



Corruption and the Rising Cost of Business Operations

Cost control is the first consideration in running any business, company, or even in preparing a realistic national budget. Losses arise when costs exceed revenues and there is no effective procedure for managing them. Finance is the lifeblood of any activity required to run a business, and all efforts are typically directed toward plugging leakages and addressing loopholes to maintain financial control.

Understanding Operational Costs

- a) **For Businesses:** Operational costs refer to the expenses incurred during a regular business cycle to keep operations running and ensure business continuity. These costs are typically met through revenues or capital injections. They include the cost of goods sold (COGS) and operating expenses such as rent, raw materials, payroll, and insurance. Businesses aim to control these costs to ensure smooth operations and long-term growth.
- b) **For Governments:** A country's operational costs include expenditures required to manage various government functions. Key areas include salaries of government employees, debt servicing, defense, healthcare, education, infrastructure, and development. These are covered through revenues, loans, and other sources, as outlined in the national budget. The outcome is either a fiscal deficit or surplus, depending on economic conditions.

What Is Considered Corruption

Corruption can be described as deceitful or unethical behavior by individuals in positions of power—such as high-ranking government officials or owners of large businesses. These individuals may abuse their authority to gain personal benefits at the expense of others. This often includes dishonest practices such as accepting or offering bribes, making secret deals, and violating the rights of deserving individuals.

More severe forms of corruption among government officials include election rigging, misappropriation of public funds, money laundering, and misleading potential investors. Such actions not only harm public

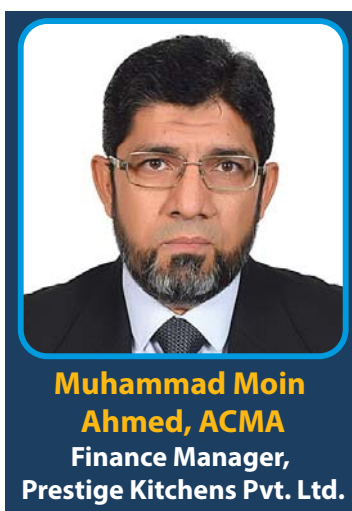
trust but also disrupt the economy, affecting private businesses - whether they are knowingly involved or not.

Corruption has significant social and economic consequences. It disproportionately affects those who are most vulnerable in the business community and limits public access to essential services like education, healthcare, and legal aid. In effect, it deprives people of their fundamental rights.

How Corruption Increases Operational Cost

Corruption can have devastating results for a country's economy and businesses. One of the major impacts of corruption is an increase in the operational costs of businesses and the country overall. There are three basic forms of corruption prevailing in almost every country:

- a) **Bribery and Undue Pressure:** It is the act of offering and accepting bribes to influence business decisions or gain favor. To run operations, businesses need different types of legal documents, permits, and licenses. When they apply for these documents, they are forced to pay bribes to government officials in various departments. After paying these undue amounts of money, the cost of running the business increases, and as a result, the prices become higher to cover the cost and profits.
- b) **Favoritism or Preferential Treatment:** It is the practice of giving favor or preference to family members in business or professional matters. It can lead to the unjustified allocation of available resources, as decisions are made based on personal connections rather than merit or economic considerations.



This can result in the misallocation of resources, leading to an increase in the actual operational costs since merit and fair practice are not considered.

- c) Misappropriation or Pilfering of Funds:** This is the act of stealing or misappropriating funds or assets entrusted to someone's authority or disposal. Various government departments have the responsibility to perform certain functions for public service and benefit. In order to perform these functions, they have some allocated funds. If government officials start misusing these funds or steal them for their personal use or benefit, it increases the operational cost of actually running these unavoidable functions for the country.

We can explain the effect of corruption on operational costs in two ways:

- **Effects on Public Sector**
- **Effects on Private Sector**

Public Sector

Corruption affects the public sector run by the Government in many ways. It can include the illegal transfer of public funds, use of authority to influence decisions against the public interest, and the unjustified allocation of public resources. Below are a few examples of public sector corruption:

- a) Kickbacks in Construction Projects:** When a construction company pays kickbacks to get a government contract to build a road or bridge, it ultimately increases the cost of completing the project. This additional cost comes out of taxpayers' money and is an undue increase in the cost of materials or labor. To cover this cost, the government contractor may also compromise the quality of work, resulting in frequent and costly repairs due to the use of substandard materials. Eventually, the project's lifetime is reduced, leading to early replacement costs.
- b) Delay in Grant of Approvals:** Corrupt government officials in various key departments often seek under-the-table payments to grant approvals, permits, or licenses for projects. If they do not receive such payments, they create unnecessary procedural delays. These delays ultimately pause the project, leading to increased material and labor costs due to the passage of time. This can also result in penalties for not completing the project on time.
- c) Uneconomical Procurement:** Government department officials may approve bids based on personal connections, ignoring other bids that offer lower prices and higher quality service. This results in taxpayers paying more for poor-quality services.

Skipping deserving companies increases project costs due to low-quality purchases.

- d) Salaries of Non-Existing (Ghost) Employees:** Sometimes government officials create false payrolls for employees who do not actually exist. Their salaries are collected by the corrupt officials who created this arrangement. These unlawful salary payments increase the country's operational budget, as there is no actual work done in exchange for the funds paid.

Private Sector

The private sector can be affected by corruption either independently or in coordination with the public sector, creating additional costs—some of which are even unknown or hidden.

Below are a few examples of how corruption in the private sector increases operational costs:

- a) Payments for Customs Clearance:** Unlawful payments are demanded from private companies by customs officials for the quick clearance of imported goods, in order to avoid demurrage charges or production delays. These payments may seem minor at first but often increase over time, making it increasingly difficult to clear consignments without paying these growing unofficial charges.
- b) Payments to Obtain Permits or Contracts:** Private businesses often pay bribes to government officials to win bids for profitable contracts. They may also have to make additional payments to obtain certain permits or licenses, simply to avoid unnecessary delays created by a corrupt system. These payments significantly add to the total project cost. Furthermore, if such a payment is made by an incompetent bidder and the contract is awarded to them over more qualified companies, it can lead to poor performance and costly rework, further raising project costs.
- c) Compliance with Complex Legal Procedures:** In environments where corruption is prevalent, governments may introduce extensive legal compliance requirements. Companies then have to hire staff to handle these procedures and invest in training. They also incur extra fees to meet various legal obligations, all of which add to overhead costs and reduce profit margins.
- d) Fraudulent Activities by Company Staff:** Sometimes corruption becomes part of the workplace culture, where individuals begin to view unethical behavior as acceptable. This happens within companies when employees engage in fraudulent acts such as creating fake invoices or embezzling funds.

There may even be internal collusion that weakens internal controls. These losses place an additional burden on businesses, forcing them to conduct cost audits or take legal action—both of which add to operational expenses.

Corruption increases the overall cost of doing business in a country and damages the country's reputation, making it less attractive for both local and foreign investors. Once a country's image is tarnished, it becomes difficult to attract new investment and restore public and international trust.

Due to the persistence of corruption, businesses that are unable or unwilling to pay bribes or kickbacks may be excluded from valuable tenders or denied certain contracts and licenses. This leads to an increase in the operational costs of key projects. Over time, the normalization of these unlawful practices creates a toxic business environment where corruption-related costs are treated as regular expenses—ultimately driving up prices for everyone.

Ways to Stop Corruption and Its Effects

To address corruption and its impact on operational costs, a multi-dimensional effort is required. Below are some practical measures to help prevent corruption:

- a) **Strengthening Institutions:** Government institutions such as the Anti-Corruption Department, National Accountability Bureau, Tax Collection Authorities, and the country's Judicial System should be made independent and as strong as possible. These institutions must be empowered to monitor and control corruption effectively across all sectors.
- b) **Ensuring Transparency:** Corruption can be reduced by promoting transparency, such as granting the public easy access to government records, implementing online tendering for public projects, and conducting independent audits. Adopting international frameworks like the United Nations Convention Against Corruption can also help improve transparency and accountability.
- c) **Expanding Online Services:** The government should provide digital platforms that allow citizens to interact directly with public institutions, minimizing or eliminating contact with departmental officials. Services such as online voting, tax filing and payment, property registration, and license or permit applications should be made accessible, secure, and user-friendly. This approach will reduce opportunities for corruption and build public trust.
- d) **International Collaboration and Research:** Working with the international community can offer valuable insights and support for combating corruption. In-depth research at the national level to identify



root causes, engagement with organizations like Transparency International, and adopting best practices from other countries can significantly help reduce corruption and its related costs.

- e) **Role of Media and Public Awareness:** Media—both social and mainstream—can play a crucial role in raising public awareness and promoting a culture of accountability. Awareness campaigns should educate citizens about their rights and encourage them to take a stand against corruption. A well-informed public is one of the strongest defenses against corrupt practices.

Conclusion

There can be many reasons for increased operational costs for a business or a country, but when this increase is linked to corruption, it reflects the state of the rule of law and the mindset of the people. Whenever costs begin to rise, several measures are taken to control and reduce them, but this always requires a clear identification of the root cause. Corruption can be difficult to overcome and involves the engagement of multiple stakeholders.

Corruption is a major challenge affecting many countries, including Pakistan. To combat it, bribery, nepotism, and favoritism in both government and business sectors must be prevented. This can only be achieved if the country's law-enforcement institutions are first made free of corruption and strengthened to the highest possible level. Only then can a country reduce operational costs and foster a business environment—across both public and private sectors—where efficiency thrives and sustainable economic growth becomes possible.

About the Author: The writer is an Associate Member of ICMA Pakistan and currently working for Prestige Kitchens Pvt. Ltd. as Finance Manager. He has vast experience working with national and multinational companies in Pakistan and abroad particularly in UAE and Saudi Arabia. He has a particular interest in current affairs and economy.