

# **Corruption and Business in Lithuania from Small and Medium Enterprises Perspective**

Dr. Aleksandras Dobryninas  
Dr. Laima Zilinskiene  
*Transparency International Lithuanian Chapter*

During last ten years, the role of private sector in Lithuanian economy increased significantly. According to the Department of Statistics of the Government of Republic of Lithuania, in 2000 the private sector produced 72% of the GDP (in 1991 – only 16%) and the share of employed in private sector was 69% (in 1991 accordingly – 30 %). However, despite of these positive indicators of the general development of private sector in Lithuania, the situation with the small and medium-sized enterprises (SMEs)<sup>1</sup> is far away from being optimistic. According to the Department of Statistics, during the 1999-2000, the number of operating SMEs decreased from 80689 until 52109, and according to the Lithuanian Free Market Institute the profitability of Lithuanian enterprises decreased from 12% in 1997 to 5% in the first half of 2000. Research data of the Public institution “Statistikos tyrimai” show that in 2000 only in two of ten Lithuanian counties – Vilnius and Kaunas - the number of established SMEs was higher than number of liquidated ones.

The major obstacle for the development of private sector in Lithuania, including SMEs, is complex and unstable business environment. According to the data of the research that has been carried by Lithuanian Development Agency for Small and Medium Sized Enterprises (SMEDA) and Private Company “Naujosios marketingo sistemas” (NMS) in 2001, the biggest business constraints for SMEs managers were weak purchasing power of consumers, high taxes, lack of working capital,

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<sup>1</sup> The definition of SMEs in Lithuania differs from EC definition. For example, by Lithuanian standards firms with number of employees below 100 are regarded as SME..

complicated borrowing conditions, etc. Among ten the most significant obstacles for business in Lithuania, respondents also mentioned corruption.<sup>2</sup>

The cost of corruption for national economies is an issue, intensively discussed among politicians, businesspeople, academicians, and public at large. Recent World Bank research on corruption in Central and Eastern European countries “Anticorruption in Transition: A Contribution to the Policy Debate” (2000) identifies Lithuania as a country with medium state capture and high administrative corruption index. Corruption in such countries has the negative impact on sales and investment growth, and is strongly related to the level of poverty. In such circumstances, as World Bank research shows, SMEs “are particularly hard hit by administrative corruption”, and “across the region pay, on average, more than twice as much of their annual revenue in bribes as do large firms”.<sup>3</sup>

It becomes obvious that the reduction of the level of administrative corruption and especially its main form – bribes - could be one of the most important factors for the improvement of the situation in SMEs’ sector in Lithuania. However, before proclaiming the attack upon SMEs’ treacherous enemy – bribes, it is worthwhile to evaluate the field of the battle, or in other terms – the institutional and geographical landscape of the corruption in Lithuania.

In order to achieve this goal, the analysis of business leader’s attitudes towards corruption, and their victimization by bribes was included in the Transparency International Lithuanian Chapter project “Map of Corruption in Lithuania: 2001”. The project was financially supported by the Lithuanian Office of The World Bank, British and Finish Embassies in Lithuania. Some methodological details of the project have been discussed with Joel Hellman (The World Bank, USA), Kauko Aromaa (HEUNI, Finland) and Rasa Alisauskiene (Baltic Surveys, Lithuania). The survey has been conducted by Lithuanian-British Market and Public Opinion Research Company

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<sup>2</sup> More detailed information about the situation with SMEs in Lithuania readers can find by visiting SMEDA’s web page: <http://www.smeda.lt> (accessed 16.09.2001)

<sup>3</sup> *Anticorruption in Transition: A Contribution to the Policy Debate*. Washington: The World Bank. 2000, p. 20.

“Baltic Surveys” (The Gallup Organization Lithuanian representative) in July-August 2001.

1005 leading representatives of SMEs<sup>4</sup> in Lithuania participated in the survey. The survey’s sample was based on multi-stage quota. The enterprises were been selected according to the firms’ register and catalogs, which provided basic information about business area, headquarters location, and number of employees. Respondents were interviewed about the conditions for doing business in Lithuania, their attitude towards corruption, the experiences of the cases of bribery in different institutions and geographical areas, and their vision of possible anticorruption remedies.

**Business environment in Lithuania.** Business leaders of SMEs stressed the following obstacles harming business management and business development:

<b>Obstacles</b>	<b>%</b>
1. Taxes	33
2. Bureaucracy and corruption	31
3. Laws	22
4. Weak demand	14
5. Lack of current assets	12
6. Unfair competition	11
7. Economic instability	11
8. Payment lag	6
9. Lack of qualified labor force	6

**Table 1. Main obstacles for business in Lithuania**

The taxation policy becomes the major obstacle first of all to the firms with less than 50 employees. . Taxes as the main obstacle for business was pointed out by the business leaders from the second largest Lithuanian city Kaunas.. Business leaders from the third largest Lithuanian city Klaipeda regarded the bureaucracy and corruption to be their main obstacle.

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<sup>4</sup> According to the EC definition.

Business leaders of SMEs were asked which institutions create most troubles for the business development. Their evaluations are presented in the following table:

<b>Institutions</b>	<b>%</b>
Tax Inspectorate	43
Municipalities	19
Social Insurance Fund	16
Customs Office	15
The Cabinet	14
The Parliament	13

**Table 2. Lithuanian institutions that create obstacles for business development**

The Tax inspectorate as the biggest obstacle was named first of all by the representatives of small firms with number of employees between 1 and 9, Klaipeda's, small and medium Lithuanian cities' business leaders.

**Attitudes towards corruption.** 71% of business leaders state that the corruption is serious obstacle or some obstacle for the business, 17% - that corruption neither prevents, nor supports business activity, and only 3% of respondents suppose that corruption can sustain business.

60% of the respondents think that the level of corruption in Lithuania is higher than in the Western countries, but the same as in Eastern and Central European countries. At the same time, 46% of businesspeople believe that the level of corruption in Lithuania is lower than in the countries of former Soviet Union, and only 38% of respondents expect the same level.

33% of SMEs' leaders insisted that during the last five years the level of corruption has not increased, while 52% of them expressed the opposite opinion. The first attitude is more popular among the representatives of manufacturing companies, while the second one – among representatives of service and retail business.

According to the respondents, the most corrupted areas in Lithuania are the following:

<b>Areas</b>	<b>%</b>
Law Enforcement	33
Governance	21
Customs	18
Health Protection	13
Privatization	10
Oil Industry	9
Energy Sector	7
Retail	6
Politics	6

**Table 3. Most corrupted areas in Lithuania, according to the SMEs leaders' opinion**

The law enforcement as the most corrupt area was mentioned first of all by the representatives of Vilnius, fourth largest city – Siauliai, medium and small Lithuanian cities. Representatives of firms with less than 50 employees regard the governance to be most corrupt area..

When asked about most corrupt institutions, SMEs leaders point on the following organizations:

<b>Institutions</b>	<b>%</b>
Customs Office	24
Courts of Justice	19
Police	10
The Parliament	10
The Cabinet	9
Tax Inspectorate	9
Municipalities	7
Healthcare	5
Privatization Office	5

**Table 4. Most corrupt institutions in Lithuania, according to the SMEs leaders' opinion**

Customs Office was mentioned as most corrupt institution by the representatives of SMEs from Kaunas and Siauliai; business leaders from Klaipeda regard Courts of Justice to be the most corrupt institutions.

**Victimization by bribes.** Leading representatives of Lithuanian SMEs were asked about bribery cases in which their own firms were involved. 57% of interviewed business leaders said that during the last five years, they have been asked to pay the bribe, and 37% said - that they have done this. For the last year, these figures were accordingly 37% and 26%. It is interesting to note, that during the last year the highest level of the requests for the paying bribe as well as the level of actual paying of bribes was for firms located in Vilnius, wit less than 10 employees, and without foreign capital.

The majority of all reported bribes – 64% - have been paid for representatives of local institutions, 50% - for regional institutions, and 25% – for the central institutions.

According to the answers of business leaders, the ten-top of “bribery-hot” institutions looks as follows:

<b>Institutions</b>	<b>Share of firms who have paid bribe for particular institution during last five years (%)</b>
1. Traffic police	13
2. Custom office	10
3. Tax inspectorate	10
4. Social security fund	5
5. Fire department	4
6. Labor inspection	4
7. Center for public health	4
8. Tax police	4
9. Municipalities	3
10. Estate cadastre	3

**Table 5. Ten “Bribery-hot” institutions in Lithuania, according to the SMEs leaders’ answers**

Next Table 6 allows to compare above-mentioned SMEs leaders' personal experience in paying bribes, with the analogous experience of their business fellows.

<b>Institutions</b>	<b>Share of knowable cases of paying bribe for particular institution during last five years (%)</b>
Traffic police	25
Custom office	24
Tax inspectorate	20
Tax police	11
Social security fund	8
Local courts	7
Labor inspection	7
Privatization office	6
Municipalities	6
Quality inspection	6

**Table 6. Ten “Bribery-hot” institutions in Lithuania, according to the information received from business fellow of SMEs leaders.**

Tables 5 and 6 let to conclude, that the Traffic police, Customs office and Tax inspectorate are “bribery-hottest” institutions according to the personal experience of respondents, as well as according to their knowledge about analogous cases, which happened with their fellows. However, bribery cases in such institutions as local courts, the Privatization office, and the Quality inspection has not the same weight as in the experience of respondent’s business fellows.

On the basis of the respondents’ answers about minimal and maximal amounts of value of bribes paid it is possible to calculate the statistically reliable mean of the minimal and maximum payments. For the traffic police, they were correspondingly 16 Lt and 720 Lt; for the custom office - 25 Lt and 8031 Lt; and for the tax inspectorate - 60 Lt and 4347 Lt<sup>5</sup>. In this financial context, the obvious “leader” in bribery is the Customs office, the second place occupied by the Tax inspectorate, and the third – by the Traffic police.

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<sup>5</sup> 1Lt=0,25 USD

It is worthwhile to remind that the Tax inspectorate and the Customs office are also mentioned by respondents as institutions creating most troubles for the business development (Table 2).

**Remedies against corruption.** Although the majority of SMEs leaders condemn corruption and openly answered about bribery cases in their business environment, 89% of victims of bribes have not appealed for any help. The main motivations of such behavior are the following:

<b>Reasons for not reporting about bribe</b>	<b>Share of victims of bribery (%)</b>
Lack of the trust in institutions	36
Expected the negative consequences to business	24
Believe in bribes as factor that can assist in doing business	16
Due to the widel spread of corruption in society	9
Have no time for fighting bribes, pay bribes voluntarily	9

**Table 7. Main reasons for not appealing for any help when victimized by bribes.**

In such context, the SMEs leaders' vision of possible means for reducing corruption in Lithuania is not very much constructive. 23% of business leaders point at the necessity for strengthening the sanctions against corrupt individuals, 17% - at tightening public official's' responsibilities, and 14% - at the improvement of laws. 23% of respondents do not have opinion on that issue at all. Remarkably, 50% of the respondents have no idea, how to solve corruption problem in their business area. The role of SMEs in anticorruption activity is about neglected by respondents.

The results of the survey clearly show that the leaders of Lithuanian SMEs regard the corruption as one of the main obstacles to develop and to manage their business. Majority of business leaders believe that main state institutions and public officials with small exceptions are highly corrupt. However, such attitude towards public officials is rather overestimated and expresses the general distrust of businesspeople

in them than points at the real state of affairs. At least the analysis of the bribery cases mentioned in the survey by the business leaders themselves does not support the popular stereotype about totally corrupt Lithuanian society.

Nevertheless, the above-mentioned analysis allowed to diagnose the “hot spots” of the corruption in Lithuanian, at least in its bribery’s form. The Traffic police, the Customs, the Tax inspectorate could be named as institutions, where the risk for SMEs to be victimized by bribes is much higher than in other Lithuanian governmental institutions. Above-mentioned “hot spots”, of course, should become a primarily target for further detailed and comprehensive investigations.

Although SMEs business leaders suggest to solve corruption and bribery problems primarily by administrative and law enforcement means, the improvement of the situation in these problematic areas requires to develop more complex strategy. Strong governmental control over various forms of the abuse of public power is necessary, but not sufficient mean for protecting business environment against corruption in Lithuania. From these perspective Lithuanian SMEs have to understand themselves not only as a victim of corruption, but also as a strategic partner in national wide coalition against corruption.