Is more competition always better? An experimental study of extortionary corruption*

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Abstract
We test the effectiveness of an anti-corruption policy that is often discussed among practitioners: an increase in competition among officials providing the same good or service. In particular, we investigate whether an increase in overlapping jurisdictions reduces extortionary corruption, i.e., bribe demands for the provision of services that clients are entitled to receive. We overcome measurement and identification problems by addressing our research question in the laboratory. We conduct an extortionary bribery experiment where clients apply for a license from one of many available offices and officials can demand a bribe on top of the license fee. By manipulating the number of available offices and the size of search costs we are able to assess whether increasing competition reduces extortionary corruption. We find that, if search costs are unaffected, increasing the number of providers may actually increase corruption. In particular, our results show that increasing competition has either no effect (if search costs are high) or a positive effect (if search costs are low) on bribe demands. We compare our findings to those obtained in a standard market environment and find evidence of different search behaviors in the two settings.

JEL classification codes: D73, D49, C91
Keywords: Competition; Extortionary Corruption; Experiment

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1 Introduction

Over the last three decades, theoretical and empirical studies have generated widespread consensus on the negative effects that corruption has on society.\textsuperscript{1} As a consequence, empirical investigations into the causes of corruption, ultimately aimed at identifying policy measures that might be successful in its mitigation, have proliferated.\textsuperscript{2} Similarly, theoretical studies have focused on the design of institutions that, through monetary rewards and penalties, can prevent public officials from abusing their positions and thus causing harm to society.\textsuperscript{3} Although the existing studies have increased our understanding of why and how corruption occurs, identifying successful anti-corruption strategies remains a challenge. The evidence suggests that the expected returns to corruption can be successfully reduced by increasing formal monitoring and punishment; however, the enforcement of severe deterrence mechanisms might be prohibitively costly, or simply unfeasible in settings where the strategic complementarities associated with corruption render rule enforcement a collective action problem. Changes in the institutional environment that do not rely on external punishment are preferable, especially in settings characterized by systemic corruption. One such change, which is often suggested as a potentially effective anti-corruption policy, concerns the organization of the bureaucracy and the relationship between public offices in charge of providing the same good or service.

Rose-Ackerman (1978, 1999) was the first to state that if officials were given overlapping jurisdictions citizens would be able to choose which official to approach when applying for a given license or service. Consequently, no official would have much monopoly power. The same argument was brought forward by Shleifer and Vishny (1993) which stated that if many officials can provide the same permit, “Bertrand competition in bribes will force the equilibrium bribe on each permit down to zero” (Shleifer and Vishny, 1993, p. 607). According to both Rose-Ackerman (1978, 1999) and Shleifer and Vishny (1993), competition among officials is likely to be effective especially in the fight against extortionary, or coercive, corruption, i.e., bribe demands for services that citizens are entitled to, as opposed to collusive corruption, i.e., bribe demands for the provision of illegal services that citizens are not entitled to receive.\textsuperscript{4} It is on payments generated by extortionary corruption that we focus in this paper; such payments are sometimes referred to as harassment bribes. Think, for instance, of a citizen applying for a passport, going to the closest passport issuing office (which might require long traveling time) and being demanded a bribe on top of the official fee. The citizen can then either pay the bribe and get the passport or refuse to pay and go to a different office hoping to be able to get the passport without having to pay a bribe. If there is no other office to go to, the citizen’s


\textsuperscript{2}For examples of studies using cross-country data, see Treisman (2000) and Serra (2006). For examples of studies using firm- or household-level data, see Svensson (2003) and Hunt (2007). For examples of studies using direct observation in the field see Olken and Barron (2009) and Sequeira and Djankov (2013). For a review of the different methodologies employed for the empirical study of corruption, see Sequeira (2012).

\textsuperscript{3}For a review of important issues see Bardhan (1997), Banerjee et al. (2012) and Ryvkin and Serra (2012).

\textsuperscript{4}Shleifer and Vishny call this kind of corruption, corruption without theft.
only option is to pay the bribe. The same applies to multiple other environments. Think, for instance, of the case of a citizen requesting connection to an electrical line or to a water pipe, or the case of a firm applying for a building permit.

Testing whether increasing competition among providers of the same government service would negatively affect the demand of harassment bribes is empirically challenging, due to both the difficulty of measuring corruption in the field and the necessity to persuade high-level government officials to experiment with the available number of service providers in a scientific way. Unsurprisingly, empirical studies on this matter are scarce. Burgess et al. (2012) investigate the effect of forestry officials’ overlapping jurisdictions in the context of logging permits in Indonesia. However, they look at quantity-based rather than price-based competition among officials in the context of collusive rather than extortionary corruption. Kiselev (2012) employs firm-level survey data and regional panel data in Russia and measures region-level competition among officials using the density of government employment in each region. He finds that (self-reported) bribe payments by firms are higher yet the (self-reported) occurrence of corrupt exchanges is lower in more competitive regions.

In this paper we employ a novel laboratory experiment to test whether increasing competition among public offices would be an effective way to fight extortionary corruption. In particular, we designed an experiment that simulates extortionary corruption in a setting where service recipient can obtain the same service from multiple offices. Our experiment represents a novel departure from all the existing corruption experiments (Abbink et al., 2002; Abbink et al., 2014; Barr and Serra, 2010; Banuri and Eckel, 2012; Cameron et al., 2008, among others), which have focused on the interaction between a potential briber, i.e., a firm or a citizen, and a public official with monopoly power over the provision of a government good or service. Contrary to previous studies, we do not exogenously match each service recipient to a possibly corrupt service provider; instead, we allow service recipients to search among multiple service providers and choose to receive a service or good from any of them. This framework allows us to investigate whether changes in the number of available offices providing the same “license” affect the demand of harassment bribes. Crucially, contrary to both Rose-Ackerman (1978, 1999) and Shleifer and Vishny (1993) we assume that searching for an honest official is costly, as it involves traveling from office to office with no guarantee that searching would pay off.

By employing a laboratory experiment, we are able to both isolate confounding effects – such as the indirect effect of increased number of providers via a decrease in search costs – and overcome implementation and measurement difficulties that would make testing our research question in the field especially problematic. It could be argued that decisions made by student subjects within the controlled environment of the experimental lab are unlikely to reflect the decisions that the same students or that average ordinary citizens would make in outside-the-lab situations. We have two answers to this possible criticism. First, we are not trying to estimate “general” corruption levels or preferences. We acknowledge that, of course, the levels of corrup-

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5 We know of only one other experimental study (Abbink et al., 2014) that, like us, focuses on extortionary rather than collusive corruption.
tion are likely to be different when using different subject pools and when moving from the lab to the field. However, like most experimental economists, we are not interested in levels; we are interested in comparative statics regarding the effects of certain incentive systems and contextual situations, and in the mechanisms underlying observed behaviors.\footnote{For a general discussion of the external validity of laboratory experiments, see Kessler and Versterlund (2011) and Camerer (2011).} Second, investigating these comparative statics in the field is often prohibitively costly or simply unfeasible. The decision-making context that we are studying is clearly an example of such infeasibility. Indeed, due to the secretive and illegal nature of corruption and the need to persuade a government to experiment with the number of offices and/or providers of the same good or service, it is highly unlikely that our research question could ever be addressed in the field.\footnote{Additionally, while proving the external validity of our design is virtually impossible, some conclusions can be drawn from the study of Barr and Serra (2010), which relies on a bribery game similar to the one used in this paper and on a sample of students coming from over 40 countries characterized by markedly different levels of corruption. Barr and Serra (2010) show that behavior of the undergraduate students in the game could be predicted by the level of corruption in the students’ home countries, as proxied by Transparency International’s Corruption Perception Index. The fact that corruption in the stylized setting of the lab experiment correlates with corruption in the participants’ home countries can be interpreted as an indication that the setting reproduced in the lab is indeed related to corruption decision-making outside the lab. Armantier and Boly (2013) show that corruption “can be studied in the lab” by comparing individuals’ behavior and responses to incentives in a bribery experiment and in an actual field experiment, in which participants, unaware of being part of a study on corruption, had to decide whether or not to engage in bribery. Both experiments were conducted in Burkina Faso. The results show that individuals’ propensities to engage in bribery were virtually identical in the lab and in the field, when controlling for individual characteristics.}

Our findings suggest that increasing the number of offices in charge of providing the same license may increase rather than decrease extortionary corruption, depending on the size of search costs. In particular, if search costs are high, increasing the number of offices has no effect on bribe demands, whereas if search costs are low increasing the number of offices leads to higher bribes. On the other hand, a reduction in clients’ search costs, keeping the number of offices fixed, unambiguously leads to lower bribes. In the field, an increase in the number of offices is often accompanied by a reduction in search costs, for example due to a more convenient geographical location of new offices for some clients. Our results suggest that such a change may lead to lower or higher corruption; while the decrease in search costs would push the bribes down, the increase in the number of offices might push the bribes up. The resulting level of corruption would therefore depend on the relative magnitude of the two opposing effects. According to our findings, corruption could be more effectively reduced by implementing policies aimed at reducing clients’ search costs directly\footnote{For example, search costs can be reduced by improving infrastructures, such as roads or public transportation, or by promoting information sharing about the size of bribe demanded by different officials, without changing the number of offices. A recent study by Ryvkin, Serra and Tremewan (2015) addresses the latter policy by testing the effectiveness of different information sharing mechanisms.} than by increasing the number of overlapping jurisdictions for the provision of government goods or services.

Given the scarcity of empirical evidence on the more general effect of competition on prices, we also test whether our results extend to a general market setting where multiple buyers can buy a homogeneous good from a low versus a high number of sellers, in the presence of low search
costs. Contrary to our corruption results, when replicating the study in a market setting we find that the number of sellers has no impact on prices. Our data provide suggestive evidence that the different effects of the number of sellers obtained in the two settings are driven by different search strategies employed by buyers depending on the context.

The paper is organized as follows. Section 2 reviews the related literature. Section 3 describes our extortionary corruption experiment and theoretical predictions. Section 4 presents the empirical results and Section 5 reports results from additional treatments employing a standard market setting. Finally, Section 6 discusses the empirical findings and concludes.

2 A review of the literature

In the last decade, a growing number of studies have applied experimental methodologies to the study of corruption. The surge of laboratory experiments, in particular, has followed from the universal desire to identify effective anti-corruption policies while facing severe measurement and identification problems in non-experimental data, as well as the difficulty of convincing (often corrupt) government to scientifically test possible policies in the field through randomization. The existing experimental literature has provided valuable insights into the effectiveness of top-down enforcement mechanisms (Abbink et al., 2002), asymmetric punishment (Abbink et al., 2014), different sets of monetary incentives (Armantier and Boly, 2013), as well as non-monetary factors (Abbink and Hennig-Schmidt, 2006; Barr and Serra, 2009), and bottom-up punishment systems (Banuri and Eckel, 2012; Cameron et al., 2009; Serra, 2011).9 Crucially, with the exception of Abbink et al. (2014) all the previous studies have focused on collusive corruption, i.e. the exchange of bribes for the provision of an illegal service. Moreover, in all the existing experiments, to the best of our knowledge, service providers, i.e. “public officials,” are granted monopoly power over the good demanded by the potential bribe-payer. In other words, each service recipient is randomly matched with a provider and given the chance to obtain the desired corrupt good only from that provider, possibly by paying a bribe. There are no experimental studies of corruption, to the best of our knowledge, that analyze bribe demands under the assumption of competition among service providers.

From a theoretical viewpoint, the prediction that increasing the number of officials in charge of providing the same permit would reduce the size of bribe-demands (Rose-Ackerman, 1978, 1998; Shleifer and Vishny, 1993) does not take into account the existence of search costs. We are not aware of any theoretical study of corruption that systematically investigates the effectiveness of competition among public offices in the presence of search costs.10

The more general theoretical literature on the effect of competition on prices under the assumption that consumers are (at least partly) uninformed about prices and therefore need to

9Significant advances have also been made in our understanding of the relationship between gender and corruption (Alatas et al., 2009), and between culture and corruption (Barr and Serra, 2010; Cameron et al., 2009).
10Drugov (2010) develops a model of competition among public officials in the presence of both extortionary and collusive corruption, but does not employ the framework of equilibrium search theory.
search, where searching is costly, is quite vast. Diamond (1971) was the first to show that when consumers are uninformed about prices and all have nonzero search costs, monopoly pricing can emerge as equilibrium in Bertrand competition of identical sellers of a homogeneous product. Applying Diamond (1971)’s theory to our extortionary corruption setting leads to the prediction that, if all applicants have positive search costs, increasing the number of available offices would not have any effect on bribe demands, since all offices would still demand the highest possible bribe. If instead we adopt an equilibrium search framework, whether increasing competition reduces or increases prices seem to depend crucially on the assumptions of the model with respect to the distribution of search costs and the search algorithm employed by consumers. In particular, we can distinguish between sequential (Stahl, 1989) and nonsequential, or fixed sample size (Burdett and Judd, 1983; Janssen and Moraga-Gonzales, 2004) search models. Sequential search models assume that consumers search until they find a price at or below a reservation value determined by the equality of their marginal search cost and expected gain from an additional search. Nonsequential search models assume that consumers decide first how many sellers to visit or search from, and then buy from the seller charging the lowest price, out of those visited. Note that the difference between the two search strategies is not the fact that the former assumes that buyers visit one store at a time, while the latter does not. Under the assumption of nonsequential search buyers might still visit each store in a sequential matter. Rather, the difference is that when search is sequential, at any given time the decision to visit an extra store depends on the prices encountered so far, whereas when search is nonsequential it does not, since buyers determine the number of stores to visit before the search process begins.

As we briefly discuss in Section 3.2 and formally show in Appendix B, sequential and non-sequential search models lead to different predictions with respect to the effect of an increase in the number of sellers on prices. This implies that there is no clear answer to whether increasing competition among public offices reduces or increases bribe demands. Instead, the answer seems to depend on the search algorithms employed by citizens, and which algorithm is employed is ultimately an empirical question.\textsuperscript{11}

The empirical evidence on the effect of increased number of sellers on pricing is also scarce. The obvious identification difficulty lies in the endogenous nature of the number of firms operating in a market.\textsuperscript{12} Experimental studies are less problematic and indeed more common. However, most studies are finalized to test for discrepancies between optimal search and observed buyer behavior while focusing on sequential search (Grether et al., 1988),\textsuperscript{13} or compare

\textsuperscript{11} The existing empirical evidence suggests that the search algorithm used by consumers is some mixture of fixed sample size and sequential search. Morgan and Manning (1985) obtain theoretically the conditions under which one of the two search algorithms, fixed size or sequential, is optimal. De los Santos et al. (2012) use detailed web browsing and purchases data and find that sequential search is largely rejected by, while fixed sample size search is mostly consistent with the observed search behavior. See Section 6 for further discussion.

\textsuperscript{12} Haynes and Thompson (2004) and Barron et al. (2004) are among the few exceptions.

\textsuperscript{13} The experimental studies of Schotter and Braunstein (1981), Harrison and Morgan (1990), Kogut (1990), Sonnemans (1998), Brown et al. (2011), among others, find significant deviations from the predictions of sequential search models. See Camerer (2005) for a review of this literature.
different search algorithms (see Harrison and Morgan, 1990). There is no study, to the best of our knowledge, that directly investigates the effect of increasing the number of sellers on prices in a context where consumers need to engage in costly search to identify the cheaper seller.

3 The experiment

3.1 Design and implementation

We designed a novel extortionary bribery game, in which we use corruption-loaded language. In the experiment, subjects are randomly assigned either the role of public official or the role of private citizen and keep that role for the duration of the experiment. There are 7 citizens and \( n \) (=3 or 7, depending on treatment) officials in each session. Each public official is in charge of an office that provides a license to private citizens. Public officials receive a lump-sum wage of 130 experimental currency units (ECU). Citizens receive an initial endowment of 80 ECU. When a citizen acquires the license she additionally gains 70 ECU. The official license fee is 20 ECU. Thus, in the absence of corruption both public officials and citizens earn 130 ECU. However, each public official can demand a bribe between 1 and 50 ECU on top of the official fee. If a bribe is demanded, citizens can either pay it and get the license, or refuse to pay and go to a different office by paying a fixed search cost. In the experiment we vary the size of the search cost and the number of available offices.

The experiment proceeds as follows. At the beginning of each of 10 rounds, public officials simultaneously decide whether they want to demand a bribe for the provision of the license on top of the official fee, and the size of the bribe, if any. Then, each citizen is randomly matched with an office and finds out the bribe demanded by the official in that office, if any. The citizen can either get the license by paying the official license fee and the requested bribe, or visit another office by paying a fixed cost \( c \). Each citizen has access to a map showing all available offices; for the offices the citizen visited, the map shows what bribes are demanded there. Citizens can costlessly go back and get the license from any of the previously visited offices by paying the corresponding bribe; they have to get the license eventually. Officials do not know the size of the bribes demanded by other officials; however, as citizens search through the offices, each official can see how many citizens visited his office, how many decided to get the license there and how many decided to leave. The official’s payoff at the end of each round is 130 ECU plus all the bribes paid by the citizens who decided to get the license at the official’s office. The citizen’s payoff at the end of each round is 130 ECU minus the bribe she ends up paying and total search costs.

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14 Davis and Holt (1996) and Cason and Friedman (2003) manipulate the size of search costs while assuming different search algorithms and both find that prices increase as search costs are increased. Davis and Holt (1996) employ sequential search, whereas Cason and Friedman (2002) employ a streamlined version of Burdett and Judd (1983)’s noisy search model.

15 Morgan et al. (2006) conduct an experiment where computerized buyers are either fully informed about the prices charged by different sellers, and therefore buy all the desired units from the cheapest sellers, or buy an equal number of unit from each seller. Morgan et al. (2006) vary the proportion of informed buyers and the number of sellers. They find that increasing the number of sellers lowers the price paid by informed consumers and increases the price paid by uninformed consumers, hence resulting in higher price dispersion.
costs, i.e. \( c \) multiplied by the total number of searches. At the beginning of each new round, officials are randomly re-assigned to different offices, so citizens cannot associate location on the map to a particular official.

We conduct different treatments where we manipulate the number of offices, \( n \), and the search cost \( c \). In particular, in the low-\( n \) treatments we set \( n = 3 \) and in the high-\( n \) treatments with set \( n = 7 \). Moreover, in half of the sessions we set \( c = 5 \) (the low-\( c \) treatments) and in the remaining half we set \( c = 10 \) (the high-\( c \) treatments). The experiment follows a 2\( \times \)2 between-subject design resulting in four treatments: low \( c \)/low \( n \), low \( c \)/high \( n \), high \( c \)/low \( n \) and high \( c \)/high \( n \).

A total of 136 subjects participated in the experiment, as summarized in Table 1. Each experimental subject participated in only one session and, hence, one treatment.

Before engaging in the corruption experiment each subject was involved in a task aimed at measuring risk preferences. Following the method first introduced by Holt and Laury (2002), we invited subjects to choose between two lotteries, \( A = (\$1.60, \$2.00; p, 1 - p) \) and \( B = (\$0.10, \$3.85; p, 1 - p) \), with probability \( p \) changing from 0.9 to 0 in decrements of 0.1; therefore, each subject went through a sequence of 10 lottery choices. After all 10 choices were made, one lottery was randomly chosen for payment, although earnings from this task were revealed to subjects only at the very end of the experimental session.

After all subjects completed the risk aversion elicitation task, the corruption experiment began. Subjects engaged in the experiment for 10 rounds, and were informed that one of the 10 rounds would be randomly selected for payment at the end of the session. The earnings from the selected round were then converted from ECU\$s to US\$ at the exchange rate of $1 for 20 ECU. The session concluded with a short questionnaire. Earnings from all parts of the experiment were disclosed only after all subjects finished the questionnaire.

We conducted all experimental sessions at the XS/FS laboratory at Florida State University between February and March 2012. The experiment was programmed in z-Tree (Fischbacher, 2007) and subjects were recruited among FSU students using ORSEE (Greiner, 2004). In order to guarantee anonymity, at the beginning of each session subjects were randomly assigned an identification number, which they kept for the duration of the experiment. At no point did we ask subjects to reveal their names during the experiment, and although actual names were used during the payment process for accounting purposes, we informed the subjects that we would not register their names and, therefore, we would not be able to link them to the choices made.

### Table 1: Summary of experimental sessions and treatments.

<table>
<thead>
<tr>
<th>Treatment</th>
<th>( n )</th>
<th>( c )</th>
<th>sessions</th>
<th>subjects</th>
</tr>
</thead>
<tbody>
<tr>
<td>low ( c )/low ( n )</td>
<td>3</td>
<td>5</td>
<td>4</td>
<td>40</td>
</tr>
<tr>
<td>low ( c )/high ( n )</td>
<td>7</td>
<td>5</td>
<td>2</td>
<td>28</td>
</tr>
<tr>
<td>high ( c )/low ( n )</td>
<td>3</td>
<td>10</td>
<td>4</td>
<td>40</td>
</tr>
<tr>
<td>high ( c )/high ( n )</td>
<td>7</td>
<td>10</td>
<td>2</td>
<td>28</td>
</tr>
</tbody>
</table>
in the experiment. Each session lasted between 60 and 90 minutes, with average earnings of around $21.60 per subject including a $10 show-up fee. Instructions were read aloud, with a printed copy distributed to subjects (see Appendix C).

3.2 Predictions

As briefly discussed in Section 2, when employing a setting where individuals have the possibility to acquire information through searching, the assumption concerning the way individuals search becomes crucial. Starting from Burdett and Judd (1983), nonsequential search models have assumed that individuals first commit to sampling a certain number of sellers (offices in our setting) and then acquire the good (license) from the seller (office) demanding the lowest price (bribe) in the sample. On the other hand, sequential search models (Stahl, 1989) assume that individuals re-evaluate their options after each search and continue searching as long as the cost of an additional search is lower than the expected benefit from such search. While the two models generate the same prediction with respect to the effect of search costs on prices (bribe demands), they lead to different predictions with respect to the effect of the number of sellers/providers on prices (bribe demands).

In Appendix B, we formally show that this is the case by applying the models of Burdett and Judd (1983) and of Stahl (1989) to our corruption setting. We, therefore, hypothesize that

Prediction 1 An increase in \( c \) will lead to an increase in bribes.\(^{16}\)

Prediction 2 An increase in \( n \) will have an ambiguous effect on bribe demands. If citizens search sequentially, an increase in \( n \) should lead to an increase in bribes. If citizens search nonsequentially, an increase in \( n \) should have a negative effect on bribes if \( c \) is low enough, or no effect if \( c \) is high.

The theoretical ambiguity of Prediction 2 makes experimental methods particularly suitable to studying the effect of competition with search costs on corruption. From a practical viewpoint, it may also be of interest to investigate how bribes are affected by a simultaneous increase in \( n \) and decrease in \( c \). Such a combined effect would result, for example, from an increase in the density of public officials in a given area. As seen from the predictions above, the two effects can either work in the same direction, reducing the bribes more than each of the changes in isolation (for nonsequential search), or they can work in opposite directions (for sequential search). This ambiguity will also be addressed empirically in our experiment.

\(^{16}\)A positive monotonic relationship between search costs and equilibrium prices is common for a variety of basic search models employing both sequential and nonsequential search algorithms, e.g., Stahl (1989), Bakos (1997). It is possible, however, for an increase in search costs to lead to lower equilibrium prices in more complex settings, e.g., in the presence of “local searchers” (Chen and Zhang 2009) or advertisement (Cason and Datta 2006, Janssen and Non 2008, Cason and Mago 2010).
4 Results

4.1 Treatment effects

The left panel in Figure 1 shows the average bribe demanded in each round, by treatment. As the figure suggests, higher bribes are demanded when the search cost is high, both for high and low $n$. The effect is especially pronounced in later rounds. As for the impact of the number of offices, it appears that higher $n$ leads to higher bribes when the search cost is low, but there is no effect of $n$ on bribes demanded when the search cost is high. The right panel in Figure 1, showing the average bribe paid by citizens, tells essentially the same story. Histograms displaying the entire distributions of bribes demanded and paid – see Figure 4 in Appendix A – show that the distributions are shifted as search costs increase, and also as $n$ increases from low to high, but only under low $c$.

Table 2 shows the average bribes demanded by public officials, average bribes paid by citizens, the average number of searches per citizen and average citizen’s earnings by treatment. In each case, the averages are shown over the entire sequence of 10 rounds (all $t$) and over the last 5 rounds ($t > 5$), with session-level clustered standard errors for each of the averages in parentheses.

For statistical comparisons between treatments, Table 3 shows the results of linear regressions of bribes demanded by public officials and bribes paid by private citizens on the dummy variables high $c$, high $n$, and their interaction, with errors clustered at the session level and adjusted for the small number of clusters using the bias-reduced linearization (BRL) procedure (Bell and McCaffrey, 2002). Consistent with the visual inspection of Figure 1, the regression results in Table 3 confirm that bribes demanded are higher when $c$ is high under low $n$ for $t > 5$ ($p = 0.031$), and under high $n$ for all $t$ ($p = 0.000$, Wald test) and for $t > 5$ ($p = 0.024$, Wald test). Also, bribes demanded are higher when $n$ is high under low $c$ for $t > 5$ ($p = 0.081$), but
Table 2: Summary statistics by treatment (standard errors in parentheses are clustered by session).

<table>
<thead>
<tr>
<th></th>
<th>Bribe demanded</th>
<th>Bribe paid</th>
<th># of searches</th>
<th>Citizen earnings</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>all t</td>
<td>t &gt; 5</td>
<td>all t</td>
<td>t &gt; 5</td>
</tr>
<tr>
<td>low c/low n</td>
<td>11.13</td>
<td>9.00</td>
<td>7.69</td>
<td>7.06</td>
</tr>
<tr>
<td></td>
<td>(2.45)</td>
<td>(1.43)</td>
<td>(0.55)</td>
<td>(0.37)</td>
</tr>
<tr>
<td>low c/high n</td>
<td>12.42</td>
<td>11.51</td>
<td>9.88</td>
<td>10.16</td>
</tr>
<tr>
<td></td>
<td>(0.25)</td>
<td>(0.11)</td>
<td>(1.04)</td>
<td>(0.50)</td>
</tr>
<tr>
<td>high c/low n</td>
<td>16.35</td>
<td>15.50</td>
<td>13.47</td>
<td>13.67</td>
</tr>
<tr>
<td></td>
<td>(2.02)</td>
<td>(2.63)</td>
<td>(2.54)</td>
<td>(2.93)</td>
</tr>
<tr>
<td>high c/high n</td>
<td>15.92</td>
<td>15.44</td>
<td>14.81</td>
<td>15.07</td>
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<tr>
<td></td>
<td>(0.96)</td>
<td>(1.73)</td>
<td>(1.09)</td>
<td>(1.44)</td>
</tr>
</tbody>
</table>

there is no effect of \( n \) on bribes demanded when \( c \) is high. Similarly, bribes paid are higher when \( c \) is high under both low \( n \) (\( p = 0.027 \) for all \( t \); \( p = 0.026 \) for \( t > 5 \)) and high \( n \) (\( p = 0.001 \) for all \( t \); \( p = 0.001 \) for \( t > 5 \), Wald tests). Finally, bribes paid are higher when \( n \) is high under low \( c \) (\( p = 0.063 \) for all \( t \); \( p = 0.000 \) for \( t > 5 \)), but there is no effect of \( n \) on bribes paid when \( c \) is high. We summarize the main treatment effects as follows.

**Result 1** For both high and low \( n \), higher bribes are demanded and paid when \( c \) is higher.

**Result 2** (a) When \( c \) is low, higher bribes are demanded and paid when \( n \) is higher. (b) When \( c \) is high, there is no difference in bribes demanded and paid between the treatments with high \( n \) and low \( n \).

It may also be of interest to compare bribes demanded and paid between treatments high \( c/low n \) and low \( c/high n \), i.e., to measure the effect of a simultaneous increase in the number of offices and reduction in search costs. Comparing the coefficients on high \( c \) and high \( n \) using Wald test, we obtain \( p = 0.054 \) for the bribes demanded over all \( t \), but there is no statistically significant difference for \( t > 5 \), and no difference in bribes paid for all \( t \) or \( t > 5 \). Thus, interestingly, a reduction in search costs alone leads to a lower level of corruption than a reduction in search costs accompanied by an increase in the number of offices.

Turning to citizens’ searching behavior, Figure 2 (left) shows the average number of searches per citizen in each round, by treatment. Overall, it appears that citizens search relatively little, and there is no obvious ranking of treatments by search intensity. Moreover the number of searches converges to zero for all treatments. Figure 2 (right) shows the histogram of the number of searches per citizen for each treatment. The histogram suggests that citizens search more as the search cost goes down, but the difference between treatments is not statistically significant. The reason is that the search behavior is determined endogenously through the bribes demanded, and those are adjusted by officials across treatments.
### Table 3: OLS regression results for average treatment effects. Session-level BRL-adjusted robust standard errors in parentheses. Significance levels: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.

<table>
<thead>
<tr>
<th></th>
<th>Bribe demanded</th>
<th>Bribe paid</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>all $t$</td>
<td>$t &gt; 5$</td>
</tr>
<tr>
<td>high $c$</td>
<td>5.21</td>
<td>6.50**</td>
</tr>
<tr>
<td></td>
<td>(3.17)</td>
<td>(3.00)</td>
</tr>
<tr>
<td>high $n$</td>
<td>1.29</td>
<td>2.51*</td>
</tr>
<tr>
<td></td>
<td>(2.46)</td>
<td>(1.43)</td>
</tr>
<tr>
<td>high $c$ &amp; high $n$</td>
<td>-1.72</td>
<td>-2.57</td>
</tr>
<tr>
<td></td>
<td>(3.33)</td>
<td>(2.77)</td>
</tr>
<tr>
<td>Constant</td>
<td>11.13***</td>
<td>9.00***</td>
</tr>
<tr>
<td></td>
<td>(2.45)</td>
<td>(1.43)</td>
</tr>
<tr>
<td>Observations</td>
<td>520</td>
<td>260</td>
</tr>
<tr>
<td>Clusters</td>
<td>12</td>
<td>12</td>
</tr>
<tr>
<td>R-squared</td>
<td>0.077</td>
<td>0.196</td>
</tr>
</tbody>
</table>

Figure 2: Average number of searches by citizens in each round, by treatment (left) and number of searches by citizens in all rounds, by treatment (right).
4.2 Individual-level analysis

Table 4 reports the results of dynamic individual-level regressions of bribes demanded by officials and paid by citizens. Specification (1) for bribe demands includes the bribe demanded by the official in the previous round \( (\text{bribe}_{\text{lag}}) \) and the fraction of citizens who obtained the license from the official relative to the number of citizens who visited his office in the previous round \( (\%\text{bought}_{\text{lag}}) \). As seen from the table, bribes are persistent to the extent that the treatment dummies become insignificant. Moreover, bribes are higher the more successful the official is at “selling” his or her service, i.e., the higher the fraction of citizens who agreed to pay the official’s bribe in the previous round. Specification (2) adds gender, whether the official is economics major, and our experimental measure of risk aversion (the number of “safe” choices, option A, in the Holt and Laury (2002) task) to the specification. We find that female officials demand higher bribes.

Specifications (3) and (4) explore the determinants of bribes paid by citizens. Both include the treatment dummies, the bribe paid in the previous round \( (\text{bribepaid}_{\text{lag}}) \) and the number of searches in the current round \( (#\text{searches}) \). Specification (4) adds the same demographic characteristics for the citizens as specification (2) for the officials. We find that there is substantial persistence in the bribes paid, although not to the extent that the treatment dummies are no longer relevant. This can be explained by the fact that citizens do not have that much control, beyond their ability to search, over the bribes they pay. Those bribes are set by the officials and are, therefore, subject to strong treatment effects even when the persistence in bribes paid is accounted for.

As expected, the number of searches has a strong negative effect on the bribes paid by citizens. The estimates in columns (3) and (4) suggest that on average one additional search reduces the bribe paid by about 1 ECU. Given the size of the search costs, searching does not seem to be beneficial. Further analysis, not reported here, shows that each search lowers average citizens’ earnings by about 8 ECU if the search cost is high and by about 4 ECU if the search cost is low. On the other hand, the higher the frequency of searches in a round, the lower the bribes set by officials in the following round and, consequently, the higher the average earnings of citizens in that round. This suggests that searchers are actually providing a public good, i.e., their searching activity reduces their current earnings but increases the earnings of all citizens in the following rounds; citizens who do not search are those who benefit most.\(^{17}\) Finally, note that none of the demographic characteristics for citizens emerge as significant factors. We summarize the results as follows.

Result 3  (a) There is strong persistence in the bribes demanded by officials and paid by citizens. For officials, bribes demanded are higher the more successful the official was in receiving the bribe for his service in the previous round.
(b) Women officials demand higher bribes than men.
(c) Citizens who search more pay relatively lower bribes, yet searching lowers their total earnings.

\(^{17}\) Detailed results are available from the authors upon request.
Table 4: OLS regression results for individual-level decisions on bribes demanded and paid. Session-level BRL-adjusted robust standard errors in parentheses. Significance levels: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$. 
5 Increasing competition in a standard market setting

As discussed in Section 2, the difficulty in conducting empirical investigations of the effect of competition on prices applies to the corruption setting studied in this paper but also more generally to standard market settings with multiple buyers and sellers, where sellers offer an homogeneous product and buyers acquire information about prices through costly search.\textsuperscript{18}

It is, therefore, of interest to test whether our results on the effect of competition in the corruption setting are consistent with those obtained in a standard market setting. As a robustness check, we conducted two additional treatments. In these treatments, we replaced the corruption frame in our experimental instructions with a market frame and test whether and how increasing the number of sellers from 3 to 7 affects sellers’ price setting behavior in the presence of costly search. Given that we identified the most interesting and significant effect of competition on corruption for low search costs, we only conducted the market setting treatments with $c = 5$ and manipulated solely the number of sellers $n$.

In the two additional treatments, $low \ c/low \ n/m$ and $low \ c/high \ n/m$, we employ exactly the same protocols and parameters as in our corruption frame treatments $low \ c/low \ n$ and $low \ c/high \ n$, respectively, except that “Offices” are now called “Stores” and “Public Officials” are now called “Owners of a Store.” We still refer to buyers as “Citizens.” Recall that in the corruption frame officials had to decide whether or not to demand a bribe for the provision of the license on top of an official fee of 20 ECU, with the fee being transferred to the government and hence not cashed by the officials. In the market frame, we give sellers the possibility to set a price mark-up on top of a fixed production cost of 20 ECU that is then subtracted from the price paid by citizens and hence not included in the sellers’ earnings. In this way, we keep monetary incentives identical in the two settings. We conducted two sessions with $n = 7$ (low $c/high \ n/m$ treatment) and four sessions with $n = 3$ (low $c/low \ n/m$ treatment). A total of 68 subjects participated in these treatments.

Figure 3 shows the average price mark-up demanded (left) and paid (right) in each round, by treatment. Table 5 shows the average price mark-ups set by sellers, the average price mark-ups paid by citizens, the average number of searches per citizen and average citizen’s earnings under low and high $n$. In each case, the averages are shown over the entire sequence of 10 rounds (all $t$) and over the last 5 rounds ($t > 5$). The standard errors in parentheses are clustered at the session level. As Figure 3 and Table 5 suggest, there seems to be no effect of $n$ on average prices or search intensity.

To test this formally, we ran linear regressions of price mark-ups set by sellers and price mark-ups paid by citizens on the dummy variable $high \ n$ using data from all 10 rounds and rounds 6-10, similar to the regressions presented in Table 3. The results are presented in Table 6. None of the regressions produces a statistically significant coefficient estimate on $high \ n$.

\textsuperscript{18}An important difference between the two settings, however, is that in the case of corruption sellers, i.e. public officials, cannot advertise their bribes, due to their illegal nature; therefore, acquiring information through office visits is even more crucial than in a standard market setting.
Table 5: Summary statistics for the market frame treatments (standard errors in parentheses are clustered by session).

<table>
<thead>
<tr>
<th></th>
<th>Mark-up demanded</th>
<th>Mark-up paid</th>
<th># of searches</th>
<th>Citizen earnings</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>all t</td>
<td>t &gt; 5</td>
<td>all t</td>
<td>t &gt; 5</td>
</tr>
<tr>
<td>low c/low n/m</td>
<td>10.55</td>
<td>(1.85)</td>
<td>6.90</td>
<td>(1.69)</td>
</tr>
<tr>
<td></td>
<td>9.20</td>
<td>(1.16)</td>
<td>6.58</td>
<td>(1.79)</td>
</tr>
<tr>
<td>low c/high n/m</td>
<td>9.41</td>
<td>(1.16)</td>
<td>7.02</td>
<td>(1.44)</td>
</tr>
<tr>
<td></td>
<td>8.40</td>
<td>(1.37)</td>
<td>7.13</td>
<td>(1.56)</td>
</tr>
</tbody>
</table>

Figure 3: Average price mark-up demanded by sellers (left) and average price mark-up paid by citizens (right) in each round, by treatment.

Table 6: OLS regression results for the effect of high n in the market setting. Session-level BRL-adjusted robust standard errors in parentheses. Significance levels: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.
Table 7: OLS regression results for individual-level decisions on mark-ups demanded and paid. Session-level BRL-adjusted robust standard errors in parentheses. Significance levels: *** - $p < 0.01$, ** - $p < 0.05$, * - $p < 0.1$.

Table 7 shows estimates of the dynamics of price mark-ups set by sellers and paid by citizens, similar to Table 4. When looking at sellers’ price setting behavior we control for the price mark-up set in the previous round ($\text{mark-up\_lag}$) and the fraction of citizens who bought the good from the seller having visited their store ($\%\text{bought\_lag}$). When looking at buyers’ behavior we control for the price paid in the previous round ($\text{mark-up\ paid\_lag}$) and the number of searches conducted in the current round. The regressions also include the same individual controls as in Table 4. The estimates in Table 7 show persistence of both prices set and paid over time, the expected response of sellers to the fraction successful sales, and the effectiveness of searching in reducing the price paid by citizens. Similar to the corruption frame treatments, since on average one additional search reduces the price paid by less than 1 ECU and each search costs 5 ECU, searching is actually not beneficial; it does, however, have an effect of a public good for other citizens. We summarize the results as follows.

**Result 4** In the market setting with low $c$,

(a) There is no difference in prices set and paid between the treatments with high $n$ and low $n$.

(b) There is strong persistence in the prices set by sellers and paid by citizens. Sellers set higher prices the more successful they are selling the good in the previous round.
<table>
<thead>
<tr>
<th></th>
<th>Search</th>
</tr>
</thead>
<tbody>
<tr>
<td>high n</td>
<td>-0.048</td>
</tr>
<tr>
<td></td>
<td>(0.318)</td>
</tr>
<tr>
<td>market</td>
<td>1.17**</td>
</tr>
<tr>
<td></td>
<td>(0.48)</td>
</tr>
<tr>
<td>mark-up or bribe paid _lag</td>
<td>-0.13***</td>
</tr>
<tr>
<td></td>
<td>(0.03)</td>
</tr>
<tr>
<td>mark-up or bribe paid _lag×market</td>
<td>0.031</td>
</tr>
<tr>
<td></td>
<td>(0.032)</td>
</tr>
<tr>
<td># searches</td>
<td>-0.070</td>
</tr>
<tr>
<td></td>
<td>(0.179)</td>
</tr>
<tr>
<td># searches×market</td>
<td>-0.58**</td>
</tr>
<tr>
<td></td>
<td>(0.28)</td>
</tr>
<tr>
<td>lowest mark-up or bribe</td>
<td>0.11***</td>
</tr>
<tr>
<td></td>
<td>(0.03)</td>
</tr>
<tr>
<td>lowest mark-up or bribe×market</td>
<td>-0.084***</td>
</tr>
<tr>
<td></td>
<td>(0.030)</td>
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<tr>
<td>female</td>
<td>0.22</td>
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<tr>
<td></td>
<td>(0.17)</td>
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<tr>
<td>econ major</td>
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<tr>
<td></td>
<td>(0.37)</td>
</tr>
<tr>
<td>risk aversion</td>
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<td></td>
<td>(0.0540)</td>
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<td>Constant</td>
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<tr>
<td></td>
<td>(0.27)</td>
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<td>Observations</td>
<td>1,052</td>
</tr>
<tr>
<td>Clusters</td>
<td>12</td>
</tr>
</tbody>
</table>

Table 8: Logit regression results for individual-level decision on search. Session-level BRL-adjusted robust standard errors in parentheses. Significance levels: *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$. 
Comparing the results obtained in the market setting with those in the corruption setting (cf. Tables 2 and 5), we observe that there are no significant differences in averages between the two settings when \( n \) is low. However, when \( n \) is high (and \( c \) is low) bribes are higher than price mark-ups; the latter stay at the same level as under low \( n \). One important conclusion we can draw from these comparisons is that the finding that an increase in the number of offices does not lead to a reduction in bribes is robust to framing. On the other hand, the result that an increase in \( n \) leads to higher prices only applies to the corruption setting. In the remainder of this section, we propose an explanation for the differential effect of \( n \) on bribes versus mark-ups.

Recall that an increase in prices with an increase in \( n \) is predicted by theory if buyers search sequentially, while there may be no effect, or a negative effect, of \( n \) on prices if search is nonsequential. Thus, one possibility is that individuals use different search algorithms in different settings, i.e., sequential in the corruption setting and nonsequential in the market setting. There is almost no empirical evidence of how individuals search. One notable exception is the recent study by De Los Santos et al. (2012). Using data on web browsing and purchasing of books online, De Los Santos et al. (2012) find that individuals’ decision to search does not depend on the outcomes of previous searches, which provides evidence of nonsequential rather than sequential search.\(^{19}\)

In order to test for possible differences in citizens’ search behavior between the two settings, we present in Table 8 the results of a logistic regression for the citizens’ decision to search combining data from the corruption frame and market frame treatments with low search costs. In addition to the treatment dummies high \( n \) and market (=1 in the market frame, 0 in the corruption frame), we control for mark-up or bribe paid by the citizen in the previous round, the number of searches the citizen undertook so far, the lowest mark-up or bribe the citizen encountered so far, and their interactions with the market dummy. The regression also includes individual citizens’ characteristics. As seen from Table 8, the price (mark-up or bribe) paid in the previous round affects the probability to search negatively, both under the corruption frame \((p = 0.000)\) and the market frame \((p = 0.000, \text{ Wald test})\). There are, however, significant differences in the effects of the number of prior searches and the lowest price encountered between the two settings. Specifically, the number of prior searches has no effect on the probability of additional search under the corruption frame \((p = 0.696)\), but it has a negative effect under the market frame \((p = 0.0027, \text{ Wald test})\). In contrast, the lowest price encountered has a significant positive effect on the probability of additional search under the corruption frame \((p = 0.000)\), but there is no effect of this variable under the market frame \((p = 0.132, \text{ Wald test})\). Similar to De los Santos et al. (2012), we can interpret the presence of a reaction to the lowest price found from previous searches, and no duration effect, in the corruption setting as evidence of sequential search, while failure to react to such lowest price, and a negative duration effect, in

\(^{19}\)In a specially designed experiment, Harrison and Morgan (1990) found evidence that individuals use a mix of sequential and nonsequential search strategies, referred to as variable-sample-size strategies (Morgan and Manning, 1985). Hong and Shum (2006) and Chen et al. (2007) use data on textbook prices to structurally estimate the distribution of consumer search costs using both the fixed sample size and sequential search models but do not conclude definitively in favor of one of the two models.
the market setting as evidence of nonsequential search. Therefore, the positive effect of \( n \) on bribes obtained in the corruption setting is in line with the predictions of a sequential search model, and the null effect of \( n \) on prices in the market setting is in line with the predictions of a nonsequential search model.

**Result 5** Citizens’ search behavior in the corruption setting is consistent with sequential search, while in the market setting it is consistent with nonsequential search.

While we did not hypothesize the observed differences in search behavior in the two settings, we can advance some speculative explanations of such differences. Since all subjects have had hands-on experience with markets outside the lab, the search patterns in our market setting are more likely to be consistent with those observed in other studies of search behavior using field data, which point in the direction of nonsequential search (De los Santos et al. 2012). The corruption setting, on the other hand, is likely to be less familiar to our subjects. Moreover, despite the structural equivalence of the two settings, individuals might simply not perceive the (possibly corrupt) service delivery environment as a market. Therefore, search patterns in this setting are likely to be more cautious and generally consistent with directional reinforcement learning, thus leading to behavior that looks more like sequential search.

6 Conclusions

Identifying successful anti-corruption policies is challenging. The most common approach is deterrence-based, i.e. it relies on policies aimed at increasing the expected monetary costs of corruption through higher threat of punishment and/or severe sanctions. However, since effective deterrence is dependent upon top-down monitoring and enforcement mechanisms, policies aimed at increasing the probability and/or severity of punishment often prove ineffective, especially in countries characterized by systemic corruption. An alternative approach would be to identify institutional changes that reduce corruption without relying on increased top-down monitoring and enforcement. In this paper, we investigated the effectiveness of one of such possible changes, which concerns the structure and organization of the bureaucracy in charge of providing a given good or service to citizens. In particular, we designed and conducted a laboratory experiment to test whether increasing the number of offices providing the same service and/or reducing the cost that citizens have to sustain to visit a new office – i.e., increasing competition among offices – would reduce the demand of extortionary bribes, i.e. bribes for the provision of goods that clients are entitled to, as first suggested by Rose-Ackerman (1978, 1999) and Shleifer and Vishny (1993).

Addressing our research question in the field is problematic due to identification and measurement problems, and the obvious difficulty to find a cooperating government willing to experiment with alternative ways to provide goods and services to citizens. We were able to overcome these challenges by conducting a specially designed laboratory experiment where, contrary to
all previous corruption experiments, we allowed for, and manipulated the extent of, competition
among public officials for the provision of the same government service in a controlled setting.

We found that increasing competition among offices may reduce bribe demands only if it
comes with a reduction in search costs, and it is the reduction in search costs that is the driver of
the reduction in bribes. Moreover, the \textit{ceteris paribus} effect of an increase in the number of offices
may actually go in the opposite direction, i.e., it can lead to an increase in bribes demanded.
Specifically, we find that if search costs stay unchanged, increasing the number of offices leads
to either no change in corruption (if search costs are high) or an increase in corruption (if search
costs are low). On the other hand, reducing search costs alone always results in lower level of
extortionary corruption.

Finally, given the possible applications of our results to general market environments, we
tested the robustness of our findings by replicating the study employing a standard market
setting, while keeping protocol and payoffs identical to the corruption setting. We found that
increasing the number of sellers in a standard market setting while keeping search costs low,
has no impact on pricing behavior. Our data provide suggestive evidence that the differential
effects of $n$ on prices in the two settings might be due to different search strategies employed by
buyers.

While the finding that increasing competition among providers may not lead to the desired
anti-corruption outcomes is certainly disappointing, it is important to recognize some specific
features of the environment we simulated in our experiment. First, we focused on corrupt
services that require one-shot interactions between citizens and officials - think, for instance,
of the provision of a passport or a drivers’ license, which remain valid for a large number of
years. A direct consequence of our design is that we did not allow for the formation of long-term
relationships between citizens and officials or for reputation building among officials. Whether
our results extend to the provision of goods or services that require frequent interactions between
the same citizens and officials – think of food handlers’ licenses or regular payments of customs
taxes – is an open question which we plan to address in future research. Another important
feature of our study is that we focused on policies aimed at increasing competition among
officials. In other words, we compared a setting characterized by a low number of offices with
one characterized by a large number of offices. We did not, however, test the effectiveness
of \textit{introducing} competition among officials where there is none. In future research, we will
investigate the extent to which bribe demands are different in a (low or high) competition setting
as compared to a monopoly setting. A final issue that is worthy of investigation is the possibility
that competition among officials providing services that require either one-shot or repeated
interactions with citizens may be compromised by collusion. This is an interesting question
given that the secrecy of corrupt transactions makes it impossible for an official to monitor
the bribe-demands of fellow officials. The study of collusion among officials in competitive
environments is part of our ongoing research agenda.
References


A Additional graphs

Figure 4: Bribes demanded by public officials in rounds 6-10, by treatment (left) and bribes paid by private citizens in rounds 6-10, by treatment (right).
B Theoretical Framework

In our corruption experiment, we use the following simple framework. There are $m$ citizens indexed by $i = 1, \ldots, m$ and $n$ offices indexed by $j = 1, \ldots, n$. The offices provide a license that has a net value of $V$ to citizens. Each office $j$ is managed by a public official who decides on the amount of the bribe, $b_j \in [0, B]$, to demand for the provision of the license. Initially, each citizen is randomly matched to an office and learns about the bribe demanded by the official in that office. The citizen can either acquire the license by paying the bribe or search, i.e., incur a search cost and visit a different office. All citizens have the same monetary cost of search $c > 0$.

Search is with recall, i.e., a citizen can always acquire the license from any previously visited office at no additional cost. The game ends when all citizens acquire the license. If a citizen searches through all available offices, she has to obtain the license from one of them. Citizen $i$’s monetary payoff is $V - b_{\bar{j}(i)} - l_i c$, where $\bar{j}(i)$ is the office where citizen $i$ eventually obtained the license, and $l_i$ is the number of searches she undertook. Public official $j$’s payoff is $k_j b_j$, where $b_j$ is the bribe she demands, and $k_j$ is the number of citizens who acquired the license from office $j$.

In addition to the common monetary search cost $c$, citizens have heterogeneous nonmonetary cost parameters $\alpha_i$ so that citizen $i$’s total search cost is $c_i = \max\{0, c + \alpha_i\}$. Parameters $\alpha_i$ can be positive or negative and represent, in a reduced form, a combination of unobserved individual-specific factors affecting search behavior, such as general propensity to search, costs of engaging in corruption, costs of time or cognitive costs. We assume parameters $\alpha_i$ are drawn independently from a commonly known distribution, resulting in a distribution $G(\cdot)$ of total search costs $c_i$. Distribution $G(\cdot)$ will have a mass at zero if there are citizens with $\alpha_i \leq -c$. This corresponds, in the language of consumer price search models, to the presence of “shoppers,” i.e., citizens who will search until they find an office that does not demand a bribe, or exhaust all available offices.

In this paper we are interested in the effect of the number of offices, $n$, on the level of bribes. We also explore the effect of exogenous variation in search costs which we manipulate by changing the monetary component of search costs, $c$. The reason is that in the field an increase in the number of available offices may or may not be accompanied by a reduction in search costs, and vice versa, and it is of interest to explore the effects of an increase in $n$ and a reduction in $c$ on corruption in isolation as well as jointly.

The characterization of equilibrium in a market with heterogeneous search costs is a complex problem. First, the results depend crucially on the search algorithm adopted by citizens. Second, even for a fixed search algorithm, the equilibrium distribution of bribes can vary depending on the distribution of total search costs $G(\cdot)$.

In what follows, we briefly present the equilibrium characterization of two models corre-
sponding to the two prominent search paradigms – nonsequential and sequential search – and summarize their comparative statics predictions related to \( n \) and \( c \).

**B.1 Nonsequential search**

When citizens search nonsequentially, they first commit to sampling a certain number of offices and then acquire the license at the office demanding the lowest bribe in the sample. We adopt the approach of Burdett and Judd (1983). Let \( F(b) \) denote the resulting equilibrium distribution of bribes. For a risk-neutral citizen with search cost \( c_i \), the optimal number of offices to visit, \( l^*(c_i) \), is given by the following cost minimization problem:

\[
\min_{l \geq 1} c_i (l - 1) + \int bl[1 - F(b)]^{l-1}dF(b).
\]

The first term represents the cost of visiting \( l \) offices (including the costless visit to the office with which the citizen is initially matched); the second term is the expected lowest bribe from a random sample of \( l \) offices.

Let \( b_{\min}^l \) denote the expected minimal bribe in a sample of \( l \) offices. Then the citizen’s expected gain from visiting one more office after having visited \( l \) offices is \( D_l = b_{\min}^l - b_{\min}^{l+1} \).

It is easy to see that \( D_l \) is decreasing in \( l \); therefore, citizen \( i \) will be searching as long as \( D_l \) exceeds \( c_i \) and will search through all available offices if \( D_{n-1} > c_i \). Given \( F \), parameters \( D_l \) determine the distribution of citizens by the number of searches. Specifically, the proportion \( q_1 = 1 - G(D_1) \) of citizens will acquire the license immediately; proportion \( q_2 = G(D_1) - G(D_2) \) will sample two offices, and so on, with the proportion \( q_n = G(D_{n-1}) \) of citizens visiting all \( n \) offices.

Assuming that there are citizens who do not search, the equilibrium distribution of bribes will satisfy the following indifference condition for all \( b \) in the support of \( F \):

\[
Bq_1 = b \sum_{l=1}^{n} q_l l[1 - F(b)]^{l-1}.
\]

The left-hand side represents an official’s expected payoff from the citizens who do not search and pay the highest bribe \( B \), while the right-hand side is the official’s expected payoff from choosing a bribe using a mixed strategy \( F(b) \). Equation (1) is an implicit equation for the equilibrium distribution of bribes \( F \).

An increase in the monetary search cost \( c \) will lead to an upward probabilistic shift of the distribution \( G \), which, in turn, will lead to an increase in \( q_1 \) and a downward probabilistic shift in the distribution of the number of searches \( q_l \). Thus, the left-hand side of Eq. (1) will increase and, to match the increase, \( F(b) \) will have to go down. The prediction, therefore, is an upward probabilistic shift of the distribution of bribes.

Consider now an increase in the number of offices, \( n \). Suppose, first, that search costs are

\[21\] Here and below, integration is over the support of \( F \) unless specified otherwise.
low enough so there is a mass of citizens who search through all available offices, i.e., \( q_n > 0 \).

An increase in \( n \) will allow those citizens to search more, which implies an upward shift in the distribution of the number of searches and, as a result, a downward shift in the distribution of bribes. If, however, search costs are so high that \( q_n = 0 \), an increase in \( n \) will have no effect.

To summarize, the nonsequential search model predicts that an increase in \( n \) will lead to more searches and a reduction of bribes if search costs are low enough, and to no change in searches and bribes otherwise, while an increase in \( c \) will lead to fewer searches and an increase in bribes.

B.2 Sequential search

Citizens searching sequentially re-evaluate their options after each office visit. Having visited an office, they can acquire the license by paying the lowest bribe encountered so far or undertake an additional search. In this section, we adopt the approach of Stahl (1989). Given a distribution of bribes \( F(b) \), the optimal sequential search algorithm for citizen \( i \) is to search until a reservation bribe \( b_r(c_i) \) is reached, which is defined as \( b_r(c_i) = \min\{z(c_i), B\} \), where \( z(c_i) \) is the solution of the equation

\[
c_i = \int_{b \leq z} (z-b) dF(b).
\]

(2)

Here, the right-hand side represents the marginal gain from one additional search given that the lowest bribe encountered so far is \( z \). We will use \( F_r \) to denote the distribution of reservation bribes in the population of citizens. The proportion of citizens for whom the reservation bribe is \( B \) is \( \alpha = 1 - F_r(B) \), and \( F_r = 0 \) at the lower bound of the support of distribution \( F \). An official demanding bribe \( b \) will only attract citizens with reservation bribes \( b > b_r \). Thus, the proportion of citizens getting the license from an office demanding a bribe \( b \) is \( \int_{b}^{B} [1 - (1 - F(b_r))^n] dF_r(b_r) \). Here, \( (1 - F(b_r))^n \) is the probability that all offices demand a bribe above \( b_r \), and the integral gives the probability that there is at least one office with bribe less than \( b_r \) averaged over the distribution of reservation bribes with \( b < b_r \) (see Hong and Shum, 2006).

Similar to the previous section, a symmetric mixed strategy equilibrium distribution of bribes \( F \) must satisfy the indifference condition for all \( b \) in the support of \( F \):

\[
B \alpha = b \int_{b}^{B} [1 - (1 - F(b_r))^n] dF_r(b_r).
\]

(3)

The left-hand side of (3) is the expected payoff of an official demanding the highest bribe \( B \), while the right-hand side gives the payoff at an arbitrary bribe \( b \). This equation implicitly determines the equilibrium distribution of bribes.

Consider an increase in the monetary search cost \( c \) leading to an upward shift of the distribution \( G \). As seen from Eq. (2), \( z(c_i) \) is an increasing function of \( c_i \); therefore, the distribution of reservation bribes \( F_r \) will also shift upward, leading to an upward shift in the equilibrium distribution of bribes.
If the number of offices \( n \) increases, the right-hand side of Eq. (3) will also increase, for a given \( F \). To compensate that increase, \( F \) should decrease, i.e., there will be an *upward* shift of the distribution of bribes (for a detailed discussion, see, e.g., Stahl 1989).

To summarize, the sequential search model predicts that an increase in \( n \) and an increase in \( c \) will both lead to fewer searches and an increase in bribes.
C Experimental Instructions (treatment low $c$/high $n$)

General Instructions

Thank you all for coming today. You are here to participate in an experiment. After playing the game you will be asked to complete a brief questionnaire. In addition to a $10 participation fee, you will be paid any money you accumulate from the experiment. You will be paid privately, by check, at the conclusion of the experiment. This study has been reviewed and approved by the FSU Human Subjects Committee. If you have any questions during the experiment, please raise your hand and wait for an experimenter to come to you. Please do not talk, exclaim, or try to communicate with other participants during the experiment. Participants intentionally violating these rules may be asked to leave the experiment and may not be paid.

Please read and sign the Consent form that you found on your desk. Please raise your hand if you have any question about any of the information on the Consent form. We will proceed with the experiment once we have collected all signed consent forms.

The number that you have found on your desk is your identification number in the experiment. We won’t ask you to write down your name at any time during this experimental session. No one, including the experimenter, will have a way to link your name to the decisions you made in the experiment. At the end of the session, you will need to show your number to the experimenter in order to receive the money that you collected in the experiment.

Earnings during the experiment will be denominated in Experimental Currency Units, or ECU. At the end of the experiment your earnings will be converted to dollars at the exchange rate of $1 for 20 ECU.

The experiment will consist of several parts and the instructions will be provided separately at the beginning of each part.

Instructions for Part 1

In each round of this series of decisions you will be asked to make a choice between two lotteries that will be labeled A and B. There will be a total of 10 rounds and after you have made your choice for all 10 rounds, one of those rounds will be randomly chosen to be played. Lottery A will always give you the chance of winning a prize of $2.00 or $1.60, while lottery B will give you the chance of winning $3.85 or $0.10. Each decision round will involve changing the probabilities of your winning the prizes. For example in round 1, your decision will be represented on the screen in front of you:

Your decision is between these two lotteries:

Lottery A: A random number will be drawn between 1 and 100. You will win

$1.60 if the number is between 1-90 (90 % chance)
$2.00 if the number is between 91 and 100 (10 % chance)

Lottery B: A random number will be drawn between 1 and 100. You will win

$0.10 if the number is between 1 and 90 (90% chance)
$3.85 if the number is between 91 and 100 (10% chance)

If you were to choose lottery B and this turns out to be the round actually played, then the computer
will generate a random integer between 1 and 100 with all numbers being equally likely. If the number
drawn is between 1 and 90, then you would win $0.10 while if the number is between 91 and 100, then
you would win $3.85. Had you chosen lottery A, then if the number drawn were between 1 and 90 you
would win $1.60 while a number between 91 and 100 would earn you $2.00.

All of the other 9 choices will be represented in a similar manner. Each will give you the probability
of winning each prize as well as translate that probability into the numerical range the random number
has to be in for you to win that prize.

At the end of the 10 choice rounds, the computer will randomly pick one of the 10 rounds to base
your payment on, and draw the random number between 1 and 100 to determine your earnings. You will
be informed about your earnings from this part of the experiment at the very end after you complete all
parts.

Are there any questions before you begin making your decisions?

You will now start the sequence of 10 choices. You will be able to go through the choices at your
own pace, but we will not be able to continue the experiment until everyone has completed this series.

**Instructions for Part 2**

This part of the experiment will consist of several decision sequences. The instructions will be given
separately at the beginning of each sequence. At the end of the experiment one the sequences will be
randomly chosen to base your actual earnings on.

**SEQUENCE 1**

You are going to participate in this experimental task in one of two possible roles. You will be
randomly assigned either the role of Public Official or the role of Private Citizen. A total of 7 Public
Officials and 7 Private Citizens will participate in the task.

Each Public Official will be in charge of an Office that provides licenses to Private Citizens, and will
receive a lump-sum wage of 130 ECU.

Each Private Citizen will start with a monetary endowment of 80 ECU and will have to get a license
from one of the 7 Offices. The license will generate a monetary benefit of 70 ECU to the Citizen. The
Private Citizen will have to pay a fee in order to get the license. The official license fee is 20 ECU.
However, Public Official can refuse to provide the license unless a bribe is paid on top of the official fee.
The bribe demanded by a Public Official can be any integer amount between 1 and 50 ECU.

At the beginning, each Public Official will decide whether or not to demand a bribe from the Private
Citizens who may visit his or her Office, and the specific amount of the bribe, in the range between 1
and 50 ECU. The decision to demand a bribe and the size of the bribe cannot be changed during the
sequence.

Each Public Official will not know if the other Public Officials chose to demand a bribe or the size of
their bribes, if any. Private Citizens will also be initially unaware of the bribes demanded by each Public
Official, if any, but they will be able to acquire such information by visiting the corresponding Office, at
the cost of 5 ECU for every new visit.

The sequence proceeds as follows:
- At the beginning, each Public Official has to decide whether he or she would like to request a bribe, between 1 and 50 ECU, for the provision of the license, on top of the official fee of 20 ECU.

- Each Private Citizen is initially randomly assigned to visit an Office and finds out if a bribe is requested by the Public Official in that Office, and if so, the size of the bribe.

- Then, the Private Citizen has to decide whether to pay the total amount requested by the visited Office, and receive the license there, or leave that Office and choose to visit any of the other 6 available Offices. Every visit to a new Office costs 5 ECU to the Private Citizen.

- The Citizen can visit as many Offices as he or she wishes, at the cost of 5 ECU for any new visit, and can acquire the license from any of the Offices previously visited by paying the amount requested by the Official in that Office.

- The Private Citizen has to get the license eventually.

The payoffs from the sequence are determined as follows:

- Each Public Official earns a lump-sum wage of 130 ECU. On top of the wage, if the Public Official decides to demand a bribe for his or her services, he or she can get additional earnings from the bribes paid by the Private Citizens who visited the Office and decided to obtain the license there, if any.

- Each Private Citizen starts with an endowment of 80 ECU. When the Private Citizen gets the license, he or she additionally receives 70 ECU, but will have to pay the total amount requested by the Public Official (that may or may not include a bribe) and the accumulated cost of office visits, which is equal to 5 ECU x (number of visited offices).

Private Citizens will see the map below, showing the available 7 Offices that they can visit to get the license. By clicking on an Office, Private Citizens will be able to visit that Office and get information about whether a bribe is requested by the corresponding Public Official, and the size of the bribe, if any.

After being initially matched with one Office, each Citizen will be able to visit as many Offices as he or she wishes, at the cost of 5 ECU per new visit. Once an Office has been visited, Citizens will be able to see the requested amount on the map, in the corresponding box. Citizens could decide to get the license from any of the Offices previously visited, or visit a new Office.
After being initially matched with one Office, each Citizen will be able to visit as many Offices as he or she wishes, at the cost of 5 ECU per new visit. Once an Office has been visited, Citizens will be able to see the requested amount on the map, in the corresponding box. Citizens could decide to get the license from any of the Offices previously visited, or visit a new Office.

Are there any questions? This part of the experiment is about to begin. We ask again that you not look at the screens of those around you or attempt to talk with other participants at any time during the session. You will be able to read through the instructions and click through the screens at your own pace. Each section of the experiment will begin after all participants have finished reading the instructions for that section and have clicked Continue. If you have any question about the instructions that you will receive on your screen, please feel free to raise your hand at any time during the session, and the experimenter will come to answer your questions in private.
Screen 1: Citizen visits the first Office

You are the Private Citizen Q

Initial Endowment: 80.00
Visit Cost: 0.00
Balance: 80.00

Revenue from License: 70.00
Obtained License: No

You have been randomly assigned to visit Office 7.

The Public Official in this Office is not willing to provide you with a license for the official fee of 20 ECU.

On top of the official fee, in order to provide the license the Public Official in this Office requests a bribe of 15 ECU.

You will now get back to the map of Offices, where you will be able to see the bribe demanded by this Office, if any. You will have the choice to either get the license by paying the amount requested by this Office or visit a new Office of your choice by paying a visit cost of 5 ECU.

Please click continue to go back to the map.
Screen 2: Citizen sees the map of Offices

<table>
<thead>
<tr>
<th>Office</th>
<th>Official Fee</th>
<th>Bribe</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Office 1</td>
<td>20</td>
<td>?</td>
<td>?</td>
</tr>
<tr>
<td>Office 2</td>
<td>20</td>
<td>?</td>
<td>?</td>
</tr>
<tr>
<td>Office 3</td>
<td>20</td>
<td>?</td>
<td>?</td>
</tr>
<tr>
<td>Office 4</td>
<td>20</td>
<td>?</td>
<td>?</td>
</tr>
<tr>
<td>Office 5</td>
<td>20</td>
<td>?</td>
<td>?</td>
</tr>
<tr>
<td>Office 6</td>
<td>20</td>
<td>?</td>
<td>?</td>
</tr>
<tr>
<td>Office 7</td>
<td>15</td>
<td>36</td>
<td>?</td>
</tr>
</tbody>
</table>

You are the Private Citizen Q
Initial Endowment: 20 ECU
Visits Cost: 5 ECU
Balance: 0 ECU
Revenue from License: 70 ECU
Obtained License: No

Waiting Screen

You must get the license from one of the 7 Offices. The license will generate 70 ECU to you. You have just visited Office 7. On the map, you can see whether the Public Official in this Office requests a bribe, and the total amount you would have to pay to get the license from this Office. You can use your Balance, at the top right corner, to either pay the requested amount or choose to visit a different Office, at the cost of 5 ECU. After you visit a new Office, you will come back to this map and will be able to get the license from any of the previously visited Offices, or visit a new Office at the cost of 5 ECU per new visit.

Please be patient as other participants make decisions.
Screen 3: Official sees who visits the Office and who buys the license

<table>
<thead>
<tr>
<th>Visited Your Office</th>
<th>Received License from You</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citizen P</td>
<td></td>
</tr>
<tr>
<td>Citizen Q</td>
<td></td>
</tr>
<tr>
<td>Citizen R</td>
<td></td>
</tr>
<tr>
<td>Citizen S</td>
<td>X</td>
</tr>
<tr>
<td>Citizen T</td>
<td></td>
</tr>
<tr>
<td>Citizen U</td>
<td></td>
</tr>
<tr>
<td>Citizen V</td>
<td></td>
</tr>
</tbody>
</table>

You have decided not to demand a bribe for the provision of the license. Below you will see when a Private Citizen visits your Office and whether or not she decides to get the license from you. Visits and license acquisitions will be marked with an X for the corresponding Citizen.

Citizen S was randomly assigned to visit your Office at the beginning of this sequence.

This sequence will end when all Private Citizens get the license.