

INSTITUTIONAL THEORY FOR EXPLAINING CORRUPTION: AN EMPIRICAL STUDY ON PUBLIC SECTOR ORGANIZATIONS IN CHINA AND INDONESIA

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Abstract

Many researches on corruption examined macro factors such decentralization, political democracy, press freedom, and economic freedom, as shown by Lecuna (2012), Alexeef and Habodazzova, (2012) and Goel and Nelson (2005). However, there are limited studies on corruption that examine this topic from organizational approach. The main purpose of this paper is to investigate existing institutional theories describing corrupt behaviour in Asian public sector organizations. A total of 171 questionnaires were distributed to public service officers who were currently enrolled as accounting postgraduate students in both China and Indonesia. The results support the institutional theoretical model used to explain corruption in public sector organizations. However, cultural differences in democracy was not a significant factor on respondent's perception concerning corruptions in both of countries.

Keywords: Institutional Theory, Corruption, Public Sector, Task Environment, Institutional Environment, Democracy

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1 Introduction

Asia is a potential region for conducting research on corruption issues (Luo, 2002). Transparency International (2013) showed high-corruption level among public sector organizations in 34 countries in Asia. As compared to other Asian Countries, Singapore, Hongkong SAR, and Japan have relatively higher Corruption Perception Index (CPI) with score of 86, 75, 74 respectively. Rank below these three countries is United Arab Emirates, Qatar, Buthan, Taiwan, Brunei, Korea Selatan and Malaysia that have CPI ranking between 50 and 70. Countries which have scored less than 50, indicate corruption is a serious problem.

Past studies on corruption have focused macro factors such as decentralization, political democracy, press freedom, economy freedom and fiscal decentralization that could affect corruption (e.g., Lecuna, 2012; Alexeef and Habodazzova, 2012; Goel and Nelson, 2005). Furthermore, limited studies have examined corruption on organizational level. The work of Luo (2002), Pillay and Kluvers (2014) are some of the examples that examined corruption in organizational level.

Luo (2005) argued corruption research that used organizational approach is vital for many reasons.

First, organization is the place where corruption may take place. Second, studying corruption among organizations may lead us to understand what drive corruption at organizational level. Third, organization is the primary lead to understand corruption level of a country. Fourth, corruption studies might significantly contribute to improve organization well being. Corruption often slows down organization performance and firms have to pay more for the damages caused by corrupt practices.

The Global Economic Crime Survey conducted by Pricewaterhouse Coopers (2011) showed that assets misappropriations, accounting fraud, bribery and corruption are considered the most fraudulent practices found in public sector organizations. Hence the research objective of this study is to provide empirical evidence on public sector organizations' involvement in corruption within the institutional framework. The model is derived from Luo model (2005) which incorporates institutional theories as the grand theory (DiMaggio and Powell, 1983; Eisenhardt, 1988; Tolbert and Zucker, 1996; Scott, 2001).

Institutional model believes that corruption at organizational level is caused by lack of support from task environment, poor comprehension of the regulations as well as execution and practices of these regulations. Other aspects are weak commitment to

eradicate corruption, lack of transparency of institutional environment and, the complexity of administration system (Luo, 2005; Pillay and Kluvers, 2014). Pillay and Kluvers (2014) provided empirical evidence of corruption at public sector organizations in South Africa which is a democratic and developing country. They managed to describe corruption at organizational level by incorporating Luo's Model in their study.

Besides the motives for corruption, studies conducted in some high corrupt level countries considered culture as a variable that is significantly correlate to corruption. For examples, Treisman (2000), and Pellegrini and Gerlagh (2008) have identified culture as a factor that contribute toward corruption.

As for the two countries in this study (based on CPI 2013 issued by Transparency International), China scored 39 which is slightly better than Indonesia with a score of 32. These scores reflected a high-level of corruption in these two countries.

The general aim of this research is to understand corruption at public sector organizations from organizational perspective. The specific aim is to examine the influence of task environment and institutional environment concern for corruption, and the culture of democracy toward corruption in China and Indonesia.

2 Literature review

2.1 Institutional theory

Institutional theory has been discussed in many research and literatures (DiMaggio and Powell, 1983; Tolbert and Zucker, 1996; Scott, 2001). However, the rationalization of corruption research has shifted from the competitive marketplace to the state and professions.

As for isomorphic process, DiMaggio and Powell (1983) had identified three mechanisms namely: coercive, mimetic and normative that could influence organizations guest for change. Coercive isomorphism describes organizational change as a result of a political decisions introduced by the authority. In public sector, an organization often must implement new regulation(s) initiated by the government. Mimetic isomorphism refers to environment uncertainty and ambiguous goals that lead organizations to imitate others. In normative isomorphism, organizations and professions are subjected to change as a result of pressure from peers.

Tolbert and Zucker (1996) explained that based on individuals' interests, they would accept and follow social norms unquestioningly, without any critical reflection or resistance. For instance, corrupt environment would lead individuals to behave corruptly as they considered it as a common norm.

2.2 Corruption

Corruption can be defined broadly or narrowly depending on the focus of study. Generally, corruption is defined as a behaviour, which deviates from the norm or violation of the rules. The motivation is personal gain by using his/her position. While the broadest sense, corruption is a deviant behaviour against individual formal responsibilities in various institutions / organizations (not just the government or the public sector) for the sake of personal gain (Luo, 2002). Corruption may be characterized based on the following nature:

Corruption is perceptual. The behaviour of an individual related to corruption due to wrong perception. This entails community perception that corruption is common.

Corruption is contextual. Corrupt behavior is influenced by ideology, paradigm, culture and other inherent corruption contexts. Politics not only affect how one understands and defines corruption, but it also generates a social behavior such as corruption itself.

Corruption is power-related. To perpetuate corruption, a corrupt person should be in a strong position in a government or an organization.

Corruption is illegal or norm-deviated. Corruption is an illegal act that is characterized by the unauthorized money transfer in which the aim is to gain a personal advantage. Violation of the regulation is one characteristic of corruption. Hence, the government should promulgate easy-to-understand laws relating to corruption for a clear-cut between corruption gift-giving, which is common in some culture.

Corruption is intentional. The motivation for personal gain is attached to the connotation of corruption.

Corruption's mode of expression is usually covert. Corruption tends to be hidden or informal, making it difficult to detect.

This study will use the generic definition of corruption, in the context of examining corruption in public sector organizations. Acts of corruption in this study also referred to theft of assets (asset misappropriation), tax fraud, accounting fraud, bribery and money laundering (Pricewaterhouse Coopers, 2011).

Luo (2005) explained that in the institutional model, the task environment and institutional environment will affect individuals in an organization to perform fraudulent acts (malfeasant behaviour). Malfeasant behaviour could led to the development of lack of focus and deterrent outcomes. This could result in the organization weak and unable to respond to environment change.

Organizational anti-corruption became mechanism described by Luo (as a mean to prevent corrupt practices) incorporates the elements of

organizational culture, organizational structure and compliance system. Organizational culture is the tradition where decision-making is morality-based, while organizational structure is a structure that aims on detecting and correcting any fraudulent act occurs within the organization. Compliance systems, on the other hand, are built to prevent corrupt practices through the development of anti-corruption programs and codes of conduct within an organization.

2.3 Corruption in China and Indonesia

CPI ranks countries based on their level of corruptions. The index indicates perception of respondents toward corruption based on a scale between 0-100. Zero score indicates highest level of corruption, while a score of 100 indicates the lowest corruption index. Based on CPI year 2013, China scored 39, which is relatively higher than Indonesia with a score of 32. This implies that China is slightly less-corrupt than Indonesia. However, both countries are the same range of score between 30-40, thus, corruption level is still considered high in both countries.

China has become one of the world economy giants and attracts large foreign direct investment. However, it continues to have a high-level of corruption. CPI issued by Transparency International (2013) ranked China in 87 position from total 177 countries with a CPI of 39.

President Xi Jinping is determined to eradicate corruption and one of his political priority is to combat corruption in China. In 2013, China Government has expelled 17 senior officials (positions equivalent to ministry-assistant and governor-assistant), conducted investigation on 197.000 corruption cases, and has sentenced up to 182.000 government employees who were involved in corrupt practices (Pei, 2014).

Meanwhile, Indonesia is also experiencing fast economy growth. However, it still ranked 114 position, with a low of CPI score 32. During 2004-2014, Corruption Eradication Commission/ Komisi Pemberantasan Korupsi (KPK) has preliminary-investigated 604 corruption cases, investigated 365 cases, charges were made to 290 cases (KPK, 2014).

2.4 Hypothesis development

DiMaggio and Powell (1983) argued that organization would change correspondingly to coercive, mimetic and normative processes. Coercive process explains that external pressure such as from the government, will direct organizational to change. Mimetic process describes that environment uncertainty and ambiguous goals that would also guide the organization for change.

Luo (2005) explained that task environment consists of information, external resources or conditions that might affect achievement of a strategy.

The concentration of powers in the government and weak regulatory oversight allow government officials to intervene policies and gain access to resources. These conditions resulted in the opportunities for the business community to co-opt with government officials with motive of achieving individual gains.

Institutional environment consists of three elements namely: transparency, fairness and complexity. Transparency is the degree of openness and ease in understanding the applicable rules. Luo (2005) found that ambiguous rules provide opportunities for government officials to engage in corrupt practices and exploit weaknesses of these rules. Fairness is described as rules that can be enforced and implemented fairly. Complexity, on the other hand is a system of rules and socio-cultural environments that are difficult to understand, subsequently, triggers people to commit corrupt practices (Luo, 2005; Pillay and Kluvers, 2014).

The hypotheses (H) for this study are stated as the follow:

H1: Task environment affects the occurrence of corruption

H2: Institutional environment affects the occurrence of corruption

2.5 Culture of Democracy

Evaluation of corruption level across countries based on empirical research is challenging because the definition of corruption is fluid influenced by different cultures and also difficult to detect corruption as it is a closed nature (Pellegrini dan Gerlagh, 2008). Hence, current research tried to compare respondents' perception towards high-level corruption countries with different cultures and democracy level.

China which is ruled by single political party (Communist Party). The Economist Intelligence Unit (2007) classified china as an authoritarian regime based on its democracy index. On the other hand, Indonesia is categorized as a flawed democracy since it has multiple political parties. Democracy index was built based on five categories; election process and pluralism, civil freedom, government function, political participation, and political cultures. Some researches argued that level of democracy correlates negatively with corruption (See Hill, 2003; Chowdhury, 2004; Bohara et al, 2004; and Pellegrini and Gerlagh, 2008). On the other hand, Treisman (2000) argued that level of democracy has no significant impact on corruption. Based on explanation above, the following hypothesis is being proposed.

H3: Level of democracy affects perception of corruption.

3 Methodology

Data presented in this paper were collected by distributing 210 questionnaires to public service officers who were pursuing postgraduate study in accounting at Faculty of Economics and Business, Universitas Jenderal Soedirman (UNSOED), Indonesia, and College of Management, Hebei University (HBU), China. They were chosen based on their work experiences in public sector organizations with a minimum of one year working experience. Out of the 210 responses, 39 questionnaires were not usable due to incomplete items. Only 171 questionnaires representing a response rate of 81,42% were valid for further analysis.

3.1 Research variables

The variables used in this study consist of task environment and institutional environment as independent variables, as well as deterrent outcomes to measure the impact of corruption among the public sector institutions. The research model was developed

from previous studies conducted by Luo (2005) and Pillay and Kluyers (2014).

The questionnaires were translated into Indonesian and Chinese language which were reviewed by language experts to avoid linguistic ambiguities. Seven items represent task environment, eight items for institutional environment, and two items for deterrent outcomes were adopted from previous studies. All items were measured using Likert scale, ranging from '1' representing Strongly Disagree, and a score of '5' representing Strongly Agree.

3.2 Validity and reliability of the questionnaires

Reliability testing (Table 1) for each variables showed Cronbach's Alpha of more than 0.60. It gave the indication of an acceptable internal consistency. Pearson Product Moment was used to confirm validity of the instrument in this research. Table 2 showed each items in questionnaires has r-value > 0.126 (r-table).

Table 1. Reliability Testing

Variables	Cronbach's Alpha
<i>Task Environment</i>	0,659
<i>Institutional Environment</i>	0,709
<i>Deterrent Outcome</i>	0,767

Source : SPSS Output

Table 2. Validity Testing

<i>Variable Task Environment</i>		
Item	r value	r table
1	0,339	0,126
2	0,493	0,126
3	0,611	0,126
4	0,485	0,126
5	0,593	0,126
6	0,636	0,126
7	0,565	0,126

Source : SPSS Output

<i>Variable Institutional Environment</i>		
Item	r value	r table
1	0,360	0,126
2	0,522	0,126
3	0,660	0,126
4	0,657	0,126
5	0,656	0,126
6	0,577	0,126
7	0,576	0,126
8	0,530	0,126

Source : SPSS Output

Table 2. Validity Testing – Continued

<i>Variable Deterrent Outcome</i>		
Item	r value	r table
1	0,905	0,126
2	0,896	0,126

Source : SPSS Output

4 Results

4.1 Descriptive statistics

A total of 171 responses were received, 89 of the respondents were from China and 82 were from Indonesia. Table 3 showed that slightly more than half

(57.9%) of the respondents were females while 42,1% were male respondents. Table 4 categorized the respondents based on job hierarchy: Low management public service officers (63.7%), middle management (24%), top management (4.1%), and others (8.2%).

Table 3. Gender

Gender	Total	Percentage
Male	72	42,1%
Female	99	57,9%

Source : SPSS Output

Table 4. Job Hierarchy

Job Hierarchy	Percentage
Low management	63,7%
Middle management	24%
Top management	4,1%
Others	8,2%

Source : SPSS Output

Table 5. Types of Corruption

	China	Indonesia
Asset Misappropriations	47,2%	32,9%
Tax Fraud	11,2%	7,3%
Accounting Fraud	4,5%	31,7%
Bribery	37,1%	28%
Money Laundering	-	-

Source : SPSS Output

Table 5 showed that asset misappropriations was the most frequent type of corrupt practices committed by respondents in China (47.2%) and Indonesia (32.9%). This result was consistent with the survey conducted by Pricewaterhouse Coopers (2011) among public sector organizations across countries. Bribery was also a common type of corruption committed by respondents in China (37.1 %).

Luo (2002) argued that corruption in Asia came from gift-giving culture (known as 'guanxi' in China; 'wa' in Japan; and 'inhwa' in Korean), and an act for keeping relationship within business environment. Under corruption motive, gift-giving culture between individuals was orientated to achieve personal gains. It

is a norm-deviated motives applied in business practice in many countries.

4.2 Hypothesis testing

The results from subsequent analysis were discussed below. Table 6 provided the results from regression analysis to test the regression model developed for this study. Unstandardized regression coefficient (B), standardized regression coefficient or beta (β), the intercepts, multiple correlation coefficients (R), and the coefficient of determinations (R^2) for the model were presented.

Table 6. Regression Result

	B	S.E	B	t	Sig
Constant	1.192			4.932	*0.000
Task Environment	0.193	0.086	0.197	2.246	**0.026
Institutional Environment	0.573	0.088	0.568	6.492	*0.000
R ²	0.540				
R	0.735				
F-Value	98.782				

Note: *p<0.01; **p<0.05

Source: SPSS Output

The next step was to examine the model R^2 . The R^2 -value for the regression model was 0.540 and, it was statistically significant at the $p < 0.05$ level. These results implied that all the independent variables had accounted for 54% of the variation in the model. The remaining variation 46% could be explained by unobserved independent variables.

Based on the information on Table 4, task environment has t-value $2.246 > t$ -table 1.653, and significant at 0.05 level ($p > 0.026$). Hypothesis 1 that stated task environment affects the occurrence of corruption was supported statistically. Institutional environment has t-value $6.492 > t$ -table 1.653, and significant at 0.05 level ($p > 0.000$). Hypothesis 2 that

stated institutional environment affects the occurrence of corruption was also supported statistically.

Hypothesis 3, examined the distinct perception toward factors (task environment and institutional environment) which affect occurrence of corruption based on different democracy-culture among countries. Table 7, presented homogeneity of variances test p-value > 0.05 . This means that there is similarity between respondent groups. Therefore, Analysis of Variance (ANOVA) was used to examine the differences between groups. ANOVA test shown that p-value > 0.05 (Table 6). Both groups have similar perceived factors (task environment and institutional environment) which trigger corruption. Hence, Hypothesis 3 could not be supported statistically.

Table 7. Homogeneity of Variances Test

Variable	Levene Statistic	Sign
Task Environment	0,126	0,723
Institutional Environment	0,146	0,703
Deterrent Outcome	0,102	0,749

Source: SPSS Output

Table 8. Analysis of Variance

Variabel	Nilai F	Sign
Task Environment	0,000	0,992
Institutional Environment	0,327	0,568
Deterrent Outcome	1,145	0,286

Source: SPSS Output

This research hypothesized that task environment and institutional environment affect the occurrence of corruption (Hypothesis 1 and 2). The multiple regression results showed the independent variables (task and institutional environment), have a positive correlation with corruption. These results provided empirical support for institutional models proposed by Luo (2005), Pillay and Kluevers (2014) developed these models further by taking into account the background of countries with relatively high level of corruption.

This study has also provided evidence on the factors that drive corruption in China and Indonesia. DiMaggio and Powell (1983) argued that organizations would respond accordingly to coercive, mimetic and normative process. The mimetic process explains that external pressure such as control of the task environment, regulations, inconsistent structure, concentration of power in a particular group, and coercive process (institutional environment) such as transparency, fairness, complexity of institutions could influence corruption level in the context of public sector organizations.

Hypothesis 3 could not be supported statistically. It could be explained that culture of democracy has no correlation with occurrence of corruption in China and Indonesia. This result is consistent with Treisman (2000) who argued that level of democracy has no significant impact on corruption level.

5 Conclusions

Task environment and institutional environment are significant factors influencing corruption in public sector organizations. Institutional theory can be used to explain the occurrence of corruption at the organizational level. However, culture of democracy has less influence on corruption in China and Indonesia. Treisman (2000) argued that level of democracy has no significant impact on corruption level.

This study contributes to corporate governance research. It is aimed to explain corruption behaviour that could be used as fundamentals in designing a management control system in public sector organizations especially in countries with high-corruption level such as China and Indonesia. The limitation of this study is that survey respondents do not represent public service officers in each department / divisions. Future research could involve respondents from wider geographical area and across departments / divisions, which in turn could enhance generalization of the results.

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