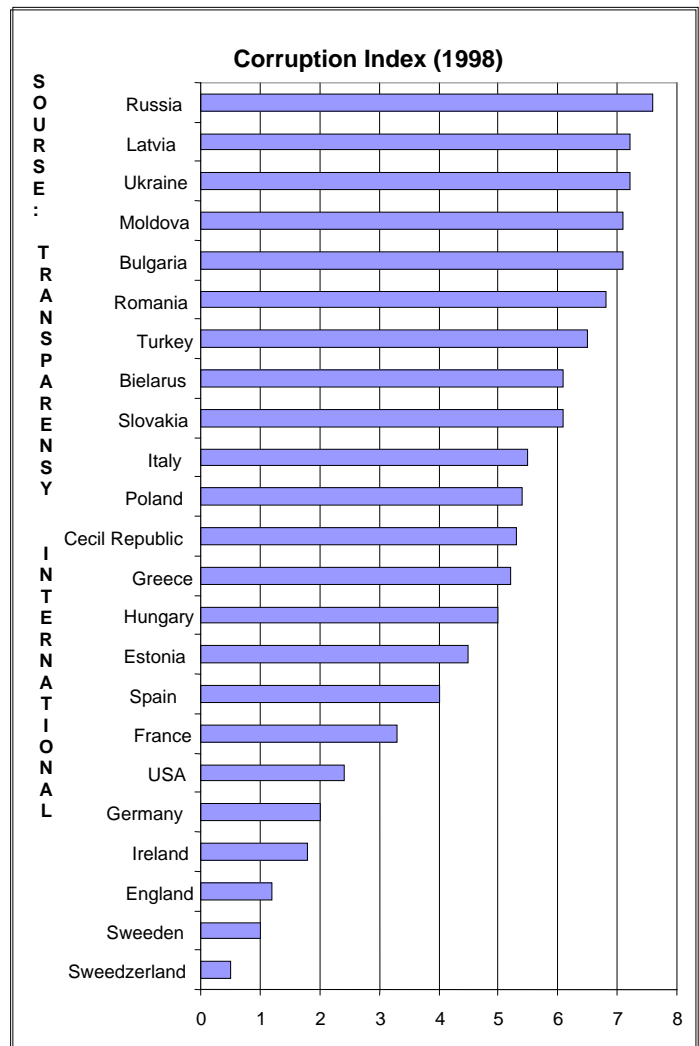
The results of numerous cross-countries comparative studies of shadow economy indexes and economic performance (Heritage Foundation, Transparency International, Freedom House

Rankings) show a quantitative relation between the growth of the degree of corruption of the country, the volume of illicit transactions and economic decline.

*Corruption index*

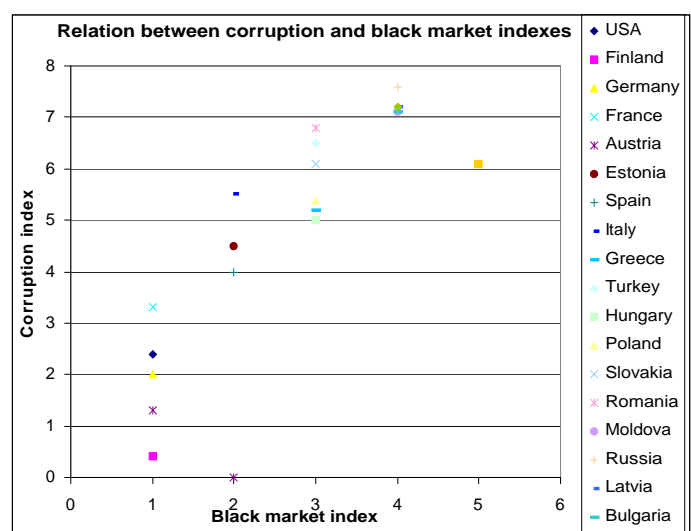
(Transparency International) in the countries of the European Union fluctuates from 0.54 in Denmark (meaning a practical lack of corruption) to 5.5 in Italy, total corruption index corresponding to the value of 10. The average for EU oscillates around 2.5. For the countries in transition, which hope to join in the EU, this index is at least 2.5 times bigger, reaching from 4.5 in Estonia to 7.6 in Russia.

On this scale Moldova is placed together with Bulgaria after Romania, and is followed by the Ukraine. However, it should be mentioned that the evaluation of the corruption index is more likely based on the evaluation of the level of perception of corruption by the population, rather than on the evaluation of its real dimensions. Therefore, in a traditionally more democratic country this index can be overestimated. At present, there are attempts to develop the Bribery Propensity Index.



High level of corruption in transition countries implies growth of black market

(Heritage Foundation), the index of black market varying from its minimum -1 in Austria, France, Germany, Finland, 2 - in Italy, Spain, Estonia, 3 - in Greece, Turkey, Hungary, Poland, Romania, 4 - in Latvia, Bulgaria, Lithuania, Moldova, Ukraine, Russia, and reaching its maximum of - 5 in Georgia and Belarus. Calculations also show a strong inverse link between the degree of corruption and GDP per capita. An inverse relation between corruption index and the index of economic performance in transition countries persists, the latter having as basic



components the politic system, the degree of mass-media freedom, the rule of law, the degree of public administration, the development of private sector. On the picture the relation between these two indexes can be clearly seen.

Freedom House Ranking - composition								
	political progres	ind.civil society	independ. mass media	legal system	public ad- ministr.	privati- zation	econ. perform.	privat share in GDP
Albania	4.25	4.25	4.75	4.75	4.75	3.75	4.25	75
Armenia	5.5	3.5	5.25	4.75	4.5	4	4	50
Belarus	6	5.25	6.25	6	6	6	6	15
Bulgaria	3.25	4	3.75	4.25	4.25	5	5.75	45
Croatia	4	3.5	4.75	4.75	4	4	3.75	50
Czech Republic	1.25	1.5	1.25	1.5	2	2	1.75	75
Estonia	2	2.25	1.75	2.25	2.25	2.25	2	70
Hungary	1.25	1.25	1.5	1.75	1.75	1.5	1.75	70
Latvia	2	2.25	1.75	2.25	2.5	2.5	2.5	60
Lithuania	2	2.25	1.75	2.25	2.5	2.25	2.75	65
Moldova	3.25	3.75	4	4.25	4.25	4	4	40
Poland	1.5	1.25	1.5	1.5	1.75	2.25	1.75	60
Romania	3.25	3.75	4.25	4.25	4.25	4.5	4.75	60
Russia	3.5	3.75	3.75	4	4	3	4	60
Slovakia	3.75	3.25	4.25	4	3.75	3.25	3.5	70
Slovenia	2	2	1.75	1.75	2.5	2.75	2	45
Ukraine	3.25	4	4.5	3.75	4.5	4.25	4.25	40

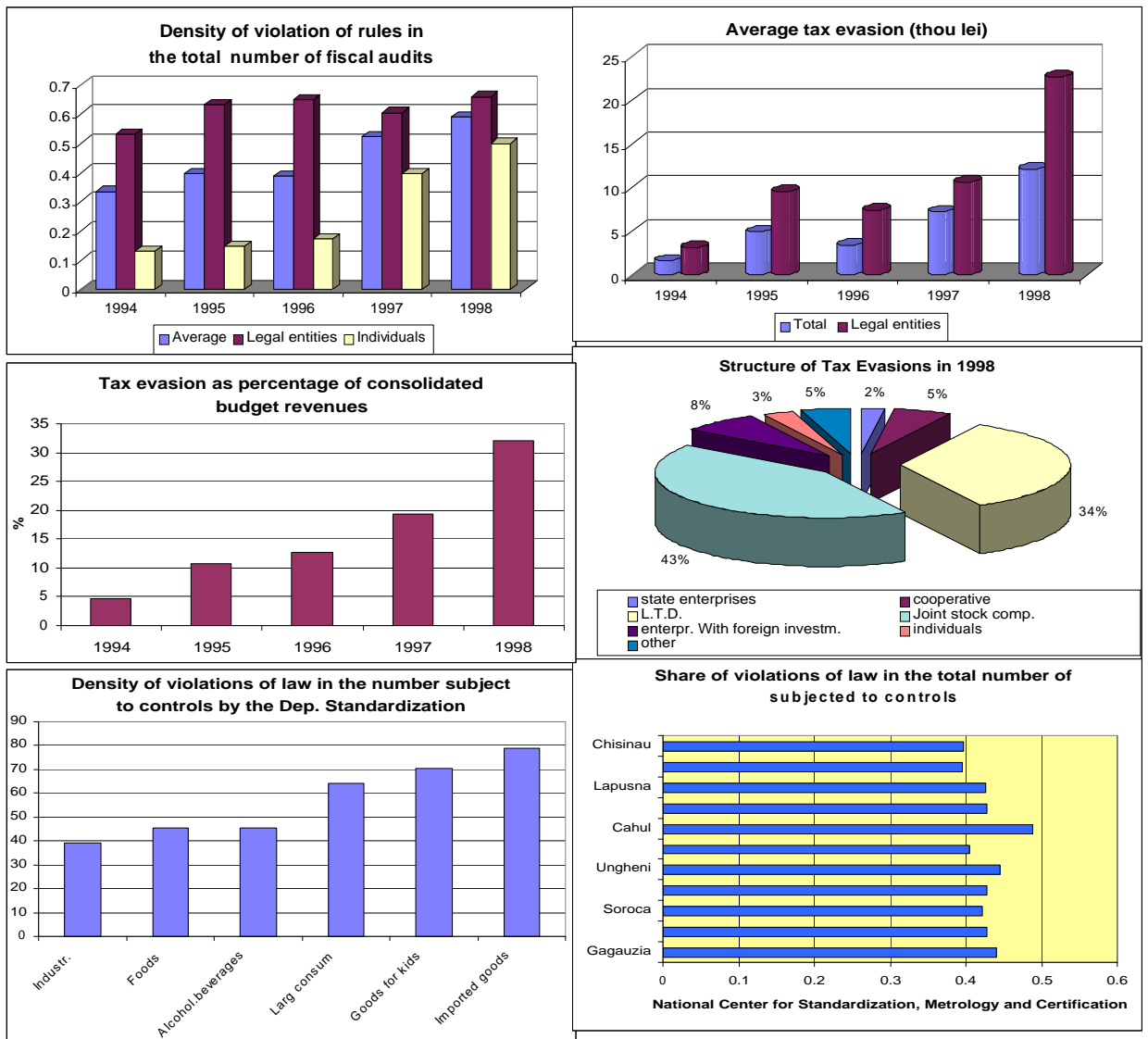
Corruption is a *self-generating process*. If the state employees do not receive their wages during 4-5 months, bribes become the only stable source of their income. Then an evolutionary shift takes place into a vicious circle: corruption → economic decline → insufficiency of sources for the budget → delays in wage payment for state workers → growth of corruption. Moreover, it is easier to blackmail and force a person perceived in corruption to repeat corruptive actions. Unwillingly, this person starts to belong to a strong repressing system.

Therefore, starting from 1998, official data regarding the results of audits and inspections became more “optimistic”. In 1998 there were registered 2910 violations of economic and financial legislation, by 244 less than in 1997, losses being estimated at 103 million lei. Chisinau City Police marked a decline by 13% in the number of registered crimes, although 298 cases of concealing crimes were discovered. There were collected 11% fewer taxes in Chisinau (853 million lei). The 10% decline in industrial production and an 18% inflation could not explain this phenomena. Two parallel processes take place: a) hiding or closing criminal files, b) decreasing rate of small crimes and growing of the big ones.

Unfortunately, the actual situation in the Republic of Moldova, as well as in many other countries in transition, does not contribute to an increase of credibility of Moldova as an economic and political partner. The share of underground economy got striking proportions and tax evasion raises continuously. The lack of control upon state employees’ activity and low enforcement, as well as delays in payment of wages to the latter, contributed to the extension of corruption and increasing level of the economic crime in the Republic of Moldova.

According to our estimates, the tax evasion in the Republic of Moldova grew up from 4% of the consolidated budget revenues in 1994 to 20% in 1997 and 32% in 1998. The average evaded tax rose from 7 thou lei per taxpayer in 1997 (10 thou lei per legal entity) to 12 thou lei in 1998 (23 thou lei for legal entity). The rate of rule breakers in the total number of entities subjected to audits grew from 305 in 1994 to 51% in 1997, and 57% in 1998.

In 1998 the collaborators of the Department of Financial Control and Revision accomplished 9506 controls, by 2353 less than in 1997. Despite of that, the total sum of losses caused by illegal expenditures to the economic agents and state, shortages and embezzlements amounted to 87.4 mil. lei, in comparison to 36.3 million lei in 1997 (a 2.4-fold growth).



Data of the National Center for Standardization, Metrology and Certification show that the rate of law violations detected during the controls of consumer goods varied from 40% for foods to 70% for the goods for children. In the division – local-imported goods most of all account for the imported goods – 79%. The quality of goods varies throughout the country.

Data of the scientific-practical conference “Organized crime and shadow economy in the Republic of Moldova” held under the aegis of the Ministry of Internal Affairs of the Republic of Moldova, Academy of Police and the Independent Association of Criminology, shows that corruption in Moldova achieved striking proportions. Lack of state power creates conditions for emerging mechanisms and structures that quickly can substitute the state structures.

*Ordered murders:* an existing practice of repeated (2-3 times) temporary releases from jail of the convicted individuals, with a view to commit an ordered murder, is recognized. There are about 300 criminal groups, 35 criminal clans, which control the economic, political, and social performance of the country. Thus, the problems of non-payments are rather solved by pressures on behalf of criminal structures, playing the role of informal courts, by charging 50% of the indebted amount.

On the territory of Moldova there are four channels of *drug trafficking*. Only the monthly traffic of heroin is estimated to reach the volume of 150-200 kg (for information: the wholesale price of 1 kg of heroin amounts to \$1.5 thou in Pakistan, 10 thou \$ in Turkey, 40 thou \$ in England, the retail price reaching \$120 thou). On the territory of Moldova there are clandestine

laboratories producing drugs based on local, much cheaper technologies, and this presents an essential threat for the local evidently poorer population. During the last five years the estimated number of addicted persons rose from 3 thou to 60 thou people. Only in 1998 their number grew 5 times in comparison to 1997. Drug industry is highly concentrated, about 60% of drug transactions are carried out by local Gypsies (for information: Gypsies make up about 0.3% of the total population of Moldova).

*The annual volume of narco-business* in Moldova is estimated at \$200–250 million, this figure *exceeding 3.5-4 times the annual direct foreign investments* in Moldova. It is clear that the “efficacy” of running this brunch is definitely “higher”. Possibilities to corrupt the state officials are extremely big. That is why the list of narcotic and psychotropic substances proposed by the specialists of the Committee of Drug Control undergone essential “modifications” by the moment of its adoption and publication in the “Official Monitor”. A number of substances, which can be easily produced on the territory of Moldova, vanished from the above-mentioned list. That is why the custom service does not have an elementary facility of drug detecting dogs, there is not any database on drug trafficking, or an unique informational system of the force ministries and the criminal files do not “reach” the court (their total number having diminished from 15 in 1996 to 10 in 1997 and 9 files in 1998). That is why extremely expensive cars with four degree of protection are used for the transportation of drugs.

*Smuggling*: According to the data of custom service, the detected volume of smuggled goods grew from 2.7% of the total export-import in 1997 to 10.6% in 1998. During the same time, the number of criminal files reaching the court diminishes continuously, criminal files are closed (from 28 open criminal files no file was investigated in 1998).

Data regarding the *volume of illegal export-import transactions* are more relevant. An accomplishment of a cross-checking of Moldovan and Ukrainian information regarding Moldovan exports to Ukraine shows that the data from the Ukrainian side is almost double. This can not be explained solely by the “role” of Transnistria. The same situation takes place in the relationships with Russia. It is little probable that workers of the Ukrainian and Russian custom services are likely to be more honest than those from Moldova, therefore the real distortions could be even greater.

This fact could be not so surprising, if to take into account the current situations when custom services detain full trains with illegally transported goods, and after a call from the “top officials”, they are constrained to let the train move ahead.

The spectrum of corrupted actions characteristic to the *management of public property, accumulation and utilization of financial resources, execution of state control* is quite wide. Amongst the most characteristic to Moldova can be mentioned the following:

- Improper formation and utilization of the state budget funds, lack of methodological norms of their formation and utilization, illegal financing of structures and activities not envisioned in current legislation;
- Inefficient and irrational utilization of budget resources by the state-owned institutions due to improper organization of state-owned budget institutions, financing that leads to laundry of enormous amounts of state funds, improper utilization of investments and donations, including in foreign exchange, as well as their transfer to certain commercial structures that use them for a long time or for a symbolic fee;
- Irrational and inefficient utilization of investments and credits as a result of a bad allocation of state resources, improper utilization of investments and credits given to economic agents;
- Evasion of taxes, fees and other compulsory payments due to the state budget;
- Violation of price discipline, especially ungrounded increase of prices;

- Waste of public property as a result of intentional non-accounting of certain objects of state property, illegal rent of premises and equipment, ungrounded or illegal privatization of state property, violations while purchasing of 20% of shares by the personnel of the enterprises without any tender, diminishing the value of property, and excluding the former staff, including outsiders in privatization process, as well as unreal evaluation of property;
- Irrational and inefficient contracts with certain economic agents, especially with non-government structures;
- Unsatisfactory accounting of financial and economic activity which enables government officers to freely dispose of the state property, including budget resources, to their personal interests.

In a short while Moldova transformed into a corrupted and kleptomanian state, with a mafia-driven psychology and culture, and immoral nepotism. How could be explained the fact, if not through corruption and lobbying, that the legislation of Moldova even does not include the term “racket”, there are not foreseen special measures towards prostitution, it is not adopted a special system of gambling taxation? Moldova, being over-indebted for energy resources, imports natural gas at prices much higher than international ones, and does not even ask for charges on the transit of natural gas through its territory (for information: the payments for the transit of gas through the territory of Ukraine exceed the GDP of Moldova). More than this: Moldova does not have gas counters at the entrance and exit from its territory. The only explanation is a group interest, which is completely opposite to the interests of the whole society.

This situation is characteristic to autocratic states, where practice is missing of self-organization, based on horizontal links, reciprocal credibility and solidarity; in this type of states for a long time a bureaucratic hierarchy based on norms, mainly vertical relations of domination-subordination and tutelary-dependence were maintained.

Fighting corruption generates *immediate profits*. Revenues from fighting corruption exceed many times the costs. According to some Western estimations, the expenditures of L1 in fighting corruption at the local level generate on average L23, and about L250 on the international level<sup>2</sup>.

The materials of the United Nations Commission for crime prevention show that the above mentioned phenomenon has widespread in the Central and East Europe during the last decade. These kinds of problems are included into the programs of seminars and congresses of many international bodies (*INTOSAI, EUROSAL, SIGMA, Accounting Court of the EU, World Bank, Working Group on bribes OECD, International Monetary Fund, etc.*).

The Defense Supreme Council of Romania adopted a proposal on establishing the National Institute for studies of corruption and organized crime under the Academy of Romania.

***The goals of fighting corruption*** can be different:

- short run efficacy in the private sector;
- long run dynamic efficacy, economic growth;
- social equity, political legacy.

***The durable strategic directions of fighting corruption in the Republic of Moldova*** should include deregulation, privatization, transparency, institutional reform, improvement of the enforcement system, reduction of the monopoly force in all spheres, clarifying the degree of discretion in the activity of decision makers.

Implementation of a ***policy fighting corruption*** needs the reform in legislation, the institutional reform, improvement of the system of regulation of fiscal audits, reduction of the public tolerance:

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<sup>2</sup> I. Bogdan, Corruption and economic crime, “Curierul Economic”, 45(347)

*Legislation reform:*

- Appealing for assistance on behalf of the international institutions in fighting corruption and economic crimes, applying for an external system of monitoring;
- Appealing to projects financed through foreign technical assistance to perform a juridical expertise of laws and amendments proposed for adoption, improving the legal system, removing of contradictions, double meanings, etc.;
- Perfecting of preventive anti-crime measures;
- A clear definition of a penalty system for law breakers;

*Amelioration of fiscal control procedures:*

- Simplification of regulations of state controls and audits;
- Systematization and unification of the work carried out by different audit agencies;
- Publishing a clear information regarding controls, rights and obligations of control agencies;
- Establishing a unit for registering and regulating the number of controls of the same enterprise;
- Reforming the fiscal and accounting systems, simplification and ensuring its transparency;
- Perfecting the qualification level of control and audit personnel;
- Publishing fiscal information, transparency of preparation and execution of state budget;
- Introduction of a mandatory tender system for public procurements.

*Institutional reform:*

- Reduction of the number of state institutions, reduction of staff;
- Substitution of the procedure of personal visits for solving problems by using mail, including e-mail system;
- De-politization of Government, introduction of an obligatory system of professional promotion on the base of performance and contest;
- Introduction of a clear and definite system of ethic standards for the state employees;
- Creation of independent institutions authorized for investigations the accusations in corruption.

*Reduction of public tolerance:*

- Coordination of efforts of educational, religious organizations and mass-media in an anti-corruption campaign;
- Assuring transparency of financing political parties;
- Training journalists in promoting a manner of balanced reporting, introduction of an ethic code for journalists;
- In order to improve the credibility of population in state structures – creation of a unique body for complaining about inadequate behavior of policemen, workers of custom service, fiscal auditors, etc.

As *immediate measures for fighting corruption* the following suggestions should be considered:

- Elaboration of a strategy for fighting corruption in terms of ministries and main directions: public procurements, public campaigns' management, urban planning, fiscal administration, customs reform, legislation;
- Formation at the national level of a coordinating body responsible for the implementation of the strategy for combating corruption;
- Identification of a number of key-agencies in the domains where a concentration of efforts is required to combat corruption during the first year;
- Applying of income declaration procedure for state employees, starting from the top level;
- In countries with a high level of corruption, where any attempt to fight corruption is treated as discrediting political opponents, a strategy of "detecting" corrupted officials at the top level in the ratio represented by parties in the Parliament (existing algorithm 2+2+1) could be applied. In order to gain the credibility of population, the cases should be proceeded publicly, by announcing the punishment of the law breakers, and the directions where obtained money are spent (pensions, wages, repayment of debts, etc.).
- An immediate installation of gas counters at the entrance and exit from the territory of Republic of Moldova.

As a set of *measures to combat corruption at the customs service* the following steps could be considered:

- a) A temporary introduction of army in customs service;
- b) Examining the possibility to transfer the customs service in private sector;
- c) Elimination of politic influence in the customs service;
- d) A decent remuneration of customs officers;
- e) Construction of customs service buildings, service modernization;
- f) Minimizing the discretion in decision making;
- g) Applying a contest system in hiring employees, training custom officers (expertise techniques, responsibilities, classification of tariffs, using computers);
- h) Enhancing fluidity of personnel within the departments for custom service control;
- i) Setting up a modern informational system;
- j) Carrying out of cross-checking information;
- k) Using X-rays in custom service;
- l) Making additional random controls (5% of total) of documentation and goods by special groups after passing the customs.

**Conclusion.** The corruption phenomenon in Moldova expanded so much, that it practically blocks the economic development of the country. Any attempt to modify the legislation targeted to the stimulation of private sector's development, encouragement of investments and innovational activities, export promotion, solving the problem of budget deficit, external debt, problems of the social and educational sectors will be unsuccessful until drastic measures to combat corruption - the moving force of the shadow economy - are not be undertaken. In order to achieve this, it is necessary to elaborate a clear strategy of fighting the above-mentioned phenomenon, by way of appealing to the experience of international organizations.