Corruption and Urban Economic Development: A Problem and
Solutions in American Cities.

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Abstract

It seems that for as long as there have been systems of political power, there has been corruption. References to the misuse of power for personal gain can be found throughout various civilizations and time periods including ancient Rome)Romeinfo.com, 2013) where Emperors were put in place based on who could pay the most for an appointment and 19th Century China, where bribery and fraud were common and practices (Csuka, A, 2012)   In these and many other historical instances, corruption has been named as a significant contributor to the downfall of those societies that could not keep their corruption under control. Corruption has been examined in many ways and in many documents, however this paper will attempt to examine the impact of corruption on the economic development of low-income communities by using historical evidence of what corruption has done to these communities in the past.. While there are many communities that could serve as case examples of corruptions negative effect, for the sake of keeping the topic concrete and focused, this paper will review literature on the relationship between corruption and economic development and the impact that corruption has had on the economic growth of low-income residents of the city of Newark, in New Jersey. The paper will attempt demonstrate the harmful effect corruption has on low-income economic development and propose the concept of economic empowerment as a method of controlling corruption while simultaneously improving economic development outcomes.

Defining Corruption

Corruption is commonly defined as the misuse of public office for personal gain. Corruptive practices include bribery, kickbacks, coercion, and related activities that provide an unfair advantage to one party. These practices undermine fair trade, waste resources, defraud the public, and increase human suffering (Vogl, 1998; Quinones, 2000).

This definition alone is enough to suggest that the term corruption exists to describe a wrong and harmful act, but Nye offers a definition of corruption that better embodies the flavor of the behaviors associated with corruption, stating that corruption is a:

"Behavior which deviates from the formal duties of a public role because of private-regarding (close family, personal, private clique) pecuniary or status gains; or violates rules against the exercise of certain types of private-regarding influence" (Nye, 1967).

Nye illuminates the counterproductive nature of corruption by pointing out that the motives for engaging in corrupt activity are generally self-centered and self-serving and the intended benefits rarely extend beyond the corrupt actor and their inner circle. While greed is one explanation for why corrupt actions usually benefit only a few, risk management is another. Increasing the number of people positively impacted by corrupt

behavior also increases the amount of exposure for the actor putting them at risk of getting caught. This makes a good case for not trying to spread the wealth gained from the illegal activity (Nye, 1967).

Robert Klitgaard (1988) **also** offers a formula for describing corruption: $C = M + D - A$. The formula effectively states that corruption occurs when there is a monopoly plus discretion, minus accountability. The two most significant components to this formula seem to be power (the power invested in the person to serve the needs of their community) and lack of effective community control over that power. In other words, when people (or groups) in decision-making and leadership positions use their power for personal gain there is corruption, unless there is effective oversight.

Klitgaard continues to say that:

> "Corruption in general is harmful to economic, political, and organizational development. But all forms of corruption are not created equal. Some forms are more harmful than others. The differences are not only just in terms of extent, which of course is important, but of the nature of the corruption and the circumstances in which it occurs" (Klitgaard, 1988).

There are multiple forms of corruption that are harmful to the community**.** For the purposes of brevity, this paper will focus on two that seem to be barriers to community and economic development. Those are police corruption and political corruption in the allocation of resources and opportunities to the community.

Corruption in the Economic Development of Newark-A Case Example.

Today, Newark is known for having high crime rates, low-incomes, and large Black and Latino populations. Newark is also quite well known for its political corruption

and misuse of resources. These negative aspects of Newark are well documented and well earned part of the city's reputation. It is important to understand that these factors because they are the factors that work to lower the desirability of a neighborhood, or even in this case a city, and have largely contributed to the continued economic decline of Newark. However, it is also important to understand that Newark's negative attributes have been directly impacted, and in some cases created by corruption among those in power. An examination of the history of Newark and its decline will help shed light on the relationship between corruption and the drastic economic decline of this once great city.

Newark once boasted a thriving and growing economy, fueled largely by the various industries that developed there. It still sits in a great location and hosts a number of successful businesses. However, these opportunities are not always available to the lower economic classes as a result of human capital and social access gaps. This becomes apparent when looking at the current demographics of Newark. According to the United States Census Bureau, about 86 percent of the city is Black or Latino, with less than 70 percent holding a high school diploma. Twenty-five percent of the population of Newark lived below the poverty level between 2006 and 2010, with the median household income being about 35,000 dollars per year. This is significantly lower than the New Jersey state median household income of a little under 70,000 dollars per year (US Census, 2010).

Corruption has been a recorded part of the political landscape of Newark, New Jersey for at least the last four decades. Currently, Newark is ranked number six (6) out

fifteen (15) most corrupt cities in the United States, with 909 federal corruption convictions from 1976-2010 (Simpson, et al, 2012). Most notably, three of the last four mayors of Newark have been convicted of corruption-related charges (Romano, 2010), In analyzing the impact of corruption in Newark, it is important to recognize that there has existed a significant power distance between the leadership of Newark and its residents. Power distance can be understood as the extent to which members of the community accept that some people have more power than others (Hofstede, 1997). The ability to monitor corruption and implement punishment can be hindered by a high level of power distance (Sims, et al, 2011). This is exemplified **by** the 1967 Newark riots, which were precipitated by at least two kinds of corruption: police corruption and political corruption.

In 1967, the largely black population of Newark rioted and caused anywhere from 10 to 25 Million dollars in property damage and destroyed the main shopping centers. The incident that sparked the riot was the brutal beating and rumored death of a Black taxi driver who allegedly drove around a double-parked police car, but the precipitating events show an ongoing pattern of political and police corruption and discrimination. According to historical reports, the majority of the population of Newark was Black, but the members of political leadership and police force were not, despite multiple promises to follow up on numerous requests for this dynamic to change. Black men were being harassed and killed by white police officers frequently, and there were very few investigations. While this could simply be a case of one group dominating another, it suggests that members of the police department at several different levels were choosing not to enforce well-established civil rights protections against racial discrimination.

Additionally, racism was becoming more blatant in the political culture as well. Perhaps one of the most glaring examples is that of then Mayor Hugh Addonizio, who chose to hire an Irish high school graduate for a school board position over an African American certified public accountant (Herman, 2002).

Concurrently, there was another example of corrupt practices working to damage the relations between the Black community and the government: the misallocation of urban renewal funds. Urban renewal funds were offered by the Federal government to improve the existing housing stock, but were instead used to build highways that divided the city into Black and Caucasian sections. The funding was also used to destroy already limited housing stock used by the Black community, in a process some jokingly referred to as "Black removal" (a play on the words urban renewal). Finally, Black neighborhoods were redlined and residents were denied housing loans which would have offered the opportunity for them to move to better housing locations or improve existing housing (Herman 2002).

Prior to World War Two, low-income, low-quality housing was constructed to accommodate the influx of European immigrants coming to the city. Shortly after the war, the middle class population, having taken advantage of the earning opportunities of the city, began to leave and move to the existing suburbs. This phenomenon is known as "White Flight" in Urban Economics. This ethnic withdrawal often carries with it a

withdrawal of a large percent of the financial and human capital which make a community economically stable. When the capital resources are removed, the poor are left behind and are not able to afford the expense of moving to better communities. This can create a set of self-reinforcing effects, and one of the axioms of Urban Economics is, "self-reinforcing effects generate extreme outcomes." (O'Sullivan, 2008) In the case of Newark, one of the self-reinforcing effects was a declining income and the extreme outcome was growing poverty and the continued decay of the housing stock (since poor people are not frequently able to afford to maintain their properties-or buy new ones), and the increasing power distance between the mostly white political and police forces of Newark and its largely Black population.

Poverty tends to be self-reinforcing, generating more poverty and other negative effects, which seem to feed off one another. In the United States, poverty seems to increase the rates of joblessness, decrease rates of literacy, and lead to poor health, crime, incarceration, homelessness, and substance abuse, all of which in turn contribute to high rates of poverty. Corruption seems to both thrive in, and contribute to, poverty through the misallocation of resources and the destruction of the relationships between those in authority and those they are meant to serve. One frequently overlooked resource that is diminished through corruption is the public trust for authorities (Klitgaard, 1989).

Our society is based on the premise that the law exists to protect its citizens, reducing the need for its citizens to protect themselves. Widespread corruption diminishes the public trust, decreasing the efficiency of the system. It might be proposed

that the 1967 riots were the Black residents' way of closing the power distance between themselves and the existing political and police force. Rampant murder of Black and Latino men by white police officers without penalty clearly demonstrated that the police force was above the law and able to do whatever they saw fit to maintain control. Rioting can be a way of shifting the power balance to show that the oppressed can fight back and harm their oppressors. However, the loss of life and property created a negative externality for the many generations to come, by depriving them of both personal property which could have serves as investment capital, as well as human capital in the form of those who were killed or traumatized by the loss of their loved ones. This supports another axiom of urban economics that states, "externalities cause inefficiencies" (O'Sullivan, 2008). In a normal system of growth, parents work hard and make sacrifices so that their children may inherit a legacy and begin their lives from positions of greater strength and influence than the generations before them. This is one way to build wealth. Stunting the growth of the previous generation, only serves to slow down the entire process of building wealth. The delay of wealth accumulation suggests a deviance from the normal wealth growth patterns and therefore suggests an ineffient transfer or wealth.

While it is imperative that we look at the history of corruption in Newark, it is just as important to note that the same kind of corruption is alive and well today. The most recent mayor to be convicted of corruption was Sharpe James, who was convicted of giving his girlfriend an unfair opportunity to purchase land at a discounted rate. The girlfriend later sold the land for a large profit. Even more recently, the former deputy

mayor Ronald Salhuddin was convicted of steering contracts to a friend in exchange for personal financial gain (Romano, 2010). Police corruption also continues to be a problem in Newark. In 2011, the Justice Department was investigating the entire Newark police department, for "claims that brutality, baseless searches, intimidation and false arrests are commonplace in the Newark Police Department" (Pérez-Pena, 2011). To be clear, it is difficult to know exactly what the motives behind the deviant behavior of the police officers, but what is clear is that they continue to use their authority to satisfy an agenda that is not in the best interest of the people they swore to serve, and these actions are covered for by other members of the force.

In the case of Mr. James, his behavior was harmful to the economic development of the community in much the same way the denial of homes loans is harmful. By removing the opportunity for interested parties to compete for the land plots, he denied fair access to housing or business capital to local residents. Mr. Salahuddin similarly denied competitive access to contracting and employment opportunities by removing or fixing the bidding process, taking jobs out of the labor market which could have benefited capable residents. The significant point here is that favoritism and non-competitive contract allocation can deny the efficient distribution of resources in a way that improves the local economy as a whole, rather than lining the pockets of a select and privileged few. This can have the effect of increasing the wealth of wealth of the few at the expense of the many.

At its core, corruption is the misuse of power for personal gain. Politicians are responsible for ensuring the fair and equitable distribution or resources for the benefit of their constituents and the police is responsible for ensuring the safety and welfare of all of the residents in its districts. When either of these groups engages in corrupt activities, they divert resources that could be used to improve the community as a whole through a public good. This is an externality because the resource-deprived parties have no input in the decisions about where public resources are directed; however they are impacted because they lose the opportunity to avail themselves of the resources because they are monopolized, or in the case of police corruption, used to harm the citizens they are meant to benefit. This is an inefficient practice because it removes resources from the mainstream and limits their utility to only a small portion of the population.

Measures for Reducing Corruption

While there is some evidence to suggest that corruption can have the beneficial effect of lubricating sticky and inefficient political systems, the remainder of the evidence suggests that corruption is a significant barrier to economic growth, in that it redirects resources in ways that are not growth promoting (Hodge, et al, 2011). Iwasaki et al. found that fundamental structural reforms are very effective in preventing corruption in transitional countries, namely the decentralization of the government (Iwasaki, et al, 2011). This evidence suggests that effective corruption control requires not only closing the power distance between politicians and citizens, but also reducing the amount of discretion politicians have over financial matters that impact their constituency. One way of achieving these goals is through economic empowerment.

Economic empowerment can best be understood as a process through which people gain power over the resources and relationships in their community by recognizing and taking advantage of the opportunities for growth and development that exist in their surroundings. Economic empowerment activities include: economic education, wealth creation, creation of self-contained, and self-sustaining economies, and community oversight of public funds. Economic empowerment is one of several forms of human development which has been shown to reduce corruption. In their study, Sims and others discuss the type of human development that has an impact on the reduction of corruption:

> "The results of this study indicate that as human development improves, corruption decreases accordingly. In general, countries with longer life expectancies, higher education and literacy, an adequate living wage, and the ability of its citizens to participate in their community, are less likely to experience increased levels of national corruption." (Sims, et al. 2011)

The study goes on to explain that human development reduces the power distance between leaders and their constituents. The above quoted statements describes countries in which citizens have access to education, capital, a the ability to contribute the political decision making process promoting their efficacy as human beings.

Wealth development is also an important part of closing the power distance. Individuals with high incomes and access to cash are more likely to get the attention of their elected officials, because politicians need money to fuel their lifestyles and campaigns. Wealth creation can be achieved through the purchase and maintenance of

quality housing stock. Housing is a largely financeable resource that allows one to gain an appreciating asset, which stores value and equity, for a relatively low initial investment. This would of course require increased bank lending and other financing to assist with the initial purchase of the property. Increased bank lending has also been correlated with effective corruption reduction (Altunbaş, et al, 2011).

Another strategy toward reducing corruption is to employ civilian oversight committees with some form of enforcement power. The problem with traditional civilian review boards is that they have no enforcement power and therefore play only an advisory role. An ideal scenario might be to use fiscal oversight committees trained in reading and interpreting financial statements and balancing budgets. Participatory budgeting is one way of involving the public in the financial decisions of municipalities. Participatory budgeting can be traced to Brazil, where in at least one city it was used almost exclusively as the financial decision-making tool. The five domains that participatory budgeting was shown to have the greatest impact on were participatory, legal, territorial, financial, and political. Examples of these benefits include reducing unnecessary taxes and increasing the efficacy of property tax collections. Additionally, participatory budgeting has been shown to increase the flow of communication between administrators and the public, as well as increase access to resources in communities that are frequently overlooked (Cabanes, 2004). Attempts have been made to use participatory budgeting in Newark; however, the literature suggests that these attempts have been met with resistance by the administration, and that further work may be needed to improve the efficacy of the process (Liao, et al. 2012). A recent New York Times

article discussed the fact that New York City has instituted a version of participatory

justice within a Brooklyn school district, in which the participants indicated that they felt

empowered by their ability to contribute to the financial decisions of their community

and would like to continue the process. The same article also mentioned that one of the

greatest barriers to the success of participatory budgeting is resistance from political

decision makers (Sangha, 2012). This seems to indicate that participatory budgeting can

work in urban communities within the United States, if political resistance is mitigated.

Further investigation into legislative solutions is recommended.

The role of civilian involvement in the allocation of resources and opportunities is

to keep politicians honest. A slight twist to the common participatory budgeting practice

would be to give the civilians enforcement power, but that enforcement power need not

be punitive in nature. Instead, the committee could be invested with the power to offer

the politician a bonus for remaining within budget and making ethical decisions,

increasing the weight of community voice and opinion, and increasing the community's

cohesion in planning its future. Additionally, this practice could be used to improve

police relations with the community by allowing the community review committee to

review police practices and make recommendations for investigative, disciplinary, and

commendation actions in response to police activities. Klitgaard argued that corruption

requires a risk/reward assessment with corruption being reduced when the risk of getting

caught outweighed the benefits of the corrupt act. Further, he emphasized the value of

incentivizing positive behavior as a way of further tipping the risk/reward scale

(Klitgaard, 1988).

Summary

Corruption can generally be said to reduce economic and social growth, and often affects the communities with the fewest resources and the greatest power distance. Newark, New Jersey is a city with vast economic potential, which has had many of its resources misallocated through corruption, favoritism, and general abuse of vested authority. One of the ways that corruption can be reduced is through the economic empowerment of the affected communities. Economic empowerment can take many forms but its ultimate goal is to create a balance of power and respect between the community and the authorities, so that community members can have access to the resources they need to achieve their goals.

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