

Corruption and COVID-19

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Abstract

The coronavirus pandemic has created incentives for corruption, fraud, and self-dealing that can be explained by the underlying political-economic incentives at work. Three characteristics of the COVID-19 crisis are especially important. First, the rapidly unfolding pandemic and the accompanying economic recession have led to fierce competition for essential resources. Second, governments have rapidly mobilized public funds (for both healthcare and economic stabilization) at an unprecedented scale, creating opportunities for rent-seeking of many kinds, including outright corruption. Third, politicians, bureaucrats and medical professionals exercise substantial discretion in the allocation of resources. A lack of transparency and weak oversight and enforcement have exacerbated the problems of corruption and fraud, and public measures against these offenses have not kept pace with the developing crisis. The paper discusses how these features interact in procurement processes, in government assistance to individuals and businesses, and in the development and licensing of pharmaceuticals. Those who benefit from corruption, be they contractors or individuals, will emerge from the pandemic better off than before it started if governments do not act. Tolerance of malfeasance will be at the expense of long-term government legitimacy and spread the virus to the most vulnerable. The need for a speedy response to the pandemic should not be an excuse for undermining institutions that strengthen governmental integrity.

Keywords

Adverse selection, beneficial ownership, coronavirus, corruption, COVID-19, fraud, government contracting, healthcare, lotteries, moral hazard, pandemic, pharmaceuticals, procurement (government), vaccine, whistleblowers.

Resumen

La pandemia del coronavirus ha generado incentivos a la corrupción, al fraude y la auto-contratación que pueden ser explicados mediante los incentivos político-económicos que se tratan en el trabajo. Tres características de la crisis de la COVID-19 son especialmente

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importantes. En primer lugar, el rápido desarrollo de la pandemia y la correlativa recesión económica han conducido a una feroz competencia por los recursos esenciales. En segundo lugar, los gobiernos han movilizado rápidamente fondos públicos (tanto para el sistema sanitario como para la estabilidad económica) en una escala sin precedentes, creando oportunidades de muchos tipos para la captación de dinero fácil, incluyendo las abiertamente corruptas. En tercer lugar, los funcionarios y los profesionales sanitarios ejercen una discrecionalidad sustancial en la asignación de recursos. La pérdida de transparencia y de debilitamiento de la supervisión y del cumplimiento de las normas ha exacerbado los problemas de corrupción y de fraude, y las medidas públicas contra esos delitos no han mantenido el paso al desarrollo de la crisis. El trabajo discute cómo esas características interactúan en los procesos de adquisiciones y suministros, en la asistencia gubernamental a las personas y a las empresas y en el desarrollo y autorización de los medicamentos. Aquellos que se benefician de la corrupción, sean contratistas o particulares, saldrán de la pandemia mejor que lo que entraron si los gobiernos no actúan. La tolerancia de las actividades ilícitas será a costa de la legitimidad del gobierno a largo plazo y extenderá el virus entre los más vulnerables. La necesidad de una respuesta rápida a la pandemia no debería ser una excusa para debilitar a las instituciones sino una razón para fortalecer la integridad gubernamental.

Palabras clave

Alertadores, coronavirus, corrupción, COVID-19, contratación pública, fraude, medicamentos, pandemia, riesgo moral, selección adversa, servicio de salud, sorteos, suministros (públicos), titularidad final, vacuna.

SUMMARY. 1. Introduction. 2. Expedited Procurement Processes. 3. Rapid Allocation of Government Assistance to Individuals and Businesses. 4. Pharmaceutical Licensing and Insider Trading. 5. Conclusions.

1. Introduction

Wars, catastrophes, and disasters breed fraud and corruption at the same time as they generate acts of self-sacrifice and generosity. Generous actions may themselves involve illicit payoffs and the breaking of rules as people bump up against institutions and practices designed for ordinary times. Nevertheless, the widespread flouting of the rules, both legal norms and social practices, can hinder efforts to bring the situation under control and have long-term effects after the end of the crisis¹. These dual short- and long-term problems are manifest in the corruption and fraud accompanying the response to the novel coronavirus. An April 2020 survey of anti-fraud professionals in 58 countries reported widespread incidents of fraud in the acquisition of personal protective equipment, black market goods, and faulty equipment. Cases of embezzlement were reported in 58 percent of countries surveyed by 19 percent of respondents, distributed unequally across the countries' surveyed. Bribes were reported in 22 percent of countries by three percent of respondents (Nemexis, 2020). Much corruption, of course, never comes to light so the study does not permit one to measure the incidence and impact of malfeasance, but other investigations and press reports document its occurrence in a wide range of countries². Furthermore, even with no explicit payoffs, contracts may favor the cronies of the politically powerful³.

¹ On corruption risks in countries emerging from civil war see: Rose-Ackerman and Palifka (2016, pp. 316-340). For more details see: Rose-Ackerman (2009).

² For example, see: Slattery and Brito (2020); URN (2020); Gascón Barberá (2020).

³ For example, see: Sishi and Winning (2020); Harris, et al. (2020); Bradley, Gebredekidan and McCann (2020); Maswood (2020).



Corruption may accompany any rapidly developing crisis that leads to loss of life, widespread injury and illness, or destruction of property. Taking a political-economy approach, this essay isolates several reasons for this connection illustrated by, but not unique to, the current pandemic⁴.

First, governments need to respond quickly to a crisis, such as a hurricane, a wildfire, or an earthquake. Some governments will have set aside reserve funds and personnel, but other polities will have skimped on spending, judging it to be improvident to divert funds from citizens' day-to-day needs or to acknowledge low-probability risks. Regardless of resource constraints, many governments simply neglect to provide for even quite predictable disasters; responses to wildfires in California, earthquakes along the "ring of fire", or urban unrest may be underfunded, and preventive actions, such as building codes, fire resistant housing, and police training may have low priority. Then, what could have been a routine response to a predictable event becomes a desperate race against time with devastating consequences⁵.

As a result, governments spend large amounts of money and make regulatory changes in a short time period with little oversight, precisely when the very speed of the response suggests that oversight is especially needed. Such haphazard responses can cement political patronage and result in waste and fraud at the expense of equity and effectiveness.

Second, in the case of COVID-19, the need for a rapid response is not the only risk factor; multiple sources of uncertainty complicate the policy response. The virus was and remains poorly understood. When the pandemic began, there were no vaccines to limit the risk of infection or proven anti-viral medicines to give to those afflicted. There was considerable uncertainty about the best strategies with respect testing, treatment, and safety protocols that balance safety with ongoing economic and social life. Several vaccines have now obtained regulatory approval in the U.S. and elsewhere, but the effectiveness of distribution networks remains uncertain (Financial Times, 2020, December 4).

Further, governments may need to make unexpected regulatory changes with few precedents to draw on. For example, governments across the world are constantly under pressure to decide on the timing, length, and severity of lockdowns, with no way to satisfy all constituencies. Utilizing the existing capability for online diagnosis during a pandemic meant resolving conflicts with privacy regulations and creating new guidelines for widespread use (Sultan Mahmood, et al., 2020).

In such situations, much depends upon the professional integrity of both market actors and government agencies to guard against the opportunities for corrupt or, at least, self-serving behavior. The corrupt opportunities presented by severe uncertainty go beyond bribery or fraud. Profit-seeking individuals and firms may take advantage of market disruptions and regulatory loopholes at the public's expense. Thus, the pandemic has exacerbated the risks of corruption that exist whenever public officials

⁴ International financial institutions, such as the World Bank and the IMF, are acutely aware of these risks. See: World Bank Group (2020, April 28); Gaspar, Mühleisen and Weeks-Brown (2020). A webpage provides links to other World Bank material on governance and the response to COVID-19: <https://www.worldbank.org/en/topic/governance/brief/governance-institutions-covid-19-response-resources>

⁵ For example, see: Sullivan (2018).

are charged with allocating scarce benefits and costs under unclear or inconsistent legal rules⁶.

Third, the healthcare sector differs from the ordinary competitive market even in normal times, and market imperfections arise in the accompanying insurance markets. Some libertarians argue that society can depend upon the private sector to respond promptly. Competitive markets, according to that view, will rush to develop the needed tests, vaccines, and anti-viral medicines, and government interventions to increase accessibility to these goods will only remove the producers' profit motives⁷. Individuals, at the same time, will take precautions to protect themselves without the need for government action. Under this view, even if society does not achieve herd immunity through widespread infection, individual choices are preferable to imposed lockdowns⁸.

However, this perspective ignores the pervasive market imperfections in healthcare⁹. Consumers are largely ignorant of the proper treatments for their ailments, reinforcing the need to enforce the professional competence and integrity of providers. Insurance is subject to moral hazard and adverse selection (Arrow, 1963; Powell and Goldman, 2020). Individuals may not truthfully reveal their underlying health conditions to insurance companies if insurers seek to set prices to reflect an individual's risk of making a claim. Once insured, they may demand excessive care because they do not bear its full cost out of their own pockets (moral hazard). Such actions will increase the breakeven cost of insurance and make certain types of coverage unavailable. In addition, if insurance companies cannot adjust their prices to reflect the risks to their bottom line, the healthy may forgo insurance, leading the insurance system to unravel because it depends upon the averaging out of claims across policyholders (adverse selection). In short, unlike many natural disasters, the underlying structure of the relevant sector (healthcare) is riddled with inefficiencies that have been exacerbated by the pandemic. Of course, there can be price gouging and corruptly obtained contracts for recovery from natural disasters and human conflicts, but having healthcare at the center of recovery creates special problems.

As the Group of States against Corruption (GRECO) of the Council of Europe observed in its guidance to member states:

[Covid-related corruption can take the form of] facilitation payments/bribes to push ahead processes that may have stalled due to shortages of staff or closure of public offices, falsification of documents to meet the conditions of State aid schemes for pandemic relief measures, bypassing product certification requirements, non-certification of alternative supply chains, donations, lack of resources to supervise misconduct by individual employees, etc. (2020, p. 5).

These three characteristics of the COVID-19 crisis, taken together, have significantly increased corruption risks. First, the rapidly unfolding pandemic and the accompanying economic recession have led to fierce competition for essential resources. Second, governments have rapidly mobilized public funds (for both healthcare and economic stabilization) at an unprecedented scale, creating opportunities for rent-seeking of many kinds, including outright corruption. Third,

⁶ The background incentives for bureaucratic corruption are outlined in: Rose-Ackerman and Palifka (2016 pp. 51-92).

⁷ See: Lybecker (2020); Swan and Gerstein (2020).

⁸ See: Brumfiel and Keith (2020); Cannon (2020).

⁹ The economics of healthcare is a well-developed field of study that was launched by a classic article by Kenneth J. Arrow, "Uncertainty and the Welfare Economics of Medical Care" (1963).

politicians, bureaucrats and medical professionals exercise substantial discretion in the allocation of resources. A lack of transparency and weak oversight and enforcement have exacerbated the problems of corruption and fraud, and public measures against these offenses have not kept pace with the developing crisis. I discuss how these features interact in procurement processes (section 2), in government assistance to individuals and businesses (section 3), and in the development and licensing of pharmaceuticals (section 4).

2. Expedited Procurement Processes

Awarding government contracts during a public emergency faces challenges that differ from those that arise in normal times. Procurement is usually a buyers' market, with the contracting agency holding significant leverage over suppliers. However, during an emergency, time pressures and a lack of qualified suppliers may undermine clarity and transparency in the contracting process, creating a favorable environment for firms to engage in bid-ridding, price-gouging, and fraud¹⁰.

Examples abound. To list just a few, in the United States, contracts worth hundreds of millions of dollars were awarded to companies with little or no prior experience in producing the needed goods, including those in the arms industry or with histories of fraud¹¹. In Slovenia, of the approximately 80 million euros in contracts awarded in the last week of March 2020, thirty-five percent went to a firm controlled by a mainstay of the gambling industry who had no previous experience in healthcare (Delic and Zwitter, 2020). In Poland, over \$60 million was wired to a supplier that never delivered the medical equipment (Slattery and Brito, 2020).

Even if goods and services are delivered, they may be supplied at much higher prices than in normal times¹². In Colombia, when officials began giving food boxes to families hit by the coronavirus lockdown, one lawmaker noted the exorbitant prices paid to vendors. An inquiry revealed that the state was paying more than double the market price of certain goods, for example \$2.81 for 250 grams of coffee that retailed for \$1.20 at grocery stores (Faiola and Herrero, 2020). Kenya's anti-corruption commission revealed a similar problem, with state agencies paying 60 percent higher for goods than their market prices (Malalo, 2020).

In several countries, contracts awarded to those with ties to those in power raised eyebrows. In the United Kingdom, contracts were given to companies whose shareholders, board members, and employees include present and former high-level public officials (Tabby Kinder, et al., 2020). South Africa's ruling party was met with a public uproar after the husband of the president's spokesperson won PPE contracts (Sishi and Winning, 2020). One study shows that local governments in Colombia with historically high levels of corruption were more likely to award contracts to campaign donors and experience cost overruns and inefficiencies during the COVID-19 crisis (Jorge Gallego, et al., 2020).

Even after fraud schemes are discovered, it is sometimes difficult or impossible to hold violators accountable and recover losses. Under-performing contractors may be judgment-proof or have disappeared into a maze of shell companies leaving no trace. The U.S. FBI identified numerous incidents of lost funds that were wired to

¹⁰ These incentives come on top of the background risks of corruption in procurement discussed in Rose-Ackerman and Palifka (2016, pp. 99-109). The relative bargaining power of public officials versus private firm suppliers determines the level of payoffs, but may not affect their incidence.

¹¹ See: Gabrielson, et al., (2020); Salman and Penzenstadler (2020); Gelles and Abrams (2020).

¹² See: Malalo (2020).



fraudulent contractors and subsequently flowed out of the jurisdiction of the U.S. (Federal Bureau of Investigation, 2020).

Several types of responses are possible, but there is little systematic evidence about how they might be prioritized or combined. The options include: open-contracting, pre-registration of suppliers, beneficial ownership information, freedom-of-information acts, limits on conflicts of interest, oversight by public bodies, and sufficient investigative resources to bring cases promptly and to protect and reward whistleblowers.

A number of international organizations and NGOs have urged the use of *open contracting* systems to combat corruption and fraud in procurement processes. As summarized by Open Contracting, an NGO, governments should make emergency procedures public, require written justification and documentation, and publish open data on contract terms to permit civil society oversight on a timely and regular basis (Open Contracting, n.d.; Amin, 2017). During the financial 2008 crisis, the American Recovery and Reinvestment Act stipulated that procurement contracts not awarded through fixed-price competitive bidding must be disclosed on a centralized online platform (Congressional Research Service, 2009). The Open Government Partnership points with approval to Ukraine's anti-corruption reforms that oblige the open publication of all emergency contracts, including terms of payment and delivery, and value. Ukrainian civil society has developed a business intelligence tool to monitor medical procurement and emergency spending. It can track price differences for COVID-19 tests in the country's regions and capital to check the price of critical medical supplies to ensure that authorities are committed to filling treatment centers, not private pockets (Gavin Hayma, 2020). It will be important to check if these reforms are able to counter Ukraine's otherwise high levels of corruption.

A complementary, strategy, used in Colombia, concentrates on *pre-registering suppliers*. An emergency decree governs public procurement during the COVID crisis, allowing expedited procedures to procure the necessary goods and services. The National Procurement Agency, *Colombia Compra Eficiente* (CCE), has asked all companies that want to supply these critical products to register. CCE verifies the information and includes qualified suppliers in a framework agreement, allowing agencies from all over the country to procure efficiently, and to compare online prices and characteristics¹³.

These measures could help limit *conflicts of interest* in times of emergency. Any realistic set of rules needs to acknowledge that, especially in small countries or for specialized procurements, there may be only a few domestic suppliers. Stringent conflict-of-interest rules may give excessive bargaining power to the few firms permitted to bid. Sometimes a better response is to permit many firms to bid and adopt open-contracting rules that impose rigorous standards and oversight to assure value for money. Procurement agencies need to face clear, written requirements to maintain complete and accurate records and procedures for measuring the contractors' suitability and performance (Office of the Inspector General for the U.S. Department of Defense, 2015; Rose-Ackerman, 2014). If emergency circumstances make timely publication of awards impossible, the contracting authority should publish a report after the fact that justifies its decisions at the time (European Commission, 2020). Public officials, on their part, should be required to place their shares in the companies

¹³ A summary is available at Submission to OECD COVID-19 Innovation Report: https://docs.google.com/document/d/1Qy_7GwHMjlt71psdSkxPLwdxL3pdOEdIiiRY5D01c7Q/edit

bidding for and benefiting from procurement contracts in a blind trust until the expiration of the programs (Oldfield, 2020).

In order to check for fraud and to recover misused funds, governments and civil-society watchdogs need to know the *beneficial owners* of the firms that obtain contracts. Certain countries have cited the crisis as a reason to delay compliance with transparency and beneficial ownership requirements. For example, the Financial Crimes Enforcement Network (FinCEN) in the U.S. Department of the Treasury has announced that for eligible federally insured depository institutions, Paycheck Protection Programs (PPP) loans “will not require reverification” of existing customers’ beneficial ownership information “under applicable BSA (Bank Secrecy Act) requirements, unless otherwise indicated by the institution’s risk-based approach to BSA compliance” (Wolf, 2020). A similar weakening of the rules has occurred in the Bahamas where the obligation to comply with the provisions of the Register of Beneficial Ownership Act has been suspended during the public emergency and for an additional 60 days after it has passed (Renee Farquharson, 2020). The Polish government extended the deadline for registering beneficial owners, which already had a low rate of compliance (Linklaters, 2020).

The weakening of transparency rules under the excuse of relieving the burden on business can backfire. Such a policy exposes businesses and individuals to a heightened risk of fraud and corruption, undermining the effectiveness of the programs. Registries of potential suppliers and data on signed contracts must make it possible to trace the beneficial owners of government contracts, especially if they reside outside a jurisdiction’s borders¹⁴. As a step in that direction, the IMF reports that Gabon, Moldova, and Nigeria have committed to publishing information on crisis-related public procurement and beneficial owners of companies contracting with the government (International Monetary Fund, 2021). The IMF hopes to use these programs as positive examples for others.

If the government’s own practices are lacking, civil society may be able to make use of the *Freedom-of-Information Acts (FOIAs)* available in many countries. These acts, which have spread globally in recent years, allow anyone –including ordinary citizens, civil society groups, and the media– to request information from the government (Ackerman and Sandoval, 2006). They can be potent tools if they do not have too many open-ended exemptions and if the government promptly and adequately responds to requests. Although up-front disclosure is a simpler and more streamlined way to provide information, ex post FOIA requests can supplement open-contracting laws by assuring that the required information is available to the public.

Yet, during a crisis, responding to such requests may be a low priority. The government may permit the temporary relaxation of FOIA rules to allow flexibility in an emergency. Some jurisdictions have explicitly extended deadlines for responding to requests until the pandemic is over, making it clear that FOIA requests will have no priority¹⁵. In the U.S., civil society groups have filed lawsuits against government agencies that have declined to release information related to the pandemic response¹⁶. It remains to be seen if they will improve the effectiveness of FOIA in checking abuse.

¹⁴ See: Open Ownership (2020).

¹⁵ See: Frary (2020); Office of the Governor State of Hawaii (2020); D.C. Policy Center (2020).

¹⁶ For example, see: Compliant for Injunctive and Declaratory Relief. *Knowledge Ecology International v. National Institutes of Health*. Case No. 8:20-cv-2927. (United States District Court for the District of Maryland, 2020). Available here: <https://www.keionline.org/wp-content/uploads/1092020KEINIHFOIAComplaint.pdf>; Complaint. *Pro Publica, Inc. v. United States Department of Health & Human Services*.

Some governments may delay meeting FOIA requests as part of an attempt to quash reforms by citing the emergency as an excuse. Such actions risk making corruption easier to hide in the short-run and can undermine government legitimacy if malfeasance surfaces later. Severe economic pressure and the difficulty of obtaining information can pose a double hurdle to local media and oversight groups. Hence, prolonged and purposeful FOIA exemptions can have long-term consequences for the quality of governance (Vittori, 2020).

Law enforcement investigations concentrate on criminal acts of fraud and corruption, but some types of misbehavior also can be prosecuted as civil offenses committed by private firms and as violations of civil-service rules and codes of ethics. In the U.S., various government institutions, including the Departments of Justice (DOJ), Homeland Security (DHS), and Health and Human Services, can bring anti-corruption and anti-fraud actions related to the Covid-19 crisis, including under the Foreign Corrupt Practices Act (FCPA), which criminalizes the payment of bribes to get business abroad¹⁷. Nevertheless, even in the U.S., the investigative capacities of government institutions remain limited relative to the magnitude of government financial outlays.

Because many types of fraud and corruption have willing participants on both sides, it is especially important for prosecutors to be able to encourage and protect *whistleblowers* (Rose-Ackerman and Palifka, 2016, pp. 219-221). The survey of anti-fraud professionals cited above indicates that whistleblower retaliation occurred in almost half of the countries surveyed (46%), and the problems to which whistleblowers pointed were diverse (Nemexis, 2020; Feinstein, 2020). Even if a whistleblower law exists, it may only protect a narrow range of individuals and disclosures, and the measures to protect the rights of whistleblowers may be inadequate (OECD Webinar, 2020, May 22). The United States generally has stronger protections for whistleblowers than many other countries, and private-sector whistleblowers can earn bounties from reporting malfeasance involving public contracts. Nonetheless, that system does not always work fairly. For example, when a former Florida Department of Health employee alleged that she was fired after refusing to manipulate COVID-19 data, Florida law enforcement raided her home under the charge that she attempted to “hack” the department by trying to log in with expired credentials (Ceballos, 2020; Chappell, 2020).

In a rapidly evolving crisis, normal procedures that take months are unlikely to allow timely disclosure and actions. If a crisis results in severe economic stress, whistleblowers may be even more reluctant to engage in behavior that might cost them their jobs (OECD Webinar, 2020, May 22). If existing protections are insufficient, it is important for the legislature to include special whistleblower protections in emergency stimulus programs and to send consistent messages to the public stressing that reporting malfeasance is important and appreciated.

Controlling price gouging needs a nuanced approach. There may be genuine shortages of certain products that produce temporary price increases. Although opportunistic cartels should be punished, price limitations may create a black market, and severe punishments can discourage the production of needed goods. However, the government can limit the upward pressure on prices by coordinating and centralizing procurement processes. State and local governments can leverage their

Case No. 20-4092 (United States District Court for the Southern District of New York, 2020). Available here: <https://www.documentcloud.org/documents/6935608-2020-05-28-DE-001-Complaint-DMWEST-40181066.html>.

¹⁷ See: Office of the Attorney General (2020); Department of Homeland Security (2020); Department of Health and Human Services, Office of Inspector General (2020).

collective buying power, while the national and federal government can assist with coordination and sourcing back-up supplies (Folliot Lalliot and Yukins, 2020).

Nonetheless, relying solely on market mechanisms is not the solution. Aside from the grave ethical implications of allowing chances of survival to depend upon existing privileges, a pure market-based allocation is also inefficient in harnessing the positive externalities of certain healthcare benefits. Furthermore, because of the social consequences flowing from the allocation of scarce benefits, their distribution should be made systemically, not left to the decisions of individual physicians.

The allocation method should depend upon the nature of supply as well as distributive justice concerns. As in wartime, *ration tickets*, *lotteries*, or *application procedures* may be necessary. During a pandemic, ensuring the supply of personal protective equipment and vaccines to medical and essential workers and then rationing their availability to others would be more effective in controlling the spread of the virus than leaving them accessible only to the well-resourced (Glazer, 2020). First-come-first-served also has little to recommend it on the grounds of either fairness or efficiency, and it can incentivize some to use unofficial and illegal means to get ahead in the line (Meskell, 2020).

Any approach should take into account the principle of fairness and the possible spillover of benefits, with appropriate safeguards against corruption (Bloom, 2020; Bersad et al., 2009). Ideally, the allocation would be based on criteria that are easy to identify in order to minimize the room for discretion and manipulation. But when faced with an overwhelming demand from a practically indistinguishable group of people, a lottery system is an alternative that is fair and can be less susceptible to corruption if operated under transparent rules (Emanuel et al., 2020; Kenen, 2020; Vogel, et al., 2020). Clear communication to the public on the need for and basis of the rules of distribution would be key to preserving the legitimacy of the intervention and reducing the motivation to bypass or disobey the rules.

An additional benefit of using a lottery to allocate a scarce experimental treatment is that it also has scientific merit. Faced with scarcity, all eligible patients are treated fairly in that all have an equal chance of being selected. In addition, as two medical doctors point out, the lottery itself provides information about the efficacy of the treatment. It permits a comparison between those who do and do not receive the treatment. If there is a reason to prioritize certain types of patients, such as front-line healthcare workers, then the lottery itself can be designed to give them a higher chance of selection (White and Angua, 2020). This example illustrates the value of nonmarket allocation methods and the need to prevent corruption and cronyism from undermining such methods. Leaving these choices in the hands of individual physicians, risks cronyism and corrupt side deals. Corrupt access is not only unfair; it also prevents an adequate test of the treatment's value in the population.

3. Rapid Allocation of Government Assistance to Individuals and Businesses

Many countries have set up programs of financial aid for households and business. The rapid rollout of emergency payments to individuals and firms amplifies bribery, fraud and embezzlement risks. Improper management of public funds can take various forms, including payments for access to medical services, payments to re-open businesses or avoid enforcement actions, payments to receive preferential forms or amounts of government assistance, and self-dealing or kickback schemes. The particular difficulty here is the large number of beneficiaries so that individual law-enforcement efforts are likely excessively costly, and lawmakers are subject to heightened interest group pressure as businesses try to shape the distribution of

benefits in their favor (Vogel, et al., 2020). Studies show that in the first quarter of 2020, when the U.S. Congress was debating the \$2 trillion Coronavirus Aid, Relief, and Economic Security (CARES) Act, lobbying expenditures noticeably increased across different sectors, with the health sector's spending and registrations rising most rapidly (Olson, et al., 2020).

It is especially important to limit corrupt incentives up-front in the fundamental structure of stimulus programs. That may mean keeping the eligibility standards simple and clear-cut, even if they would not be the ideal standards in a perfectly honest world. For example, a World Bank study notes that in regions where the state's administrative capacity remains weak, categorical targeting based on easily observable characteristics that are highly correlated with poverty can substitute for eligibility criteria that are more difficult to measure, such as income (Tabor, 2002). Regardless of which criteria are used, information about eligibility and the scope of benefit should be easily accessible and be accompanied by outreach to enhance public understanding of the intended beneficiaries (United Nations Office of Drugs and Crime, 2020, p. 2; Ellena, Brown and Dreher, 2020, p. 13).

However, ex post monitoring and review remain important. Unfortunately, in the U.S. there appear to be weaknesses in the CARES Act's oversight mechanisms. Oversight is a necessary condition to prevent malfeasance and to punish those who step over the line. The CARES Act mandates that the program will be overseen through three key mechanisms: the Congressional Oversight Commission, which submits monthly assessments of the Department of the Treasury's \$500 billion stabilization fund; the Pandemic Response Accountability Committee, which oversees the implementation of the CARES Act to detect and prevent fraud, waste, and abuse; and the Special Inspector General for Pandemic Recovery, nominated by the President to report on the appropriateness of the spending by the Treasury Department (Mellman and Eisen, 2020).

Even though the act was passed in late March 2020, the Special Inspector General, who is supposed to oversee the Treasury Department's activities, was not confirmed by the Senate until mid-June, more than two months after the CARES Act was signed (Rappeport, 2020). The chairperson of the Congressional Oversight Commission had not been confirmed by mid-February 2021 (Congressional Oversight Commission, 2021). After President Trump removed the initial chairperson of the Pandemic Response Accountability Committee, a group of 21 inspector generals (IGs), the committee went ahead without an officially appointed new chairperson. The group is now led by the IGs from the Department of Justice and NASA (PRAC, 2021; The White House, 2020, March).

Past emergencies illustrate how difficulties can arise. Consider Hurricane Katrina in the U.S. and the Ebola epidemic. Hurricane Katrina made a direct hit on New Orleans in August 2005. As reported by *The Hill*, the Government Accountability Office estimated that by June 2006 approximately \$1 billion in Hurricane Katrina aid was improperly distributed and potentially fraudulently obtained. By 2011, 1,439 people spanning 41 federal districts were federally charged with hurricane related fraud against the government. By 2014, the seventeenth New Orleans area public official had been arrested on federal corruption related charges, including a school board member, a state senator, a state representative, a judge, multiple city council members, a coroner, and multiple mayors. To this day, it is unclear how much aid from Hurricane Katrina was lost to fraud and corruption (Cortese, 2020).

Ebola hit West Africa in 2014-2016. The International Red Cross estimated the cost of corruption associated with the outbreak in Guinea and Sierra Leone to be more

than US\$6 million. Reports show that the Ebola epidemic resulted in the diversion and mismanagement of funds, misreporting of salaries, payments for duplicate supplies, and bribery of health professionals to receive medical care and leave quarantined zones (Divjak and Dupuy, 2015).

To complement and encourage low-income countries to spend responsibly, multilateral and bilateral donors could incorporate stronger anti-corruption measures into aid packages. Earlier this year, the IMF and World Bank were flooded with requests for foreign assistance¹⁸. The multilateral lenders have maintained that all funds will be subject to pre-existing integrity requirements, perhaps, in part, due to continued lobbying by several anti-corruption NGOs. As the IMF Fiscal Affairs Department stated in 2020: “Do what it takes, but keep the receipts” (International Monetary Fund Fiscal Affairs, 2020). Its Managing Director stated that “We don’t want accountability and transparency to take the back seat” (International Monetary Fund, April 15, 2020). The IMF notes that 58% of all financial agreements contain specific commitments to control the risk of corruption, such as auditing of COVID-19 spending and publishing procurement information (Berazategui, 2020; International Monetary Fund, 2020, June 30).

These signaling and voluntary commitments are not sufficient to ensure that the funds will be spent responsibly, especially in countries with histories of endemic corruption. Careful documentation of spending is a necessary condition for accountability, but is it sufficient? What does “do what it takes” mean? It signals the IMF’s deference to member countries’ choices about how to respond, but in many cases, that may simply cement connections based on cronyism and patronage. Although one can understand the unwillingness of the IMF to get involved at the micro level in directing policy, citizens within individual countries and organized business, labor and civil society should not be content with ex post accountability alone. Even if no bribes were paid, outright fraud can occur in cases where receipts exist but where the contracted-for supplies were not delivered or were defective.

Several measures have been proposed to control the risk of corruption in foreign aid. In the US, the Carnegie Endowment has highlighted the Countering Russian and Other Overseas Kleptocrats (CROOK) Act (H.R. 3843/S. 3026). The bill would form an Anti-Corruption Action Fund to rush support to countries eager to take rapid action against corruption, as the current crisis demands (Bellows, 2020). The proposal is budget-neutral and enjoys bipartisan support. However, as one observer notes, the CROOK Act does not address the causes of corruption arising from personal interactions and discretion created by various trade barriers and other distortionary regulations (Koehler, 2020). A draft bill passed by the Senate in 2019 would have required the State Department to assess corruption risks in countries receiving certain U.S. foreign aid and develop appropriate anti-corruption mechanisms¹⁹. This year, Germany’s development ministry announced a plan to reduce the number of aid recipients and make good governance, respect for human rights, and tackling corruption the criteria for future aid cooperation (Deutsche Welle, 2020, May 5). Other suggested mechanisms include linking the disbursement of aid to evidence of outcomes, such as testing and vaccination levels (Loayza, 2020).

Although it is true that states vary in their capacity to enforce rigorous oversight, most states have the infrastructure and resources necessary for a basic level of budget controls. In the past and during the current pandemic, donor countries and agencies

¹⁸ See: World Bank Group (2020, May 19); International Monetary Fund (n.d.)

¹⁹ Combating Global Corruption Act of 2019, S.1309, 116th Cong. (2019). Available here: <https://www.congress.gov/bill/116th-congress/senate-bill/1309/text>

were able to work with local governments to develop tracking systems to identify intended beneficiaries of relief programs (International Monetary Fund, 2020, May 19). Oversight in times of crisis is not a privilege reserved for developed countries. If they centralize and streamline crisis response spending, minimize extra-budgetary funds, and introduce ex-post verification, even low-income countries can significantly reduce lost resources.

4. Pharmaceutical Licensing and Insider Trading

The pandemic has generated a flood of new money into drug research and development, most of it from public sources. The speed with which policymakers are seeking solutions to the pandemic creates opportunities for companies to bypass the usual regulatory review to get drugs to market or into publicly financed programs. It can also help some drug developers to secure preferential treatment for not only licensing but also favorable tax treatment and other benefits. At the same time, intellectual property laws limit transparency in product development, reducing the ability of third parties to challenge company behaviors.

One type of favorable treatment is “fast-tracking”. For example, U.S. Food and Drug Administration (FDA) rapidly granted Gilead Sciences “orphaned drug status” for an experimental drug to treat COVID-19, a designation usually reserved for drugs treating rare diseases. That status comes with market exclusivity, tax breaks, and the waiving of regulatory fees (Chua and Cont, 2020). The company eventually gave up that status following outcry (Lupkin, 2020). The U.S. federal contracting standards for subsidizing medical research during the pandemic could weaken the government’s ability to license generic competitors if the subsidized company fails to make the product accessible on reasonable terms (Rowland, 2020). Under normal circumstances, the business practices of this industry have raised ethical concerns, and during the pandemic private companies may use this opportunity to enrich themselves at the expense of the public interest.

The promising vaccines now receiving regulatory approval suggest that the pandemic may be tamed in 2021, but it will be important for governments to remain vigilant. Of course, drug firms should be able to make a profit from their discoveries, but they should not exploit the vulnerable positions of governments and patients, especially in low-income countries.

Insider trading may be a concern. Four U.S. Senators were publicly accused of insider trading after it appeared that they personally profited from trades following a private all-senators coronavirus briefing (Lipton and Fandos, 2020)²⁰. This prompted the Securities and Exchange Commission to issue a warning on non-public material information related to the virus (Avakian and Peikin, 2020).

Medication and medical device production chains frequently extend across national boundaries, but the COVID-19 crisis has disrupted regular patterns of manufacture, sale, and export. As mentioned earlier, the need to contract with new vendors in an emergency can circumvent normal due-diligence processes. The imperative to obtain healthcare supplies as quickly as possible may stimulate the payment of bribes, for example, by company agents to regulatory and customs officials. Law firms are quick to point out that firms that respond rapidly potentially expose themselves to liability under foreign bribery and anti-money laundering laws²¹.

²⁰ Three cases were closed in May 2020.

²¹ For example, see: Kostolampros, et al. (2020).

Open-contracting initiatives and beneficial ownership registries can be helpful here, just as they can be for any kind of procurement.

But the corrupt incentives go deeper than in other types of procurement because of the distinctive features of the healthcare sector. The risks arise not just from the need for speed and the possibility of privileged insiders obtaining special benefits. In addition, consumers' lack of expertise, and the moral hazard and adverse selection that characterize insurance markets can raise the stakes in the fight against corruption in the pandemic (Arrow, 1963; Powell and Goldman, 2020). The study of corruption always raises the question of when to use the price system and the private market to allocate scarce goods and services and when to select allocation methods based on desert, efficacy, or over-all social value. Poor information about the future is a problem for everyone and can lead to fatalism or to the creation of insurance markets to spread the risk over a certain population –for automobile accidents, life expectancy, risks of fire and theft– and, of course, healthcare.

Poor information, however, is not the only problems. In addition, the same dollar price represents a trivial outlay to one person and a major sacrifice to another. The private market is a poor mechanism for the redistribution of income to those at the bottom. Furthermore, if consumption by one person creates spillover benefits and costs for others, the purchaser may not take these external effects into account. Some commodities cannot be parsed into individual consumption bundles. They are consumed in common. Even if a vaccination provides a personal benefit to an individual, a widespread vaccination program benefits even those who do not choose to get a shot.

The healthcare sector is a prominent illustration of these distributive effects and market failures. Thus, even without the overlay of a pandemic, an unregulated competitive healthcare market is neither efficient nor fair. Rather, public policies should accommodate both distributive justice concerns and take account of informational weaknesses and external effects. In fact, the healthcare sector is hedged about with public programs and regulations in all polities. Health insurance is a complex mixture of public and private provisions in most countries, although a few have sought to outlaw both private provision and private insurance. For healthcare, where scarcity combines with regulation and where the public sector determines who is qualified to provide and to receive treatment, corrupt incentives exist in ordinary times and have increased during the pandemic²².

For health insurance, responding to the problems of moral hazard and adverse selection can create corrupt incentives. Consider moral hazard. Individuals may demand healthcare with little concern for the social costs if their own out-of-pocket costs are low or nonexistent. However, there is an opposite force at work during the pandemic. Prevention and treatment are troublesome and costly for individuals, but the benefits of their actions are partly felt by other people who face less risk of exposure because of others' preventive actions. These external benefits are a strong justification for requiring individuals to take costly actions that benefit both themselves and others. Because some of these benefits flow to strangers, individuals may not take them into account. To some extent, the two effects may balance out, but unfortunately, actions that protect others are not always the same as the ones that benefit yourself, your family, or your religious community. Thus, corruption and other types of shirking will predictably occur in those situations. For example, a restaurant owner might pay off inspectors to cut corners on sanitizing the premises and might fail to purchase

²² For example, before the pandemic, pharmaceuticals and medical equipment became major profit centers for Chinese hospitals and suppliers paid bribes to get contracts (Rose-Ackerman and Tan, 2015).

effective personal protective devices for staff. Suppliers of such devices might pay off officials to get approval for inadequate products that can be sold as compliant. Police may let people avoid lockdowns and quarantines in return for bribes²³. Businesses using these products have little incentive to check them for efficacy partly because they do not have the expertise to make quality judgments and partly because their main concern is to attract customers by claiming to follow government guidelines.

Now consider adverse selection where low-risk individuals opt out of insurance. One response to this problem is to require everyone to obtain coverage or to charge a fee to those who opt out, as was done in the original version of the U. S. Affordable Care Act²⁴. If governments enact such rules, low-risk individuals could make payoffs to avoid a citation for non-compliance, or they might avoid a fine through paying a bribe. This incentive exists under any effort to avoid adverse selection, but it has additional costs during a pandemic. Now, low-risk individuals who opt out may infect others if they do become sick. Those who opt out may include, not only those at low-risk, but also those who are more tolerant of risk than the average person. If that is true, the external costs of their lack of insurance will be especially socially harmful if they do become infected. Adverse selection can lead the entire insurance program to unravel as the refusal of some low-risk people to join increases the overall risk of the program, causing the newly marginal people to exit and so forth. In contrast, if those who opt-out are not low risk but rather have a high tolerance for all levels of risk, then the insured pool will not unravel. It will just cover fewer people. However, that latter version of adverse selection will be especially damaging in the context of a highly contagious disease. Now, risk-acceptant people with no social conscience may spread the virus to others who are either more risk averse or more susceptible to catching the disease and/or have life-threatening health conditions. Thus, once again there is a strong case for requiring everyone to take precautions and to have insurance coverage. The goal is not just to spread the costs broadly but also to implement preventive measures. Denying care or charging for uninsured healthcare may provide an incentive to sign-up, but those who remain outside the insurance system are imposing costs on others. The penalties need to reflect the external costs imposed by the uninsured on everyone else. However, if the program did reflect those costs, the individual incentives to seek an exception through corrupt payoffs could be high. Corrupt officials could register individuals in the program even though they had paid nothing to the regulatory authority. Alternatively, if the state makes insurance free to all so that no adverse selection occurs, moral hazard will remain a problem. Then, the incentives for corruption are identical to those that arise whenever the government provides a public service that can vary in quality across beneficiaries. Corruption would be an allocation mechanism that favors the wealthy and the unscrupulous, as occurred in the healthcare system of Eastern Europe after the fall of the socialist systems. In those countries, healthcare remained a public responsibility but was not funded well enough to satisfy middle-class demands (Rose-Ackerman, 1995; Kornai and Eggleston, 2008; Stepurko, et al., 2015). As a result, a flourishing, but illegal private market for healthcare existed in many countries that permitted the old system to survive, but at low quality and with vastly unequal levels of care. If that system had coincided with a pandemic, the result could have been tragic.

²³ See: Transparency International (2020).

²⁴ The mandate under the Affordable Care Act levied a fee on those who did not sign up for insurance under the ACA or for an equivalence or better plan. That portion of the act was repealed, effective in 2019 (Eibner and Nowak, 2018).

5. Conclusions

The political economy of the coronavirus pandemic has created incentives for corruption, fraud, and self-dealing. Along with the generous behavior of many millions of front-line workers, government officials, and private individuals and firms, others have sought to take advantage of the situation to benefit at the expense of the public and of victims of the pandemic. This anti-social behavior is readily explained by the underlying economic incentives at work in a health-related crisis where government must act quickly in a haze of uncertainty about the best path forward. Unlike other sorts of catastrophes, related to the weather, earthquakes, or volcanic eruptions, a health emergency raises special problems. Patients face problems of moral hazard and adverse selection that undermine free market solutions and demand a public sector response, even in ordinary times. Furthermore, neither a vaccine nor an anti-viral medicine existed when the coronavirus began to spread worldwide. The rapid response of pharmaceutical researchers produced several vaccines in record time, but this effort co-existed with both fraudulent cures and over-priced or useless protective equipment.

Although some malfeasance was probably inevitable in a pandemic, it should not be ignored. Overall, those who benefit from corruption, be they contractors or individuals, will emerge from the pandemic better off than before it started if governments do not act. Tolerance of malfeasance will be at the expense of long-term government legitimacy and lead to the spread of the virus to the most vulnerable. The need for a speedy response should not be an excuse for undermining institutions that strengthen governmental integrity.

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