Analysis of predictors of organizational losses due to occupational corruption

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A B S T R A C T

This article focuses on the empirical analysis of individual level predictors of organizational losses due to occupational corruption – intentional actions, in which employees misuse their influence in business transactions in a way that violates their duty to the employer or in order to gain a direct or indirect benefit at the cost of the employer. Although organizations suffer enormously from occupational corruption, so far no empirical studies link micro and macro data on occupational corruption together in order to explain what predicts these losses. In this study, I examine intra-class correlations for assessing the impact of micro and country level predictors of organizational losses due to occupational corruption, and propose a linear model for estimating micro level predictors since they account for the largest percentage in the variance of organizational losses. For the purpose of analysis, I have used the original global micro level data based on victimization survey on 1694 occupational corruption cases reported by certified fraud examiners of 37 countries between January 2002 and December 2011. The results determine that in order to prevent losses due to occupational corruption, organizations should care more about individuals they employ rather than the country or industry they operate in or organization type they have, although minor differences in issue-specific predictors inside and outside the US exist.

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1. Introduction

Previous investigations in organizational misconduct typically distinguish between governmental and corporate (Finney & Lesieur, 1982); collective and individual (Brief, Buttram, & Dukerich, 2001; Palmer, 2008); actively participated and passively acquiesced (Daboub, Rasheed, Priem, & Gray, 1995); non-intentional (accidental) and intentional (Baucus, 1994); beneficial (corporate) and cost-creating (occupational) corruption (Clinard & Quinney, 1973).

The last distinction requires additional clarification. In corrupt organizations, employees do not enrich themselves; instead, corrupt organizations expect and encourage their employees to facilitate criminal behavior to attain organizational goals and achieve advantages for their organization in an illicit manner (Pinto, Leana, & Pil, 2008). Here, corruption is a customary behavior, and employees actually behave criminally in a more or less corrupt environment. Moreover, employees facilitate corruption in collaboration with their colleagues for the benefit of the organization as a whole (Palmer, 2008; Pinto et al., 2008). Corrupt organizations systematically receive illegitimate or illicit benefits such as advantages in competitions or relaxations of political regulations. For example, The Fiscal Times (2011) published a summary of the top ten recent global business corruption cases that occurred in the years 2008–2011, where the settlement amount varied from $70 million to $1.6 billion. Association of Certified Fraud Examiners (ACFE, 2014) reported that every third organization suffers from occupational corruption recently losing $250,000 in median.

While sometimes organizations are considered to benefit from unethical behavior of their employees (Umphress & Bingham, 2011), in this article, I take a perspective of corruption where employees behave in a way that violates their duties to the employer in order to gain a direct or indirect benefit, even though a more or less non-corrupt environment surrounds them. In general, such organizations do not tolerate corrupt behavior and punish these employees (Pinto et al., 2008). In this paper, I treat corruption as occupational intentional actions, in which employees misuse their influence in business transactions in a way that violates their duty to the employer in order to gain a direct or indirect benefit at the cost of the organization (e.g., schemes involving bribery, illegal gratuities, conflicts of interest and economic extortion), conducted either individually or collectively in organizations of any type.

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What are the most important predictors – micro or macro level? What are the effects of these predictors on losses due to occupational corruption? These questions arise immediately when one deliberates this problem. I agree with Tenbrunsel and Smith-Crowe (2008, p. 591) who, argue in their review, "a connection between ethical decision making and organizational ethics – the micro and the macro – could produce significant new insights." Empirical studies suffer from the lack of multilevel analysis, which could solve this micro-macro problem by assessing the impact of variables of each level into losses due to occupational corruption, as well as investigations assessing the impact of predictors on these losses. With this study, I intend to bridge the gap that has existed for so long by reason global victimization micro level data on organizational losses due to occupational corruption have become available only recently.

From a practitioner's point of view, this question is of great importance because both organizations that have and have not already suffered from occupational corruption are interested in preventing or at least decreasing future losses. In contrast to prior empirical studies which typically consider either country or organizational or individual level variables, in this study I focus on identifying the most important predictors of organizational losses due to occupational corruption and further assess the impact of these variables.

For the purpose of the study, I employ multilevel model to estimate intra-class correlation using the original global micro level data on corruption collected by the certified fraud examiners to determine which variables are the most important in the existing hierarchy of the individual, organizational, industry and country level predictors of organizational losses due to corruption. By developing literature based hypotheses and intuition driven predictions that essentially determine that organizational losses due to occupational corruption are mainly driven by issue-specific micro level variables, I have found some supporting empirical evidence and designated horizons for further research aimed at fraud prevention. From a practitioner's prospective, the results essentially determine that in order to prevent losses due to occupational corruption, organizations should care more about individuals it employs rather than the country or industry they operate in or organization type they have, although there are minor differences in issue-specific predictors inside and outside the US.

Following this introduction, I present a review of the related literature that covers the theoretical and empirical studies on corruption. Next, the method is introduced to reveal the most significant predictors of organizational losses due to corruption and assess their effects through analysis and discussion of the results. This paper closes with major contributions, limitations and justified suggestions for further research on the topic.

2. Theoretical and empirical background

2.1. What do we know?

To begin, it is necessary to distinguish between determinants of corruption as a phenomenon and predictors of organizational losses due to occupational corruption, although, the difference may seem insignificant at the first glance. Technically speaking, determinants of corruption as a phenomenon can be identified either experimentally or empirically if one has either a full sample or at least a reference group of cases that includes cases with similar characteristics free from corruption. This is applicable to theory as well because one has to possess either complete or representative information to understand what has gone wrong in cases with corruption. Since one can hardly envision this, it is possible to identify only predictors of losses due to corruption once one has it as a dependent variable. In this study, I concentrate on

these predictors, assuming a certain degree of their similarity to determinants of corruption. These predictors only inform about correlation with losses due to occupational corruption rather than causation. Although there are no studies that show the relation among these predictors and driving forces, I assume that they are highly correlated. By this reason, it seems logical to start with summarizing theoretical and empirical findings on corruption as a phenomenon and its determinants to determine some fruitful insights for further analysis of predictors of losses due to occupational corruption.

Corruption has been studied across several disciplines, which usually examine this phenomenon at a particular level of analysis: individual (psychology, economics, or business ethics), organization (accounting, sociology) or economy (political science). In the next two subsections, I summarize the recent theoretical and empirical findings.

2.2. Microeconomic determinants

There are three major streams of research here (for a meta study see Kish-Gephart, Harrison, & Treviño, 2010; for extensive reviews see Grève, Palmer, & Pozner, 2010; Tenbrunsel & Smith-Crowe, 2008) which concentrate on either individual, organizational level (see Table 1) or only country level determinants.

The first stream focuses on revealing individual level determinants associated with corruption and misconduct in organizations (Treviño, Weaver, & Reynolds, 2006; Reynolds, 2006). Rest's (1986) theoretical framework, which lays out four steps for ethical decision making: moral awareness (the interpretation of a situation or issue as a moral question), moral judgment (the decision as to which course of action is morally right), moral intent (the prioritization of moral values over other values) and moral behavior (the execution of moral intent), has significantly influenced this stream. Rest (1986) argues that misconduct is the consequence of a failure at any of these four steps.

O'Fallon and Butterfield (2005), through reviewing empirical studies, analyzed the effects of different independent variables at individual levels such as cognitive moral development (how individuals advance in their thinking in moral dilemmas), job satisfaction, locus of control (beliefs about whether the outcomes of our actions are contingent on what we do or determined by outside forces), Machiavellianism (usage of interpersonal relationships opportunistically and deceiving others for personal gain), value orientation and demographics or organizational level (ethical climate, ethical culture, organizational size, codes of conduct and industry type) on each of Rest's four variables.

Essentially, scholars have considered individual predispositions, such as, low level of cognitive moral development, high Machiavellianism, external locus of control and job dissatisfaction, strain and individual unfairness perception, such as, feeling underpaid to be determinants of corruption. Some researchers often use demographic determinants such as age, gender, tenure, nationality, religion, education, social class and self-control to predict corrupt behavior, although they have been strongly criticized (Lawrence, 1997; Priem, Lyon, & Dess, 1999).

Treviño (1986) established the relationship between individuals and external determinants in her model, in which she argued that both individual level and situational variables, such as the ethical climate of an organization and its code of ethics, influence ethical decision-making. Similarly, Jones' (1991) model introduced the notion of "moral intensity" to highlight the effect of issue-specific determinants, such as social consensus about morality of the issue and the perceived magnitude of consequences.

The second stream of research on corruption and misconduct in organizations focuses on organizational determinants. For example, the cultural perspective attempts to explain corruption and