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Socioeconomic Consequences of Corruption and Financial Crimes

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ABSTRACT

Corruption and financial crimes are major obstacles to the socioeconomic development of many countries in the world. This study employed descriptive research design to assess the socioeconomic consequences of these crimes. The data were collected through questionnaire from 200 respondents. The study results indicate that financial crimes and corruption both have significant socioeconomic consequences by destroying public confidences, weakening public service delivery such as education, health service, it also demolishes private sector particularly small business growth which ultimately affect employment level, GPD and, life expectancy, defeat culture, values, ethics of the society and finally eliminates trust, partnership and collaboration among business organization, public institutions, and society. Moreover, the socioeconomic consequences of these crimes include inequality and poverty in the country. The study recommends strengthening the capacity of public institutions, good governance, strengthening internal control systems, establishing effective monitoring frameworks, promoting accountability and transparency of the public sector, establishing legal frameworks and anti-corruption strategies, and supervision mechanisms in public institutions.

Keywords: Corruption, Financial Crime, Socioeconomic Consequences, Somalia
JEL Classifications: A10, D17, E26, 017

1. INTRODUCTION

The phenomenon of corruption and financial crimes is certainly not new but it is old and considered as universal challenge due to the nature, scope, risk and costs related to them. The need to study of corruption and financial crimes remain higher and for that, researchers and institutions paid their attention to this area do to these factors. Both are non-violent crimes committed by professionals, public officers, politicians, administrators, leaders and even employees. Corruption is understood as "abuse of public office to gain personal or private gain" (Dong, 2011). Financial crimes involve taking money or other property that belongs to others through illegal means (Ryder, 2011). According to the International monetary fund (2001), financial crime refers to "any non-violent crime that generally results in a financial loss." Corruption and financial crime are directly related to societal development and change, according to Achim and Borlea (2020), and Dong (2011). Corruption and financial crime may even emerge as a result of individuals' innovation for adapting to the changes in a society that evolves on its own through continual change. For some reasons, corruption and financial crimes are everywhere in the world and many studies conducted in different countries showed that financial crimes destroy social and economic development. There is a distressing upsurge in the number of fraudulent activities some countries like Nigeria and Kenya (Golicha and Onsiro, 2022; Abdullahi and Mansor, 2018; Ojaide, 2000). This increase of corruption and financial crime is due to the system complexity and development of information technology systems in the digital era (Sukardi, 2022).

Ajide and Ajisafe (2017) stated that these crimes have an impact on entrepreneurship development and socioeconomic growth. When the crime rate increases, level of social development, quality of life, and social progress will decline. More broadly, corruption and forms of financial crime effect directly on business growth, service delivery and human capital management since these crimes create unemployment, inequality and poverty (Free, 2015). Furthermore, crime deters growth, investment, and development, since no investor or business wants to make investments in an area with a high percentage of financial crime, due to protection of their money and emotions. The victims of these crimes experience a range of short- and long-term emotions (Gouseti and Jackson, 2015). This problem can be viewed as one of the causes for some countries' failure to advance socially and economically, as their institutional and procedural crime rates are typically high. Numerous studies have attempted to estimate the direct and indirect effects of crime on society's growth, including Kulmie, 2023; Aidt, 2011; McCollister et al. (2010) and Anderson (1999). The results of some studies on financial crimes and socio-economic development report that financial crime has a very significant negative influence on economic growth (Jonathan et al., 2021; Koech, 2019; Detotto and Otranto, 2010; Cárdenas-Santamaría, 2007), while others like Goulas and Zervoyianni (2012) and Burnham et al. (2004) concluded that the association between the financial crimes and socio-economic development is uncertain or even absent (Mauro and Carmeci, 2007; Ray et al., 2009).

According to BTI report (2022) Somalia is a fragile country and there is no strict separation of powers. However, nepotism, corruption and clan-based decision-making impede the institutional independence and effective resource management. Among others, public financial crimes are considered a major contributor of poverty and the socioeconomic challenges in Somalia (Kulmie, 2023). While 70% of the Somali population is living below the poverty line, the country's main target is to improve the social and economic issues (BTI report, 2022; Nor, 2021; Pape and Wollburg, 2019). According to a BTI study from 2022, politicians often engage in illegal transfers of resources, and their society is distinguished by a high level of inequality, poverty, and unemployment, Additionally, Transparency International reported in 2022 that Somalia is highly corrupted and less progressive country. Free (2015) argued that service delivery, and efficiency is very low where financial crimes exist and ultimately, these crimes destroy socioeconomic development of a given country. Therefore, this study attempts to assess the socioeconomic consequences of corruption and financial crimes.

2. LITERATURE REVIEW

2.1. Corruption

Corruption exists at all societal, business, and institutional levels. When the term "corruption" is used in public institutions, what is typically meant is the abuse of public authority for one's own gain or benefit. Corruption in the public sector can be seen in the transfer or sale of public property, improper handling of public procurement, bribes, and kickbacks committed by public officials (Svensson, 2005). This phenomenon involves illegal means or action for private gain at the expenses of public at large. Corruption is like cancer, and exist at different degrees in different countries (Elijah, 2007). Banerjee et al. (2012) stated that research on corruption has two main obstacles: theoretical and empirical. In the empirical side is measurement. Measuring corruption across countries is a problematic, difficult and challenging task, due its secretive nature and variety forms it takes. In the past, researchers believed that corruption cannot be measured due to its intrinsic nature (Elijah, 2007). On the other hand, the misconception did not deter researchers from trying to do so (Farida and Ahmadi-Esfahani, 2007). Various studies in the literature used many different approaches for measuring or evaluating corruption. These approaches include Economic growth approach which assesses the link among corruption, financial crimes and economic growth. Researchers like Hellman (2000); Bardhan (1997); Mauro (1997); Mandapaka (1995) and Murphy et al., (1993), used this approach to measure corruption where some of the findings revealed these crimes affect negatively economic growth, development. Also researchers satisfy to some extent the need to understand the nature, forms, types, causes and consequences of corruption.

According to Ibodullaevich and Kizi (2021), corruption can be classified in three levels: corruption in everyday life where ordinary citizens and officials involve in it; corruption in business where government and business interact; and finally, corruption in high power where people in political leadership and supreme courts in the democratic system deal with corruption to pursue their personal interests which harm the interests of the public. Ronan and Jenkins (2017) stated that there are different forms of corruption in Somalia such as political and business corruption. However, political corruption is more popular in Somalia. For intense, at least \$20 million has been exchanged during parliamentary elections (Gettleman, 2017). These forms of corruption effected mainly fundamental sectors of the country, including healthcare, security sector, natural resource management and development assistance provided by partners and donors (Bharti, 2022; Hadžić, 2020; Ronan and Jenkins, 2017 and Gettleman, 2017). Despite political corruption and bureaucratic corruption, there are other forms of corruption such as; bribery, fraud, embezzlement, Extortion, Favoritism and Nepotism (Urien, 2012). However, the common issue that people generally understand is that corruption is the biggest difficulty and hindrance of human development (Mishra and Abdullahi, 2020).

2.2. Financial Crimes

Financial crime is non-violent fraudulent behavior that uses concealed practice against the property of others for personal gain (Turner, 2023; Perri, 2011; Andvig et al., 2001). These crimes happen when an individual or entity gets money, goods, or services illegally or dishonestly in order to benefit themselves. So, these crimes are considered one of the major risks that society faces (Wanjiku, 2019). It ranges from simple fraud to large-scale operations committed by internal or external people which affect individuals, organizations, governments, and societies (Albrecht et al., 2015; Waziri, 2011). Similarly, financial crimes are non-violent crimes on assets targeted at illicit financial gains at the expense of their victims (Mohammed, 2012). The researchers stated that financial crime has existed since the earliest days of man and can be found in any culture, regardless of its level of development. As a result of the actions of criminals worldwide, many innocent people sufferer, making financial crime one of the issues governments around the world have to deal with (Jonathan et al., 2021; Hashim et al., 2020). Topologies of financial crime are becoming more complex as they increasingly more sophisticated and dynamic (Omar, et al., 2016). Some researchers consider it as operational risk while others see it as multifaceted crimes with no specific nature. Financial crimes include market manipulation, money laundering, financing of terrorism, tax evasion, insider dealing, fraud and bribery (Biasucci and Prentice, 2020; Rider, 2015; Muriithi and Louw, 2017).

3. THEORETICAL FRAMEWORK

3.1. Theories of Corruption

There are massive literature presenting different explanations on the nature and causes of corruption. Principal-agent theory, collective action theory, institutional theory, and game theory are among the theories that explain why corruption exists. According to the principle-agent theory, public servants (the agents) work on behalf of the interests of the general public (the principal), and this interaction is referred to as a principal-agent relationship. When the interests of the principal (the general public) and the agent (public officials) diverge, an agency dilemma occurs. However, the principal-agent theory of corruption has been criticized by a number of researchers, including Persson et al. (2013), Mungiu-Pippidi (2011), Bauhr and Nasiritousi (2011), and Rothstein (2011), because anti-corruption strategies and policies based solely on this assumption have failed.

The theory of Collective Action by Mancur Olson, published in 1965, is when the collective action theory appeared as an alternate explanation for why systemic corruption exists (Marquette and Peiffer, 2015). This paradigm views systemic corruption as a collective concern because people rationalize or justify their own behavior based on the perceptions of what other people will do in similar circumstances. According to this model, corruption becomes a social norm when everyone starts seeing it simply as the way to get things done. Collective action theory sees corruption more broadly than traditional principal-agent relationships because it points out the importance of factors including trust and how people perceive other people's actions. In this sense, systemic corruption is viewed as societal issue that affects society significantly (Persson et al., 2013). However, people continue to act corruptly despite the negative consequences because they believe that "it doesn't make sense to be the only honest person in a corrupt system" (Marquette and Peiffer, 2015).

In addition, there is the institutional theory (also known as institutionalism theory) that analyzes corruption in the public sector by using institutional characteristics of the country and the public sector, such as anti-corruption structures, institutions and norms, rule of law, and enforcement authorities (Module 4, Public Sector Corruption, UNODC). This theory looks at the process by which rules, standard, structures and procedures emerge and established as guidelines for social behavior (Peters, 2022; Amenta and Ramsey, 2010; Scott, 2004). Therefore, institutional theory believes that political system and institutions have an impact on corruption. Generally, researchers identified several factors that contribute the existence of corruption at country level, namely; country size and age, political instability, government size, nature of bureaucracy, social capital, salaries, absence of rule of law, conflicts of interest, failure of governance (Biygautane, 2023; Corrado and Rossetti, 2018; Ferguson, 2017; Locatelli et al., 2017; Goel and Nelson, 2010; Shah, 2006). Based on these assumptions, Somalia's public sector corruption is a result of weak institutions, a lack of merit-based hiring, a lack of an anti-corruption commission, and a lack of anti-corruption laws (Mohamed, 2021). However, each theory of corruption explains corruption in terms of its nature, perception, causes, and effects, which aids in our understanding of corruption and enables us to create effective preventive measures and counteract it.

3.2. Theories of Financial Crimes

Understanding the evolution of fraud theory will be extremely beneficial in preventing the occurrence of fraud in the future and its relevance to fraud risk control in the government (Vousinas, 2018). All fraud theories attempt to find answers to some inquiries related to the fraud occurrence and how can be prevented. In the beginning, Edwin H. Sutherland developed the idea of "white-collar crime," or crime performed by professionals, in 1944. Before this date, the term "crime" referred more to street crime or violent crime. Sutherland (1940-1944) asserted that financial or economic crime was frequently committed by professionals, which makes it difficult to identify the perpetrators of these types of offenses properly. In the 1950s, criminologist Donald R. Cressey made an observation about Sutherland's study. Cressey's work has been termed "the fraud triangle." Under this theory, three elements i.e., pressure, rationalization and opportunity were considered as a root cause of fraud. However, regulators, experts, and scholars frequently rely on Cressey's concept, which explains why trust violators perpetrate fraud (Kassem and Higson, 2012).

Albrecht's Fraud Scale (1984) is another fraud theory in addition to Cressey's Fraud Triangle (Uygur and Napier, 2023). The Fraud Scale identifies three elements that influence whether fraud occurs: Situational pressures, opportunities for fraud, and personal integrity. Albrecht replaced the justification element to "personal integrity" to make it stand out more and visible. Individuals' personal integrity or ethics can be traced back to their past behavior, whereas rationalization is more abstract to be known by others. Recent studies indicate that there is a great demand for ethical training programs currently due to many forms of fraud and that these programs act as a preventive tool against these different forms of financial crimes (Rahman and Anwar, 2014). Many researchers, particularly economists and sociologists, are interested in fraud, corruption, and financial crimes. Similarly, regulators, auditors, and the public concentrated on this kind of crimes due to their effects on society, organization and governments. The researchers proposed theories and models that also explain the nature and reasons behind committing fraud. In 2009, Ramamoorti developed A-B-C model to classify fraud three types of fraud namely; a bad Apple, a bad bushel and a bad crop. When one individual committed fraud is termed bad Apple, while the fraud committed in collusion is referred as collusive fraud. The third category is bad Crop which occurs when fraud is committed in collusion with social and cultural mechanism (Ramamoorti, 2008).

4. SOCIOECONOMIC CONSEQUENCES OF CORRUPTION AND FINANCIAL CRIMES

Financial crimes and corruption are major challenges that societies face. Broadly speaking, financial crime affects the economical, spiritual, physical, psychological well-being of the society (Eidell and Ellis, 2010). The United Nations Office on Drugs and Crime (UNODC) stated that crime, whether in public or private, fuels mismanagement, political instability and undermines the economic growth and development of society (Jonathan et al., 2021). The psychological challenges of public financial crime to the society include insecurity around people, worry, and fear (Okpuvwie and Toko, 2020). Corruption in public institutions as well contributes to frustration among otherwise talented and honest civil officials (Gould et al., 2012). Salim (2015) pointed out that poverty; family stability; individual and societal health are related to the crime.

According to some studies, including Schleimer et al., (2022) and Abdi (2022), unemployment contributes to crime in society because it puts people under financial stress since they need money but are unable to find it, and corruption itself brings unfairness in employment and hiring process. Since unemployment and poverty are twin problems, there is no doubt that they are closely related to crime and corruption (Adegoke, 2014). In its broader scope, financial crimes destroy all aspects of society particularly economic and social assets. Due to this, poverty is a major obstacle to participation in larger social networks and advancements (Matthews and Besemer, 2014; Portes, 2000). Further, poverty is one of the world's primary concerns for developing and poor countries. Although the level and severity of poverty varies among nations, it remains the largest impediment to the optimal utilization of human resources for both social and economic development (Nor, 2021). Public financial crimes remain a huge challenge to Somalia as these crimes avert and prevent Somalia from its target to end poverty in 2063.

Several research findings, crime has a detrimental effect on development and growth (Mauro and Carmeci, 2007). For instance, Ndikumana (2006), pointed out that Corruption harms economic performance by reducing private investment and also reducing the quality of public infrastructure. Similarly, it harms country's opportunity of foreign direct investment (FDI) since multinational enterprises (MNEs) prefer to invest the location with good economic institutions and political stability (Warsame, 2021). Corruption has negative distributional impacts in addition to inefficiency effects, which cause lower growth for a given endowment in resources and technology. In addition to the inefficiency costs, corruption has negative distributional impacts because it disproportionately affects the poor. In Africa, several studies conducted in Nigeria, Kenya, and Somalia have found evidence that financial crimes have a negative impact on the expansion and development of enterprises in Africa. According to the literature, Nigeria is not immune from the list of many countries that are vulnerable to huge economic backwardness as a result of an increase in the amount of fraud and other fraudulent acts, particularly in the public sector, however, identifying and preventing financial is hard, because it necessitates extensive understanding on the nature of financial crimes, how it can be performed, and how it can be concealed by the fraudsters (Abdullahi and Mansor, 2018).

According to Olongo (2013), Waziri (2011) and Gould et al. (1983), corruption and of financial crimes massively affect entrepreneurship, business development, economic growth, social development, public management, business development and economic growth. Ndikumana (2006), high corruption countries have lower literacy rates, higher death rates, and generally worse human development results for a given level of government spending and national revenue. Because of this, concern over how corruption affects administrative effectiveness has grown in recent years in many different countries around the world (Almustafa et al., 2023; Arayankalam et al., 2021; Bahoo et al., 2020; Gould et al., 1983). In Kenya, compliance with financial crime regulations is one of the most difficult challenges in the financial service sector (Wanjiku, 2019). According to a Price Waterhouse Coopers (2018) survey, Kenya ranks second in the world in terms of economic crime and fraud. According to a Price Waterhouse Coopers (2018) survey, Kenya is ranked second in the world for economic crime and fraud, with a prevalence of 75% of financial crimes. In Somalia, corruption and financial crimes impeded the management and distribution of public resources as well as socioeconomic growth (Kulmie, 2023). Equally, other scholars such as Tripathi, (2023); Nwambuko, et al., (2022); Lagazio, et al., (2014); Kramer, (1999) discovered that financial crimes damage public institutions' reputations and diminish public trust and resources. Further, it is observed that greater economic growth frequently coexists with lower levels of corruption (Bai et al., 2013). Studies from both the past and the present support the idea that neglecting to fight financial crimes

Table 1: Demographic information

Category	Frequency	Valid percent
Gender		
Male	160	80
Female	40	20
Total	200	100
Age		
20-30	93	46.5
31-40	76	38
41-50	19	9.5
Above 50	12	6
Total	200	100
Educational level		
Bachelor	85	42.5
Master	88	44
PhD	5	2.5
Others	22	11
Total	200	100
Levels of experience		
<2 years	32	16
3-4 years	60	30
5-7 years	62	31
Above 7 years	46	23
Total	200	100

Table 2: Social economic consequences of corruption of financial crimes

Statements	Responses %				
	SD	DA	N	A	SA
Corruption and financial crimes result luck of confidence in government institutions	7.5	7.5	11.5	42.5	31
Corruption and financial crimes cause poor public service delivery to the society	7.5	6.5	15	38	33
Corruption and financial crimes in public sectors disrupt business growth and development	4.5	10	14.5	47.5	23.5
These crimes cause unemployment, low income, poor education,	7.5	10.5	15.5	49.5	17
Corruption and financial crimes in public institutions undermine integrity, culture and ethics	6	5.5	12.5	46.5	29.5
Corruption and financial crimes in public sector led to inequality and poverty and low life expectancy	8	7	9	43	33
Corruption and financial crimes derails socioeconomic development	7	7	11	41	34

can cause a considerable financial loss (Kulmie, 2023; Wanjiku, 2019; Waziri, 2011; Eidell and Ellis, 2010).

5. METHODOLOGY AND DATA ANALYSIS

This study was an attempt to assess the socioeconomic consequences of corruption and financial crimes. The study used descriptive survey research design. Descriptive research provides an overview of the specific aspects of a social situation, scenario, or relationship (Neuman and Robson, 2014). This study employed a questionnaire with five Likert Scale, as data collection tool to collect information from 200 respondents from ministry of justice and constitutional affairs, ministry of finance, the ministry of planning, investment and economic development, and the central bank of Somalia.

The study used simple random sampling method since it gives the whole element the same opportunity to be chosen without bias. This survey consisted of two sections. In the first section, background data on the respondents, including their age, gender, and level of education, were to be gathered. The first section intended to collect background information of the respondents such as age, gender, and education. The second section addressed the socioeconomic consequences of corruption and financial crimes. The date collected from these participants were analyzed using the computer application known as Statistical Package of Social Science, with specific references of frequencies and table in order to analyses and present adequately.

6. RESULTS AND DISCUSSION

In this section, the study's research participants' opinions are presented. First, demographic information such as gender, age, education and experience are provided. This information is presented with frequencies and percentages with tables. Second, participants' responses on socioeconomic consequences is also presented with percentages.

6.1. Demographic Information of Respondents

Table 1 indicates that 20% of the research participants were female whereas 80% were male. This demonstrates how few women are employed in the government agencies compared to the number of men because of cultural constraints. Additionally, the table reveals that among all age groups, those between the ages of 20 and 30 had the highest number of responders (93), with a proportion of 46.5%. The second-highest group of respondents, consisting of 76 people, was between the ages of 31 and 40. Additionally, 19 people, or 9.5% of respondents, were between the ages of 41 and 50. The least number of participants, 12 people over the age of 50, made up 6% of the total respondents. According to statistics, 75% of Somalia's population is under 30 years old, hence this outcome may be related to that age group. On the other hand, in the table above, the respondents' educational backgrounds are presented. Participants amounting 85, or 42.5%, hold bachelor's degrees, 88 of them, or 44%, hold master's degrees, and 5 or 2.5% hold PhD, while 22 (11%) respondents have other education background. Furthermore, the table demonstrates the respondents' level of experience. The number of respondents with <2 years' experience was 32, or 16%, while the number of respondents with 3-4 years' experience was 60, or 30%. This result shows that 62% of public sector employees have between 5 and 7 years of experience, whereas only 46% of respondents have more than 7 years of experience.

6.2. Socioeconomic Consequences of Corruption of Financial Crimes

Table 2 shows that 73.5% of the participants both corruption and financial crimes cause lack of public confidence in government institutions, and 71% of the participants responded that these crimes cause poor public service delivery. Additionally, 71% stated that these crimes impede the growth and development of businesses, while 66% of respondents, or 76%, claimed that these crimes are reasons for unemployment, low incomes, and inadequate educational opportunities. Further, 76% indicated that corruption and financial crimes undermine integrity, culture, ethics and other social values of the society. Finally, respondents amounting 75% stated that corruption and financial crimes derails socioeconomic development in the country. These results depict the socioeconomic consequences of corruption and financial crimes. However, the findings of this study concerning the socioeconomic consequences resulted from the existence of corruption and financial crimes are consistent with findings of several previous studies conducted. According World Bank reports, Somalia ranked 190 since 2017 in the ease of doing business and identified as the worst country in terms of doing business, meaning low ranking nations reflect that public sector is not accountable and efficient (Business, 2020). According to Forti and Visconti (2019) and Elijah (2007), corruption reduces economic development, progress, and efficiency; it harms the nation's reputation; it diminishes the worth of human life; it deprives hospitals, schools, welfare agencies and agricultural industries. These crimes reduce public revenue, and increase government disbursements. In order to prevent financial loss caused by corruption and financial crimes, it is necessary to establish and implement an integrated financial system which is fundamental in public financial management (Nor, 2019).

7. CONCLUSION AND RECOMMENDATIONS

Corruption in public sector is committed by people through power abuse for private gain due to the absence of effective control system and proper accountability. The results revealed that financial crimes occur in government agencies due to lack of good governance and accountability and remains undetected for long period of time. The study found that financial crimes and corruption have significant socioeconomic consequences by destroying public confidences, weakening public service delivery and demolishing private sector growth and development which ultimately affect GPD, employment level, living standard and create inequality and poverty. Corruption and financial crimes defeat culture, values, ethics which eradicate trust, partnership and collaboration among business organization, public institutions, and society. Based on the findings, the study recommends the following suggestions:

1. Promoting good governance practices and strengthening public institutions' capacity of planning and management
2. Strengthening internal control mechanisms and establishing strong monitoring frameworks to encourage transparency and accountability of the public institutions, particularly public financial management, procurements, and development programs
3. Establishing legal frameworks through developing polices and anti-corruption strategies and improving supervision procedures in public institutions
4. Conduct comprehensive ethical training programs to enhance moral integrity and awareness of public employees.

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