

2014

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### Recommended Citation

Scheherazade S. Rehman & Frederick V. Perry, *Corruption, Constitutions, and Crude in Latin America*, 20 LAW & BUS. REV. AM. 163 (2014)  
<https://scholar.smu.edu/lbra/vol20/iss2/2>

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# CORRUPTION, CONSTITUTIONS, AND CRUDE IN LATIN AMERICA<sup>1</sup>

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## ABSTRACT

*This paper examines the perception of corruption that exists throughout Latin America, and analyzes the importance of the institutional environment in Latin American countries, which are both richly endowed with and dependent on oil and natural gas. First, we look at corruption generally in the region and then carry our analysis by looking at various countries' GDP per capita versus several indices measuring different dimensions of countries' economic development, political progress, and social performance. We also combine corruption indices and separate them by typology of corruption in order to investigate the particular facets of corruption that pose the greatest impediment to economic growth. We do this against the backdrop of national constitutions and criminal codes that appear to outlaw corrupt behavior.*

*The paper's finding is that corruption has a differential impact on business as opposed to political environment. In investigating the business environment, we find that the "business/legal system" component, which captures corruption as perceived by a number of stakeholders, including foreign investors, indeed plays a significant role in the context of corruption and economic growth. The "electoral system" component—which combines such variables as a presence of electoral democracy, state of the country (free/not free), and whether the country is autocracy or democracy—is found to have a U-shape relationship with the measures of economic and human development. The Latin American countries that are rated as more corrupt have a larger export dependency on the sales of oil and gas. Having an electoral democracy seems to have no significant effect as all the Latin American countries enjoy approximately similar levels of*

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1. This article is a variation and adaptation of the work published in HOSSEIN ASKARI, SCHEHERAZADE REHMAN AND NOORA AFRA, CORRUPTION AND ITS MANIFESTATIONS IN THE PERSIAN GULF (Edward Elgar Pub October 2010). This work focuses on Latin America whereas the above-mentioned book focuses on the Persian Gulf.

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*human development and the laws that are supposed to guard against such behavior have little salutary effect.*

For many Latin Americans, oil is *el excrement del diablo*. . . .<sup>2</sup> In the popular imagination, and not only there, the progressive and beneficial side of the oil industry—provision of lighting, heating, travel opportunities and astonishing innovations in petrochemicals—has been tied inextricably with a darker side which has featured massive corruption . . . .<sup>3</sup>

## I. INTRODUCTION

IN Venezuela, the world's fifth largest producer of oil, the percentage of its population that is poor has increased from 43 percent in 1998, when oil traded at fifteen dollars per barrel to 53 percent in 2005 when the world price for oil was fifty dollars per barrel.<sup>4</sup> So, economic resources and terms of trade do not appear to guarantee economic development.<sup>5</sup> In the recent past, corruption scandals have caused the downfall of governments in Brazil—Collor de Mello<sup>6</sup>—and Venezuela—Carlos Andres Perez<sup>7</sup>—paving the way for the election of the populist Hugo Chavez in Venezuela. In 2008, the accounting firm KPMG conducted a survey of fraud and corruption in Mexico, and determined that 44 percent of the companies that operate in Mexico paid some type of bribe to a government official during the prior year.<sup>8</sup> Corruption is costly; it has been argued that when corruption is allowed to flourish, it is in the interest of government officials to make and increase bureaucratic hurdles and red tape, because this provides for more opportunity to demand bribes.<sup>9</sup>

Although the level of corruption and restrictions on economic freedom are high in many countries that rely heavily on oil and gas production as a source of GDP and exports, their impact on economic

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2. The devil's excrement.

3. GEORGE PHILIP, OIL AND POLITICS IN LATIN AMERICA: NATIONALIST MOVEMENTS AND STATE COMPANIES 1 (1982).

4. Alvaro Vargas Llosa, *The Case of Latin America, in MAKING POOR NATIONS RICH: ENTREPRENEURSHIP AND THE PROCESS OF ECONOMIC DEVELOPMENT* 189, 192 (Benjamin Powell ed., 2008).

5. *Id.*

6. Fernando Affonso Collor de Mello served as president of Brazil from 1990 to 1992, when he resigned to avoid impeachment over alleged influence peddling. DONALD V. COES, MACROECONOMIC CRISES, POLICIES, AND GROWTH IN BRAZIL, 1964–90 29 (1995).

7. Carlos Andres Perez was President of Venezuela from 1974 to 1979 and from 1989 to 1993, when he was accused of embezzlement and misuse of public funds. The Supreme Court found him guilty and he was imprisoned for two years. See *Carlos Andres Perez Facts*, ENCYCLOPEDIA BRITANNICA, <http://www.britannica.com/EBchecked/topic/451417/Carlos-Andres-Perez> (last visited May 2, 2014).

8. KPMG, *Encuesta de Fraude y Corrupción en México* 4 (2008), [https://www.kpmg.com/MX/es/IssuesAndInsights/ArticlesPublications/Documents/Estudios/Encuesta\\_fraude\\_en\\_Mexico\\_2010.pdf](https://www.kpmg.com/MX/es/IssuesAndInsights/ArticlesPublications/Documents/Estudios/Encuesta_fraude_en_Mexico_2010.pdf).

9. See GUNNAR MYRDAL, ASIAN DRAMA: AN INQUIRY INTO THE POVERTY OF NATIONS, VOLUME II (1968).

growth is not clear-cut. Corruption may have little or no impact on overall GDP growth of these economies because world demand for oil and gas is projected to rise steeply and thus many of these countries should continue to benefit from oil and gas sales for the foreseeable future.

Countries dependent on oil and natural gas, are faced with a number of challenges—including how to diversify their economies, attract foreign investment and integrate their economies into the global economic framework (by joining organizations such as the World Trade Organization—WTO)<sup>10</sup>—and in the process how to reduce corruption and improve their overall business environment and economic freedom.<sup>11</sup>

Many economists appear clear in their belief that from the standpoint of creating sustainable growth, eliminating corruption, and increasing economic freedom, with equal access for all players would play an important and positive role in development, because corruption and the absence of economic freedom adversely affect growth.<sup>12</sup> The United Nations, for example, is “[c]oncerned about the seriousness of problems and threats posed by corruption to the stability and security of societies, undermining the institutions and values of democracy, ethical values and justice and jeopardizing sustainable development and the rule of law,”<sup>13</sup> and has, among other things, promulgated the United Nations Convention Against Corruption.<sup>14</sup> The American economist Benjamin Powell has said:

In recent years the economics profession and policy world have begun to pay more attention to the institutional environment necessary for economic growth. Geography and other explanations for success have begun to be pushed aside as institutions have become increasingly recognized as the main driver of economic success. . . . In Washington DC people in policy circles now generally, though incompletely, acknowledge the need for private property rights and the rule of law for economic development.<sup>15</sup>

In this article, we discuss the impact of oil and gas resources on the oil and natural gas exporting countries.<sup>16</sup> Accordingly, we shall introduce a definition of corruption and provide an introduction to some manifestations of corruption in the Latin American oil-exporting countries. We will focus slightly on the law as it deals with corruption in the region; and

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10. Elisa Diehl, *Sound Policies Behind Strong Growth*, INT’L MONETARY FUND (June 7, 2007), <https://www.imf.org/external/pubs/ft/survey/so/2007/CAR066A.htm>.

11. ASKARI ET AL., *supra* note 1, at 77.

12. Paolo Mauro, *Corruption and Growth*, 110 Q.J. ECON. 681, 700–701 (1995).

13. United Nations Convention Against Corruption, Oct. 31, 2003, 2345 U.N.T.S. 41.

14. *Id.*

15. Llosa, *supra* note 4, at 2.

16. Those countries in the region that are engaged the export of oil and/or natural gas are Argentina, Bolivia, Brazil, Colombia, Ecuador, Mexico and Venezuela. CIA, *The World Factbook*, <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2241rank.html> (last visited May 2, 2014).

finally we will take a look at the impact of oil and gas dependency on corruption.

In addition, we will examine how corruption is generally measured, and then attempt to determine whether corruption is more prevalent in Latin America than in other similarly situated petroleum- and gas-exporting countries, and whether the incidence of corruption in those Latin American countries with abundant supplies of oil and natural gas is different either in scope or amount than in countries not so well endowed with natural resources. We will then take a look at how corruption affects economic and social development. We will examine the way that constitutions and laws deal with the subject.

Corruption gives rise to a vicious and troubling cycle for the countries of the region, because according to the United Nations, corruption is "insidious . . . and [has] . . . damaging effects . . . on the welfare of entire nations and their peoples. Corruption not only distorts economic decision-making, it also deters investment, undermines competitiveness and, ultimately, weakens economic growth."<sup>17</sup> In fact, corruption makes for an uneven playing field, and those with influence or money or both get things, while those who are simply deserving or good at what they do, do not. Investors—including foreign investors—who do not have confidence either in the economy, the regime, or the courts are reluctant to invest, so that much needed foreign investment is scared away. Economists' research has proven this to be the case; and this negative effect on investment has an accompanying negative effect on beneficial economic growth.<sup>18</sup> This negative impact has a knock-on effect on other areas of growth because it affects government expenditures, and economist Paolo Mauro finds corruption and political instability to be "negatively and significantly" correlated to the portion of government spending on education as a percentage share of total government spending.<sup>19</sup>

If the institutional environment is impersonal and tends to decentralize power, providing citizens with a certain amount of security regarding their property and the contracts into which they choose to enter with others, the result tends to be sustained economic growth and therefore long term prosperity. If the rules limit the capacity of the authorities or of third parties to invade the sovereign sphere of the individual by the use of superior force, the effect will usually be a framework that creates incentives for creative initiative as well as for saving and investing, thereby triggering an increase in productivity.<sup>20</sup>

Some view unfettered entrepreneurship as both a measure of and a means of combating corruption. Entrepreneurship can be either con-

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17. UN OFFICE ON DRUGS AND CRIME, *THE GLOBAL PROGRAM AGAINST CORRUPTION: UN ANTI-CORRUPTION TOOLKIT*, 5 (3rd ed., 2004).

18. Mauro, *supra* note 11, at 700–01.

19. *Id.*; Alberto Ades & Rafael Di Tella, *The New Economics of Corruption: A Survey and Some New Results*, in *COMBATING CORRUPTION IN LATIN AMERICA* 22 (Joseph S. Tulchin & Ralph H. Espach eds., 2000).

20. Llosa, *supra* note 4, at 193.

structive or parasitical, according to how the rules that govern economic life determine the payoffs to different entrepreneurial activities.<sup>21</sup> This idea of parasitic entrepreneurship has been defined as a “tendency to seek profits and alter market conditions by political means.”<sup>22</sup> Some say that corruption has always existed; at least as long as human social organizations have existed.<sup>23</sup> Corruption is generally considered pervasive around the world, and no region of the world is considered immune from it.<sup>24</sup> It is also often said that countries endowed with heavy deposits of natural resources, especially petroleum reserves, are especially susceptible.

What is “corruption?” What do the measurements tell us about how much of it goes on and where? There are a variety of measurement indices used to measure corruption and a number of definitions used. Many such definitions were devised by international organizations, primarily with the view to stamping out corruption,<sup>25</sup> and these organizations engage in a myriad of activities toward this end, including measuring states’ compliance with their agreements to implement anti-corruption legislation and campaigns within their boundaries.

The most commonly used definition by U.S.-based international lawyers is “the abuse of public office for private gain.”<sup>26</sup> Those same lawyers of course argue over the definition of each of the words in the foregoing definition and their implication because they generally use such definitions to bring charges or defend against such charges before courts or other decision making institutions with the authority to mete out punishments.

For the World Bank, corruption is seen as:

[T]he abuse of public office for private gain. This private gain could be in the form of money or favors for the benefit of family or friends—or for the benefit of special interest groups such as a political

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21. William J. Baumol, *Entrepreneurship: Productive, Unproductive, and Destructive*, 98 J. OF POL. ECON. 893, 894 (1990).
  22. STANISLAV ANDRESKI, *PARASITISM AND SUBVERSION: THE CASE OF LATIN AMERICA* 77 (1969).
  23. ASKARI ET AL., *supra* note 1.
  24. Press Release, Transparency Int’l, *Corruption Threatens Global Economic Recovery, Greatly Challenges Countries in Conflict*, (Nov. 17, 2009), *available at* [http://www.transparency.org/news/pressrelease/20091117\\_corruption\\_threatens\\_global\\_economic\\_recovery](http://www.transparency.org/news/pressrelease/20091117_corruption_threatens_global_economic_recovery).
  25. United Nations Convention Against Corruption, Oct. 31, 2003, 2345 U.N.T.S. 41; Organisation for Economic Cooperation and Development, *Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*, Nov. 21, 1997, 37 I.L.M. 1, *available at* [http://www.oecd.org/daf/anti-bribery/ConvCombatBribery\\_ENG.pdf](http://www.oecd.org/daf/anti-bribery/ConvCombatBribery_ENG.pdf); Inter-American Convention Against Corruption, Apr. 29, 1996, 35 I.L.M. 724; *Annual Integrity Report: Fiscal Years 2005–2006*, THE WORLD BANK, <http://documents.worldbank.org/curated/en/2006/06/7538030/annual-integrity-report-fiscal-years-2005-2006> (last visited May 2, 2014); *Governance & Anti-Corruption*, THE WORLD BANK, <http://go.worldbank.org/KUDGZ5E6P0> (last visited May 2, 2014).
  26. JOHN W. HEAD & DAVID FRISCH, *GLOBAL BUSINESS LAW: PRINCIPLES AND PRACTICE OF INTERNATIONAL COMMERCE AND INVESTMENT* 651 (2nd ed. 2007).

party seeking to obtain or retain power. Such behavior by persons concerned with the procurement process often leads to economic losses for the public. Thus, many lose for the benefit of a few.<sup>27</sup>

Further, the UN believes that “[c]orruption is one outcome of poor governance, involving the abuse of public office for private gain.”<sup>28</sup> The International Monetary Fund (IMF) also “views these two concepts as “closely linked” and says that “a poor governance environment offers greater incentives and more opportunities for corruption.”<sup>29</sup>

There are now also a number of private definitions used to measure and indicate global corruption. In February of 2006 the African Development Bank Group, Asian Development Bank, European Bank for Reconstruction and Development, European Investment Bank Group, International Monetary Fund, Inter-American Development Bank Group and the World Bank Group met to establish a Joint International Financial Institution Anti-Corruption Task Force, whose charge it was “to work towards a consistent and harmonized approach to combat corruption in the activities and operations of the member institutions.”<sup>30</sup>

The members of the task force recognized that: “[c]ritical to the success of a harmonized approach is a common understanding of the practices prohibited.”<sup>31</sup> Accordingly, the task force agreed that for them the following would be the “standardized definitions of fraudulent and corrupt practices” to be used by them for investigating and measuring such practices with an eye to stamping them out within the states covered by their member institutions:<sup>32</sup>

- A corrupt practice is the offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence improperly the actions of another party.
- A fraudulent practice is any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a party to obtain a financial or other benefit or to avoid an obligation.
- A coercive practice is impairing or harming, or threatening to impair or harm, directly or indirectly, any party or the property of the party to influence improperly the actions of a party.

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27. WORLD BANK, STRENGTHENING WORLD BANK GROUP ENGAGEMENT ON GOVERNANCE AND ANTICORRUPTION 67 (Mar. 21, 2007) available at [http://www-wds.worldbank.org/external/default/WDSPContentServer/WDSP/IB/2007/03/22/000020439\\_20070322090727/Rendered/PDF/390550replacement.pdf](http://www-wds.worldbank.org/external/default/WDSPContentServer/WDSP/IB/2007/03/22/000020439_20070322090727/Rendered/PDF/390550replacement.pdf).

28. *Id.* at i.

29. *The IMF and Good Governance: Factsheet*, INT’L MONETARY FUND (Mar. 18, 2014), available at <http://www.imf.org/external/np/exr/facts/pdf/gov.pdf>.

30. INT’L FIN. INSTS. ANTI-CORRUPTION TASK FORCE, UNIFORM FRAMEWORK FOR COMBATING FRAUD AND CORRUPTION (2006), available at <http://www.afdb.org/fileadmin/uploads/afdb/Documents/Generic-Documents/30716700-EN-UNIFORM-FRAMEWORK-FOR-COMBATTING-FRAUD-V6.PDF>.

31. *Id.*

32. *Id.*

- A collusive practice is an arrangement between two or more parties designed to achieve an improper purpose, including influencing improperly the actions of another party.<sup>33</sup>

As can be seen from what appears below, corruption appears to be pervasive throughout the Latin American region. Some might say it is because there are no rules in these countries, or those rules and laws that do exist are simply too primitive fully to deal with issues like sophisticated or comprehensive corruption. As will be seen, however, nothing could be further from the truth. Most countries do indeed have a highly developed set of laws and rules that very clearly outlaw corruption.<sup>34</sup> In fact, most countries in the region outwardly accept the connection between corruption and stunted economic growth; and they accept that a country's natural resources belong to the state and are to benefit its citizens.

## II. CORRUPTION IN LATIN AMERICA: THE GENERAL PERCEPTION

For decades many have acknowledged that corruption exists in Latin America in a very deep and pervasive way, though it has not been until recently that researchers have tackled this issue in order fully to define it, expose its manifestations, and suggest ways to combat it.<sup>35</sup> Whenever a sexy or juicy high-profile case of corruption is uncovered, it makes the headlines. People are duly scandalized by it; and this occurs with frequency in Latin America. However "[b]eyond the more high profile cases—the tips of real and imagined icebergs—substantial evidence suggests that in much of Latin America corruption permeates daily life."<sup>36</sup> And this corruption is "often the rule rather than the exception," tainting the acquisitions of varied licenses and permits and in dealing with routine traffic infractions.<sup>37</sup> The perception of Latin America in the industrialized nations of the world was formed early and has remained.

In the late nineteenth century, and then growing inexorably in the twentieth, the industrialized world, especially the United States and the United Kingdom, began to engage in exploration and the exploitation of oil concessions in Latin America. This was a risky proposition for them, but world demand was growing and some made large profits. Others did not do so well.<sup>38</sup> From the very beginning, it was clear to those foreign companies that corruption was rampant and bribery was the watchword

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33. *Id.*

34. See Lei No. 12.846 de 1 de Agosto de 2013, Diário Oficial da União [D.O.U.] de 2.8.2013 (Braz.) available at [http://www.cov.com/files/upload/E-Alert\\_Attachment\\_Brazilian\\_Clean\\_Companies\\_Act\\_Original.pdf](http://www.cov.com/files/upload/E-Alert_Attachment_Brazilian_Clean_Companies_Act_Original.pdf) (Clean Company Act).

35. Charles H. Blake & Stephen D. Morris, *Political and Analytical Challenges of Corruption in Latin America*, in CORRUPTION & DEMOCRACY IN LATIN AMERICA 10 (Charles H. Blake & Stephen D. Morris, eds., 2009).

36. *Id.* at 2.

37. *Id.*

38. See PHILIP, *supra* note 3, at 12–14 (1982).



of the day if they expected to get much accomplished. As an example, in Peru: “[t]he great advantage of foreign firms was that . . . they were prepared to pay bribes.”<sup>39</sup>

With respect to Bolivia, the British Minister reported in the early twentieth century, in connection with the negotiation for oil concessions that “[b]lackmail is a thriving business and gives occupation and a means of livelihood to Senators, Deputies and others who have studied it . . . to a fine art.”<sup>40</sup> The same was true in Venezuela and elsewhere in the region.<sup>41</sup> The foreign oil companies were complicit in corruption. Many times the Latin American nationalists in their various countries believed—and often still do—that the foreign oil companies wished to keep the governments of the region weak or corrupt so that they could more easily get what they wanted—lucrative concessions for exploitation—through bribery.<sup>42</sup>

In the early 1900s, British Lord Cowdrey, then head of the Mexican Eagle Oil Company, a British oil company, received a letter from his envoy who was exploring the possibility of negotiating concessions for British oil interests in South America, which stated that:

I have no doubt that you realize that the sort of concession that we are trying to get does not appeal to any government and that it is very difficult to obtain it in a country enjoying a real parliamentary system; it is to my mind only easy in countries of a one man government like Mexico under President Díaz,<sup>43</sup> Venezuela under Gomez<sup>44</sup> or Columbia under Reyes.<sup>45</sup>

To one degree or another, these countries have established subsidized housing, education and other programs for some decades, which of course amount to a way of sharing oil revenues with the population.<sup>46</sup>

39. *Id.* at 32.

40. *Id.* at 33.

41. *Id.* at 33 (citing FO 371 A 2334/2334/55, Annual Report for Bolivia (1930)).

42. *Id.* at 32.

43. José de la Cruz Porfirio Díaz Mori (1830–1915) was President of Mexico from 1876 to 1911, except a four-year term served by a political ally. Díaz was overthrown in the Mexican Revolution of 1910 and forced into exile in France in 1911. *Biographies: President Porfirio Díaz*, PBS.ORG, [http://www.pbs.org/kera/usmexicanwar/biographies/porfirio\\_diaz.html](http://www.pbs.org/kera/usmexicanwar/biographies/porfirio_diaz.html) (last visited May 2, 2014).

44. Juan Vicente Gómez Chacón (1857–1935) was de facto ruler of Venezuela from 1908 to 1935. He was president three times during those years, and died in office. *Juan Vicente Gómez*, BIOGRAFÍAS Y VIDAS, [http://www.biografiasyvidas.com/biografia/g/gomez\\_juan.htm](http://www.biografiasyvidas.com/biografia/g/gomez_juan.htm) (last visited May 2, 2014).

45. Rafael Reyes was President from 1904 to 1909 as a military ruler representing the Conservatives. “In the course of his regime, Reyes improved the country’s finances, expanded roads and railroads, and encouraged increased coffee production. Large U.S. investments and purchases of coffee and minerals contributed to Colombia’s economic growth.” However, Reyes (1849–1921) ruled Colombia as a dictator, and was eventually forced into exile in 1909. *History, Loss of Panama*, COUNTRIESQUEST.COM, [http://www.countriesquest.com/south\\_america/colombia/history/loss\\_of\\_panama.htm](http://www.countriesquest.com/south_america/colombia/history/loss_of_panama.htm) (last visited May 2, 2014).

46. Jose Gregorio Pineda & Francisco Rodríguez, *Curse or Blessing? Natural Resources and Human Development*, in *THE OXFORD HANDBOOK OF LATIN AMERICAN ECONOMICS* 421 (José Antonio Ocampo & Jaime Rose eds., 2011).

But this activity has not benefitted all people equally and of course they have not fully concerned themselves with what happens to future generations. At times when high oil revenues allow for greater subsidies to the population at large, corruption can be disguised or hidden somewhat, but when revenues decrease and subsidies are not forthcoming, the population begins to ask questions. In addition “[m]ost oil exporting countries tend to use oil rents to provide employment guarantees in the public sector, leading to often non-value added jobs with little room for advancement” and often bloated individual drive and ambition.<sup>47</sup>

According to some researchers, the faulty allocation of talented people from productive economic sectors to those activities that merely seek what economists call rents—simply money with no real production or beneficial effects to show for the activity—has had a real negative impact on overall economic growth.<sup>48</sup>

Democracy is on the rise in Latin America, and is generally considered to be governing all countries in the region except Cuba.<sup>49</sup> Democracy with reduced economic roles for government, increased transparency and increased accountability was expected to bring about a concomitant reduction in corruption. Many have been disillusioned by reality.<sup>50</sup> As a result of the democratization of Latin America in the 1980s, the activities of politicians became somewhat more transparent, or at least that is what the concept of democracy is supposed to entail. Populations who were now in a position to expect more from their elected governments began to demand more, and whereas in the old days they either did not have a great collective notion of corruption or did not think they could voice an objection to it, now they voice their concerns and disillusionment with such activity. But some say democracy does not always prevent corruption.<sup>51</sup> In fact, some say that corruption has increased in Latin America since the transitions to democracy.<sup>52</sup>

Studies suggest that democracy does have an ameliorating effect on corruption,<sup>53</sup> but it still persists in Latin America, and some believe that

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47. ASKARI ET AL., *supra* note 1, at 21.

48. See Carlos Leite & Jens Weidmann, *Does Mother Nature Corrupt? Natural Resources, Corruption, and Economic Growth* (Int'l Monetary Fund, Working Paper WP/99/85, July 1999).

49. See DEMOCRACY IN LATIN AMERICA: (RE)CONSTRUCTING POLITICAL SOCIETY (Manuel Antonio Garretón M. and Edward Newman, eds., 2001); Moisés Nafm, *Democracy Dictates Latin America's Future*, FIN. TIMES, April 26, 2002.

50. See COMBATING CORRUPTION IN LATIN AMERICA, *supra* note 19.

51. Stephen D. Morris, *Corruption and Democracy at the State Level in Mexico*, in CORRUPTION & DEMOCRACY IN LATIN AMERICA 171 (Charles H. Blake & Stephen D. Morris eds., 2009).

52. *Id.* (citing Laurence Whitehead, *High Level Political Corruption in Latin America: A Transitional Phenomenon?* in POLITICAL CORRUPTION: CONCEPTS AND CONTEXTS 801–818 (Arnold J. Hidenheimer & Michael Johnston eds., 3rd ed. 2002); Kurt Weyland *Politics of Corruption in Latin America*, 9 J. DEMOCRACY 108–121 (1998)).

53. Strom C. Thacker, *Democracy, Economic Policy, and Political Corruption in Comparative Perspective*, in CORRUPTION & DEMOCRACY IN LATIN AMERICA 26 (Charles H. Blake & Stephen D. Morris eds., 2009) (citing Charles Blake & Chris-

the beneficial effects of democracy on corruption will take time.<sup>54</sup>

Law is considered to be an instrument of social control. The idea is that society attempts to achieve uniform behavior generally by describing behavior that is prohibited. The desired behavior is then encouraged by discouraging the undesired behavior through punishment. The populations of many states today consider themselves to be living under the rule of law. They believe that the rule of law bestows upon them, as citizens, the advantages of the prevention of arbitrary and corrupt government, the restraint of vengeance, and the provision of individual liberty and economic prosperity.

Some of the very first principles of the concept of the rule of law are that a law must be made public and must be reasonably clear in meaning and specific in what it prohibits. And, of course, it must be applied equally to all, that is, without discrimination. The rule of law is considered an essential element of a functioning democracy and a functioning economy. This sentiment has been echoed time and again by many, including the United Nations itself, which said:

Promoting the rule of law at the national and international levels is at the heart of the United Nations' mission. Establishing respect for the rule of law is fundamental to achieving a durable peace in the aftermath of conflict, to the effective protection of human rights, and to sustained economic progress and development. The principle that everyone—from the individual right up to the State itself—is accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, is a fundamental concept which drives much of the United Nations work.

Another principal tenet of the rule of law is that government should maintain peace and order, for the most part through a system of laws or rules that specify both violations and their corresponding sanctions accruing to violators . . . . This leads to the notion that no act can be regarded as a crime unless there is a specific law prohibiting it and no one can be punished unless they have committed an unlawful act described as a crime. Legal scholars refer to these concepts as *nullum crimen sin lege* (no crime without a law) and *nulla poena sin crimine* (no punishment without a crime). In other words, crimes must be clearly defined.<sup>55</sup>

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topher Martin, *The Dynamics of Political Corruption: Reexamining the Influence of Democracy*, 13 *DEMOCRATIZATION* 1–14 (2006); Alok K. Bohara, Neil J. Mitchell & Carl F. Mittendorf, *Compound Democracy and the Control of Corruption: A Cross-Country Investigation*, 32, *POL'Y STUD. J.* 481–99 (2004)).

54. *Id.* at 27.

55. Frederick V. Perry, *Multinationals at Risk: Terrorism and the Rule of Law*, 7 *FIU L. REV.* 43, 61–62 (2011) (citing WILLIAM LAWRENCE CLARK & WILLIAM LAWRENCE MARSHALL, *A TREATISE ON THE LAW OF CRIMES* 1–4, 64 (Marian Quinn Barnes ed., 7th ed. 1967); Andrew Altman, *ARGUING ABOUT LAW: AN INTRODUCTION TO LEGAL PHILOSOPHY* 5, 18 (Peter Adams et al. eds., 2d ed., 2001); O. Lee Reed, *Law, the Rule of Law, and Property: A Foundation for the Private Market and Business Study*, *AM. BUS. L. J.*, Apr. 1, 2001, available at <http://www.allbusiness.com/legal/3484583-1.html>; UNITED NATIONS & THE RULE OF LAW <http://www.un.org/en/ruleoflaw/index.shtml> (last visited May 2, 2014)).

As will be seen, acts generally considered acts of corruption are unlawful in the countries examined in this study. It appears therefore, as will be seen from what appears below, that while laws do exist, the “rule of law” lags behind.

### III. CORRUPTION IN LATIN AMERICA: LOOKING AT THE LAW

It is not as if corruption is allowed under the laws of the countries in Latin America. It is unlawful on a variety of levels. It is clearly against international law as recognized in Latin America, since all the nations of Latin America (except Suriname) are signatories of the United Nations Convention Against Corruption.<sup>56</sup> The UN Convention defines corruption<sup>57</sup> and requires states to implement measures and legislation to outlaw corrupt activities in their countries.<sup>58</sup>

The Organization of Economic Cooperation and Development (OECD) Anti-Bribery Convention was signed by forty countries, including five countries from Latin America: Argentina, Brazil, Chile, Colombia, and Mexico.<sup>59</sup> The OECD convention was negotiated and signed at the request of the U.S. Congress and the President of the United States<sup>60</sup> inasmuch as the United States had been alone among the industrialized world in prohibiting its citizens from engaging in the bribery of foreign government officials under its own Foreign Corrupt Practices Act of 1977.<sup>61</sup> The OECD convention calls for those countries that have signed and adopted the convention to make the bribery of foreign government officials to obtain business a crime and it puts in place a way for states to monitor the compliance of other signatory states.<sup>62</sup>

The collective lip-service and law of the hemisphere also deals with the subject. In its Declaration of Principles, the Summit of the Americas of 1994 stated that: “[e]ffective democracy requires a comprehensive attack on corruption as a factor of social disintegration and distortion of the economic system that undermines the legitimacy of political institu-

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56. G.A. Res. 55/61, U.N. Doc. A/RES/58/4 (Nov. 21, 2003), *available at* [http://www.un.org/en/ga/search/view\\_doc.asp?symbol=A/RES/58/4&Lang=E](http://www.un.org/en/ga/search/view_doc.asp?symbol=A/RES/58/4&Lang=E) (United Nations Convention Against Corruption, 140 nations are signatories).

57. *Id.* at ch. I.

58. *Id.* at ch. III, art. 15.

59. OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, Dec. 17, 1997, 37 I.L.M. 1, *available at* [http://www.oecd.org/daf/anti-bribery/ConvCombatBribery\\_ENG.pdf](http://www.oecd.org/daf/anti-bribery/ConvCombatBribery_ENG.pdf); *Country Reports on the implementation of the OECD Anti-Bribery Convention*, OECD, <http://www.oecd.org/investment/countryreports/ontheimplementationoftheoecdanti-briberyconvention.htm> (last visited May 2, 2014).

60. JOHN W. HEAD, *GLOBAL BUSINESS LAW: PRINCIPLES AND PRACTICES OF INTERNATIONAL COMMERCE AND INVESTMENT* 665 (3d. ed. 2007).

61. Foreign Corrupt Practices Act of 1977 § 104(a), 15 U.S.C. § 78dd-1-2 (2012).

62. OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, *supra* note 59, arts. 1, 12.

tions.”<sup>63</sup> The following Summits of the Americas either repeated or built upon these principles. The thirty-four participating heads of state, including all in the hemisphere except Cuba, signed the foregoing declaration, and nearly all countries of the hemisphere have signed subsequent ones.<sup>64</sup>

The Inter-American Convention Against Corruption adopted in Caracas, Venezuela on March 29, 1996, signed by thirty-four and ratified by thirty-three of the nations in the hemisphere,<sup>65</sup> including all those Latin American states included in this study, states in its preamble: “that fighting corruption strengthens democratic institutions and prevents distortions in the economy, improprieties in public administration and damage to a society’s moral fiber.”<sup>66</sup> It further requires that the signatory states maintain and strengthen:

1. Standards of conduct for the correct, honorable, and proper fulfillment of public functions. These standards shall be intended to prevent conflicts of interest and mandate the proper conservation and use of resources entrusted to government officials in the performance of their functions. These standards shall also establish measures and systems requiring government officials to report to appropriate authorities acts of corruption in the performance of public functions. Such measures should help preserve the public’s confidence in the integrity of public servants and government processes.
2. Mechanisms to enforce these standards of conduct.
3. Instruction to government personnel to ensure proper understanding of their responsibilities and the ethical rules governing their activities.
4. Systems for registering the income, assets and liabilities of persons who perform public functions in certain posts as specified by law and, where appropriate, for making such registrations public.
5. Systems of government hiring and procurement of goods and services that assure the openness, equity and efficiency of such systems.
6. Government revenue collection and control systems that deter corruption.
7. Laws that deny favorable tax treatment for any individual or corporation for expenditures made in violation of the anticorruption laws of the States Parties.

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63. Summit of the Americas, Declaration of Principles, Dec. 11, 1994, *reprinted in* MIAMI HERALD, Dec. 12, 1994, at A12–13, *available at* [http://www.summit-americas.org/i\\_summit/i\\_summit\\_dec\\_en.pdf](http://www.summit-americas.org/i_summit/i_summit_dec_en.pdf).

64. See Alfredo Prieto, *Everybody But Cuba*, HAVANA TIMES (Apr. 15, 2009, 7:25 AM), <http://www.havanatimes.org/?p=7477>.

65. Against Corruption: Signatories and Ratifications, ORGANIZATION OF AMERICAN STATES [OAS], <http://www.oas.org/juridico/english/Sigs/b-58.html> (last visited May 2, 2014).

66. INTER-AMERICAN CONVENTION AGAINST CORRUPTION, pmbl., Mar. 29, 1996, 35 I.L.M. 724 (1996), *available at* <http://www.oas.org/juridico/english/treaties/b-58.html>.

8. Systems for protecting public servants and private citizens who, in good faith, report acts of corruption, including protection of their identities, in accordance with their Constitutions and the basic principles of their domestic legal systems.
9. Oversight bodies with a view to implementing modern mechanisms for preventing, detecting, punishing, and eradicating corrupt acts.
10. Deterrents to the bribery of domestic and foreign government officials, such as mechanisms to ensure that publicly held companies and other types of associations maintain books and records which, in reasonable detail, accurately reflect the acquisition and disposition of assets, and have sufficient internal accounting controls to enable their officers to detect corrupt acts.
11. Mechanisms to encourage participation by civil society and non-governmental organizations in efforts to prevent corruption.
12. The study of further preventive measures that take into account the relationship between equitable compensation and probity in public service.<sup>67</sup>

In other words, the signatory countries agreed to make corruption unlawful and to rid their countries of corruption.

Article VI of the Convention defines corruption as follows:

#### Acts of Corruption

1. This Convention is applicable to the following acts of corruption:
  - a. The solicitation or acceptance, directly or indirectly, by a government official or a person who performs public functions, of any article of monetary value, or other benefit, such as a gift, favor, promise, or advantage for himself or for another person or entity, in exchange for any act or omission in the performance of his public functions;
  - b. The offering or granting, directly or indirectly, to a government official or a person who performs public functions, of any article of monetary value, or other benefit, such as a gift, favor, promise, or advantage for himself or for another person or entity, in exchange for any act or omission in the performance of his public functions;
  - c. Any act or omission in the discharge of his duties by a government official or a person who performs public functions for the purpose of illicitly obtaining benefits for himself or for a third party;
  - d. The fraudulent use or concealment of property derived from any of the acts referred to in this article; and
  - e. Participation as a principal, co-principal, instigator, accomplice, or accessory after the fact, or in any other manner, in the commission or attempted commission of, or in any collaboration or conspiracy to commit, any of the acts referred to in this article.
2. This Convention shall also be applicable by mutual agreement between or among two or more States Parties with respect to any other act of corruption not described herein.<sup>68</sup>

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67. *Id.* art. III.

68. *Id.* art. VI.

That is what international law says for the Latin Americans. Inasmuch as these conventions are treaties, they have the force of internal law within each country.<sup>69</sup> The constitutions of the various countries are also very clear on the subject of—in some cases also corruption, but always—the use of natural resources. A state's natural resources belong to the people and they must be exploited and shared in order to benefit the people,<sup>70</sup> and accordingly the misuse of a state's natural resources is contrary to the provisions of the constitutions of nearly all of the states in question.<sup>71</sup> Similarly corruption and the acceptance of bribes is a violation of the criminal laws of these Latin American countries.<sup>72</sup>

So there is no dearth of rules in Latin America, all of which make it very clear that corruption and bribery—of government officials in most cases, but bribery in general in many cases—are outlawed with heavy sanctions for the transgressor, if caught.

#### IV. CORRUPTION IN LATIN AMERICA: MEASURING CORRUPTION

Measuring manifestations of or the perception of corruption across similar countries is not an easy task, but it is much for difficult and fraught with problems when one attempts to devise a useful, single index to measure and then rank corruption over such a diverse range of countries as those making up the Latin American region. There are a variety of methods that have been used to measure corruption within countries and they can generally be grouped into three fairly broad categories: (1) measures devised by mostly private firms who earn their living advising and consulting in the area of political risk; (2) indices that are based on what is termed "perception," designed by NGO's or advocacy groups; and (3) wide ranging governance indices that their designers view as related to corruption.

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69. MALCOM N. SHAW, *INTERNATIONAL LAW* 926 (6th ed. 2008).

70. In some countries where the constitution appears ambiguous, such as that of Colombia, legal scholars assure us that inasmuch as the Spanish Crown was the original owners of all mines and subsoil rights, those subsoil rights passed on to the newly independent state of Columbia, and that national ownership—and the attendant obligation to exploit those rights for the people—was never derogated. See, e.g., LUÍS ENRIQUE CUERVO PONTÓN, *La Propiedad y los Yacimientos de Hidrocarburos en el Derecho Colombiano*, in *INTRODUCCIÓN AL DERECHO Y LA POLÍTICA DE PETRÓLEOS*, 74 (2001).

71. See, e.g., CONSTITUCIÓN DE LA REPUBLICA DEL ECUADOR art. 246, Registro Oficial 449, 20 de Octubre de 2008; Constitución Política de los Estados Unidos Mexicanos [C.P.] art. 27 Diario Oficial de la Federación [DO], 5 de Febrero de 1917 (Mex.); Venez. Const. art. 12; Art. 41, CONSTITUCIÓN NACIONAL [CONST. NAC.] (Arg.); Constituição Federal [C.F.] [Constitution] art. 176 (Braz.).

72. See CÓDIGO PENAL arts. 198–203 (Venez.); Cód. Pen. art. 264 (Ecuador) (likewise art. 204 of the Constitution of Ecuador outlaws bribery and corruption); CÓDIGO PENAL [C. PEN.] arts. 404–412 (Colom.); CÓDIGO PENAL [CÓD. PEN.] arts. 266–68 (Arg.); Código Penal Federal [CPF] [Federal Criminal Code], *as amended*, arts. 215, 217–18, 220, Diario Oficial de la Federación [DO], 14 de Agosto de 1931 (Mex.); CÓDIGO PENAL [C.P.] arts. 316–17 (Braz.).

Each of the ways of looking at corruption as espoused by each of the foregoing types of measurements has its strength and weaknesses. Each of these approaches vary in the scope and precision of metrics that they employ; they vary in the ways they measure and assess corruption and its impact on business or other institutions of civil and political society along with the mechanisms in government or otherwise, which either encourage or inhibit corruption.<sup>73</sup>

#### A. PRIVATE MEASUREMENT

Private institutions like the Economist Intelligence Unit (EIU) and Political Risk Services (PRS) use data collected from correspondents with certain specific country expertise, business related surveys and other data. PRS's International Country Risk Guide attempts to describe and measure the extent and likelihood of government officials demanding bribes.<sup>74</sup> Since most subscribers to the PRS are banks, multinationals, and investors, the assessments generally focus on items of interest to business.<sup>75</sup> Of course such a bundle of measurements would ideally be simply a component of a general overall measurement of corruption in a given country.

#### B. ADVOCACY GROUP AND NGO DESIGNED SURVEYS

The most widely known set of indices in this group are the ones devised by the Berlin based Transparency International (TI) and the World Bank Institute (WBI), both of which measure corruption by means of a series of surveys reported by the general public and representatives of business. These indices assume that the perception of specific groups of respondents, such as business leaders, public servants and the general public, accurately reflects the levels and patterns of corruption in a given country. These indicators generally are designed to measure the levels of governance and corruption in order determine the need for assistance by international organizations or NGO's in the areas of governance, rule of law, and the like. The TI index, known as the *Corruption Perception Index* (CPI) is generally considered the most widely known and used. The CPI is not based on TI's own experts, rather on outside experts and surveys. The survey is issued annually; a score of 100 represents a total absence of corruption and a zero represents total corruption.<sup>76</sup>

73. See Stephen Knack, *Measuring Corruption in Eastern Europe and Central Asia: A Critique of the Cross-Country Indicators* (World Bank Policy Research, Working Paper 3968, July 2006).

74. Jakob Svensson, *Eight Questions about Corruption*, 12 J. ECON. PERSP. 19, 22 (2005).

75. See Carlos Leite & Jens Weidmann, *Does Mother Nature Corrupt? Natural Resources, Corruption, and Economic Growth* (Int'l Monetary Fund Working Paper WP/99/85, July 1999).

76. *Corruption Perceptions Index: In Detail*, TRANSPARENCY INT'L, [http://www.transparency.org/cpi2013/in\\_detail](http://www.transparency.org/cpi2013/in_detail) (last visited May 5, 2014).



The CPI uses from three to sixteen sources, requiring at least three. The WBI's *Control of Corruption Index* (CCI) on the other hand, requires only one source per country. The WBI maintains that the CPI has limitations and that the CCI is better, since those poorer and less developed countries are those where fewer sources are used by the CPI and thus, according to the WBI, the levels of corruption may be higher in such countries, yet the available measurements are far fewer. The CCI uses units that range from -2.5 to +2.5 in its measurements; the higher the values, the better the governance—and therefore less corruption. Some commentators criticize these indices for use in country comparison purposes because the number of sources and the very sources themselves are not consistent across countries.<sup>77</sup>

Another criticism of such indices is that they are based on perception, and in oil-rich countries when oil prices are high there is the possibility (or probability, depending on one's point of view) that economic growth, ease of doing business, and general overall feeling of ease is due to a strong inflow of petro revenues, and that such a feeling will decline with the decline in world oil prices. Despite such criticism, given the sinister nature of corruption a completely accurate empirical measurement system may not be possible.

### C. BROAD GOVERNANCE INDICATORS

These indices are also developed by advocacy organizations though the corruption component is just one component of a larger set of governance indicators, since these organizations generally start from the idea that corruption is a product of weak governance. For this type of index, corruption is considered to be related to government policies and to the nature of institutions within a state, for example the level of bureaucracy, the way that business is regulated, and the level of economic, civil and political liberties and the like. While these indices of course may not be exact measures of corruption, it can be argued that inasmuch as they are empirical measurements, they are superior to perception based indices.

Tables 1–3 reflect a summary of a number of measurements by a variety of institutions that measure government, legal and political corruption in a number of ways<sup>78</sup>

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77. See ASKARI, ET AL., *supra* note 1.

78. ASKARI ET AL., *supra* note 1, at 14.

TABLE 1: MEASURING GOVERNMENT CORRUPTION

Type	Definition	Source
Governance	Governance is the traditions and institutions by which authority in a country is exercised for the common good. This includes the process by which those in authority are selected, monitored, and replaced (the political dimension); the government's capacity to effectively manage its resources and implement sound policies (the economic dimension); and the respect of citizens and the state for the country's institutions (the institutional respect dimension).	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)
Public Governance	"Public Governance" is the response to the challenges of globalization in terms of effectiveness, efficiency and responsiveness facing the public sector. It also addresses the dramatic changes that regulation and management of society have undergone over the past decades. Public governance seeks to understand and conceptualize appropriate forms of state-society relations that are capable of responding to this complex environment. By addressing institutional capacity and constituting the framework for equitable and legitimate political structures, it has become a key concept for public management reform.	Basel Institute on Governance
Rent Seeking	It is the extra amount paid (over what would be paid for the best alternative use) to somebody or for something useful whose supply is limited either by nature or through human ingenuity.	IMF
Government Effectiveness	Measuring the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)
State Capture	The survey design permits an in-depth empirical analysis of governance and corruption, unbundling governance into its component dimensions. This allows a more detailed quantitative assessment of corruption, a more nuanced understanding of the causes of the problem and as a result a stronger foundation for policy advice. Particular attention is paid to "state capture" by parts of the corporate sector (i.e., the propensity of firms to shape the underlying "rules of the game" including "purchase" of legislation and court decisions).	WB Business Environment and Enterprise Performance Survey (BEEPS)

Voice and Accountability	Measuring the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)
Control of Corruption	Measuring the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)
Regulatory Quality	Measuring the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)

TABLE 2: MEASURING RULE OF LAW AND CORRUPTION

Type	Definition	Source
Rule of Law	Measuring the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, the police, and the courts, as well as the likelihood of crime and violence.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)
Conflict of Interest	Conflict of interest: a situation in which a party has interests that could improperly influence that party's performance of its official duties or responsibilities, contractual obligations, or compliance with applicable laws and regulations.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)

TABLE 3: MEASURING THE POLITICAL CORRUPTION

Type	Definition	Source
Political stability and Absence of Violence	Measuring perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including domestic violence and terrorism.	WB Control of Corruption Governance indicators (Kaufmann, Kraay, and Mastruzzi)
Lobbying	The EBRD-World Bank Business Environment and Enterprise Performance Survey (BEEPS) compiles the experiences of approximately 20,000 firms in twenty-six transition countries plus Turkey in three rounds: 1999, 2002 and 2005. The survey examines the quality of the business environment as determined by a wide range of interactions between firms and the state.	WB Business Environment and Enterprise Performance Survey (BEEPS)

Political Party Financing	The Global Integrity Report is a tool for understanding governance and anti-corruption mechanisms at the national level written by local researchers and journalists. Each country assessment contained in the Global Integrity Report comprises two core elements: a qualitative Reporter's Notebook and a quantitative Integrity Indicators scorecard, the data from which is aggregated and used to generate the cross-country Global Integrity Index. An Integrity Indicators scorecard assesses the existence, effectiveness, and citizen access to key governance and anti-corruption mechanisms through more than 300 actionable indicators. It examines issues such as transparency of the public procurement process, media freedom, asset disclosure requirements, and conflicts of interest regulations.	UNDP and Global Integrity
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V. CORRUPTION IN LATIN AMERICA:  
LOOKING AT THE DATA

To assess the impact of corruption and economic freedom on economic growth in oil and gas-rich Latin American countries, we broaden the sample of countries beyond those in the Latin American region by including groups of oil-rich and oil and gas-dependent countries in different per capita income brackets and with different measured levels of corruption and economic freedom. We examined the GDP per capita of these countries and assessed their broader economic development performance by looking at their political progress and their social achievements. We also combine corruption indices and separate them by typology of corruption in order to investigate the particular facets of corruption that pose the greatest impediment to economic growth. Our analysis identifies a link between corruption and sustainable economic growth (an inverse positive relationship). The electoral system component was found to have a U-shaped relationship with the measures of economic performance and human development.

VI. OIL AND GAS DEPENDENCY

“To classify the dependence of countries on oil and gas, we use two measures: (1) the share of oil and gas exports in total exports and (2) government revenues from oil and gas as percentage of total government revenues.”<sup>79</sup>

Based on their oil and gas dependency we have identified the following countries: OPEC countries (Algeria, Angola, Ecuador, Iran, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, UAE, Venezuela and Iraq), Argen-

79. ASKARI ET AL., *supra* note 1, at 77–78.

tina, Brazil, Canada, Colombia, Russia, Mexico, Norway, Azerbaijan, and Kazakhstan.<sup>80</sup> The oil, refined products, and gas exports of the Latin American countries, except for Venezuela, comprise about 20–40 percent of their total exports and their governments receive around 30–40 percent of their revenues from oil and gas sales.<sup>81</sup> In addition, we use the World Bank country income classification to distinguish between the lower-middle, upper-middle, and high-income countries. In Table 1, we list the countries with oil and gas dependency which are determined by the exports of oil and gas as a percentage of total exports and by the revenues from oil and gas as a percentage of total government revenues.<sup>82</sup> If we look at the Latin American countries over time, we observe a great variation in oil dependency. Mexico seems to be the only country where the oil dependency is falling over time due to an increase in exports of merchandise other than oil and gas.<sup>83</sup>

TABLE 4: OIL DEPENDENCY

	Oil And Gas Exports as a Percentage Of Total Exports	Oil And Gas Revenue as a Percentage Of Total Government Revenues
	2002–2007	
High income countries:		
Canada	18.94	36.00
Kuwait	93.78	77.83
Norway	46.35	38.00
Qatar	88.76	65.73
Saudi Arabia	88.49	87.26
UAE	46.09	74.33
Upper-middle income countries:		
Algeria	97.98	73.86
Argentina	16.64	n/a
Brazil	6.09	n/a
Colombia	36.29	9.4
Kazakhstan	65.39	30.94
SP Libyan AJ	95.83	88.03
Mexico	13.09	36.39
Russia	58.09	62.84
Venezuela	85.46	45.7*

80. Iraq was not included in the study due to lack of reliable data. We added Brazil due to the largest oil discoveries in recent years. U.S. ENERGY INFO. ADMIN., BRAZIL, <http://www.eia.gov/countries/analysisbriefs/brazil/brazil.pdf> (last visited May 5, 2014).

81. See *infra* Table 1.

82. *Id.*

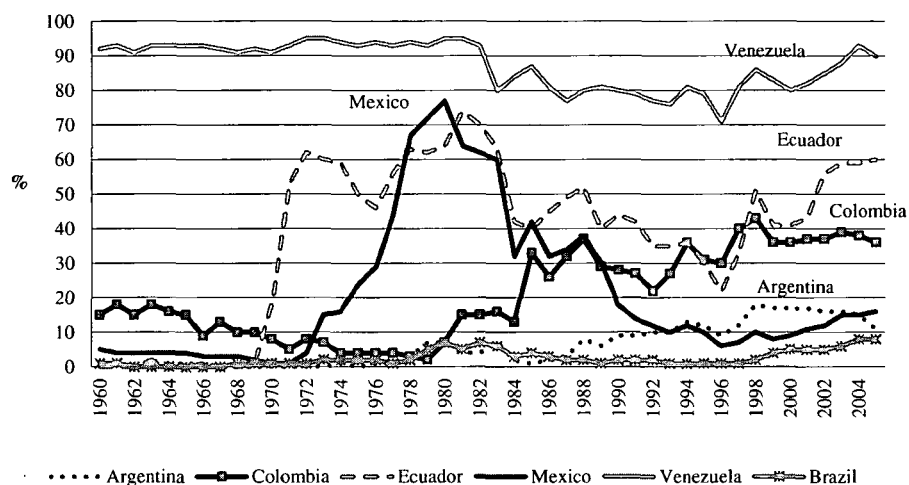
83. See *infra* Figure 1.

Lower-middle income countries:		
Angola	96.51	78.74
Azerbaijan	82.19	44.66
Ecuador	53.07	29.81
IR Iran	86.13	67.71
Nigeria	96.56	76.19

\*Average during 1997–2000

Source: **Regional Economic Outlook: Middle East and Central Asia**, International Monetary Fund (2008); AGUSTÍN CARSTENS, THE UNIVERSITY OF CHICAGO, **MEXICO IN A GLOBALIZED WORLD** (2007) available at <http://research.chicagobooth.edu/igm/events/speaker-series/docs/mexicoinaglobalizedworld.pdf>; Ehtisham Ahmad & Eric Mottu, *Oil Revenue Assignments: Country Experiences and Issues* (Int'l Monetary Fund Working Paper No. 02/203, 2002), available at <https://www.imf.org/external/pubs/ft/wp/2002/wp02203.pdf>; **International Trade Centre, Trade Competitiveness Map**, [http://legacy.intracen.org/appli1/TradeCom/TP\\_TP\\_CI.aspx?RP=008&YR=2010](http://legacy.intracen.org/appli1/TradeCom/TP_TP_CI.aspx?RP=008&YR=2010) (last visited May 5, 2014); **World Development Indicators 2009**, THE WORLD BANK (2009).

FIGURE 1: FUEL EXPORTS OF LATIN AMERICAN COUNTRIES, 1960–2007



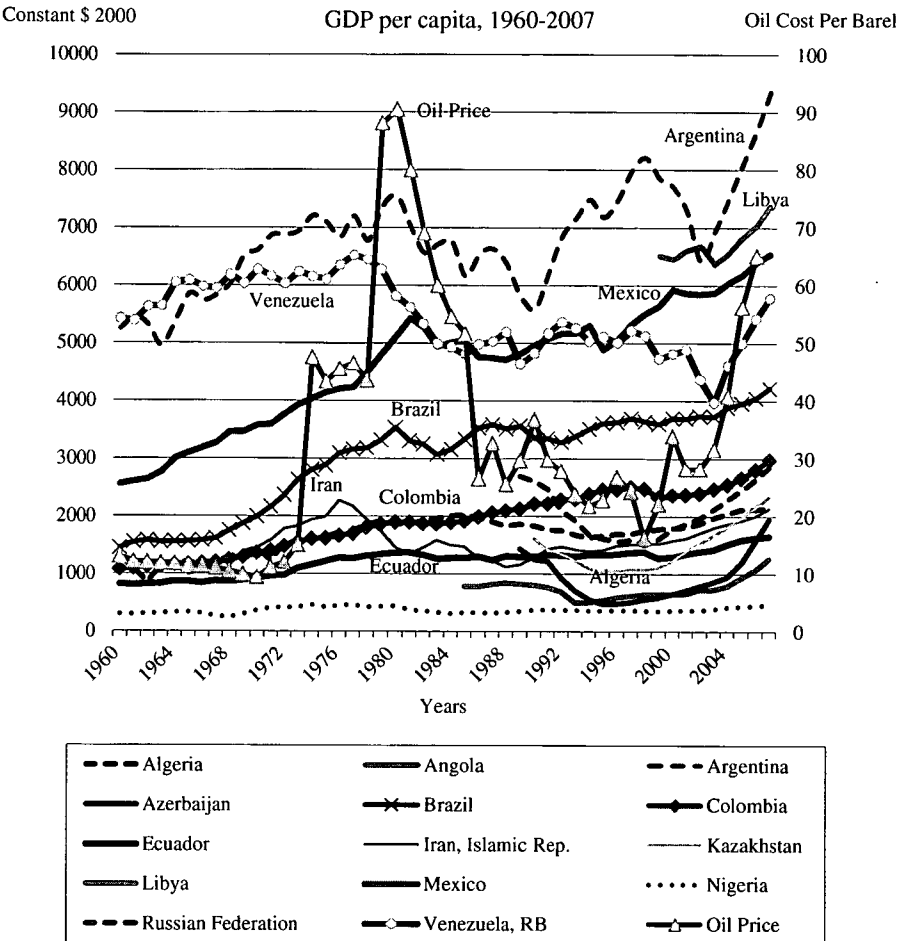
Source: THE WORLD BANK, WORLD DEVELOPMENT INDICATORS.

## VII. ECONOMIC DEVELOPMENT, POLITICAL PROGRESS, AND SOCIAL PERFORMANCE IN PETROLEUM DEPENDENT ECONOMIES

Among the upper- and lower-middle income countries, Argentina, Venezuela, Mexico, Libya and Brazil demonstrate the highest real GDP per capita.<sup>84</sup> Of these nations, only Mexico and Brazil seem to follow a relatively steady growth pattern while the growth of the other economies, for the most part, closely tracked changes in oil prices.

84. For the GDP per capita between 1960–2007 of petroleum dependent countries in the upper- and lower-middle income bracket (listed in Table 1), see *infra* Figure 2.

FIGURE 2: GDP PER CAPITA, CONSTANT US\$ 2000, 1960–2007



Source: WORLD BANK, WORLD DEVELOPMENT INDICATORS, BRITISH PETROLEUM (2008).

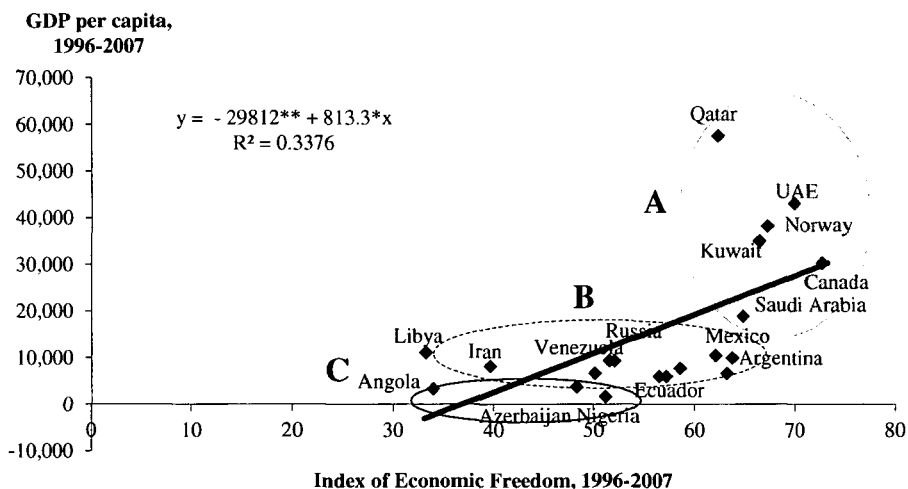
To further investigate the link between economic freedom, corruption and economic growth, we examine the relationship between the measure of economic growth using GDP based on purchasing power parity (ppp) per capita and nine indices measuring different dimensions of economic development, political progress, and social performance. These indices include the Index of Economic Freedom, Human Development Index, Business Environment Score, Failed State Index, Corruption Perception Index, Global Integrity Index, Governance Indicators, Polity Index and Corruption as perceived by foreign investors. As mentioned before, we use the World Bank classification to distinguish between the high-income, upper-middle-, and lower-middle countries.

The figures below show that, on average, higher income oil exporters tend to do better on all the indicators related to their economic/business,

political, institutional environment. However, there are some exceptions to this general observation.

The Index of Economic Freedom assesses ten specific freedoms ranging from property rights, government size, trade and monetary freedom to entrepreneurship. Figure 3 shows the relationship between GDP per capita (expressed in terms of ppp unless noted otherwise) and the Index of Economic Freedom. It would appear that among the lower-income countries Ecuador tends to do better and is closer in performance to the upper-middle income countries such as Brazil and Algeria. Libya, on the other hand, falls far behind its counterparts in the upper-middle income countries. Venezuela seems to perform on par with Russia in terms of economic freedom and is far behind other Latin American countries such as Argentina and Mexico.

FIGURE 3: RELATIONSHIP BETWEEN GDP PER CAPITA AND THE INDEX OF ECONOMIC FREEDOM



Source: WORLD BANK, WORLD DEVELOPMENT INDICATORS, HERITAGE FOUNDATION (2009).

Note: GDP per capita is expressed in PPP<sup>85</sup>

A = high income, B = upper-middle income, and C = lower-middle income countries<sup>86</sup>  
Y refers to GDP per capita ppp and X refers to the Index of Economic Freedom

\* = indicates a statistical significance at 0.01 level, \*\* = indicates a statistical significance at 0.05 level

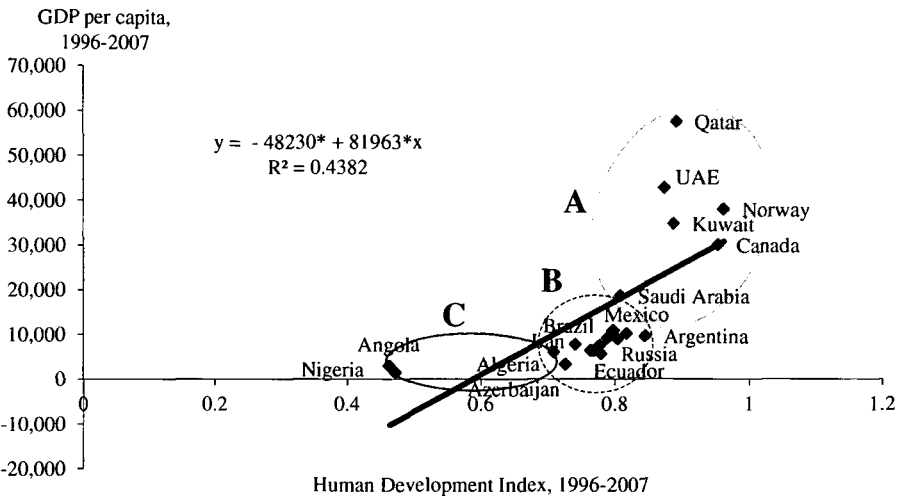
The Human Development Index (HDI), which is a combination of education, life expectancy and income indices, is typically used to measure a country’s overall economic development, political progress, and social development. Azerbaijan, Ecuador, and Iran seem to have better overall human development as opposed to their counterparts in the same lower-

85. GDP is expressed in PPP unless otherwise noted in all charts and figures.  
86. Area A countries are high income, Area B countries are upper-middle income, and Area C countries are lower-middle income countries. This holds the same for all charts.



income group. On the other hand, Saudi Arabia and Algeria are lagging behind their counterparts in their respective groups. Figure 4 shows the relationship between GDP per capita and the Human Development Index.

FIGURE 4: RELATIONSHIP BETWEEN GDP PER CAPITA AND THE HUMAN DEVELOPMENT INDEX



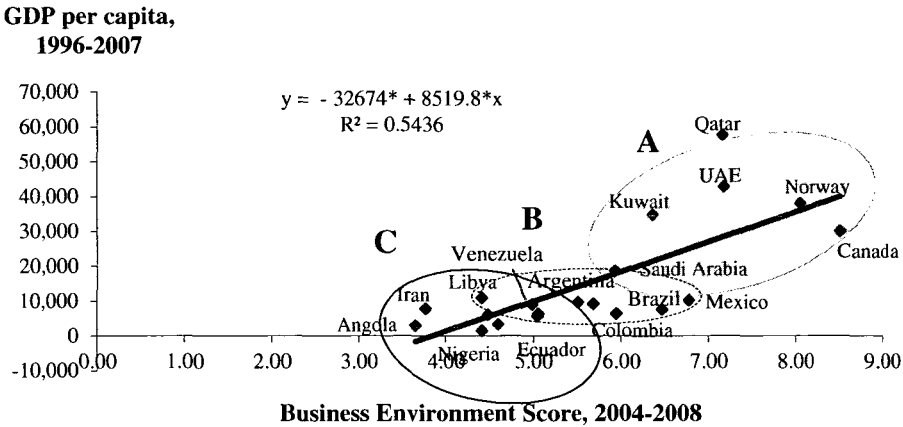
Source: WORLD BANK, WORLD DEVELOPMENT INDICATORS, UNITED NATIONS DEVELOPMENT PROGRAM

Note: Y refers to GDP per capita ppp and X refers to the Human Development Index

\* = indicates a statistical significance at 0.01 level

The overall Business Environment Score is used to quantify the attractiveness of the business environment with indicators varying from the political environment, the macroeconomic environment, market opportunities, policy towards free enterprise and competition, policy towards foreign investment, including ease of starting a business, foreign trade and exchange controls, taxes, financing, the labor market and infrastructure. The analysis shows that Brazil and Mexico have better business environments, while Algeria is scoring poor in comparison to the other countries in the upper-middle income group. In terms of its business environment Ecuador is leading in the lower-middle income group, it is comparable to the upper-middle income countries such as Kazakhstan and Venezuela. Figure 5 displays the relationship between GDP per capita and the Business Environment Score.

FIGURE 5: RELATIONSHIP BETWEEN GDP PER CAPITA AND BUSINESS ENVIRONMENT SCORE



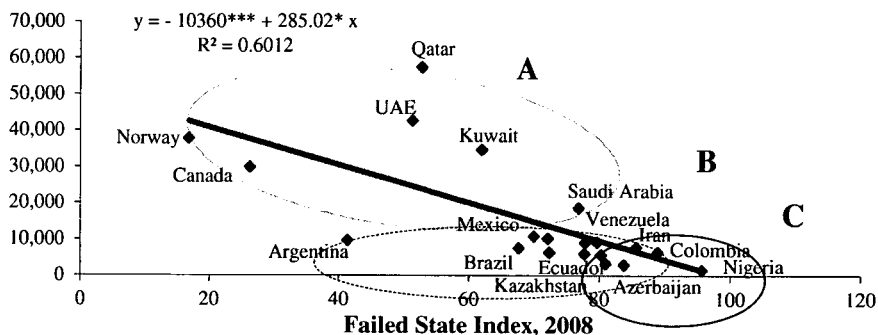
The Failed State Index comprises of twelve indicators covering a wide range of elements of failed state: inability to collect taxes, extensive corruption, criminal behavior, inequality, discrimination, severe demographic pressures, brain drain and environmental decay. Figure 6 shows the relationship between GDP per capita and the Failed State Index. The analysis shows that Saudi Arabia is an outlier among high-income countries due to the growing population of young people that need jobs, low tax base, group grievance, uneven development, security issues, factionalized elites, legitimacy of the state (lack of representation since political parties only exist on the local level), and arbitrary application of the Rule of Law. Although Argentina and Ecuador seem to do relatively well when compared to other countries in their respective income categories, both countries still suffer from numerous problems. For example, Argentina faces “[large income inequality], poverty, extensive deforestation, human rights abuses by police and corrupt relations between governors and judicial system in the provinces.”<sup>87</sup> High incidence of “migration [of skilled workers], lack of political leadership [in the form of constant change of constitutions, among other things], drug-trafficking network within the country” prevail in Ecuador.<sup>88</sup> Venezuela in the same way as Russia and Kazakhstan, is falling behind the upper-middle income countries due to “existing [income inequality among the population, massive and endemic] corruption in [the judicial system or profiteering by ruling elites], legitimacy of the state, [lack of political opposition], high media scrutiny, [human rights violations], and [fragmentation of the ruling]

87. THE FUND FOR PEACE, COUNTRY PROFILE: ARGENTINA (2009).  
88. THE FUND FOR PEACE, COUNTRY PROFILE: ECUADOR (2009).

elites.”<sup>89</sup> Colombia, with its “ongoing insurgencies heavily financed by an illegal drug trade and [significant violations of] human rights, [limited access to education, and high] poverty” leans towards the lower-middle income group of countries.<sup>90</sup>

FIGURE 6: RELATIONSHIP BETWEEN GDP PER CAPITA AND FAILED STATE INDEX

GDP per capita,  
1996-2007



Source: WORLD BANK, WORLD DEVELOPMENT INDICATORS, FUND FOR PEACE.

Note: Y refers to GDP per capita ppp and X refers to the Failed State Index

\* = indicates a statistical significance at 0.01 level, \*\*\* = indicates a statistical significance at 0.10 level

The Corruption Perception Index (CPI) measures the overall level of corruption and not the expected outcome. It is a mix of third-party surveys to sample public perceptions of corruption through a variety of questions, ranging from “Do you trust the government?” to “Is corruption a big problem in your country?” In the upper-middle income group, Mexico, Colombia and Brazil have a relatively low level of corruption as opposed to Argentina and Libya. Venezuela is lagging behind, along with Russia and Kazakhstan, due to considerable “illegal flight of capital, corrupt practices,<sup>91</sup> risk of expropriation,<sup>92</sup> extensive bribes extorted to facilitate services, secure procurement contracts, and clear customs.”<sup>93</sup> Figure 7 illustrates the relationship between GDP per capita and the Corruption Perception Index.

89. THE FUND FOR PEACE, COUNTRY PROFILE: VENEZUELA (2009).

90. THE FUND FOR PEACE, COUNTRY PROFILE: COLOMBIA (2009).

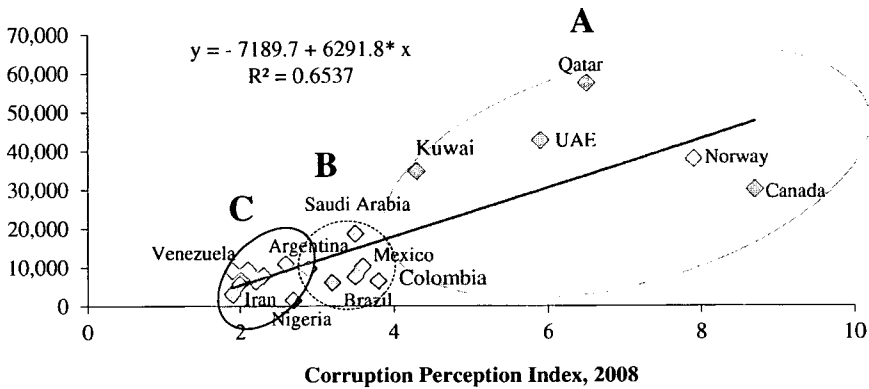
91. See generally Raymond W. Baker, *The Biggest Loophole in the Free-Market System*, 22 WASH. Q., Autumn 1999, at 27.

92. See generally Francisco Monaldi, Sunk-Costs, Institutions, and Commitment: Foreign Investment in the Venezuelan Oil Industry (Dec. 2001), available at <http://www.stanford.edu/class/polisci313/papers/MonaldiFeb04.pdf>.

93. See generally TRANSPARENCY INTERNATIONAL, REPORT ON THE TRANSPARENCY INTERNATIONAL GLOBAL CORRUPTION BAROMETER 2007 (Dec. 6, 2007), available at [http://archive.transparency.org/policy\\_research/surveys\\_indices/gcb/2007](http://archive.transparency.org/policy_research/surveys_indices/gcb/2007) (last visited Mar. 19, 2014).

FIGURE 7: RELATIONSHIP BETWEEN GDP PER CAPITA AND THE CORRUPTION PERCEPTION INDEX

GDP per capita,  
1996-2007



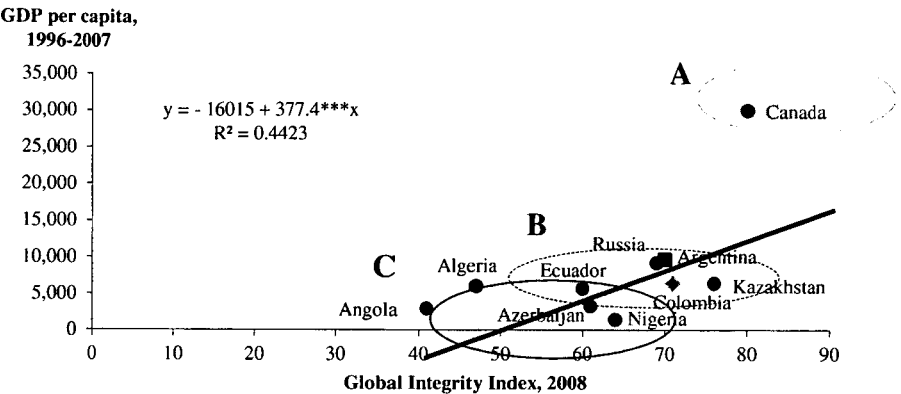
Source: World Bank (World Development Indicators), Transparency International  
Note: Y refers to GDP per capita ppp and X refers to the Corruption Perception Index  
\* = indicates a statistical significance at 0.01 level

The Global Integrity Index annually evaluates the existence and citizen access to national-level anti-corruption mechanisms. The Index does not measure corruption; instead, it examines the spread of corruption and investigates the mechanisms to combat it—government accountability, regulation, the rule of law, transparency, and citizen oversight. The Index is comprised of 15,000 peer-reviewed questions. Figure 8 displays the relationship between GDP per capita and the Global Integrity Index. Ecuador and Kazakhstan score higher when compared to their respective counterparts, while Algeria is a laggard due to its recent civil war troubles.<sup>94</sup> While plagued by corruption in the form of politicized appointments and an ineffective public procurement process, Ecuador, unlike other countries in its respective group, still enjoys a media that acts as an “effective watchdog.”<sup>95</sup>

94. THE GLOBAL INTEGRITY REPORT, ALGERIA, *Corruption Timeline* (2007).

95. THE GLOBAL INTEGRITY REPORT, ECUADOR, *Country Assessment* (2008).

FIGURE 8: RELATIONSHIP BETWEEN GDP PER CAPITA  
AND GLOBAL INTEGRITY INDEX

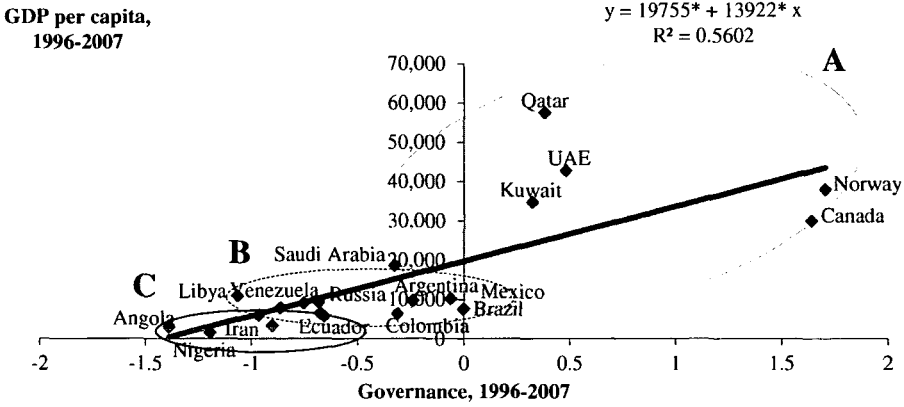


Source: World Bank (World Development Indicators), Global Integrity  
Note: Y refers to GDP per capita ppp and X refers to the Global Integrity Index  
\*\*\* = indicates a statistical significance at 0.10 level

The World Bank Governance Indicators include six dimensions: Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption. These governance indicators are measured in units ranging from about -2.5 to 2.5; higher values correspond to better governance outcomes. These indicators reflect the quality of governance as seen by a large number of enterprise, citizen and expert survey respondents, as reported by a number of survey institutes, think tanks, non-governmental organizations, and international organizations.

Figure 9 shows the relationship between GDP per capita and Governance. In terms of overall governance, Saudi Arabia is again an outlier among all high income oil and gas-rich countries. Argentina, Mexico and Brazil tend to score relatively well compared to other countries in the upper-middle income group. Venezuela is among the countries that had a significant decline on this indicator due to significant media restrictions, political instability, poor law enforcement, and a poor judicial system. Respondents in Venezuela, Argentina, and Ecuador have a low confidence in the ability of their governments to formulate sound policies and promote private businesses. On the other hand, Colombia and Algeria managed to increase their government efficiency over this period of time. Yet, Ecuador seems to have higher government accountability compared to the lower-middle income group, and Algeria is scoring low in comparison with its counterparts. There is also a big gap within the high-income countries group with nations ranging from Saudi Arabia in a lower tier to Norway and Canada in an upper income tier.

FIGURE 9: RELATIONSHIP BETWEEN GROWTH IN GDP PER CAPITA AND GOVERNANCE



Source: World Bank (World Development Indicators and Governance Indicators)

Note: Y refers to GDP per capita ppp and X refers to Governance

\* = indicates a statistical significance at 0.01 level

The regression results for growth in GDP per capita versus indicators, such as Index of Economic Freedom, Human Development Index, Business Environment Score, Failed State Index, Corruption Perception Index, Global Integrity Index, Governance, did not seem to be statistically significant. The correlation between GDP per capita and growth in GDP per capita and two indicators of Polity Index and Corruption (PRS Group) were not statistically significant either.

To summarize, we find countries such as Argentina, Azerbaijan, Ecuador, Iran, and Mexico to have relatively high level of human development, in terms of health, education and income. Brazil, Mexico, Argentina, and Ecuador possess an environment that is conducive to business and tends to have lower levels of both corruption and problems with government accountability as opposed to Russia, Venezuela, Kazakhstan, and Algeria. While the more democratic Ecuador rates high for its income, level of human development, business environment, governance and accountability, and a “relatively free media,”<sup>96</sup> it is still among the group of failed states such as Russia and Algeria. This is largely due to “a high “migration [of skilled workers], lack of political leadership [in the form of constant change of constitutions], and a drug-trafficking network within the country.”<sup>97</sup> One of the most successful among these Latin American countries is Mexico with a high literacy rate similar to that of Russia, and a significant increase in merchandise exports other than petroleum. However Mexico still struggles with “law enforcement [challenges], corruption in [its] police forces, human rights [violations] and [a weak] judiciary branch to fight organized crime.”<sup>98</sup> Another leading

96. *Id.*

97. THE FUND FOR PEACE, COUNTRY PROFILE: ECUADOR, *supra* note 88.

98. THE FUND FOR PEACE, COUNTRY PROFILE: MEXICO (2009).

country, Brazil, enjoys a “thriving business environment, [and a good] system of free public university [education].”<sup>99</sup> Yet, it also has “unequal income distribution, poverty, poor access to public services, and human rights abuses. Argentina, which is far from being called a “failed state,” still faces “[large income inequality], poverty, extensive deforestation, human right abuses by police and corrupt relations between governors and the judicial system in the provinces.”<sup>100</sup> Venezuela, perceived as the most corrupt in the Latin America, falls behind its counterparts in the upper-middle income group due to “existing [income inequality among population, massive and endemic] corruption in [the judicial system or profiteering by ruling elites], legitimacy of the state, [lack of political opposition], high media scrutiny (that is, the media is highly scrutinized and harassed), [human rights violations], and [fragmentation of ruling] elites.”<sup>101</sup> Colombia, with its “ongoing insurgencies heavily financed by an illegal drug trade and [significant violations of] human rights, [limited access to education, and high] poverty”<sup>102</sup> is close to the lower-middle income group of countries. We can conclude that with all the challenges they face, Mexico, Brazil and Ecuador are still at the forefront of the oil and gas dependent countries of the Latin America.

### VIII. MEASURING CORRUPTION

In this section, we look at the factors that are generally seen as strongly associated with corruption: level of political and civil liberties, governance, and qualities of democratic or autocratic authorities in governing institutions. Some major studies (Mauro, 1997) on corruption have tended to use corruption indices to statistically explain growth through the composition of government expenditure and investment ratios, while others (Svensson, 2005) found human capital, openness to trade, freedom of press, and regulation of entry start-ups to be important elements of not only defining but measuring the degree or level of corruption. Given the recent advances in efforts to quantify corruption through indexing and ranking, we investigated corruption indices developed by various well-established research institutions and multilateral agencies. We further subdivided these indices based on their methodologies and typologies: (i) ranking-based, (ii) survey-based, and (iii) special projects indexes. Table 3 shows some of the major indices that attempt to measure corruption. Due to the lack of consistent data, we are forced to utilize only a portion of available methodologies. Our sample period is from 1996 to 2007 and our assumption is that a wide variety of economic conditions can be captured during this particular twelve-year timeframe.

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99. THE FUND FOR PEACE, COUNTRY PROFILE: BRAZIL (2009).

100. THE FUND FOR PEACE, COUNTRY PROFILE: ARGENTINA, *supra* note 87.

101. THE FUND FOR PEACE, COUNTRY PROFILE: VENEZUELA, *supra* note 89.

102. THE FUND FOR PEACE, COUNTRY PROFILE: COLOMBIA, *supra* note 90.

TABLE 5: VARIOUS METHODOLOGIES FOR MEASURING CORRUPTION

<b>RANKING-BASED</b>	<b>INSTITUTION</b>
International Country Risk Guide	Political Risk Services, Inc.
Financial Ethics Index (FEI)	Business Environment Risk Intelligence (BERI)
Public Integrity Index	Global Integrity
<b>SURVEY-BASED</b>	
Corruption Perception Index	Transparency International
Global Corruption Barometer	Transparency International
Bribe Payers Index	Transparency International
The Worldwide Governance Indicators (WGI) project	World Bank
Business Environment and Enterprise Performance Survey (BEEPS)	EBRD, World Bank
Anti-corruption Assessment Index (ACAI)	World Bank
Business International	IMF, Economist Intelligence Unit
Freedom	Freedom House
Electoral Democracies	Freedom House
Failed State Index	Fund CAST
Open Budget	Open Budget Initiative
Polity index	Center for Intern. Dev. and Conflict, University of Maryland
Opacity Index	PricewaterhouseCoopers/MIT Sloan
<b>SPECIFIC PROJECTS</b>	
Revenue Transparency Project	Transparency International
Public Accountability Project	World Bank
Publish What You Pay	Open Society Institute

## A. VARIABLES AND MEASURES

### 1. *Corruption Measurements*

To derive our independent variable of corruption we used the well-established Political Risk Services, Inc.'s (PRS) International Country Risk Guide—an annual index which is commonly used in the literature.<sup>103</sup> This particular index measures the degree of corruption as perceived by foreign investors. The value of this variable ranged from 0 to 6, with 0 indicating a high level of corruption and 6 representing a low level. According to the PRS, this variable is a measure of corruption within the political system that is a threat to foreign investment by distorting the economic and financial environment, reducing the efficiency of government and business by enabling people to assume positions of power

103. See, e.g., Stephen Knack & Philip Keefer, *Does Social Capital Have an Economic Payoff? A Cross-Country Investigation*, 112 Q. J. ECON. 1251, 1266 (1997).



through patronage rather than ability, and introducing inherent instability into the political process.

Another variable we use is Freedom in the World from the Freedom House, which is a combination of political rights and civil liberties as measured by the World from Freedom House. "F," "PF," and "NF," respectively, stand for "Free," "Partly Free," and "Not Free." We have assigned the following values to the countries: "free" countries-3, "partially free" countries-2, and "not free" countries-1, so that 3 signifies a higher level of country's freedom. Dummy variables are used for electoral democracies from the Freedom House index (Yes=1 indicates that a country was considered to be an electoral democracy for the year; No=0 indicates that a country was not).

We also utilize the World Bank Governance Indicators, which include six dimensions such as: Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption. These governance indicators are measured in units ranging from about -2.5 to 2.5; higher values correspond to better governance outcomes. These indicators reflect the quality of governance as seen by a large number of enterprise, citizen and expert survey respondents, as reported by a number of survey institutes, think tanks, non-governmental organizations, and international organizations.

We used the Polity Index because its approach is unique in that it examines concomitant qualities of democratic and autocratic authority in governing institutions, rather than discreet and mutually exclusive forms of governance. The "Polity Score" captures a regime's authority spectrum on a 21-point scale ranging from -10 (hereditary monarchy) to +10 (consolidated democracy). The Polity scores can also be converted to regime categories: we recommend a three-part categorization of "autocracies" (-10 to -6), "anocracies" (-5 to +5 and the three special values: -66, -77, and -88), and "democracies" (+6 to +10).<sup>104</sup>

## 2. *Economic Performance Indicators*

To investigate the impact of corruption on economic development, we use the following economic performance indicators to measuring various aspects of development i.e. standard of living: GDP per capita growth (annual percentage), GDP per capita, PPP (current international \$), HDI, and the Index of Economic Freedom.

The data on GDP per capita, PPP and annual growth rate of GDP per capita were obtained from the World Bank World Development Indica-

104. The Polity scheme consists of six component measures that record key qualities of executive recruitment, constraints on executive authority, and political competition. It also records changes in the institutionalized qualities of governing authority. The Polity data include information only on the institutions of the central government and on political groups acting, or reacting, within the scope of that authority. It does not include consideration of groups and territories that are actively removed from that authority (i.e., separatists or "fragments").

tors. The Index of Economic Freedom obtained from the Heritage Foundation assesses ten specific freedoms ranging from property rights to entrepreneurship. We use it as a measure of potential output. The Human Development Index (HDI) is a combination of education, life expectancy, and income indices is used to measure country' development; however, we believe that it deficient in the arena of human rights.

### 3. *Control Variables*

To control for oil dependency, we utilize the variable that we used in the first part of our paper—the share of oil and gas exports in total exports. The data are taken from the International Monetary Fund, the International Trade Center Trade Competitiveness Map, and World Bank Development Indicators.

## IX. ECONOMETRIC FRAMEWORK

In trying to measure corruption and its impact on economic development we use the following econometric methodology. We use a dynamic panel with data averaged over three-year periods from 1996–2007. Our primary hypothesis is as follows:

Hypothesis 1: **Other things being equal, high corruption is associated with low levels of economic development in oil- and gas-rich countries.**

As to be expected, corruption indicators seem to be highly correlated with each other. On the one hand, that shows consistency of given indicators, but on the other hand, we introduce the issue of multi-collinearity into the estimation. In order to reduce the subjectivity of the individual indices, as well as deal with the multi-collinearity, we have used the Principal Components Analysis to best capture opinions of the observers who constructed the corruption indices. It allows for constructing the standardized uncorrelated variables with mean 0 and variance 1.

To analyze the Latin American region in detail, we have formed a second hypothesis:

Hypothesis 2: **Other things being equal, high corruption is associated with low levels of economic development in Latin American oil- and gas-rich countries.**

## X. RESULTS

Tables 6 and 7 provide the descriptive statistics and the most and least corrupt countries, respectively. Not surprisingly, Colombia and Venezuela demonstrate a lack of political stability. Interestingly, Ecuador, which is perceived to be the least corrupt by its foreign investors among these countries, still faces a significant decline in government effectiveness.<sup>105</sup> As mentioned before, Venezuela, with its socialist policies, is

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105. See *supra* Table 5.

seen to perform the worst in terms of regulatory quality, or the perceptions of the ability of the government to formulate sound policies to promote private sector development. Also, the country faces a low confidence in the quality of property rights, the police and the courts, as well as a lack of mechanisms to control corruption.

Interestingly, other Latin American countries such as Brazil, Mexico, and Argentina, unlike the Persian Gulf countries, seem to have democratic authorities in place. The extent to which the citizens of these three countries can participate in the election process and express their freedom of speech is close to that of Canada and Norway. Mexico is also among the top five performing countries in terms of regulatory quality, or the ability of government to promote private businesses, which is not surprising given its proximity to the United States.

On the other hand, small and politically stable states of the Persian Gulf, such as the UAE, Kuwait, and Qatar demonstrate high levels of government effectiveness, regulatory quality, rule of law, and control of corruption.

TABLE 6: SUMMARY STATISTICS, 1996-2007, 3-YEAR PERIODS, N=80

	Mean	Standard deviation	Minimum value	Maximum value
Growth rate of GDP per capita	3.37	4.54	-3.89	27.36
GDP per capita, PPP	15,901	15,976	1,221	72,239
HDI	0.77	0.12	0.45	0.97
Index of Economic Freedom	56.21	11.78	23.96	77.06
PRS's Corruption	2.57	1.12	1.00	6.00
Freedom in the World	1.77	0.77	1.00	3.00
Electoral Democracy	0.45	0.49	0.00	1.00
Polity Index	0.64	7.18	-10.00	10.00
WB Voice	-0.46	0.88	-1.91	1.58
WB Political Stability	-0.39	0.96	-2.30	1.43
WB Government Effectiveness	-0.14	0.89	-1.33	2.14
WB Regulatory Quality	-0.24	0.87	-2.14	1.58
WB Rule of Law	-0.27	0.96	-1.62	2.00
WB Control of Corruption	-0.18	0.99	-1.54	2.23
Oil Dependency	62.34	32.58	1.00	99.55

TABLE 7: THE MOST CORRUPT OIL AND GAS RICH COUNTRIES (BOTTOM 5)

Country	Corruption (PRS)	Country	Polity	Country	Voice and Accountability	Country	Political Stability
Nigeria	1.33	Saudi Arabia	-10	Libya	-1.78	Colombia	-1.74
Russian Federation	1.71	Qatar	-10	Saudi Arabia	-1.54	Nigeria	-1.73
Azerbaijan	1.88	UAE	-8	Angola	-1.28	Algeria	-1.62
Kazakhstan	1.88	Kuwait	-7	Iran	-1.23	Angola	-1.32
Algeria	1.92	Libya	-7	Algeria	-1.06	Venezuela	-0.99

Country	Government Effectiveness	Country	Regulatory Quality	Country	Rule of Law	Country	Control of Corruption
Angola	-1.18	Libya	-1.57	Angola	-1.42	Nigeria	-1.25
Nigeria	-1.03	Iran	-1.45	Nigeria	-1.34	Angola	-1.24
Libya	-0.84	Angola	-1.36	Venezuela	-1.09	Azerbaijan	-1.03
Ecuador	-0.81	Nigeria	-1.03	Kazakhstan	-0.89	Venezuela	-0.97
Venezuela	-0.78	Venezuela	-0.83	Russia	-0.88	Kazakhstan	-0.96

Note: time period 1996-2007

TABLE 8: THE LEAST CORRUPT OIL AND GAS RICH COUNTRIES (TOP 5)

Country	Corruption (PRS)	Country	Polity	Country	Voice and Accountability	Country	Political Stability
Canada	5.46	Canada	10.0	Norway	1.56	Norway	1.33
Norway	5.08	Norway	10.0	Canada	1.51	Canada	1.08
Iran	3.00	Brazil	8.00	Brazil	0.35	Qatar	0.83
Ecuador	2.96	Argentina	7.75	Argentina	0.28	UAE	0.74
Libya	2.87	Mexico	7.16	Mexico	0.12	Kuwait	0.19

Country	Government Effectiveness	Country	Regulatory Quality	Country	Rule of Law	Country	Control of Corruption
Norway	2.08	Canada	1.48	Norway	1.94	Norway	2.08
Canada	2.02	Norway	1.33	Canada	1.77	Canada	1.99
UAE	0.67	UAE	0.71	UAE	0.77	Kuwait	0.83
Qatar	0.41	Mexico	0.42	Kuwait	0.74	Qatar	0.78
Kuwait	0.24	Qatar	0.31	Qatar	0.62	UAE	0.77

TABLE 9: CORRELATION MATRIX, 1996-2007, THREE-YEAR PERIODS, n=80

	Growth rate of GDP per capita	GDP per capita, PPP	HDI	Index of Economic Freedom	Corruption	Freedom in the World	Electoral Democracy	Polity Index	WB Voice	WB Political Stability	WB Government Effectiveness	WB Regulatory Quality	WB Rule of Law	WB Control of Corruption	Oil Dependency
Growth rate of GDP per capita	1														
GDP per capita, PPP	-0.07	1													
HDI	-0.12	0.691*	1												
Index of Economic Freedom	-0.19***	0.56*	0.613*	1											
Corruption	-0.22**	0.26**	0.473*	0.24**	1										
Freedom in the World	-0.23***	0.02	0.418*	0.474*	0.48*	1									
Electoral Democracy	-0.26***	-0.14	0.35**	0.35*	0.33*	0.84*	1								
Polity Index	-0.2***	-0.27*	0.194	0.21***	0.42*	0.81*	0.88*	1							
WB Voice	-0.17	0.31*	0.56*	0.61*	0.67*	0.87*	0.73*	0.75*	1						
WB Political Stability	-0.06	0.74*	0.77*	0.54*	0.49*	0.29*	0.07	-0.01	0.56*	1					
WB Government Effectiveness	-0.14	0.69*	0.74*	0.71*	0.67*	0.52*	0.32*	0.30*	0.79*	0.80*	1				
WB Regulatory Quality	-0.15	0.61*	0.67*	0.88*	0.46*	0.55*	0.39*	0.32*	0.76*	0.71*	0.89*	1			
WB Rule of Law	-0.19***	0.79*	0.75*	0.71*	0.63*	0.37*	0.14***	0.08	0.66*	0.86*	0.94*	0.84*	1		
WB Control of Corruption	-0.19***	0.79*	0.75*	0.69*	0.65*	0.39*	0.17	0.13	0.68*	0.80*	0.95*	0.83*	0.95*	1	
Oil Dependency	0.14	0.05	-0.40*	-0.41*	-0.38*	-0.69*	-0.67*	-0.69*	-0.69*	-0.29*	-0.44*	-0.55*	-0.26**	-0.28**	1

\* = indicates a statistical significance at 0.01 level

\*\* = indicates a statistical significance at 0.05 level

\*\*\* = indicates a statistical significance at 0.10 level

Note: This table is based on common sample of 20 countries using the data averaged over 3-year periods.

As to be expected, corruption coefficients are highly correlated with each other (Table 9). We decided to carry the Principal Component Analysis (provided in Table 10) to group the corruption variables in similar groups. We dropped the Voice/Accountability from the WB Governance Indicators because it had high loads on more than one component; hence, it was not considered as a pure measure of any one construct.

Table 8 shows the variability in the set of individual indices explained by each principal component, as well as the correlation of the first two components with each of the individual indices. In each case, the first two principal components explain close to 90 percent of the variability among the individual indices and have high positive correlations with each of them. Thus, we only use the first two principal components in our regression analysis. Using the factor loading of 0.40 or greater as a cutting threshold, we find Freedom, Electoral Democracies and Polity index to load on the first component, which we subsequently labeled "electoral system component." Six items: Corruption, Political Stability, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption, loaded on the second component, which was labeled "business/legal system component."

TABLE 10: PRINCIPAL COMPONENT ANALYSIS

Component	Variation Proportion	Cumulative	Correlations Variable	Factor 1 – Business/ Legal System	Factor 2 – Electoral System
Factor 5	0.0144	0.9708	WB Voice and Accountability*	0.62568*	0.75548*
<b>Business/Legal System</b>					
Factor 1	0.6314	0.6314	Corruption	0.62785	0.39078
Factor 6	0.0120	0.9828	WB Political Stability	0.89940	-0.01588
Factor 7	0.0095	0.9923	WB Government Effectiveness	0.93887	0.27880
Factor 8	0.0033	0.9956	WB Regulatory Quality	0.83327	0.33046
Factor 9	0.0027	0.9982	WB Rule of Law	0.98366	0.07144
Factor 10	0.0018	1.0000	WB Control of Corruption	0.96811	0.11323
<b>Electoral System</b>					
Factor 2	0.2413	0.8727	Freedom	0.31460	0.88740
Factor 3	0.0582	0.9309	Electoral	0.05834	0.94997
Factor 4	0.0255	0.9564	Polity	0.01779	0.96443

\* We dropped this variable as it does not determine any variable in particular.

TABLE 11: REGRESSION ANALYSIS USING PRINCIPAL COMPONENTS OF CORRUPTION INDICES

Dependent variable	GDP per capita, PPP			Growth rate of GDP per capita		HDI			Index of Economic Freedom		
	6977 (<.0001)	10073 (<.0001)	2196 (<.0001)	2.37 (0.039)	5.98 (0.004)	0.825 (<.0001)	0.829 (<.0001)	0.779 (<.0001)	61.9 (<.0001)	58.96 (<.0001)	53.52 (<.0001)
Constant											
Business/ Legal System	14205 (<.0001)	13774 (<.0001)	11773 (<.0001)	-0.44 (0.405)	-0.255 (0.69)	0.088 (<.0001)	0.088 (<.0001)	0.076 (<.0001)	7.162 (<.0001)	7.571 (<.0001)	6.188 (<.0001)
Electoral System		-2163 (0.108)	-1664 (0.1893)		-1.402 (0.058)		-0.003 (0.83)	-0.0007 (0.956)		2.053 (0.129)	2.398 (0.071)
Electoral System *2			6528 (0.006)		-1.452 (0.196)			0.042 (0.045)			4.513 (0.027)
Oil Dependency	143.14 (<.0001)	93.48 (0.03)	116.41 (<.0001)	0.02 (0.33)	-0.019 (0.423)	-0.001 (0.021)	-0.0007 (0.071)	-0.001 (0.15)	-0.09 (0.003)	-0.044 (0.301)	-0.028 (0.501)
Number of observations	80	80	80	80	80	73	73	73	80	80	80
R <sup>2</sup> adjusted	0.737	0.746	0.781	0.067	0.087	0.617	0.617	0.639	0.449	0.529	0.559

Note: A panel data, 3-year averages from 1996-2007.



Table 11 provides the results of the dynamic panel regression, which incorporates the Principal Component Analysis results. We find the corruption indices that belong to the so-called “business/legal system” to be statistically significant. This component deals with corruption “as perceived by foreign investors,”<sup>106</sup> a diverse range of households and firms, as well as thousands of experts from NGOs, public sector agencies and private sector.<sup>107</sup> It captures the extent, to which public power is exercised for private gain, and to which agents abide by the rules of society; it also evaluates the quality of public services, property rights, the ability of the government to formulate sound policies to promote private sector, the likelihood of crime and violence and the likelihood that the government may be overthrown by violent means.<sup>108</sup> We believe that they can also be used to make predictions about a country’s economic, as well as human development, performance. The greater values of this component are associated with the lower levels of corruption as determined above. These finding support our first hypothesis that high corruption is associated with low levels of economic development in oil- and gas- rich countries. However, it only holds for such characteristics of corruption such as those combined under Factor 1 (Business/Legal System): investment climate, political stability, quality of regulatory framework, and measures to control corruption.

When we start looking at corruption from the perspective of “electoral system,” we find a quadratic non-linear relationship between the corruption indices associated with this component and the measures of economic performance.<sup>109</sup> Both types of countries, autocratic and democratic, seem to enjoy relatively high human and economic development. The relationship between them has a U-shaped form.

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106. INTERNATIONAL COUNTRY RISK GUIDE METHODOLOGY, THE PRS GROUP; Zohal Hessami, On the Link Between Gov’t Ideology & Corruption in the Public Sector (June 15, 2011), *available at* <http://extranet.isnie.org/uploads/isnie2011/hessami.pdf> (unpublished paper for 2011 ISNIE Meeting at Stanford University).

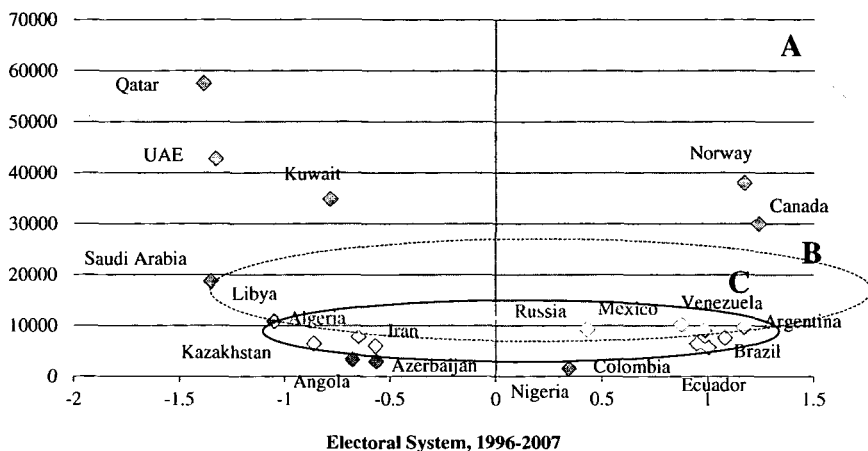
107. Daniel Kaufmann, Aart Kraay, & Massimo Mastruzzi, *Governance Matters VIII: Aggregate & Individual Governance Indicators 1996–2008* 4 (The World Bank Dev. Research Grp., Working Paper No. 4978, June 2009).

108. *Id.* at 5–6.

109. *See, e.g., supra* Figure 10.

FIGURE 10: RELATIONSHIP BETWEEN GDP PER CAPITA  
AND ELECTORAL SYSTEM

GDP per capita, PPP, 1996–2007



Note: a panel data, 1996–2007.

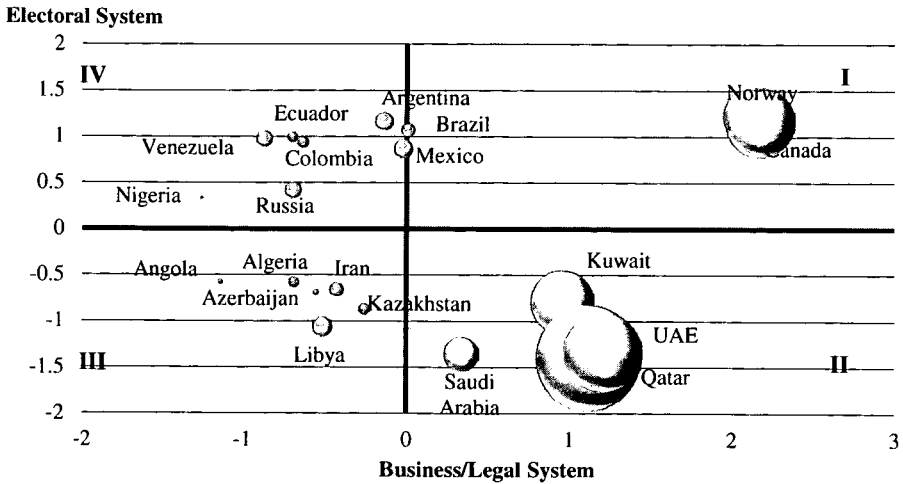
Source: WORLD BANK, WORLD DEVELOPMENT INDICATORS (2009) (authors' calculations).

These analyses identify a paradox in the linkage between corruption and sustainable economic growth in oil- and gas-based dependent countries. It turns out that corruption has a differential impact on countries' economic performance and human development; the nature of relationship changes depending on which dimension of corruption we are investigating.

When combining different dimensions of corruption, we find the countries under consideration fall into four quartiles.<sup>110</sup> In the first quartile we see the least corrupt and most democratic oil- and gas-rich countries of Norway and Canada. The Persian Gulf countries, with the exception of Iran, fall into the second quartile. The Latin American countries in the fourth quartile can be characterized as free or partially free democracies with regularly held elections and civil rights, allowing citizens to express their political views. The greater the political rights and civil liberties of citizens are, the greater should be the proclivity of the government officials to be elected. The more democratic the authorities that govern institutions are, the better the country's economic and human development should be. Yet, the Latin American countries are still relatively more corrupt in terms of government efficiency, law enforcement, and promotion of private business than the Persian Gulf countries. Also, given the fact that all the Latin American countries are in more or less the same phase of having electoral democracies, it is interesting to see that their GDP per capita level is still relatively low when compared to countries of approximately same level in quartile I.

110. See *supra* Figure 11.

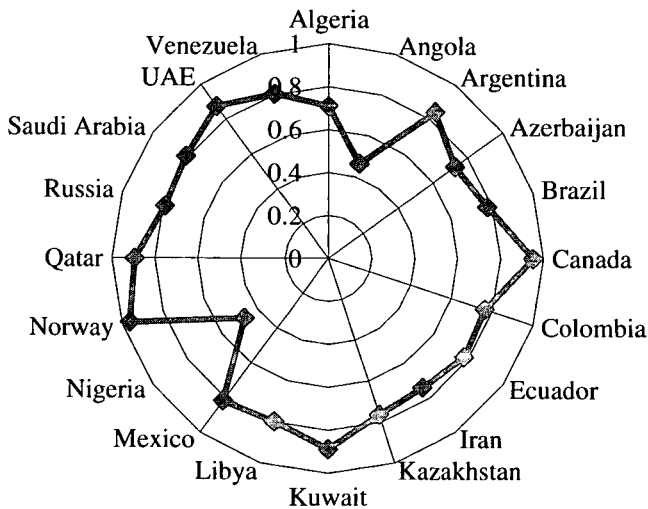
FIGURE 11: RELATIONSHIP BETWEEN BUSINESS/LEGAL, ELECTORAL SYSTEMS, AND GDP PER CAPITA



Note: Size of bubbles equals GDP per capita. We use a panel data, 1996–2007.

Source: INTERNATIONAL TRADE CENTER, TRADE MAP-TRADE COMPETITIVENESS MAP (2010); WORLD BANK, WORLD DEVELOPMENT INDICATORS (2009) (authors' calculations).

FIGURE 12: HDI PERFORMANCE



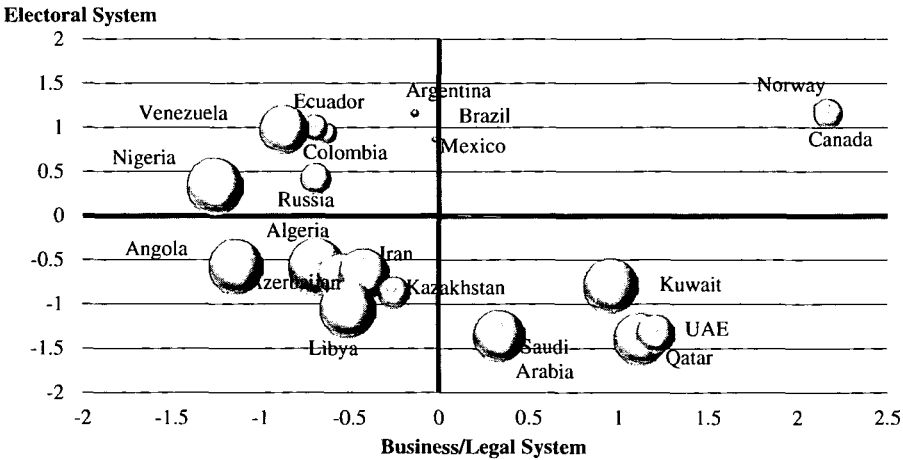
Note: a panel data, 1996–2007.

Source: UNITED NATIONS DEVELOPMENT PROGRAMME, NATIONAL AND REGIONAL HUMAN DEVELOPMENT REPORTS (2009).

Given such a difference in GDP per capita for the level of their electoral system and the levels of corruption in business/legal system between Venezuela and, for example, Brazil, Argentina, and Mexico, it is surprising to find that there is not much variability in the levels of human development across the Latin American region. When we further investigate which countries in this region have a more corrupt business and legal

environment, we see an inverse relationship between how corrupt governments are and how dependent the governments of these countries are on oil and gas. Argentina, Brazil, and Mexico, which are relatively less dependent on oil and gas exports, tend to have lower levels of corruption as perceived by foreign investors, NGOs, and many other experts, as opposed to Venezuela, Ecuador, and Colombia.

FIGURE 13: RELATIONSHIP BETWEEN BUSINESS/LEGAL, ELECTORAL SYSTEMS, AND OIL DEPENDENCY



Note: Size of bubbles equals Oil Dependency (Oil and gas exports as % of total exports). We use a panel data, 1996–2007.  
Source: INTERNATIONAL TRADE CENTER, TRADE MAP-TRADE COMPETITIVENESS MAP (2010) (authors' calculations).

While in the above analysis we try to define the factors that are responsible for successful economic performance of oil-and gas-rich countries, it should be noted that this type of analysis has significant limitation. The lack of consistent and reliable data continues to plague this type of research even though recently a wide variety of corruption indicators have been developed. Also, the statistical information submitted by the governments of some countries is incomplete and varies in quality. Most certainly we face the causality issue when conducting this type of research. Many studies claim corruption evolves (or devolves) in response to changes in the economic development of a country. Poor governments are not capable of sustaining a high wage for public officials, and it is well documented in the literature that low civil services wages (below private markets wages) breeds corruption.<sup>111</sup> On the other hand, rapid moderni-

111. Jie Bai, Seema Jayachandran, Samuel P. Huntington, *Does Economic Growth Reduce Corruption? Theory & Evidence from Vietnam* (Nat'l Bureau of Econ. Research, Working Paper No. 19483, Sept. 2013); Caroline Van Rijckeghem & Beatrice Weder, *Corruption & the Rate of Temptation: Do Low Wages in the Civil Service Cause Corruption?* 1–2 (Int'l Monetary Fund, WP/97/73, June 1997).

zation in the country may cause higher corruption.<sup>112</sup> It is, however, equally important to recognize that corrupt institutions may, in fact, determine the economic development and success of country.

## XI. CONCLUSIONS

In the first part of this study we found that even though there is high corruption, several countries still exhibited good economic performance. This is true, for example, in Libya and Kazakhstan. Furthermore, it is interesting to note that when the World Bank Governance indicators are used, several small oil- and gas-rich Persian Gulf countries (Qatar, Kuwait, and the UAE) show that they are relatively less corrupt on all the indicators (except voice and accountability) ranging from rule of law, control of corruption, and political stability. In Latin America, all countries, except Venezuela, offer an environment conducive to business as opposed to other countries in this upper middle income category, such as Russia and Algeria, which were found to have environments hampering the growth of private businesses. This suggests, for example, a differential effect of corruption on the business as opposed to the political environment.

Next, in investigating the political environment, we found that the "electoral system" component—which combines such variables as a presence of electoral democracy, state of the country (free/not free), and whether the country is an autocracy or a democracy—has a U-shaped relationship with countries' economic performance and human development. This suggests that countries at both ends of the spectrum ranging from autocratic to democratic regimes may still enjoy relatively similar levels of human and economic development.

The laws guarding against corruption related to the exploitation of natural resources are simply not respected or enforced. The "business/legal system" component, which tries to capture corruption as perceived by a large number of stakeholders, including foreign investors, NGOs, and public service, indeed plays a significant role in the context of corruption and economic growth (an inverse positive relationship). The link between business/legal framework and economic growth manifested a positive correlation between economic and human development and the "business/legal system" component.

There is a huge disparity among the Latin American countries in terms of business and legal environment. Countries that are rated as more corrupt demonstrate a larger export dependency on the sales of oil and gas. Interestingly, all the Latin American countries attain approximately the same level of human development and civil liberties. This suggests that corruption in the business and legal environment may significantly hinder the businesses in countries that are heavily dependent on oil and gas exports. Having an electoral democracy seems to have no significant effect,

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112. SAMUEL P. HUNTINGTON, *POLITICAL ORDER IN CHANGING SOCIETIES* 32 (1968).

as all the Latin American countries enjoy relatively similar levels of human development. It is possible that countries heavily dependent on oil and gas such as Venezuela, Ecuador, and Colombia can afford to subsidize the social programs for their citizens.

The timeframe of our analysis is too short to fully gauge the effect of corruption on sustainable economic growth. With corruption, the time horizon should be measured in decades, rather than in years. In the long run, countries that have higher freedom tend to have higher non-oil GDP growth. No highly corrupt country with low freedom can gain a growth advantage over a country that has had two decades or more of low corruption and high freedom.

