

# Corruption or Incompetence?

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We study situations in which inefficiencies in public procurement managed by politicians come from two sources: corruption (moral hazard) and incompetence (adverse selection). We assess the respective impact of judicial and accounting courts on the cost effectiveness of procurement and the level of corruption. We show that, although improving the quality of both courts matters as a direct deterrent of corruption, it may also indirectly decrease the quality of the pool of politicians and hence deteriorates the cost efficiency of procurement.

## DISTINGUISHING CORRUPTION FROM INCOMPETENCE

When public sector services costs more than they should, it is hard for voters to know if it is due to the corruption, to the incompetence or simply to the bad luck of the politician running the procurement process. If the higher than needed cost reflects rents extracted by a competent but corrupt politician, the issue is moral hazard. If the poor cost performance is linked to poor skills, the voter is facing an adverse selection problem.

For voters, assessing the skills and honesty of politicians is particularly difficult because any politician delivering a project at high cost would claim bad luck rather than admitting corruption or incompetence. When bad luck cannot be blamed, the least scrupulous politicians can use this confusion to claim to be incompetent rather than corrupt.

In most countries, the judicial system is expected to mitigate the moral hazard problem associated with corruption. The adverse selection problem linked to poor skills is expected to be mitigated by the diagnostics of independent public sector auditors. These two types of courts depend on each other. A judge uses the information provided by an accounting court. The auditors rely on the judicial system to address any evidence on cost or process abuses and corruption. **The objective of our paper is to understand how the interaction between these courts affects the characteristics of the individuals choosing to become politicians with respect to skill and the corruption level.**

## OUR APPROACH

We build a theoretical model to understand the respective incentives of citizen with different abilities to enter politics. We assume that, while coming from different sources, corruption and incompetence have a similar impact on the cost of procurement projects. We define a court quality by the precision of its assessment. An accounting court is only able to observe the cost efficiency of a project imperfectly. A judicial court is only able to observe the honesty of a politician imperfectly. **A basic intuition is that the higher the quality, the lower the risk of excessive costs resulting from the procurement process.** The main purpose of this paper is to assess the robustness of this intuition.

We make two assumptions that rule out trivial solutions. First, we rule out the fact that some politicians are genuinely honest and derive no utility from bribes. Second, we assume that each politician choosing to enter the pool of applicants is selected with equal probability, implying that voters cannot screen based on skills. Recent work by Todorov et al. (2005) and Antonokis and Dalgas (2009) indeed show that inferences of competence, based solely on the facial appearance of political candidates are excellent predictors of electoral results.



## WHAT DO WE LEARN?

We find that, as intuition suggests, the direct effect of both institutions is to decrease the probability of corruption. However, we also identify an indirect and possibly detrimental effect: the influence of the quality of a court on the incentives to become a politician. **A better judicial system may decrease the quality of the pool of applicants.** This is because better judges, by separating better incompetent from corrupt politicians, make politics more attractive to the least competent politicians. This reinforces the fact that the least competent politicians have a lower opportunity cost of being in office and hence their best option is to be in politics. Better accounting courts can also decrease the quality of the pool of applicants when they make the profession of politicians more (when only the very best apply), or less (when only the least able apply) attractive to politicians with average ability. When the negative indirect effect outweighs the direct effect on corruption, courts of higher quality may actually decrease the cost efficiency of procurement.



**We then characterize an “ideal” institutional design** that minimizes the expected cost of the projects, the level of corruption and the cases of wrongful convictions. It implies sufficiently good accounting courts, sufficiently bad judicial courts, and a high punishment for those convicted of corruption. It also implies a sufficiently high wage for the most able politicians to enter, but not high enough for the less able to be willing to take the risk of being convicted. We further derive local conditions for a marginal increase in the quality of the judicial and accounting courts, in the wages of politicians and in the punishment of those convicted of corruption to decrease the expected cost of procurement. For instance, it can be locally beneficial to increase the quality of the judicial court when the main driver of high costs is corruption and not incompetence.

## POLICY IMPLICATIONS

The most important implication is that **the three possible leverages a society has on the quality of its politicians are not substitutes, and should be used to solve different problems.**

**First**, if only the most mediocre individuals enter politics, offering higher wages can be a good idea to convince the most able citizens to join the pool of applicants. It does however nothing to prevent corruption and, most importantly, can attract the wrong people if the most able politicians are already interested in politics.

**Second**, investing in better judges and more thorough detection of cases of dishonesty is useful when the main problem is corruption, but can be counterproductive if the problem is that too many incompetent individuals want to become politicians.

**Third**, investing in better accounting courts and cost assessment of public projects also deters corruption, but may worsen the selection problem if only the least able citizens enter politics.

Another implication brings us back to our assumption that voters are not able to screen the cost efficiency of politicians. The ambiguous impact of both courts studied in the paper makes the case even stronger for a higher quality of the democratic screening, such as increasing transparency over the costs of public procurement.

The main message of our paper remains that, as in many policy issues, good intentions building on intuition have their limits since they can lead to perverse effects on the population of politicians.

### References

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