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Corruption and Fraud: A strategic management perspective
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Corruption and Fraud: A strategic management perspective

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Corruption cost/concern

Financial Costs

Real cost

Effects on allocation and efficiency of capital

Effect on delivery of services

Cost/Concerns on Corruption

- Overall world cost estimate; US $ 1 trillion
- US Economy estimate; US $ 190 billion
- EU Economies estimate; US $ 120 billion
- African Economies estimate; US $ 300 billion
- Kenya estimate; Ksh690 billion

Implication: Without corruption most economies will not have current debts and budget deficits

Corruption as a positive impact?

- Claims that corruption greases the wheels and by-passes bureaucratic processes (Ngunjiri, 2010; Huntington, 1968; Leff, 1964)
- Macro-level country research suggests otherwise (Milgrom *et al.*, 1990; North, 1991).
- Informal payments increase cost and uncertainty and reduce investment returns (Shleifer and Vishny, 1993)

Corruption: Allocation and efficiency of capital

Corruption has negative effect on allocation and efficiency of capital

- Driver of allocation of capital to projects may be higher returns in bribes and favours
- Corruption kills incentives (Ngunjiri, 2010)
- Sands rather than greases the wheels of an economy or entity (Meon and Sekkat, 2005)
- Reducing corruption increases the efficiency of capital (O' Toole and Tarp, 2014)

Corruption as barrier to service delivery

- Corruption is disruptive to service delivery
- This cost often goes unmeasured and could be the most destructive.

Effective corruption and fraud prevention capabilities can have significant macro and micro-economic impact in any country. It can also increase visible social development.

Corruption defined

- WB (2004) extent to which public power is exercised for private gain
- TI (2003) abuse of entrusted power for private gain which hurts everyone who depends on the integrity of people in authority
- UN (2004: 24) : Act of conferring a benefit in order to improperly influence an action or decision'.
- Agency as genesis of corruption (Gambetta, 2000)
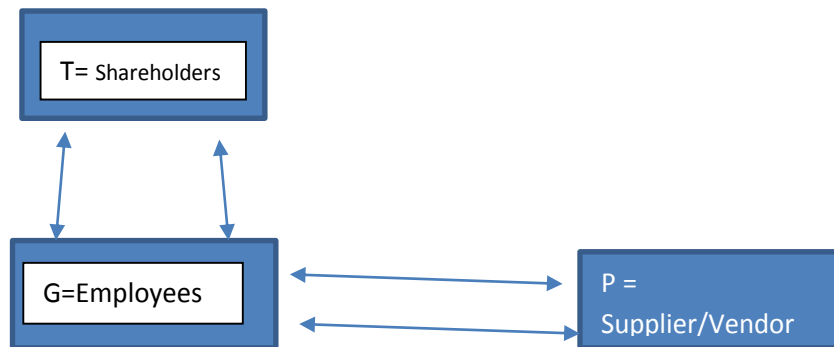- Grand corruption Vs. Petty Corruption (UN 2004)

Corruption as an embedded parasitic product of organizational processes

Corruption defined

Primitive Model

Fig 1: Primitive model of corruption based on a company

One of each pair of arrows represents things to be done according to rule of the game and the other represents situation when corruption occurs.

Adopted from Situngkir, n.d. The Structural Dynamics of Corruption: Artificial Society Approach

Corruption defined

- An understanding of corruption would require a better definition that appreciates the causes of corruption in agents and processes.
- Definitions are often by discipline. Not capturing the quintessential properties of corruption.
- Current definitions cause problems in measurement (Malito, 2014) and corruption management/control strategies.
- Etymology: imagery of decay/ utterly broken.

Current Studies

- Profound interest in area
- Studies mostly by multi-lateral institutions
- Mostly give political and economic perspectives

Current Studies

- Organizations treated as deviant (Moore, 2009)
- Criticized as too macro/high a level(Douglas, 1977; Heffernan & Kleinig; Simon, 1999)
- Betray a sense of frustration; introducing subjectivity in the studies leading to subjective descriptions e.g. as 'mind blowing', 'Cancerous phenomena...(Etyang, 2014), 'worse than prostitution'(Kraus, 1874-1936; Lumumba, 2014) etc.

Current Studies

Specific case studies show mixed results:
- oUSA: From New Deal to now; corruption reduced but position upset by the recent financial crisis
- oEU: Many initiatives at EU and country levels. Mixed results but still high corruption in some countries
- oAfrica/Kenya: Many initiatives e.g. almost every other country has an anti-corruption body. No methodology for measuring progress. Mostly deals with postmortems

Need for a change of strategy.

Epistemology/Theoretical basis of possible studies

- Need for serious theoretical foundation in the study of corruption
- Interpretivism captures the essence of social relations but could be subjective. Results from different perspectives may be difficult to reconcile
- Positivism is a good scientific base but requires well defined problem corruption problem is not well defined and lies in different disciplines
- Critical realism may be preferred as it embraces both human and non human nature of systems

Organizations, Managerialism, systems view and Actor-Network Theory

- Organizations – Theatre of corruption
- Organizations, formal or informal, states, corporations or other institutions are formed for a purpose.
- Management as a discipline is an integrating activity which coordinates and guides members of an organization to achieve the desired organizational goals.
- social exchange theory
- Complex webs of power relationships influence the social exchanges that result into uneven balance of outcomes (Mullins, 2013. P.16 & 17).
- Psychological Contracts

Management as a discipline

- Management as a discipline offers a model that provides a useful, heuristic framework within which to address specific, concrete problems and decisions (Squires, 2001).
- Concept : Organization (Organization field) within an environment and with management systems
- Four major functions:
  - Planning: Visualizing the what and how of the components of the organization;
  - organizing: the logical and effective arrangements of parts to achieve the plans;
  - leading is invoking action for movement in a particular direction
  - controlling: the alignment to keep on track.

Each of these can further be described as having an environment, input, processes, output plus feedback and feed forward processes. It is more than what can be captured in laws, regulations, policies, rules and procedures.

Strategic Management perspective

- In an expansive, competitive, complex and changing world management (executive and leadership) needs to anticipate situations and make decisions that are comprehensive and that have the scale and scope to deal with these conditions.
- Strategic management does just that; deals with the ends, ways, means and risks Lykke, Jr.'s (1997)to an organization's long term objectives
- Takes into account its resources and capabilities in the context of a dynamic, complex and uncertain environment.
- That is how an entity builds its unique and dynamic capabilities (re-generative properties), including those to protect it from malfunctions and abuse, that often culminate in frauds and corruption.
- Strategic management not a substitute of management as a discipline. It is part of
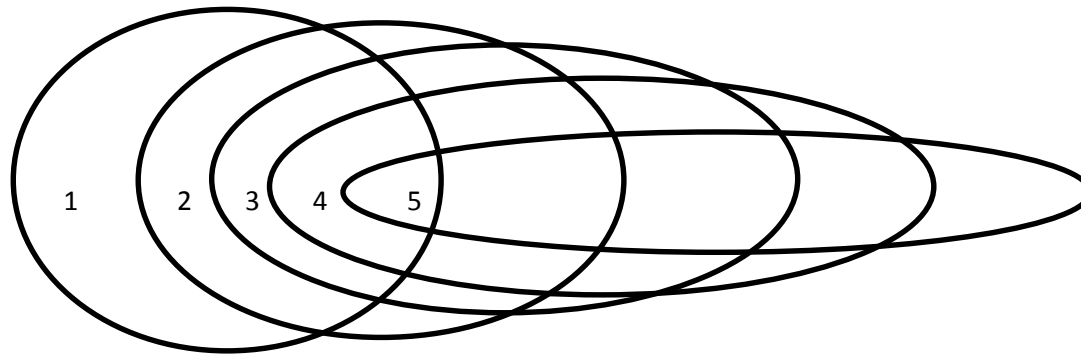
A case for systems thinking

- A system can be defined as a set of interrelated parts that function as a whole to achieve a common purpose.
- Subsystems are components of a system.
- Change in one part of the system affects other parts/processes/results
- Humans have limited cognitive and computational capabilities.
- When faced with complex and far reaching problems as those presented by organizational systems they are forced to make decisions within bounded rationality or decision heuristics (Colisk; 1996).
- Systems thinking assists in the cognitive process by focusing on the relationships between the parts forming a purposeful whole.

A case for systems thinking

- **Systems thinking> one has ability to see the system as an irreducible whole, its distinct elements, and the complex and the changing interaction between those elements.**
- **has intellectual integrity drawn from established fields such as philosophy, sociology, organization theory, feedback thought and critique on other methods of science.**
- **benefits from system dynamics methodologies for studying and modelling of complex problem situations including behavioral ones**
- **it makes latent, unknown or less obvious causal relationships and dynamic complexities.**
- **System dynamic models can incorporate soft factors such as motivation and perceptions (Caulifield and Maj, 2002)**
- **Technique is suited for conceptualizing problems that have wide scope and deep complexity as corruption has.**

Concept of Peter Senge's Causality circles

1. Political-State

2. Economical-Business Organizations

3. Social-Social Organization

4. Professional Organization

5. Individual

Systems theory base for study of corruption

- Situngkir (n.d) studied structural dynamics of corruption through two dimensions; as state capture and as administrative corruption in order to grasp the quintessence of the corruption cases
- Concluded - should not be seen as a mono-dimensional spectacle.
- Found that corruption is not merely economic phenomena
- Corruption is deeply rooted in many aspects of social dynamics, politically and economically embedded inside culture of entire societies in all social hierarchies.
- Provided results of experiments through simulation in order to construct an understanding of (distinct analytical) structural properties of corruption, giving way to consider corruption, not as an isolated phenomenon, but conclusively, <u>as an interdisciplinary problem that should be handled holistically through interdisciplinary fields.</u>

Systems theory base for study of corruption

- Georg Hegel (1770- 1831) believed that the truth about reality could not be found by studying phenomena in isolation and a higher more abstract philosophical vantage point was necessary.
- Conceived the idea of an 'enormously broad, holistic way of thinking which had room for everything-in whatever form whether logical, natural, negative feedback loop and that the tension between thesis and antithesis between the actual state and the actual eventually forces a new state or synthesis.
- Durkheim (1858 -1917) was not happy with scientific reductionism. He felt that the causal analysis (the why) of social phenomenon was necessary in addition to functional analysis (the what). The whole is more than its parts. Causal relationships may for example include the social and historical contexts although this condition is not necessarily superior to the system's individual parts but is different and requires an appropriate explanation.

Systems theory base for study of corruption

- Barnard (1938) acknowledged that there are bounds of rationality and adaptive, sequential decision making that is vital to organizational effectiveness. He advanced the systems view of the organization and said that systems of cooperation of human activity fail due to inability to accomplish stated goals/motives of individuals.
- Implication with social theory and psychological contract in mind : where management systems are weak organizations become theatres of corruption and fraud as individuals and groups seek to increase benefits from the organization when investing as little as possible.
- Parsons (1902-1979) advocated a structural functionalist approach to analyzing social systems. This approach focuses on concepts of holism, interrelationships between parts, structure, functions and needs.

General systems theory : foundations for systems theory

- Holistic view of a system may exist in many disciplines where each discipline, say in the case of corruption, politics, economics, sociology, psychology, law, accounting, human rights, education, ethics, religion (use its own elements of complexity and language unique to its environment.
- Von Bertalanffy(1968) proposed general systems theory to reconcile these and proposed that organisms be studied as irreducible, whole systems.
- Laszlo(1972): " .. there is an organized reality underlying the phenomenal world and general systems theory (GST) can guide us towards an understanding of it which systems philosophy seeks to elucidate."
- It is this underlying order and relationships that a systems approach can help identify by crossing the boundaries between different perspectives and disciplines.

A case for Actor-Network Theory (ANT)

- Systems theory can be further enhanced by Actor Network Theory (ANT) or what is referred to as the sociology of translation, a conceptual frame for exploring social-technical processes of which organizations are.
- ANT emerged in the 1980s.
- 'Actors' refers to things and identities
- does not differentiate between science (knowledge) and technology (artifact).
- Possible to incorporate any organizational process, whether scientific or social in the detailed system maps of any phenomena.

A case for Actor-Network Theory (ANT)

- ANT would be suitable in the study of corruption as it advances a relational materiality which presupposes that all entities achieve significance in relation to others such that each of the entities or agents involved in the creation and construction of the corruption systems, and their relationships are taken into account when studying the phenomena
- ANT does not subscribing to the division between society and nature, truth and falsehood, agency and structure, content and context, human and non human, micro level phenomenon and macro level phenomenon, knowledge and power. Nature and society, subjectivity and structure, fact and fiction are all effects of collective activity.

A case for Actor-Network Theory (ANT)

- ANT the agency of non humans (takes seriously machines, texts, hybrids, among others)
- Georg Hegel (1770- 1831) view that the truth about reality cannot be found by studying phenomena in isolation. ANT can be that higher more abstract philosophical vantage point that he proposed
- terms in actor and network are linked in an effort to bypass the distinction between agency and structure, a core preoccupation within sociology (as well as other disciplines) where perhaps the structural changes approach to many a corruption riddled system comes from

A case for Actor-Network Theory (ANT)

- *ANT is interested in the ways in which networks overcome resistance and strengthen internally, gaining coherence and consistence (stabilize); how they organize (juxtapose elements); and convert (translate) network elements;*

- ANT deals with power as ordering struggles with displacement in the process of translation. Translation is considered as transport with deformation as distinguished from diffusion defined as transfer without distortion.

A systems approach to anti-corruption in Kenya

- Kenya can benefit from a systems approach to financial management, prevention and detection of corruption and fraud without disruption of services; rather while enhancing services.
- Need for managerial thought.
- Build links between various organizations, standalone pieces of legislation that address corruption and fraud that offer disjointed/incomplete solutions.
- Needs system study of management processes including both people and technology
- Proper managerial discipline within and without
- Use of experts in interactive formations
- Separation of powers. Explore current legal/structural barriers

Summary and conclusion

- Corruption has profound effect on society
- Current methods of study and action too general and disjointed in different disciplines
- Need for good theoretical foundations in the study of corruption and fraud, take into account the expansive, dynamic, complex hence multidimensional nature of phenomena
- Actor-Network methodology can be applied.
- Merge all multilateral and other initiatives and have one systems based approach.