

THE OTHER SIDE OF THE COIN

The UK and Corruption in Africa



A report by the Africa All Party
Parliamentary Group. March 2006

***The Other Side of the Coin:
The UK and Corruption in Africa***

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The report was drafted by Penny Jackson on behalf of the AAPPG, in consultation with the Steering Committee and with editorial advice from Richard Dowden. The final report was approved by the Steering Committee.

List of Abbreviations and Acronyms

AAPPG	Africa All Party Parliamentary Group
APRM	African Peer Review Mechanism
ARA	Assets Recovery Agency
CBI	Confederation of British Industry
CD	Crown Dependency
CPS	Crown Prosecution Service
DRC	Democratic Republic of the Congo
DTI	Department of Trade and Industry
ECA	Export Credit Organisation
ECGD	Export Credits Guarantee Department
EITI	Extractive Industries Transparency Initiative
EU	European Union
FCO	Foreign and Commonwealth Office
FSA	Financial Services Authority
G8	Group of Eight Nations
HMRC	Her Majesty's Revenue and Customs
IMF	International Monetary Fund
JMLSG	Joint Money Laundering Steering Group
MDB	Multilateral Development Bank
MLAT	Mutual Legal Assistance Treaty
MOD	Ministry of Defence
NCIS	National Crime Intelligence Squad
NEPAD	New Partnership for Africa's Development
NGO	Non-Governmental Organisation
OECD	Organisation for Economic Cooperation and Development
OFR	Operating and Financial Review
OT	Overseas Territory
PEP	Politically Exposed Person
POCA	Proceeds of Crime Act
PRBS	Poverty Reduction Budget Support
ROC	Republic of the Congo
SAR	Suspicious Activity Report
SFO	Serious Fraud Office
SOCA	Serious Organised Crime Agency
UK	United Kingdom
UN	United Nations
USA	United States of America

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1. Chairman's Summary

The Africa APPG decided to carry out an inquiry into corruption and money laundering for four reasons. Firstly, the scale, extent and impact of corruption and related capital flight undoubtedly present a critical obstacle to development in Africa. Secondly, our 2005 report *"The UK and Africa in 2005: How Joined up is Whitehall?"* identified corruption and money laundering as areas which require better policy coherence. Thirdly, the UK fully endorsed the report of the Commission for Africa which made a number of recommendations on how western governments can support Africa's battle against corruption. The UK also chaired the 2005 G8 Summit which committed G8 countries to take action on this issue. Finally, the issues of corruption and money laundering were raised with us in consultations with members of the African Diaspora living in the UK.

"The Other Side of the Coin" looks at the responsibility of the UK to combat corruption and money laundering. We recognise the extent of the problem globally, but we focus on Africa because this is of special interest to the Africa APPG. We examine what the UK can do to support African countries to tackle corruption, because UK policy is our area of potential influence. We do not excuse corrupt rulers from their ultimate culpability for stealing from their people.

This report is by no means exhaustive but we identify three areas where the UK can and should contribute to the fight against corruption in Africa:

- A. By tackling the supply side of corruption; bribe payments and mechanisms in international trade and credit that facilitate corruption.
- B. By tackling the laundering of the proceeds of corruption.
- C. By safeguarding aid to ensure it does not become caught up in corruption or inadvertently support corrupt leaders, but is used to fight the problem.

Our detailed recommendations follow as Section 2 of this report. All are important if the UK is to address this issue comprehensively and across all departments. In particular we wish to stress the need for the UK government to:

- 1. Rigorously enforce existing laws and sanctions against international bribery, corruption and money laundering.
- 2. Bring to Parliament before the end of 2006 a new Anti-Corruption Bill which addresses the concerns raised about the 2003 draft Bill by the Joint Parliamentary Committee and the OECD Phase Two Review.

3. Fully implement the Third EU Money Laundering Directive as soon as possible and well before the 2007 deadline.
4. Ensure that Crown Dependencies and Overseas Territories deal with corruption and money laundering as robustly as the UK.
5. Report to Parliament annually on international development spending with a particular focus on transparency, effectiveness and details of support for anti-corruption priorities and strategies.
6. Appoint an Anti-Corruption champion for a two year period to coordinate policy coherence and implementation across Whitehall and to work with devolved executives, Crown Dependencies, Overseas Territories and international partners.

A handwritten signature in black ink, appearing to read 'Hugh Bayley', with a long horizontal stroke extending to the right.

Hugh Bayley MP
Chairman
The Africa All Party Parliamentary Group

2. Recommendations to Her Majesty's Government

Headline Recommendations

- 1. Rigorously enforce existing laws and sanctions against international bribery, corruption and money laundering.**
- 2. Bring to Parliament before the end of 2006 a new Anti-Corruption Bill which addresses the concerns raised about the 2003 draft Bill by the Joint Parliamentary Committee and the OECD Phase Two Review.**
- 3. Fully implement the Third EU Money Laundering Directive as soon as possible and well before the December 2007 deadline.**
- 4. Ensure that Crown Dependencies and Overseas Territories deal with corruption and money laundering as robustly as the UK.**
- 5. Report to Parliament annually on international development spending with a particular focus on transparency, effectiveness and details of support for anti-corruption priorities and strategies.**
- 6. Appoint an Anti-Corruption champion for a two year period to coordinate policy coherence and implementation across Whitehall and to work with devolved executives, Crown Dependencies, Overseas Territories and international partners.**

Further Recommendations

Tackling the supply side of corruption

A. The Framework

- 7. Establish effective systems to monitor the implementation of the UN Convention Against Corruption by its signatories.**
- 8. Ensure the full extension of the UN Convention Against Corruption and the OECD Convention on the Bribery of Foreign Public Officials to the UK's Crown Dependencies and Overseas Territories.**

B. Investigations

- 9. Take a pro-active approach to detecting international bribery, opening investigations and actively cooperating with mutual legal assistance requests. Require all government departments including HM Revenue and Customs to pass on evidence of bribery they come**

across. Provide training to Revenue and other staff on detecting signs of bribery.

10. Ensure that new arrangements between investigating and enforcement agencies are backed with resources and the necessary powers to carry out investigations. Ring-fence human and financial resources for investigating international corruption to ensure this area is not squeezed out by other priorities.

C. Policy Coherence

11. By the end of 2006 review the anti-corruption policies of all UK Government departments particularly in relation to procurement and encourage the devolved executives, Crown Dependencies and Overseas Territories to do the same. By the end of 2007, in line with World Bank procedures, introduce a list of companies barred from government procurement because of corruption convictions or overwhelming evidence.
12. Robustly enforce the newly revised ECGD anti-bribery and corruption guidelines¹ and work with other export credit agencies to continually review best practice and ensure a high standard globally.
13. As soon as possible carry out a review of international safeguards against mispricing and examine the impact on developing country capital flight. The review should include:
 - the introduction of mandatory price-related signatures from buyers and sellers for all transactions over £10,000
 - the links with international tax evasion and transfer pricing and the capital flight involved

D. Working with Business

14. Following the passing of a new Anti-Corruption Bill through parliament conduct a thorough prevention and education campaign for the UK business sector.
15. Use Government trade support and advocacy services to inform companies about the illegality of bribe payments, the damage they do to development, and methods of avoiding solicitations for bribes; for example through the UK Trade and Invest literature.
16. Require companies receiving Government trade support and advocacy or companies seeking government funded contracts to sign no bribery warranties from mid 2006 onwards.

17. Bar those convicted of corruption offences from receiving government trade assistance, including participation in trade missions.
18. Educate UK companies about the use of mispricing in transactions as a mechanism to embezzle and launder funds, using an information campaign and existing government to business services.
19. Encourage UK banks to re-assess the compatibility of commodity backed loans with their corporate social responsibility guidelines and encourage them to take advice from the international financial institutions on appropriate levels of disclosure and oversight mechanisms for money disbursed.
20. Encourage UK businesses to take an active role in the UN Global Compact and other voluntary initiatives and support UK companies in implementing the initiatives throughout their operations.
21. Discuss with UK business leaders how best to monitor implementation of voluntary anti-corruption initiatives externally.

<i>Tackling Money Laundering</i>

A. Investigations

22. Work to improve inter-agency coordination and ensure there is clarity on who is ultimately responsible for money laundering investigations.
23. Give a high priority to investigations into the laundering of the proceeds of corruption, and to tracing, freezing and repatriating these funds where possible. These activities should have earmarked funds to ensure they are not sidelined by the focus of investigative and enforcement agencies on drugs and anti-terrorism.

B. Closing the loopholes

24. Include within the Company Law Reform Bill a requirement for UK registered companies to declare beneficial ownership and end the practice of directors of registered companies being themselves companies, unless beneficial ownership can be shown. Encourage the UK's Crown Dependencies and Overseas Territories to introduce similar legislation where they have not done so already.

C. The Third EU Money Laundering Directive

- 25. In implementing the Third EU Money Laundering Directive, clearly identify corruption within the working definition of a serious crime and highlight the relevance of offshore transactions as a sign of possible corrupt activity.**
- 26. In the run up to the implementation of the EU directive engage in an information campaign targeting all UK businesses that may be affected to ensure they are aware of their responsibilities regarding due diligence checks, politically exposed persons and suspicious activity reports and what signs they should look out for.**
- 27. Work closely with the EU on ensuring continental implementation of the Third EU Money Laundering Directive.**
- 28. Encourage Crown Dependencies and Overseas Territories to introduce legislation along similar lines to the Third EU Money Laundering Directive and the recommendations of the Financial Action Task Force (FATF), where they have not done so already.**

<i>Aid and Corruption</i>

A. Safeguarding Aid

- 29. Apply the highest levels of financial reporting and accountability to *both* general *and* sectoral forms of direct budget support in Africa; ensure design of UK budget support contributes to increases in financial transparency and broader governance improvements across recipient governments.**
- 30. Continue to freeze budget support where its integrity can no longer be assured and ensure such decisions send a clear message that the donors no longer turn a blind eye to corruption.**
- 31. In assessing suitability for budget support take into account any results from the African Peer Review Mechanism and encourage prospective recipients of UK aid to take part in the process.**
- 32. Work with multilateral organisations to ensure that anti-corruption strategies, including financial accountability and management, are implemented in all programmes. Ensure increased support for anti-corruption projects and systems that support transparency and accountability.**

- 33. Work with the other major donors to assist the non governmental sector to improve transparency and ensure anti-corruption strategies are mainstreamed throughout their work.**

B. Mutual Transparency

- 34. By the end of 2007 create a list of companies, individuals and organisations convicted of corruption or where overwhelming evidence exists, and debar them from DFID (and all UK Government) programmes and contracts. Provide an anonymous anti-corruption hotline or e-mail, accessible from any country.**
- 35. Encourage the EU to report back to the EU Parliament annually on international development spending with a particular focus on transparency and effectiveness. Include where possible estimates of leakage through corruption and details of the EU's efforts to minimise leakage and utilise aid to increase transparency and ensure effectiveness.**
- 36. Encourage the multilateral development banks and other multi-lateral organisations to increase the involvement of parliamentarians in both donor and recipient countries in discussing developmental priorities and improving scrutiny and transparency.**

C. Aid to fight corruption

- 37. Prioritise support for anti-corruption programmes in Africa including anti-corruption commissions, audit offices and programmes to improve the management of public finances, revenue collection and management. Encourage the ratification and implementation of UN and AU conventions relating to corruption. Increase the resources available for such programmes and encourage multi-lateral and other bilateral donors to do the same.**
- 38. Significantly increase support for systems and projects which contribute to the domestic-led fight against corruption in recipient countries. These include support for:**
- The development of independent media
 - Civil society organisations working on anti-corruption and transparency
 - Anti-corruption schemes within the judiciary
 - Parliamentarians in their role as monitors of the executive and scrutinisers of government budgets, particularly public accounts committees
 - National audit offices

3. Background: Corruption's scale, costs & mechanics

The Scale of Corruption

The World Bank estimates that US\$1 trillion is paid in bribes each year globally². Add to this an unknown figure for the embezzlement of public funds or the theft of public assets by corrupt officials. For example, it is thought that President Mobutu Sese Seko of Zaire (now the Democratic Republic of the Congo) and President Abacha of Nigeria each embezzled around \$5 billion³. Then add the Bank's estimate of 'tainted procurement' at US\$1.5 trillion and the unquantified volume of fraud within the private sector.⁴ The extent of petty corruption varies enormously and is even harder to quantify. It is clear that, overall, the scale of corruption is immense.

The Costs of Corruption

Corruption obstructs development, and hurts the poorest people. It also impedes business growth. The World Bank has identified corruption as the single greatest obstacle to global development⁵. In an investment survey of nine African countries the World Bank identified corruption as the biggest impediment to investment⁶. Both petty and grand corruption are costing economic development dearly.

The impact of corruption itself may vary, for example according to how much of the proceeds are then banked or spent overseas, rather than domestically. In Africa capital flight is a major problem and it is arguable that corruption's impact is greater because of the tendency of the proceeds to be banked overseas.

But the developmental costs of corruption extend beyond the actual money lost; indirect effects include losses in investment, private sector development and economic growth. Where corruption becomes endemic the drag on development can be all encompassing. The World Bank estimates that a 300%⁷ - 400%⁸ 'governance dividend' can in the long run follow good governance and corruption control. That translates as a three or four fold increase in income per capita and major reductions in other manifestations of poverty, such as child mortality⁹. Researchers have also estimated that 2 - 4% of annual growth can be shaved off by corruption.¹⁰

Corruption can also reduce tax revenues by as much as 50%¹¹ reducing the funds available to government for public spending.

Poor people bear the brunt of corruption. Public services are undermined and the cost of provision inflated. For example one study of water utility provision in Africa indicated that graft was so high in the sector that nearly two thirds of the

operating costs were due to corruption¹². These extra costs are transferred to the consumer. Some services are simply not provided because of corruption. It is the poor who rely most on public services and are worst affected by their absence, over-pricing or underperformance.

Likewise the cost of other consumer goods inflates because of corruption, by as much as 20% in some cases¹³. Such costs swallow up a higher proportion of the income of a poor family.

The poor too are expected to pay bribes where petty corruption exists, but a higher proportion of their income will be taken up in bribe payments. For example research by Transparency International Kenya suggests that in 2002 average expenditure on bribery per month, something they have termed the 'bribery tax', reached US\$52 in 2002, this in a country where average GDP per capita has not exceeded US\$500 in the last decade¹⁴. Thankfully, by 2003 the figure had decreased to US\$16 though the average size of bribes solicited had increased¹⁵.

A direct effect of corruption on business is to drive up the cost of capital investment. Recurrent corruption payments will also increase business costs and therefore reduce profitability¹⁶. Corruption also increases business risk as the sanctity of agreements reached corruptly is already in question and legitimate agreements may be undermined if an official receives a better offer elsewhere¹⁷. The cost of goods can increase by as much as 20%¹⁸. One study found that corruption's impact on foreign direct investment can be equal to an extra 20% in tax – discouraging investment and reducing profit margins¹⁹. The IMF has estimated that corruption reduces investment by around 5%²⁰ and one Harvard scholar that an increase of 1 point in the corruption index can result in a reduction of foreign investment by as much as 8%²¹. Corruption also has a negative effect on a country's ability to compete in international trade.²²

Smaller companies tend to suffer more as bribe payments will constitute a larger proportion of their revenue, leaving them unable to compete with bigger companies where large bribes are required to secure a contract. In the African context this can translate into a bias against domestic companies which tend to be smaller than foreign competitors. Domestic business growth is retarded by corruption and foreign business investment is also discouraged.

The possible impacts of corruption on democracy are impossible to quantify. But corruption can undermine democratic systems by infiltrating the highest levels of governments and the most basic levels of public services. The links between corruption, money laundering, organised crime and security, including terrorism, are also yet to be fully explored.

Corruption in Africa

Corruption is a global problem. Any country that believes it is totally free of corruption is deceiving itself and its people. However, Africa has developed a particularly bad reputation for corrupt practices. The reigns of Presidents such as Mobutu of Zaire and Abacha of Nigeria are some of the world's most infamous kleptocracies. The whole continent has suffered from this reputation which reduces business confidence and investment. The Transparency International Corruption Perceptions Index (PCI) demonstrates this poor reputation. Of the 20 countries rated most corrupt in the index, 10 are in Africa²³.

In one country alone, Nigeria, the National Economic and Financial Crimes Commission estimates that in the past £220 billion was stolen or misused by the country's past rulers between 1960 and 1999 and much of this was held overseas. This figure is similar to the amount of international aid given to the entire continent in four decades²⁴. It also helps to explain why, despite being one of the world's most resource-rich countries, with around US\$300 billion earned through oil since the mid seventies, average Nigerian per capita income in 2002 was a quarter of its mid seventies peak and below the level at independence²⁵.

While actual sums lost from non-resource rich states may be smaller, they can be enormously damaging. A study by one Tanzanian NGO indicated that the annual loss to the country through corruption could be nearly as high as the country's total annual revenue collection²⁶.

Weak governance greatly increases the opportunities for corruption. Some African countries' weak governance and lack of institutional structures have contributed to corruption and in turn may have been perpetuated by it. Countries recovering from conflict, of which there are several in Africa, rightly need to concentrate on ensuring security, but such initiatives are also undermined by corruption. Research by Congolese anti-corruption campaign groups indicates that only 3% of government procurement contracts in the Democratic Republic of the Congo involve a proper tendering process²⁷. The opportunities for corruption without such safeguards are enormous.

Africa has also suffered particularly because the proceeds of corruption tend to be banked or spent outside of the continent. Capital flight is possibly Africa's biggest financial problem. The African Union estimates that \$148 billion a year leaves the continent because of corruption²⁸. This represents a quarter of the continent's GDP²⁹. Other estimates of the amount of total illicit proceeds coming out of Africa (including corrupt, commercial and criminal proceeds) are in the order of \$100-200 billion³⁰. This dwarfs the aid and debt relief Africa is receiving:

"We have been putting some \$25 billion a year of foreign aid into Africa in the most recent years. Compare that with my estimate of the amount of money that goes illegally out of Africa and ultimately into Western coffers, \$100-200 billion. In other words, for every \$1 of foreign aid that

we are generously handing out across the top of the table, we are taking back some \$4-8 in dirty money under the table.”³¹

Furthermore, in Africa’s case the outflow of illicit money tends to be permanent – estimates suggest that 80-90% of the illicit outflows are not returned to the continent³². It is also estimated that African political elites hold somewhere in the range of \$700 to \$800 billion in accounts outside the continent.”³³

The Mechanics of Corruption

Transparency International defines corruption as “the abuse of entrusted power for private gain”. Such gain is not necessarily straightforward personal financial benefit and nor is corruption limited to only the public or private sectors. Both the distinction and linkages between petty and grand corruption must also be considered in any definition.

Within this report corruption is considered to include soliciting and accepting bribes and embezzlement. Embezzlement can take place through mechanisms which include siphoning off funds to non-existent companies (see for example box 5.4) and fake or mispriced transactions.

As much as 60% of trade transactions into or out of Africa are estimated to be mispriced by an average of 11%, which translates into annual capital flight in excess of \$10 billion³⁴. Fake transactions are estimated to account for a further \$150-200 billion³⁵.

Grand, petty and all damaging

Grand corruption refers to corruption on a major scale usually by high level officials or politicians. Infamous cases of grand corruption in kleptocracies in Africa include Zaire under Mobutu (who saw little distinction between his personal and state bank accounts and used the latter to fund a series of mansions in Europe and Africa, and a lifestyle so lavish it is hard to comprehend)³⁶; Nigeria under a series of brazenly corrupt leaders; Kenya with the Goldenberg scandal in which the country was fleeced of US\$600million - \$1 billion in just three years with the connivance of leading politicians and officials³⁷. There are many more examples from across the continent and elsewhere and unfortunately, the examples of grand larceny are not confined to deceased or deposed African leaders. Information is regularly seeping out of countries including Equatorial Guinea, Kenya, Angola and the Republic of Congo indicating that the age of the ‘big man’ is not over³⁸.

‘Petty’ corruption refers to smaller scale acts of corruption, such as the extortion of bribes by customs officials, police officers and civil servants, to carry out - or not to carry out – their duties as the case may be. Petty corruption is caused by a number of factors including impunity and low wages. Where corruption contaminates an organisation it becomes hard for those wishing not to engage in

corrupt practices to stick to their principles as they may be expected to take bribes and to pass on a proportion of the proceeds to their superiors. When such low level corruption becomes endemic its impact is far from petty. It can displace all other structures and systems of public transactions. People assume they will need to pay bribes, informal guidelines as to the size of a bribe develop and corruption becomes an integral part of the system.

In Zaire, President Mobutu once told his party conference that it was acceptable to steal a little – as long as theft remained within informal limits.³⁹ In Cameroon, police have been accused of supplementing their wages by regularly charging taxi drivers for imaginary offences as bizarre as ‘having a double windscreen’ for drivers who wear glasses. Taxi drivers did eventually go on strike in protest in 2004, not at the fact they had to pay so many bribes to police officers, but that not all officers were sticking to the generally accepted rate for payments.⁴⁰

Box 3.1 **Culture and Corruption**

Some have argued that in Africa corruption is an unavoidable reflection of a culture of reciprocity. The AAPPG sees this as an excuse used by African governments and the international community not to take a hard line on corruption. As Olusegun Obasanjo, since elected President of Nigeria, said in a letter to the Financial Times in 1994:

“I shudder at how an integral part of my continent’s culture can be taken as a basis for rationalising otherwise despicable behaviour...In no society is it acceptable to the people for their leaders to feather their own nest at public expense.”⁴¹

More and more, African civil society groups are speaking out against corruption and electorates using their votes and voices to push corrupt leaders out of office.

The Kenyan electorate in 2002, made a choice to vote in a new government, which they hoped would clean up corruption in that country. Since the recent corruption scandal has rocked the new government, the electorate are already showing signs that they will no longer tolerate grand corruption⁴². In South Africa the government has responded to pressure from civil society and the media to apply the full force of the law to those accused of corruption. They know the South African electorate will not stand for corruption. A number of African governments are rolling out progressive anti-corruption programmes and others have embarked on groundbreaking prosecutions, such as the Lesotho Highland Water Project case and the recent prosecution of former Malawian Minister for using government money to fund his wedding party⁴³.

The pressure faced by politicians and senior officials to support extended families and friends can be substantial. In some countries a display of wealth and generosity is part and parcel of re-election, as the prevalence of the ‘*harambee*’ in the 2002 Kenyan general election showed. In some contexts, not limited to Africa, getting elected is a very expensive business and candidates may find themselves captured by sponsors. Some people think that a politician without access to funds will not be capable of bringing benefits to the local community. In some contexts if he cannot maximise financially while in office a politician or official may be viewed as lacking in enterprise, or ‘*ye ye*’⁴⁴.

This pressure, however, does not imply that politicians have an infallible excuse for engaging in corruption, as in the end this will not help their local community. A redefining of the relationship between politicians and the electorate, a clearer definition of how the former serve the latter, greater transparency around party and individual funding and an end to impunity are all required.

Petty corruption, even where it has become the norm, is caused more by economic, rather than cultural, factors. Low wages can encourage public servants to supplement their income by soliciting bribes. Even for high level public servants, economics can be a contributing factor. For example, as one Congolese judge put it:

*"There are three sorts of judges here in Kinshasa. One gives judgements on the merits of the case and does not ask for anything. These are very rare. Then there are those who talk to the litigants and give the judgement to the highest bidder. There are many like that. The third category are those who try to make a fair judgement but then go to the winner afterwards and ask them for some payment. This is what I do. If I did not I could not feed my family."*⁴⁵

However it can become integrated into a system, or even replace legitimate structures and systems of (public) transactions where it becomes endemic. One example is the of the constant use of Article 15 following Mobutu's edict that the people of Zaire should use their initiative and '*debrouillez-vous*' (look after themselves).

Secondly, where corruption is endemic in an organisation it is difficult to break the spiral of corruption once it infects an organisation⁴⁶. Individuals have few incentives not to engage in it, indeed they may face pressure from their superiors to solicit bribes or even work within an organised system in which superiors require a cut from each transaction. Economic levers, such as decent wages, are needed to address this problem in concert with protection and support for whistle blowers and strong action taken against those who do engage in corrupt practices. Impunity breeds illegality.

Corruption can be minimised by institutional checks and transparency. In countries where corruption is relatively low it is usually because people know they will be caught and punished, not because of some inherent cultural difference.

Corruption Hot Spots

Corruption can and does affect all sectors. But it usually pervades some areas more than others. For example corruption seems to affect the security sector particularly, probably because of its lack of transparency. The corruption scandals implicating several high level Kenyan politicians and officials that were recently revealed in the report by Kenya's former Anti-Corruption officer, John Githongo, are mainly related to security sector contracts⁴⁷. One of the cases included a contract for a naval vessel at double the price some military analysts suggest such a vessel could be purchased⁴⁸.

One sector particularly prone to large scale corruption is the extractive industries. In the 1990s, Zaire's state mining company, whose profits should have been boosted by the high price of copper, was actually losing hundreds of millions of dollars a year to looting by the President's office⁴⁹. In the oil sector, the sheer

volume of money that this black gold produces has led to grand scale corruption in the past in countries including the Republic of Congo, Angola and Nigeria. Sections of the industry and some countries are showing marked improvements in transparency, but in Equatorial Guinea the spending of oil earnings remains an official 'state secret'⁵⁰. In Angola the government reprimanded one oil company for agreeing to reveal details of its payments to the state⁵¹.

Box 3.1

Corruption in the Construction Sector

The construction sector is highly prone to corruption. One analysis by Transparency International has identified 13 features of construction projects which make them particularly prone to corruption⁵². As well as the sheer size of such projects their complexity - i.e. the number of phases and layers of different contractors and subcontractors - provides many more opportunities for corruption that may go unnoticed. Uniqueness of projects often leave governments with no comparable costings. This lack of information or 'information asymmetry' can provide lucrative opportunities for corruption⁵³.

There are also prospects for corruption at each stage of a construction project, beginning at planning and design where prices may be inflated in anticipation of opportunities to skim off resources. In the award of large contracts, bribery is not unusual, indeed common according to some professionals⁵⁴. Bribes may also be channelled through complicated sub contractual arrangements. Some cases of 'anticipatory awards' or 'mobilisation fees' of as much as 50% of the full contract price have been uncovered in an audit inspection in Nigeria. In some cases mobilisation fees were collected but the contract was never completed⁵⁵. Corrupt practices do not end with the awarding of a contract but often continue during construction, operation and maintenance of the completed project⁵⁶. Mechanisms include deferment of earlier agreed bribes, deliberate delays which incur compensation payments and substandard work⁵⁷.

As one construction expert described:

*"You need certificates every month of what has been done and someone is certifying that. To get your certificate you may have to pay every month. Once you have your certificate you need to get the payment, but to get your payment you may have to pay. In order to get your equipment through Customs & Immigration you will probably have to pay and to get your visas. This is perpetuated all the way down the contractual hierarchy, through the subcontractors and the sub-sub-contractors. You also have fraud occurring in that claims put forward may be enhanced or inflated for false reasons and false costs. You get this whole contractual structure of hundreds of companies...That is why costs can overrun by 50 or 100 per cent sometimes."*⁵⁸

The impact of corruption in the construction sector damages the sector itself, increasing the costs of capital, by as much as 40-50%⁵⁹. The higher costs mean that less can be purchased with a set amount of money because of inflated prices, known as a 'substitution effect'⁶⁰. Recurrent corruption also raises the cost of running infrastructure services and can reduce standards; these costs are transferred to the consumer. Substandard construction, caused by corruption can also put public safety at risk⁶¹.

The granting of concessions or licenses, particularly for primary resource exploitation has in the past been used by corrupt leaders to make money, while also underselling their nation's national wealth.

Another sector in which corruption is particularly rife is in the construction sector, including infrastructure and engineering. The large size of such contracts, their complexity, often involving numerous sub-contracts can make infrastructure or large construction projects particularly prone to corruption. (See box 3.1)

Like other public services the health sector has long been prone to petty corruption. However, in the past few years major problems have been identified in the sector, in particular in relation to health equipment such as medicines. The work of the Nigerian National Agency for Food and Drug Administration and Control indicates both how big the problem of fake drugs had become in Nigeria and how it can be tackled if the political will and resources are available. Secondly, large new aid flows have provided opportunities for corruption as donors have injected money to fight against major crises such as HIV/AIDS (see for example Section 6 on the problems faced by the Global Fund to Fight AIDS TB and Malaria).

In many countries the public also see political parties and parliaments as some of the most corrupt organisations in society⁶². Political corruption often links in with other mechanisms to skim off money through contracts from particular sectors. For example the Githongo report, which alleges grand corruption by leading politicians through security sector procurement, shows that the money was sought to fund party political campaigns, rather than simple personal enrichment⁶³. This raises issues about official political party funding, or limits on candidate expenditure. Judicial systems are also prone to corruption.

One area which is no less prone to corruption than many others and yet few within that industry are willing to talk about it, is within the aid industry itself. Aid agencies may find themselves paying bribes to get shipments through and obtain permits just as businesses do. This issue is looked at in section 6.

Supply and Demand

Clearly those who solicit bribes, embezzle funds and so on are the primary culprits. In the case of Africa it is up to national governments, regional and civil society to root out and punish the corruption that damages the continent so badly. There is a role for parliamentarians in this battle, for example through holding the executive to account by scrutinising budgets and spending. There is also a role for the international community to support those determined to fight corruption, and building capacity in anti-corruption institutions.

However, as well as supporting African organisations and individuals fighting corruption in their own countries, the international community must do more. We

must address the other dimensions of the corruption process, in which western governments, organisations, companies and individuals have been implicated - the other side of the coin.

We have to understand supply as well as the demand side of corruption. Who is offering the bribe and who is laundering the proceeds of corruption? In many cases western companies and western agents have been guilty of offering and paying bribes to government officials to secure contracts and other advantages. Western banks have been implicated in laundering the proceeds of corruption and western shell companies and trusts have been set up to facilitate this. Western financial experts have also been accused of assisting corrupt officials to launder their illicit funds. And the international community, both donors and the private sector, have been guilty of turning a blind eye to rampant kleptomania.

There are numerous cases that demonstrate the role played by foreign companies in Africa in paying bribes, and facilitating other forms of corruption (see section 4). Despite much anecdotal evidence from businessmen themselves and investigative journalists, there are few quotable cases involving UK companies because at the time of writing, no UK company or individual has been prosecuted in the UK for bribery of a foreign public official. Unfortunately this does not mean it is not taking place.

Secondly it is worth noting that large inflows of money to a government that does not have either the political will or the institutional capacity to ensure that money is fully accounted for, can in effect fuel corruption. Such money may come through FDI where resources such as oil are found, or in the form of aid, or loans. If western companies, governments and multi-lateral donors do not insist on high anti-corruption standards, they may be adding to the problem.

Fear of detection means that the proceeds of corruption, like other 'dirty money', need to be laundered. The international financial system is riddled with loopholes. Poor enforcement of laundering regulations lead some experts to suggest there is as much as \$1 trillion of illicit cross border flows annually⁶⁴. Unfortunately the UK, including the City of London and Overseas Territories and Crown Dependencies, has been implicated in this practice. The laundering of the proceeds of corruption and efforts to trace, freeze and repatriate stolen assets will also be looked at in this report.

Accusations of hypocrisy have been levelled against the UK and other western countries for condemning corruption in Africa without their role addressing supply side and laundering issues:

*"With one hand, the West has pointed its finger at corrupt African leaders, whilst, with its other hand, its bankers, lawyers, accountants, art dealers, health authorities, universities, estate agents and embassies have been actively or passively encouraging wealth out of Africa into the West's economies."*⁶⁵

If we want to be taken seriously by African leaders and African citizens when we condemn corruption and increase aid, we must address the corruption problem holistically. Because the UK has taken a lead in the international community on supporting development in Africa, there is now a call for the UK to take a similar leadership role in tackling the international structures that support corruption.⁶⁶

Without this type of action – in effect, putting our own house in order and ensuring our own policies are joined up⁶⁷ – African efforts to tackle corruption will be undermined, as will our programmes designed to support anti-corruption efforts and, more generally, our aid and Africa's development. It is a matter of policy coherence.

This report concentrates on the role played by the West in Africa's corruption problem and the role we should be playing to help combat it. Specifically, the report focuses on the UK including its Overseas Territories and Crown Dependencies.

This is not to infer that corruption in Africa is all the fault of the West, but that if we really expect progressive leaders in Africa to tackle corruption successfully then we must support their efforts and ensure our own policies, our companies and our citizens, are supporting, not undermining, that aim.

4. Our Role in Tackling Corruption

As already stated the AAPPG does not seek to make excuses for corrupt officials and politicians in Africa who have damaged their countries' economic development. In the first and last instance corruption has to be tackled at the level of the nation state with heads of state leading the fight. However, the AAPPG does wish to point out the ways in which we in the West and specifically the UK contribute to the problem and facilitate corruption and where our practices need to change as part of a coordinated battle against corruption.

This chapter looks specifically at the role of international actors who offer and pay bribes and concludes that the UK Government should take a stronger international lead by improving our legislation and enforcement and deterring UK involvement in international bribery. The chapter also examines the role of export credit agencies, in particular the anti-bribery guidelines of the Export Credit Guarantee Department (ECGD). In addition it looks at some of the transnational mechanisms by which embezzlement can take place such as mispricing and opaque international loans. The chapter then goes on to explore the role of international business in tackling corruption.

Our International Commitments

The UK has signed up to several legally binding international conventions:

- The 1997 OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. The convention was ratified by the UK in 1998 and came into force in 1999.
- The 1999 Council of Europe Criminal Law Convention on Corruption. The convention was ratified by the UK in 2003 and came into force in 2002
- The 2003 UN Convention Against Corruption. The convention came into force in 2005 but was not ratified by the UK until February 2006.

The UK has also made a number of other commitments. At its launch the Prime Minister fully endorsed the report of the Commission for Africa, which he chaired, and declared it to be UK policy. The report included a number of recommendations on governance and corruption; some aimed at African governments others at western governments. These included recommendations on ratification of the UN Convention Against Corruption during 2005 and higher standards for transparency amongst export credit agencies. Box 4.1 gives more detail of some of the Commission for Africa's recommendations.

Box 4.1

The UK's broader commitments

Recommendations made by the Commission for Africa:

- Developed country governments, company shareholders and consumers should put pressure on companies to be more transparent in their activities in developing countries and to adhere to international codes and standards for behavior.
- Principles of transparency such as those in EITI should be extended to other natural resource sectors, including forestry and fisheries.
- Developed countries should encourage their Export Credit Agencies (ECAs) to be more transparent, and to require higher standards of transparency in their support for projects in developing countries. Developed countries should also fully implement the Action Statement on Bribery and Officially Supported Export Credits agreed by members of the industrialised nations group, the OECD.
- Countries and territories with significant financial centres should take, as a matter of urgency, all necessary legal and administrative measures to repatriate illicitly acquired state funds and assets. We call on G8 countries to make specific commitments in 2005 and to report back on progress, including sums repatriated, in 2006.
- All states should ratify and implement the UN Convention against Corruption during 2005 and should encourage more transparent procurement policies in both Africa and the developed world, particularly in the areas of construction and engineering.”⁶⁸

Commitments made at the 2005 G8 Summit in Gleneagles:

Work vigorously for early ratification of the UN Convention Against Corruption and start discussions on mechanisms to ensure its effective implementation. Work to establish effective mechanisms, consistent with the provisions of UNCAC and previous G8 commitments, within our own administrations for the recovery of assets, including those stolen through corruption, taking into account final disposal of confiscated property where appropriate, and to return assets to their legitimate owners. We encourage all countries to promulgate rules to deny entry and safe haven, when appropriate, to officials and individuals found guilty of public corruption, those who corrupt them, and their assets.

To further protect the international financial system from illicit corruption proceeds, we encourage all countries to require enhanced due diligence for financial transactions involving politically exposed persons. In addition, we urge all countries to comply with UN Security Council resolution 1532 to identify and freeze the assets of designated persons. Reduce bribery by the private sector by rigorously enforcing laws against the bribery of foreign public officials, including prosecuting those engaged in bribery; strengthening anti-bribery requirements for those applying for export credits and credit guarantees, and continuing our support for peer review, in line with the OECD Convention; encouraging companies to adopt anti-bribery compliance programmes and report solicitations of bribery; and by committing to co-operate with African governments to ensure the prosecution of those engaged in bribery and bribe solicitation.

Take concrete steps to protect financial markets from criminal abuse, including bribery and corruption, by pressing all financial centres to obtain and implement the highest international standards of transparency and exchange of information. We will continue to support Financial Stability Forums ongoing work to promote and review progress on the implementation of international standards, particularly the new process concerning offshore financial centres that was agreed in March 2005, and the OECD's high standards in favour of transparency and exchange of information in all tax matters.⁶⁹

Under British Chairmanship the 2005 G8 Summit at Gleneagles committed members to a number of relevant actions by G8 leaders to support African anti-corruption efforts. These included commitments to ratification of the UN convention, vigorously enforcing laws on international bribery and more action on freezing and repatriation of assets, which will be looked at in section 5. Box 4.1 provides relevant extracts from the G8 communiqué.

The UK made the decision to take a lead internationally on issues relating to Africa during 2005. The AAPPG commended this decision and more recent statements by the Government indicating their intention to follow these commitments with implementation. Some can be implemented unilaterally, others will require multi-lateral action. It is therefore disappointing that we are failing to take the lead on some of the anti-corruption commitments. Indeed there is evidence of delays in domestic legislation, in enforcement of existing legislation, and in ratification of the UN Convention and there has been a dilution of ECGD guidelines. These delays do not sit comfortably with the UK's wish to take a lead on African issues and the AAPPG calls on the government to address these inconsistencies as a matter of urgency.

Furthermore, these conventions and commitments do not appear to have been comprehensively adopted and implemented in all of the UK's Crown Dependencies and Overseas Territories.

The UN Convention

In endorsing the Commission for Africa report the UK Government committed itself to ratifying UN Convention Against Corruption and said that it would be in a position to do so during 2005. While narrowly missing this target the UK has now ratified the Convention (in February 2006). This is most welcome. By ratifying relatively early the UK can be represented at the conference of state parties. This will provide an opportunity to take a leadership role in pushing for *implementation* of the convention amongst signatories and for effective monitoring mechanisms that can report back on progress, possibly along the lines of the peer review mechanism used by the OECD. Some form of monitoring of the UN Convention's implementation across the world is needed if the Convention is to have teeth.

Secondly, the UK must ensure that the Convention is extended to all the Crown Dependencies and Overseas Territories.

Bribery

The World Bank's Global Governance Director says that a conservative estimate puts bribes paid globally each year at US\$1 trillion⁷⁰.

Bribes vary in size, from the petty corruption of a police officer who solicits bribes from the general population to the grand corruption of senior government officials who may accept large sums for example to bypass government tendering processes. Companies may pay bribes to secure contracts, influence or other undue advantage. Local and international companies have been found to pay bribes, including British companies (see for example box 4.2). It is this supply side to corruption – paying the bribes to foreign public officials - that is the central concern of this section.

Box 4.2

UK Companies implicated in Lesotho bribery scandal

Lesotho, a small country in Southern Africa, surprised many by taking action against large scale corruption in its now infamous Highlands Water Project. Several senior government officials have now been prosecuted. A number of international companies were implicated in the payment of bribes in the construction project either individually or as members of a consortium. These include British firms Balfour Beatty, Sir Alexander Gibb and Company, Stirling International Civil Engineering and Kier International⁷¹. The alleged offences took place before the 2001 Anti-Terrorism Act outlawed the bribery of foreign public officials.

The Lesotho prosecution service has invested time and money in the prosecution. They have already successfully prosecuted a Canadian and a German company and are collecting evidence against others involved⁷². Where the UK can support Lesotho's investigators' requests they should do so.

The UK's Legislation

Despite ratifying the OECD Convention on Bribery of Foreign Public Officials in 1998 the UK only enacted legislation to outlaw the practice in 2001. In 2002 Section 12 of the Anti Terrorism Act came into force. In some countries bribery is still not a prosecutable offence, while in others, such as the USA, the bribery of foreign public officials has long been outlawed⁷³.

The AAPPG believes that the UK must tighten its own anti-bribery and anti-corruption legislation. Current legislation relating to anti-corruption and bribery, particularly relating to overseas acts is not sufficiently comprehensive, robust or clear. The OECD is amongst a number of organisations which have strongly criticised the UK's existing legislation (see box 4.3). Having signed the OECD convention, which includes provision for monitoring implementation, this is criticism the Government must attend to.

In 2003 the UK Government sought to address this widespread criticism by bringing a Draft Corruption Bill to Parliament. In examination a joint committee of both Houses of Parliament strongly criticised several assumptions in the bill and some of the details of its drafting.

Key areas of criticism related to the lack of clarity of the Bill and its reliance on the 'agent-principal' relationship⁷⁴. The draft Bill utilised the concept of agent and

principle in order to define bribery, in which the agent is the employee and the principal is the boss or company. However, the use of such a framework excludes cases where the head of a company bribes the head of another rival firm as no agent would be involved in this act. There is no reason why such a form of corruption should not be covered by the new Bill, if it is to be comprehensive. It is not sufficient to say that such issues are addressed by the Enterprise Act. The definition also creates an artificial divide between corruption in the private and public sectors. While different, both are types of corruption and both should be outlawed by an effective and comprehensive new Bill.

Any new Bill should also include a provision to outlaw an employer permitting and employee accepting a bribe from, say, a contractor or buyer, or in issues such as planning permission. This is not clearly identified in the 2003 draft.

The joint committee also complained that the Bill was unnecessarily confusing to those who would need to understand it including juries, lawyers, business and the public. It is not clear why the drafters of the bill decided to use a definition of corruption different from the international norm, given the need for international cooperation on corruption.

Since then the Government has undertaken to bring a new Bill to parliament, but has not seen fit to fast track legislation, despite ongoing criticism from the OECD and non governmental organisations. The AAPPG was very pleased to see a consultation document issued by the Home Office and hopes that a new and improved Bill will be brought to parliament this year. The AAPPG made a submission to the consultation, in which the following issues were stressed:

Four overarching principles should be applied in the re-drafting of the Bill:

1. Effectiveness - in tackling corruption at home and abroad (to be effective loopholes must be closed, and enforcement must be a priority)
2. Clarity – ensuring legislation will be understandable by all stakeholders domestic and international and particularly that it is clear to business
3. Compliance - ensuring it enables the UK to comply with international obligations.
4. Policy coherence – ensuring all UK Government departments, devolved assemblies etc support crosscutting commitments – this includes the commitment by the Prime Minister in the 2005 G8 communiqué and the report of the Commission for Africa to tackle international bribery, with the UK at the forefront.

A new Bill should:

- Be clear and readily understandable to audiences in both the UK and overseas, in business and other sectors
- Be comprehensive and criminalise all conduct which is corrupt. Having one single anti-corruption bill is important. Plasters designed to cover gaps

- in existing laws would be a wasted opportunity for improving and simplifying the legislative framework.
- Create a clear, specific offence of “offering or giving undue or improper advantage to a foreign public official”
 - Make it unlawful to make payments to a third party or agent that may be used to give undue advantage to a foreign public official.
 - Make UK companies liable for acts carried out by subsidiaries (including foreign subsidiaries)
 - Make it an offence for a company to fail to take adequate measures to satisfy itself that subsidiaries and joint ventures are implementing suitable anti-corruption procedures
 - Make trading in influence an offence to bring us into line with the Council of Europe Criminal Law Convention
 - Award special investigatory powers to the authorities investigating, prosecuting and enforcing bribery cases.
 - Remove the requirement for the Attorney General’s consent for investigations and prosecutions.

Action beyond legislation

As well as creating comprehensive legislation the UK Government also needs to take action to improve prevention, investigation and enforcement.

Prevention

Following new legislation the Government should launch a pro-active prevention effort including an information campaign about what exactly is outlawed and what penalties will be incurred by companies or individuals who break the law.

Prevention work undertaken by other OECD signatories such as Australia indicate that there is scope for a broad information campaign amongst the UK business community⁷⁵. Despite recent changes in attitude amongst the business community towards paying bribes, the problem has not gone away. The illegality and the negative impacts of corruption on business operations at home and abroad must be made central to all government advice to business.

The UK’s Trade and Invest service recommends business agents to UK companies wishing to work overseas. But it appears to undertake no due diligence checks on these agents, nor use the opportunity to warn UK companies of the central role that agents can play in payment of illegal bribes.⁷⁶ This advice could and should be used as an opportunity to warn UK companies about the role of disreputable agents and only provide the details of those who have not been implicated in corruption scandals.

The UK Government plays a central role in facilitating UK companies seeking contracts and trading opportunities abroad, including through trade missions. In

the USA such export advocacy is dependent on US companies making a no bribery undertaking in writing, or 'no bribery warranty', which applies to it *and* its affiliates. The AAPPG sees no practical reason why any UK Government export advocacy, whether involving the FCO, DTI, ECGD, MOD or other department should not be subject to the signing of comprehensive no bribery warranties.

Furthermore such warranties, together with robust internal anti-corruption guidelines, should be applied to Government procurement both at home and abroad. Few companies would wish to automatically debar themselves from lucrative government procurement contracts by declining to sign no-bribery warranties.

All government departments should regularly review anti-corruption policies, ensuring cross-Whitehall coherence, particularly in relation to procurement. The same anti-corruption guidelines should apply to devolved authorities and local governments.

Investigation and Enforcement

Systems of pro-active detection of bribery should also be put in place. In a number of cases relating both to bribery and corruption the UK authorities have been unable to prosecute companies because of lack of evidence. However they have not been proactive in seeking such evidence. As one witness described the current situation:

"Because it is so hard to get evidence on overseas corruption, we have a situation where you do not get the evidence unless you open an investigation, but you cannot open an investigation unless you have the evidence, and that is a vicious cycle. I think that is what the intelligence gap is, that there is a need for someone to be building up the evidence from when an allegation first comes in. The question is: Who should do it and do they have the resources to do it?"⁷⁷

Where accusations of certain other crimes are made, the investigative authorities should seek out evidence and if possible, bring a prosecution. The same pro-active investigation should be applied to cases of corruption, both internally and domestically. The OECD has criticised the UK for considering possible impacts on the UK's economy and relations with other states when deciding whether to take investigations forward (see box 4.3). Crime should not be investigated so selectively.

Evidence uncovered during tax audits by the HM Revenue and Customs, which indicates a bribery offence may have taken place or might contribute evidence to an existing investigation, should be passed over to the investigating authority. At present HMRC is able but not obliged to do so⁷⁸. It is important that all other Government departments, which may come across evidence of bribery, including HMRC, support the investigating and prosecuting authorities by passing on relevant information. Specialist training should be provided to Revenue staff to enable them to detect signs of bribery.

It is also imperative to be able to provide protection for whistle-blowers.

Enforcement is also central to an effective anti-bribery regime, indeed to law in general. In Phase Two of its review of the UK, the OECD Bribery Working Group criticised the fragmentation of the investigatory and prosecuting authorities in the UK, making enforcement difficult. Indeed no British individual or organisation has yet been prosecuted for bribery of a foreign public official, indicating that enforcement is an area of particular weakness. The Home Office itself forecast in 2001 that there would be 10-20 investigations and 1-2 prosecutions per year. The reality has fallen far short of both targets – with no prosecutions to date and only three full investigations (around 20 are under consideration for investigation) although there have been around 60 allegations reported to the law enforcement agencies.⁷⁹

In a letter to the AAPPG the Commissioner of Police for the City of London, who holds the Economic Crime Portfolio within the Association of Chief Police Officers stated that the primary obstacles faced by the police in mounting investigations into cases of bribery overseas are lack of funding and expertise⁸⁰. Indeed, when UK Police forces have targets to meet in other areas, such as in street crime, international drugs supply and anti-terrorism, it is easy to see why overseas bribery has not been a focus of investment.

The lack of resources made available to teams working on foreign corruption cases within the law enforcement agencies gives a clear indication as to why the Home Office targets have proved elusive. The law enforcement agencies need a core of specialised staff or a specialised unit to investigate and prosecute offences of overseas corruption and they need a central contact point to which all allegations can be directed. Resources must be provided to train staff and ensure teams are big enough to address the workload.

The establishment of the Serious Organised Crime Agency (SOCA), which will absorb the National Criminal Intelligence Service (NCIS) and the National Crime Squad, is aimed at improving coordination, powers and resourcing of SOCA priorities such as drugs and immigration crime. Anti-corruption will not be a SOCA priority but they will be tasked with taking over the Suspicious Activity Reporting system (see section 5). The AAPPG is pleased to note that the Home Office has now added bribery and corruption offences to the list of offences in the Serious Organised Crime and Police Act of 2005, using secondary legislation, this is an important clarification for investigative and enforcement agencies⁸¹.

The AAPPG was pleased to see the Home Office's consultation paper re-visiting the issue of enhancing the investigatory powers of the SFO in foreign bribery cases. This will be particularly important once SOCA takes over from NCIS and could help bridge the intelligence gap identified under the previous system⁸². As the consultation paper says "the buck stops with the SFO in foreign bribery

cases.”⁸³ To make progress the SFO needs the high burden of proof required to open an investigation to be lowered and it should take a pro-active approach to evidence gathering to build cases for prosecution. However, such powers will not be a panacea and the resources must be provided to ensure that they can be properly utilised. The full range of detective and investigative police powers should also be used in conjunction with new SFO powers.

The limbo-like state of anti-corruption legislation, the fragmentation and under-resourcing of investigatory and enforcing agencies all indicate a lack of political will at the highest levels to take a lead in tackling global corruption. The AAPPG hopes that following the new commitment to Africa shown during 2005 through the G8 and the Commission for Africa this will be remedied quickly.

In addition to prosecutions, civil and administrative sanctions are also necessary for an effective enforcement system. A system of debarring companies from public procurement (including individuals and agents) convicted of corruption, or where evidence of corruption is overwhelming, should be introduced. The World Bank makes publicly available the list of all those companies barred from World Bank contracts. At the time of writing over 40 of these were UK based⁸⁴. In implementing the EU Procurement Directive it is important that the responsible agency, the Office of Government Commerce, monitor progress and make explicit the reasons for any utilisation of the exception provided for in the directive. It should set up a national database and push for an EU wide database to exclude companies convicted of corruption from public procurement across the EU.

In line with USA practice, companies convicted of foreign bribery offences, whether at home or abroad, should also be barred from receiving UK Government export advocacy, including trade missions and export credit.

The Government should also consider suspending export advocacy for UK companies who have bribery cases pending. At least one major UK company under investigation by the SFO for foreign bribery continues to receive export advocacy from the UK Government as well as export credit. Losing government support can be as great a threat to a large company than a fine and the Government should review at what precise stage such benefits might be suspended; when the investigation opens, when a charge is brought or once a conviction is made. Although the principle of innocent until proven guilty should not be undermined, the advantage of using such sanctions early on is that it will encourage a company to cooperate with an investigation to ensure swift completion. In the USA procurement officials base debarment not simply on conviction but on an assessment of evidence available.

International Cooperation

Clearly, the international nature of the problem of corruption requires high levels of international cooperation in terms of prevention, investigation and prosecution. The AAPPG recommends the UK government continue to work with international partners on raising anti-corruption standards. One important way in which the UK Government can do this is by actively supporting non-OECD members to sign up to the OECD convention and join the Working Group on Bribery in International Business Transactions. Other countries, attempting to tackle bribery, can learn from the peer review process. Already Estonia and Bulgaria are taking part and it would be beneficial if larger non OECD trading partners such as India, China and Brazil decided to do the same.

BOX 4.3

The OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (1997) Phase Two Review (2005)

The UK ratified the OECD convention on bribery in 1998 and it came into effect in 1999. In its most recent (Phase Two) evaluation of the UK's adherence to the convention the OECD Working Group on Bribery identified a number of outstanding issues as well as areas where significant progress had been made. The report also praised the professionalism and cooperation of the UK officials.⁸⁵

The report states that there had been "no significant progress" on this issue of comprehensive legislation since the Phase One report, issued in 2000⁸⁶. The report criticises existing anti-corruption legislation as "characterised by complexity and uncertainty"⁸⁷ it has significant gaps such as foreign members of parliament and third party beneficiaries, and criminal liability for legal persons

The report also criticised the draft corruption bill, which has also been criticised by the Joint Parliamentary Committee. In particular the draft did not mention the categories of foreign public officials the OECD convention identifies, and it meant that for a bribe to be illegal the bribe giver must believe that the official would act 'primarily' because of the bribe - a belief which would be difficult to prove of a defendant in a court of law. The draft also left the loophole for bribe paying through an intermediary (even though this is most often the process) or for benefiting a third party.

The OECD report stresses that it is "surprising" that no company or individual has yet been brought to court for bribing a foreign public official. The report was highly critical of the coordination of the numerous UK agencies involved in enforcement and stated that efforts are fragmented and expertise dispersed.

The OECD is also critical about the "extremely high level of proof required to open an investigation into suspicious transactions"⁸⁸, the lack of use made of investigative tools outside of the domestic sphere and the lack of a pro-active approach to foreign bribery.

The OECD also points out that in deciding whether to take a case forward the UK authorities have been taking into consideration possible impact on the UK economy or its relations with other states - something which is specifically proscribed by Article 5 of the Convention. Indeed, the current requirement for law enforcement authorities to seek the

consent of the Attorney General, to inform the FCO and - where involving defence - the MOD, all led the OECD to conclude that these stipulations must be for political purposes.

They also suggested that greater use could be made of the Asset Recovery agency and its power under the Proceeds of Crime Act in confiscation of assets relating to foreign bribery cases.

Other OECD countries' progress

The UK is not alone in receiving criticism from the OECD Working Group on Bribery, and in some respects it is important to note it may be ahead of some other countries.

For example, while the Working Group noted commendable efforts in Belgium it also points out that tax deductibility of undue advantages is still possible under certain conditions, it also called for increased support to enforcement agencies.

- Sweden was praised for investigation of bribery, for securing convictions in 2004 and for the particularly high level of awareness of the crime of foreign bribery. However the Working Group asked Sweden to better address their system for corporate liability.

- The Working Group described the number of investigations currently being conducted by German authorities as 'impressive' and praises numerous initiatives to raise awareness of the crime. But the Group advises better protection for whistle-blowers and an increase in the level of corporate fines.

- In Austria the Working Group lauded the significant legislative efforts, including laws to exclude companies convicted of corruption from participation in public contracts, but was disappointed at the lack of awareness of the offence of foreign bribery amongst Austrian business.

- Australian authorities were praised by the working group for their strong commitment and the efforts of the taxation office to detect and prevent bribe payments to foreign public officials, but were advised to make a significant increase in the recommended corporate fine.⁸⁹

Export Credit Agencies

Using taxpayers' money export credit agencies underwrite export contracts, thus reducing risk for companies wishing to export, particularly to countries with less than perfect credit histories. Most OECD countries have an export credit agency.

If a project underwritten by an export credit agency has been secured or maintained by using bribes, in effect taxpayers' money is used to underwrite bribery. The AAPPG believes that export credit agencies should therefore have the highest anti-corruption standards in order to protect the integrity of taxpayers' money.

In the UK the Export Credits Guarantee Department (ECGD) reports to the Department of Trade and Industry. The ECGD's outturn figures for the value of guarantees and insurance in financial year 2004-05 was around £2 billion⁹⁰.

In May 2004 the ECGD issued new and robust anti-corruption guidelines, giving the UK a reputation of leadership on the issue anti-corruption in export credit. However, these guidelines were modified following concerns raised by some of

ECGD's regular customers in a CBI led group⁹¹. The AAPPG was very disappointed with the modified guidelines then issued, without public consultation, in December 2004.

To settle a court case brought by the NGO Corner House the ECGD agreed to hold a public consultation, to which the AAPPG made a submission. The key point in our submission related to the use of agents in bribe payments, which we felt were better addressed in the May 2004 guidelines than the December 2004 version. The AAPPG appreciates that agents can be very useful in international transactions and business deals but also believes that the ECGD should have the right to check that such agents are not engaging in corruption on behalf of a sponsored company. If companies are not prepared to allow ECGD to make their own checks and provide ECGD with the identity of any agents and details of their commission then they can take their business elsewhere. Companies receiving UK export credit should not allow agents to tarnish their reputation or indeed - by extension - the UK's reputation.

It is precisely through the use of these agents that companies have been able to keep within UK law while turning a blind eye to corrupt practices, carried out on their behalf and often with their tacit but not explicit approval. Such practices make a mockery of attempts by the UK Governments and by African Governments to crack down on corruption. The AAPPG also expressed concern about the inclusiveness of no bribery warranties and the removal of the right of ECGD to conduct spot checks on companies without prior warning.

The AAPPG reiterates the recommendation made by the Commission for Africa and the G8 communiqué regarding higher standards amongst ECAs (see box 4.1). Given it is now up to the UK to take the lead within the international community in implementing the Commission for Africa's recommendations, and the decisions of the Gleneagles G8 summit chaired by the UK, it was embarrassing that we watered down our own export credit anti-bribery standards. Indeed, it created discomfort among both anti-corruption campaigners and UK business leaders who want to be at the vanguard of anti-corruption and CSR initiatives. As one business expert, who was present at UN Global Compact meetings in New York, said:

"...The decision made to water it [ECGD anti-bribery guidelines] down had a profound impact internationally, and not to the UK's advantage. Frankly it undermined the UK in international discussions on corruption."⁹²

Latest Developments

In March 2006 the Government published its Final Response to the Export Credits Guarantee Department's consultation on the changes made to its anti-bribery and corruption procedures in December 2004. The Government was undoubtedly faced with representations from anti-corruption campaigners and

businesses which would not always be easy to reconcile. The AAPPG is very pleased that in producing new guidelines the Government has taken on much of the criticism made about the changes made to the guidelines in 2004 and in effect re-affirmed its commitment to ending bribery in sponsored projects, while also considering concerns of businesses such as commercial confidentiality.

In particular the new guidelines will require exporters to provide the ECGD with the name of any agent acting 'on their behalf' in a transaction. The AAPPG believes that this is a welcome and important change ensuring that exporters will no longer be able to refuse ECGD access to such information on grounds of commercial confidentiality. We hope the ECGD will ensure that no loophole is left for use of undeclared agents by another member of the consortium. Secondly the ECGD guidelines will include anti-corruption declarations which must include affirmation they have carried out checks on parent and sister companies, joint venture partners and agents. However, the AAPPG is not clear why non-controlled subsidiaries should not be subject to similar checks.

Also the AAPPG is pleased to note the re-introduction of ECGD's powers to conduct random audits or spot checks on sponsored companies, where corruption is suspected, this should be an important deterrent to companies not to turn a blind eye to corrupt practices.

The AAPPG looks forward to robust implementation of the new guidelines and would welcome annual publication of any information of how the procedures are working in practice.

The UK is now in a better position to take a strong stance at the OECD negotiations for improving the OECD Action Statement on Combating Bribery in Officially Supported Export Credits and thus help to raise the international bar in terms of transparency and integrity in all export credit sponsored projects.

BOX 4.4

Example: Bonny Island LNG Plant, Nigeria

The French and US authorities have opened investigations into allegations of bribery by a major consortium, TSKJ, in securing contracts for a liquefied natural gas (LNG) plant in Nigeria at Bonny Island. The UK authorities have not opened their own investigation even though one of the consortium member companies, MW Kellogg, is UK based and the agent alleged to have facilitated the bribes is British, resides in the UK and uses a company registered in Gibraltar. Furthermore the UK's ECGD gave £127 million worth of support to MW Kellogg, the UK Subsidiary of US company Halliburton, for the project⁹³. The consortia are also alleged to have met in a London hotel⁹⁴.

Because the French investigating authorities have made public much of the information it is known that the agent is UK based lawyer named Jeffrey Tesler, whose fee, subject to securing of a contract for TSKJ, appears to have been US\$51 million. It is alleged that the agent was the channel through which bribes were paid to Nigerian officials in order to secure the contract. Halliburton has admitted to the US Securities and Exchange Commission that such payments were made⁹⁵. Mr Tesler also apparently admitted to

making two payments totaling \$75,000 to M.D. Yussuf, former chairman of the Nigeria Liquid Natural Gas project, for helping to arrange meetings between the consortium and the then President, General Sani Abacha⁹⁶. Documents relating to the French investigation have also led prosecutors and journalists to allege that a \$180 million slush fund was set up by a part of the consortium⁹⁷.

In securing export credit from ECGD MW Kellogg had signed a no bribery warranty for the project, stating that neither it nor anyone acting on its behalf would pay a bribe. The ECGD also claimed in 2004 that it undertook usual due diligence checks, which revealed nothing adverse in relation to the parties involved in the transaction⁹⁸. This raises questions about the effectiveness of ECGD's due diligence checks at that time in so far as they did not raise any suspicions about large payments being made to a UK based agent for ill-defined services.

In the version of the ECGD guidelines published in May 2004 due diligence procedures would have meant MW Kellogg would have had to declare that an agent had been employed by its affiliate companies in the consortium and state what services the agent was providing. The bribery warranty, under the May guidelines, would have included a declaration by MW Kellogg that "to the best of its knowledge and belief" none of its affiliates or any agents would pay bribes. However, under the revised December 2004 guidelines MW Kellogg would not have had to declare use of an agent by the consortium⁹⁹. ECGD should consider carefully whether its new guidelines would have addressed this issue comprehensively.

Despite US investigations into Halliburton, in September 2004 the ECGD issued its subsidiary Kellogg Brown and Root with an offer of export credit for a major project in Kazakhstan,¹⁰⁰ something that might be better put on hold until investigations were completed.

Mispricing

The practice of mispricing is alarmingly widespread but even more alarmingly under-reported. The method is used to move money illegally between countries by companies and individuals, to avoid tax or misappropriate or embezzle funds. It is a simple practice: a secret agreement by the buyer and seller to misprice a project or item to allow the difference between the real price and the book price to be diverted, often to a private offshore bank account.

Mispricing is a global problem, but developing countries seem to be hit particularly hard as it is an effective vehicle for looting and laundering government resources. While by its nature it is difficult to estimate the volume of such hidden transactions, research suggests that mispricing drains \$100-150 billion flows out of developing and transitional economies each year¹⁰¹. One estimate suggests that in Africa 60% of trade transactions are intentionally mispriced by an average of over 11%¹⁰². One study suggested that capital flight from Russia to the USA via mispricing scams in the latter half of the 1990s could add up to as much as US\$8.92 billion¹⁰³.

As with many other scams President Mobutu of Zaire was a pioneer. Millions of diamonds were exported from Zaire, via the state company *Gecamines*, for

prices as low as \$8.55 per carat (well under market price), while the rest of the value of the stones was deposited in Mobutu's overseas accounts¹⁰⁴. In effect mispricing was being used as a mechanism for massive embezzlement and laundering of government money.

The mechanism also works in the opposite direction, with corrupt officials arranging for the import of items at inflated prices, for the purpose of government accounts, with the extra, or the 'kickback' being diverted to personal accounts, again usually abroad. Examples include the importing of handcuffs to Kenya at a delivered value of 1,000 Kenyan Shillings, but invoiced at 3,500 so that somebody made more than 150% profit on each set¹⁰⁵. In the health sector also there have been serious problems of inflated prices in procurement of pharmaceutical drugs¹⁰⁶. Mispricing in public procurement means government resources are being embezzled.

Companies may agree to irregular payment methods, not necessarily so they can share in the kickback with the corrupt party - though this may also take place - but simply in order to secure a desired sale or purchase. Western companies, including British companies are implicated in some mispricing or re-invoicing scandals. UK banks and offshore shell companies are implicated in laundering the proceeds.

Mispricing is not only a problem for public procurement and national exports. Cases exist from Nigeria and elsewhere of privately owned firms being purposely run at a loss – according to the books – because imported goods used by the company are being bought at hugely inflated prices, the difference being siphoned off into private offshore and tax free bank accounts¹⁰⁷. In effect a company owner or manager may run his own company into the ground to make a quick and tax free profit. Such a company does not contribute to the development of an economy but is merely a vehicle for tax evasion and capital flight.

A number of London listed companies have been implicated in the UN oil for food scandal. For example, a mispriced contract allegedly inflated by \$8million was reportedly used to recover debts owed to BHP Billiton¹⁰⁸. This case indicates that it is possible to uncover mispricing where the will and mandate exists to do so. Information regarding the involvement of UK-listed Sphynx UK in mispricing oil exports from the Republic of Congo's state oil company have come to light only because of a UK Court case brought by the government's private creditors who have suffered from oil backed loans they provided to the Republic of Congo's government (see box 5.4).

The AAPPG does not pretend that tackling the problem of mispricing will be easy. However, more has to be done to make a dent in the practice, particularly where it occurs in the public sector. More transparency and greater detail in government and company financial reporting are required. This would at least reveal if a country is importing bicycle tyres for \$364 dollars each. In the USA

such information is available – allowing one researcher to point out that Russia was indeed purchasing bicycle tyres from the USA for that price, despite their average cost being around \$3. In the UK such information is not available, though the same researchers, using US statistics, say one USA importer bought toothbrushes from the UK at a cost of \$5,655.55 per unit¹⁰⁹.

Secondly in the paper-work of all import-export transactions both buyer and seller should be required to put their signatures to the price to confirm that the price quoted in the paper work is both the price paid and the price received. This simple mechanism could have a major impact on the scam and therefore on corruption, tax evasion and capital flight.

We urge the UK Treasury, which has already expressed its commitment to supporting international development, to review urgently national and international safeguards against mispricing and its impact on development and capital flight.

Transfer Pricing

Some transnational companies use a similar practice known as transfer pricing in which internal mispricing helps minimise tax payments in various jurisdictions in which they operate. One ex-Jersey resident has recounted in detail how his work for a trust and company administration business revolved around facilitating and laundering the proceeds of transactions many of which removed profits from African divisions of a company to the Jersey division. Thus the profits show up in Jersey, where tax on profits is low, rather than in the jurisdiction where the profits were made¹¹⁰.

Transnational companies should provide financial reporting figures disaggregated for each of their subsidiaries, so that if, for example, an oil company appears to be making minimal profit in its operations in an oil producing country yet a very high profit in its offshore subsidiary, questions can be asked. A number of NGOs are calling for an International Financial Reporting Standard, which would involve companies divulging more details about where profits are made within its international operations¹¹¹.

A leading researcher in this area estimates that \$200-280 billion per year leaves developing and transitional economies through the transfer pricing mechanism¹¹².

Much of this work is the *raison d'être* for some companies. For example 'Offshore Inc.' gives a detailed explanation for newcomers about re invoicing; how it is done and how it can help them accrue profits in tax havens to minimise tax payments¹¹³. 'International Tax Adviser' boasts its use of offshore companies to avoid tax and the use of re invoicing to transfer profits overseas¹¹⁴. Trident Trust

offers a 'comprehensive re-invoicing service' to help trading companies 'reduce their overall tax burden'¹¹⁵. The list goes on.

While tax avoidance is not illegal, tax evasion is. The UK Exchequer would benefit greatly from focussing on the illegal side of this practice. A review of the problem, its effect on capital flight from developing countries and the implications for developing country revenue collection should be carried out.

Commodity Backed Loans

Developing countries are eligible for loans from international financial institutions and aid donors at repayment rates lower than those offered by the private sector. In response to corruption in some developing countries, international bilateral and multi-lateral donors have implemented safeguards, which, while not foolproof, reduce large scale opportunities for misappropriating these loans and other international aid. However some countries have instead chosen to take out high interest loans with private consortia, which are guaranteed by the borrower's future earnings through resource exploitation. One well-known example is the Angolan government's oil backed loans. The IMF offers better terms for long term loans than these private consortia but more than once the Angolan government has chosen to use private oil-backed loans. One NGO reports that the Angolan government raised US\$3.05 billion in one year alone, through oil backed loans, despite agreement with the IMF to limit borrowing¹¹⁶. One 2003 loan is serviced through a Special Purpose Vehicle in the Cayman Islands (a UK Overseas Territory). A 2004 loan of US\$2.35 billion came from a private consortium including UK-based Standard Chartered, Barclays and Royal Bank of Scotland, according to Global Witness. Despite public criticism of the loan, Global Witness allege the London branch of a company is arranging a \$2 billion follow up deal¹¹⁷.

Oil backed private loans taken out by the Republic of Congo (ROC) have been condemned by the IMF as a breach of its commitment to agreements with the Fund.¹¹⁸ These short term advances from oil buyers to the ROC state oil company have also been blamed for much of the country's debt, and their use seems hard to justify. With average terms of just 27 days but annualised costs of 40% in 2004 and 170% in 2003 they are poor value for money for the ROC Treasury and indicate poor fiscal management and possible corruption. One short term advance to the ROC made by a UK registered company is estimated to have cost the ROC almost US\$5 million¹¹⁹.

Such loans – some of them from British banks¹²⁰ – are perfectly legal but they are condemned by the IMF and World Bank because they do not adhere to the same transparency guidelines and undermine their efforts towards fiscal transparency. They may also conflict with the banks' own corporate social responsibility guidelines. With poor transparency which facilitates theft by officials, such loans often leave lenders out of pocket as borrowing governments default on loans¹²¹. In cooperation with the IMF and international donors already working on with

such countries on transparency banks and companies should review transparency and accounting requirements, including disclosure and oversight mechanisms on government borrowers for such loans.

Business leadership?

The AAPPG is grateful to those businesses which responded to our call for written evidence¹²². It is clear that some companies are serious about internal anti-corruption and in some cases anti-money laundering strategies. This shows an encouraging high level commitment to fighting corruption and money laundering.

Corruption is becoming less and less acceptable within the private sector. Few business leaders will now publicly repeat the old adage that you simply cannot operate in Africa without paying bribes. However, despite recent significant progress, the practice still exists. UK companies are not the worst offenders – the UK is ranked eighth by the Transparency International Bribe Payers Index of those least likely to pay bribes in a survey of 21 countries¹²³. However the AAPPG believes that UK companies, with Government support, could and should lead the way in integrity in international business transactions and work with companies from other countries which are just beginning to re-assess such practices.

On the other hand some business leaders fear that advances in corporate social responsibility amongst western companies may put them at a disadvantage to Chinese, Russian and other companies that are now big players in international markets, not least in Africa. However, this should be seen as an opportunity for UK companies to share best practice with new players. Indeed one UK business expert described Chinese business leaders as “hungry for information” and “anxious” to know how western companies now operate in developing countries¹²⁴.

Larger companies can and should also take the lead by supporting small and medium enterprises at home and abroad to develop robust anti-corruption strategies as part of broader CSR policies. For example, Indonesian small businesses are using a training pack developed by BP¹²⁵. Business groups such as Business Action for Africa and the country networks of the UN Global Compact are also contributing to this.

Organisations which provide companies with access to capital have a key role to play in turning the tide against bribery. Major stock markets, fund managers and others who wish to ensure their investments are socially responsible can make demands on companies with regards to corporate social responsibility, including anti-corruption, and these can have a real impact on companies internal anti-corruption policies and practices.

As discussed above private lenders can also look at how to ensure their lending to governments with major corruption problems can be responsible by working with the International Financial Institutions also working in those countries to improve fiscal transparency.

The introduction of anti-bribery criteria to the FTSE4Goods Index Series is a good example of how countering bribery is now an important issue for investors¹²⁶.

Voluntary Initiatives

The AAPPG welcomes the work of the UK Government to establish and support the Extractive Industries Transparency Initiative. It is testament to the initiative's success that there are calls for similar initiatives in other industries.

However, recent research by UK NGOs indicates that the flexibility available within EITI means that some companies are working harder than others to improve transparency and their internal anti-corruption initiatives. In a survey of 25 international companies the NGOs scored companies on a combination of transparency of revenue payments, supportive disclosure and anti-corruption and whistle-blowing; Canadian company *Talisman* scored highest, British-Dutch *Shell* scored third British company *BP* sixth and UK based *Premier Oil* scored 20th.¹²⁷

A group of UK based NGOs are now calling for an International Financial Reporting Standard (IFRS) for the extractive industries. They say further disclosure would improve both transparency and tax collection within countries where profits are accrued¹²⁸. The UK Government should consider taking this initiative forward with a group of UK companies willing to take a lead.

Clearly the EITI is no panacea but its progress so far is very welcome and the AAPPG commends the UK Government, particularly DFID, for its continued support for the initiative and its continuing efforts to implement the initiative in resource-rich countries and amongst extractive industry companies internationally.

DFID has supported the development of EITI and other initiatives, including the diamond development initiative. But, it is unclear how much similar support for progressive CSR policies have come from other Government departments such as the DTI and FCO.¹²⁹ Given the commitments made by the UK Government as a whole, international CSR, including anti-corruption, should be a matter for all three departments. Indeed the recent announcement by the Chancellor of the Exchequer to abolish the Operating and Financial review (OFR), apparently without broad public consultation, does not seem consistent with this priority¹³⁰.

The UN Global Compact is a voluntary initiative to encourage responsible corporate action on all fronts from the environment to human rights. Its 10th

principle calls on business to work against all forms of corruption including bribery and extortion. The UK Network on the Global Compact lists 78 participants¹³¹.

Other business-led initiatives also exist, some industry specific, some broader; some in partnership with government or NGOs, others designed by business groups. Indeed some companies have complained that there are so many initiatives that it can be difficult to know which to choose¹³².

One industry specific initiative set up by business with the support of Transparency International is the UK Anti-Corruption Forum – which concentrates on the infrastructure construction sector, considered the most prone to corruption of all sectors. The Forum has produced an action statement which both acknowledges the continuing existence of corruption in the construction sector, calls for actions from construction companies, associations, banks, export credit agencies and governments. It also recommends a blacklisting system. The World Bank uses a blacklisting system to ensure corrupt companies are banned from bidding for contracts. This system helps honest companies who may withdraw from bids when they find themselves competing with companies that are known to use bribes.

Companies may publicly embrace these voluntary anti-corruption initiatives but *monitoring the implementation* of voluntary initiatives throughout their operations is minimal and usually internal. This means that companies can sign up to initiatives but do little to ensure they implement them or abide by their principles, undermining efforts made by those companies that do so. A three phased approach to monitoring may be helpful. In the early stages companies can conduct internal reviews, as described in the TI Business Principles on Countering Bribery. Many companies are already doing this. Some companies involved in the Global Compact are also now discussing the establishment of peer review panels to monitor implementation within business. Ultimately external review should be the goal; but given the difficulty in achieving this on a voluntary basis, structured peer review, involving external experts on the panel should be encouraged and supported.

Policy Coherence

With so many strands in tackling this problem and so many different Government Departments involved, the AAPPG recommends that the Government appoints an Anti corruption champion, for a limited period such as two years to coordinate and progress policy coherence and implementation across Whitehall and to work with the devolved executives, Overseas Territories and Crown Dependencies to do the same. This person should be of a senior level, who commands respect across Government departments.

Headline recommendations to tackle corruption

All the recommendations of the AAPPG are given in Section 2. Those most relevant to the issue of tackling the supply side of corruption are also given below.

Rigorously enforce existing laws and sanctions against international bribery, corruption and money laundering.

Bring to Parliament before the end of 2006 a new Anti-Corruption Bill which addresses the concerns raised about the 2003 draft Bill by the Joint Parliamentary Committee and the OECD Phase Two Review.

Ensure that Crown Dependencies and Overseas Territories deal with corruption and money laundering as robustly as the UK.

Appoint an Anti-Corruption champion for a two year period to coordinate policy coherence and implementation across Whitehall and to work with devolved executives, Crown Dependencies, Overseas Territories and international partners.

Further Recommendations

<i>Tackling the supply side of corruption</i>
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A. The Framework

Establish effective systems to monitor the implementation of the UN Convention Against Corruption by its signatories.

Ensure the full extension of the UN Convention Against Corruption and the OECD Convention on the Bribery of Foreign Public Officials to the UK's Crown Dependencies and Overseas Territories.

B. Investigations

Take a pro-active approach to detecting international bribery, opening investigations and actively cooperating with mutual legal assistance requests. Require all government departments including HM Revenue and Customs to pass on evidence of bribery they come across. Provide training to Revenue and other staff on detecting signs of bribery.

Ensure that new arrangements between investigating and enforcement agencies are backed with resources and the necessary powers to carry out investigations. Ring fence human and financial resources for investigating international corruption to ensure this area is not squeezed out by other priorities.

C. Policy Coherence

By the end of 2006 review the anti-corruption policies of all UK Government departments particularly in relation to procurement and encourage the devolved executives, Crown Dependencies and Overseas Territories to do the same. By the end

of 2007, in line with World Bank procedures, introduce a list of companies barred from government procurement because of corruption convictions or overwhelming evidence.

Robustly enforce the newly revised ECGD anti-bribery and corruption guidelines¹³³ and work with other export credit agencies to continually review best practice and ensure a high standard globally.

As soon as possible carry out a review of international safeguards against mispricing and examine the impact on developing country capital flight. The review should include:

- the introduction of mandatory price-related signatures from buyers and sellers for all transactions over £10,000
- the links with international tax evasion and transfer pricing and the capital flight involved

D. Working with Business

Following the passing of a new Anti-Corruption Bill through parliament conduct a thorough prevention and education campaign for the UK business sector.

Use Government trade support and advocacy services, to inform companies about the illegality of bribe payments, the damage they do to development, and methods of avoiding solicitations for bribes; for example through the UK Trade and Invest literature

Require companies receiving Government trade support and advocacy or companies seeking government funded contracts to sign no bribery warranties from mid 2006 onwards.

Bar those convicted of corruption offences from receiving government trade assistance, including participation in trade missions.

Educate UK companies about the use of mispricing in transactions as a mechanism to embezzle and launder funds, using an information campaign and existing government to business services.

Encourage UK banks to re-asses the compatibility of commodity backed loans with their corporate social responsibility guidelines and encourage them to take advice from the international financial institutions on appropriate levels of disclosure and oversight mechanisms for money disbursed.

Encourage UK businesses to take an active role in the UN Global Compact and other voluntary initiatives and support UK companies in implementing the initiatives throughout their operations.

Discuss with UK business leaders how best to monitor implementation of voluntary anti-corruption initiatives externally.

5. Our Role in Tackling Money Laundering

In addition to contributing to the supply side of corruption in Africa, as discussed in the previous section, the West has historically also played a major role in laundering the proceeds. This chapter looks at the issue of money laundering, the role of the West in laundering the proceeds of corruption, current mechanisms for tackling it and remaining loopholes. The focus is on the UK, its Overseas Territories and Crown Dependencies.

Background

By its very nature laundered money is impossible to quantify accurately. The IMF has estimated that money laundering may account for as much as 5% of the world economy¹³⁴. One researcher suggested that globally, illicit cross border flows are in the order of US\$1 trillion and that around half of this comes out of developing and transitional economies¹³⁵. It is further estimated that US\$100-200 billion is from Africa – that is 10-20% of the total of illicit cross border flows is coming out of the continent that produces just 3% of world GDP¹³⁶.

The subtotal for illicit proceeds laundered internationally which are directly attributable to corruption is estimated at US\$50 billion. The bulk of the remainder comes from the proceeds of crime and illicit commercial activities, including tax evasion. But the dividing lines between the criminal, corrupt and commercial components of this figure are blurred. For example mispricing is classified as commercial but can be used in the public sector to misappropriate public funds (see Section 4). Similarly, corruption and organised crime can be linked.

The proceeds of corruption do not always need to be laundered internationally. Often transactions take place in cash and never show up in any documentation since they are spent locally (or internationally) in cash. Clearly in the case of petty corruption money is solicited and spent locally, but this is also true of much large scale corruption. However, the proceeds of many of the biggest thefts of public property, have to be laundered, either as money or as goods such as real estate and fine art.

While Switzerland and Lichtenstein gained international infamy during the 20th Century for a secretive banking industry which facilitated money laundering, other financial centres have also been implicated. Indeed some recent research suggests that in some respects the City of London is lagging behind the Swiss in tightening up on money laundering and implementing commitments to repatriate the proceeds of international crime and corruption.¹³⁷ Houses in expensive London suburbs such as Notting Hill have joined Monaco on the list of favourite real estate acquisitions for corrupt leaders from across the developing world. There have even been concerns raised regarding sales of sports clubs in the UK¹³⁸. Some pundits have begun referring to the City of London as 'The Laundry

of Choice' causing embarrassment to the UK's international reputation¹³⁹. Furthermore, many of the most active offshore banking jurisdictions are UK Crown Dependencies or Overseas Territories, further complicating the UK's role in facilitating money laundering.

Box

General Abacha and the missing billions

One of the world's most infamous kleptocrats, General Sani Abacha, was President of Nigeria between 1993-1998. In that time it is estimated he, his family and close associates, managed to steal between \$3 billion and \$5 billion from the Nigerian people¹⁴⁰. Investigations following a change of Government in Nigeria have revealed a great deal about how and where the money was laundered and the difficulties in tracing, freezing and repatriating the stolen funds.

Abacha money in the UK

Investigations by the Financial Services Authority (FSA) completed in 2001 indicate that in excess of US\$1.3 billion linked to Abacha went through 42 bank accounts in the UK between 1996 and 2000. This figure represents more than 20% of the estimated total stolen by Abacha and his entourage.¹⁴¹

The FSA found that 15 UK banks had 'significant weaknesses' and that 98% of the money went through those banks¹⁴². The FSA did not declare the names of the banks involved despite the decision by the Swiss authorities to do so with Swiss Banks. This led to significant criticism of the FSA for protecting the culprits and lessons can be drawn and applied for similar cases in future. The experience of this investigation in tracking stolen assets showed both what can be achieved and the recurrent problems, in particular the time lag difficulty: it takes longer to launch an investigation and track assets in order to be at the stage of freezing those assets than it does for an accountant or banker to move those assets elsewhere.

The Abacha case was a watershed investigation in the UK and one that we should both learn from and build on. The UK Government has since established a 'Preventing a Future Abacha' Working Group, set up in 2004 and reporting to the Corruption Overseas Committee in September 2004. The working group noted that one problem was the lack of powers to freeze assets at the investigation stage¹⁴³.

Freezing and Recovering Abacha Money: Civil Action by the Government of Nigeria

The Nigerian Government has attempted to recover \$2.2 billion looted directly from the state by Abacha and close family and associates. Much of this has been recovered or frozen, as follows:

- Voluntary returns made by the Abacha family: \$750m
- Funds paid in settlement of claims against Bagadu, Abacha's 'right hand man': \$150m
- Repatriated from Switzerland, following supreme court proceedings: \$600m
- Monies frozen in Lichtenstein, Luxembourg and Jersey: \$750m
- Further monies to be remitted from Switzerland, pending a court cases: \$70m
- Sums frozen in British banks: \$40m¹⁴⁴

The AAPPG would like to emphasise that the UK financial sector is generally well regulated and internationally well regarded and we see its profitable operation as an important part of the UK's economy and international reputation. London as a financial centre is a world leader, with a 50% share of European Banking activity, the world's top city for institutional equity holding it also has 36% of the global

turnover of the 'over the counter' derivatives trading market and more *foreign* banks than any where else. By mere virtue of its size of London's financial sector is at risk of laundering more money than a smaller financial centre despite good regulation and practice. We therefore feel that the term 'laundry of choice' may be unfair.

We do however, feel that one or two areas could be further tightened up in order to assure the sector's reputation as a world leader not only in terms of profitability but also in terms of responsibility. We believe the UK financial sector has the capacity and skills to take that lead internationally. We also believe the UK should be working to ensure the same issues are addressed in its Crown Dependencies and Overseas Territories.

Box 5.2 **Equatorial Guinea and Friendly International Bankers**

The IMF has raised concerns about discrepancies in the Government of Equatorial Guinea's transparency and the lack of development for the vast majority of the country's population, despite earning hundreds of millions of dollars from oil. In response to requests for greater transparency the government spokesman said that it was up to the government what it does with the money¹⁴⁵. Investigative journalism has revealed that much of this money has been looted by government officials, not least by the President and his family, and laundered and banked overseas.¹⁴⁶

The LA Times reported that US\$300-500 million had been deposited in a Washington DC Branch of Riggs Bank. The article also suggests that this account was controlled personally by President Obiang and that it had received payments from Exxon Mobil and Amerada Hess. The Government of Equatorial Guinea says this account was an official Treasury account. However the same banker who managed this account also facilitated Obiang's personal purchase of two luxurious houses in the USA and another by his brother, who is also head of Equatorial Guinea's armed forces.¹⁴⁷ A US Senate Minority Report revealed that there were over 60 accounts in Riggs belonging to Obiang and his government containing around US\$700 million. At one point, Riggs accepted over US\$11 million paid in from suitcases for an offshore account controlled by Obiang and his wife, according to the report¹⁴⁸. Following a federal investigation Riggs was penalised for its activities in 2004.

UK based HSBC and Spanish Abbey owner BSCH have also been implicated in this case. Both received transfers from official oil accounts at Riggs to offshore accounts which US investigators believe to be controlled by Obiang. HSBC apparently opened accounts for one such company in Luxembourg and Cyprus. Banking secrecy laws have protected the beneficial owners of these accounts, blocking further investigation by US authorities¹⁴⁹.

Recent Changes to the Legal and Regulatory Framework

General Abacha and many other criminals were able to launder the proceeds of their corrupt activities through the UK because of significant loopholes in the regulatory system at that time and because of the low priority placed on, or even ambivalence to, the fight against global corruption by both Government and the financial sector. Since then the situation has changed significantly but problems remain.

The global political will to fight money laundering has grown since 2001, as the financing of terrorism became an issue. The Financial Action Task Force (FATF) has produced an updated version of its '40 recommendations' and later issued a further nine recommendations specifically to cover terrorist financing. In response to this the EU has produced three money laundering directives. The Third is yet to be implemented by the UK and much of the EU.

The FATF set global standards on issues to which a blind eye was previously turned. For example, the FATF points out that financial institutions have traditionally afforded discretion to the financial activities of Politically Exposed Persons (PEPs) and their representatives. They now see this practice as an obstacle to both detection and investigation of crimes in which such people may be involved.¹⁵⁰ Their recommendations have set the trend for showing enhanced 'due diligence' for international PEPs. This has fed into domestic and regional legislation, including in the EU.

The Regulatory and Legal Framework in the UK Today.

Inter-Agency Relations

The Financial Services Authority (FSA) is the regulatory body for the financial sector in the UK. Its objectives include to promote confidence in the UK financial system and to reduce the scope for financial crime¹⁵¹. It works with representatives of the regulated sector, including the Joint Money Laundering Steering Group (JMLSG) which provides non-compulsory industry led guidelines.

HM Treasury takes the lead in developing the UK's anti-money laundering strategy and implementing the relevant EU directives. The Home Office is responsible for primary legislation including the Proceeds of Crime Act. The National Criminal Intelligence Service (NCIS) receives Suspicious Activity Reports (SARS) and forwards these to the relevant law enforcement authorities including police authorities and the Serious Fraud Office (SFO). The usual devolved prosecution authorities are responsible for bringing prosecutions. The recently established Assets Recovery Agency (ARA) is responsible for domestic asset recovery and under the 2002 Proceeds of Crime Act has some power to assist overseas authorities in relation to civil cases. Where there is a criminal investigation/prosecution in another jurisdiction the CPS' central confiscation branch, would be the point of contact, not the ARA.¹⁵²

The pending dissolution of NCIS and establishment of the Serious Organised Crime Agency (SOCA) means that the intelligence dimension of the system is currently in flux. In a recent consultation paper the Home Office has suggested increasing the intelligence remit and 'Chapter Two' powers of the Serious Fraud Office in cases of foreign bribery, suggesting that the 'buck stops with the SFO' in such cases. Taking a similar approach to money laundering might be useful. Because there are several agencies involved in preventing, investigating, acting

on and enforcing money laundering issues, there needs to be more clarity on who is ultimately responsible. SOCA is tasked with concentrating on international drugs and terrorism and the AAPPG suggests that international corruption should receive similar attention and resources.

The New Legal Framework

The UK's anti-money laundering regime is based on the 2003 Money Laundering Regulations, which followed two EU Directives and recommendations made by the FATF. These regulations are far more comprehensive than previous ones and they include less obvious sectors through which monies may be laundered, such as real estate, bureaux de change, the art market and casinos.

However Transparency International has criticised the UK's failure to implement an "effective supervisory regime" to regulate those providing services to trusts and unlisted companies.¹⁵³

Since then the international bar has been raised and the UK now needs to implement the Third EU Money Laundering Directive, as soon as possible, the AAPPG hopes well before the December 2007 deadline. This directive was agreed following further recommendations made by the FATF. In particular it includes:

- Explicit coverage of terrorist financing
- New definitions of 'politically exposed person', 'beneficial owner' and 'business relationship'
- More detail on customer due diligence requirements, and a risk based approach
- Licensing and registering of trust and company service providers
- Monitoring and supervision of trust and company service providers and estate agents (addressing earlier criticisms from TI)

All these are welcome additions to EU wide anti-money laundering regulations but concern has been expressed because they do not explicitly define corruption, embezzlement or misappropriation of public property, as serious crimes¹⁵⁴. It is obvious that the proceeds of corruption are the proceeds of a crime but this should be made explicit, given the confusion expressed by some including members of the regulated sector who are expected to perform due diligence checks and make suspicious activity reports. With regards PEPs it would also be beneficial to highlight the relevance of monies which have travelled through complex transactions via offshore companies, trusts and multiple jurisdictions, which should be seen as warning signs in 'due diligence' and 'know your customer' checks.¹⁵⁵

The AAPPG notes, however, that in negotiating the Third EU Directive the UK sought to keep it at "as high level as possible with the detail to be left to member

states”¹⁵⁶. The AAPPG therefore recommends the UK should use this flexibility to clarify these two issues in its domestic implementation. It is also imperative that whistle-blowers are afforded full protection to encourage them to come forward with evidence.

The AAPPG also calls on the UK to work closely with the EU on ensuring implementation of the directive right across the Union. We call on the UK Government to require Crown Dependencies and Overseas Territories to fully address the same issues within their domestic legislation and enforcement mechanisms.

The AAPPG also notes the introduction of the EU Savings Directive, the implementation of which should help the UK Exchequer tackle major tax evasion via credit cards registered to offshore bank accounts and increase the exchange of information between EU banking jurisdictions and offshore locations such as Jersey and Guernsey¹⁵⁷. Such increases in exchange of information about bank holdings will also be important in tracking the proceeds of corruption.

Box 5.3

Incorporating a Company in the UK: One day e-formation - no hassle

Company service providers are legitimate businesses which, amongst other things, assist people to register and incorporate businesses in the UK and elsewhere. However, incorporation of a company through these service providers is now taking place via the internet with little or no checks on who is setting them up or what they are for. Many also offer services for incorporation in offshore locations and nominee director and secretary services, to ensure anonymity of beneficial owners in the annual reports filed at Companies House.

For example, one UK based company service provider is also offering incorporation of a UK company with ‘bearer shares’. According to their website for just £495 a London based company can do the paperwork and register a UK company for anyone with a credit card and access to the internet, with bearer shares. This will, apparently, take place within 6-8 working hours, when bearer shares and the minutes of the first meeting will be e-mailed to the applicant. The same service can be provided to register a UK company without bearer shares for just £42 also in 6-8 working hours.¹⁵⁸ They also offer services to assist people wishing to set up offshore bank accounts.

Another London based company offers same day UK incorporation for £50 and they also provide nominee secretaries if required. Incorporation in Jersey, Guernsey, the Isle of Mann, Gibraltar, the Bahamas and British Virgin Islands and other offshore jurisdictions can also be arranged, though it is a little pricier. For example in the Bahamas basic incorporation starts at £485, provision of a registered office is £225, nominee directors and secretaries are £200 and nominee shareholders just £60. All this can be done over the internet and discretion is assured.¹⁵⁹

Implementation and loopholes that need to be closed

Shell Companies

In 2000 a cross-departmental government report stated: “Almost all the most complex laundering operations involve UK shell companies”¹⁶⁰. Shell companies are, as their name suggests, front companies with little or no trading operations. They are often used to hide money, because disclosure of who really owns companies - beneficial ownership - is not a legal requirement under UK law and in many offshore jurisdictions, companies can be registered as directors of other companies making it very difficult to investigate who the real beneficiaries or users are. Such companies have been used to launder the proceeds of corruption in a number of cases, including the Anglo Leasing scandal currently engulfing Kenya’s government and the stolen oil wealth of the Republic of Congo laundered through Sphynx UK. In other cases UK companies or individuals have acted as agents for shell companies registered elsewhere, as apparently the case with the recent Anglo Leasing scandal in Kenya¹⁶¹.

Where such allegations are made the UK authorities need to investigate the role played by UK registered companies, service providers and individuals. This of course is hampered by the lack of information legally required in registering a company in this country. The AAPPG would endorse the statement from the Policy Innovation Unit:

“A regulatory requirement for company formation agents and other company administration agents to register the identity of beneficial owners would not only help financial investigators but greatly assist bankers and other providers of financial services to identify the customers underlying their corporate clients as part of the ‘know your customer’ requirements.”¹⁶²

In a 2004 report Transparency International UK recommended the monitoring of financial service providers. In particular they were concerned about the service of acting as a nominee director which allows the real or beneficial owner of a company to remain secret and about the UK law that allows registered directors of UK companies being themselves companies.

The Company Law Reform Bill is currently going through Parliament. Given the above recommendations made by both an NGO and the Prime Minister’s Policy and Innovation Unit (now the Strategy Unit) it is unfortunate that the drafters of the bill have not seen fit to adequately address either the issue of beneficial ownership or of corporate directorship. If an applicant has to fill in a form to register a company, provide an address and at least some nominee directors, does it take significantly more time or bureaucracy to provide the name of the real or beneficial owner, rather than rely on nominee directors or company names? The argument that it would create time-consuming red tape does not stand up to scrutiny. The real sticking point is that the secrecy currently provided by shell companies is highly valued by some, not least those who use such

companies, possibly in cooperation with offshore accounts, to launder money or evade tax.

The AAPPG recommends that relevant amendments are tabled and are supported by the Government. To fail to use the Company Law Reform Bill to address the loophole following our commitments to tackle money laundering made by the G8 and Commission for Africa, would be embarrassing. Without action UK registered companies will continue to be implicated in money laundering scandals including - but not limited to - the proceeds of corruption (see box 5.1 for the example of Sphynx UK and the Republic of Congo's missing oil money).

The AAPPG further calls on the UK Government to push for similar regulation and disclosure internationally, to remove the layer of secrecy that hides money laundering and also to encourage a level international playing field. In particular the UK must ensure that it's Crown Dependencies and Overseas Territories are not lagging behind.

Box 5.4

The Republic of Congo's missing oil money and a UK shell company

A recent UK court case, brought by a private creditor of the Republic of Congo (ROC), revealed important information about the use of UK and UK Overseas Territory registered shell companies. Sphynx UK, and Sphynx Bermuda, by corrupt Congolese officials to divert the proceeds of oil sales in order to conceal them from official government figures so they could avoid paying the government's private debts and, it appears, to skim off a profit by mispricing the oil sales.

In 2003 Sphynx bought oil from the ROC oil company for an average of 9.6% below the official ROC tax price, resulting in a loss of revenue of around US\$15 million. The company also gave ROC short term loans or advances on each cargo of oil at inflated interest rates, costing the ROC a further US\$5 million. Investigations by Global Witness indicate such transactions continued into 2004.

Sphynx UK bought oil from ROC and sold that oil to Glencore UK, based just a few streets away from each other in central London. Glencore then sold the corruptly obtained oil on to BP, who paid market price for it¹⁶³. Evidence indicates that at the time of these transactions Sphynx was managed by Denis Gokana who was also Special Advisor to the President and later became President and CEO of the state oil company.

Sphynx UK is a UK registered company, established in 2002. It is owned by Litchfield Development, a Bermudan registered company. Annual filings at Companies House report no revenues and costs of £83,480 in the year to January 2004 and £108,627 in the preceding year. Therefore Sphynx UK has no UK tax liability. The UK Court judgement stated that Sphynx UK 'plainly exists for no other purpose than to act as a service company for Sphynx Bermuda'

One of the men listed as Directors of Sphynx UK and therefore one of the signatories on the annual filing at Companies House said in a telephone conversation with Global Witness; "I was never shown any documents, I never signed any document, I did not sign any financial statements... and I was not kept informed of how the company was managed."¹⁶⁴ This case raises serious questions about the loopholes in the UK's company registration and annual report filing system

Financial Intelligence and Investigation

The effective use of intelligence is key to a successful anti-money laundering regime. A major component of intelligence is the Suspicious Activity Reports (SARs) made to NCIS – soon to be replaced by SOCA.

A report in 2003 identified failings in the way SARs were investigated¹⁶⁵. Another in 2005 pin-pointed under-resourcing, insufficient training, poor communication and lack of ownership as the problems with the regime.¹⁶⁶ As early as 2000 a government report recommended target for NCIS to turn around disclosures passed to them, and for funding to be provided to ensure these targets are realisable¹⁶⁷.

Under-resourcing of NCIS has meant that it has been unable to look into the many suspicious activity reports received each month.¹⁶⁸ However concerns have also been expressed about defensive or over-reporting by financial organisations, which simply ensure they cover their own liability¹⁶⁹. Likewise, law enforcement agencies have had insufficient information to make use of SARs and no performance indicators to incentivise the use of SARs.¹⁷⁰

A report commissioned by the Association of Chief Police Officers proposed that to remedy these problems the SARS regime needs a clear institutional 'owner' such as NCIS/SOCA.¹⁷¹ However since SOCA is not prioritising corruption it is unclear how the organisation will be given an incentive to address current problems.

In a recent speech on terrorism and its financing, the Chancellor of the Exchequer made a clear commitment that HM Treasury will work more closely with the financial sector in identifying suspicious transactions. He compared the forensic accounting measures required to tackle terrorist financing with the groundbreaking achievements at Bletchley Park during the Second World War. The AAPPG welcomes his commitment to tackle terrorist financing and his commitment to use the latest technology and techniques to track and freeze terrorist assets. This is welcome and should also be applied with the same vigour and supportive resources to the proceeds of corruption as well as the financing of terrorism.¹⁷² After all, if a country's health budget, is misappropriated, for example, the results can also threaten public safety¹⁷³.

Freezing and Repatriating Assets

The freezing and repatriation of assets is a highly charged issue. As noted in box 5.1 the Nigerian Government has sought repatriation of assets stolen by General Abacha through civil court proceedings in various countries. The Mutual Legal Assistance channels between the UK and Nigeria were slow to produce results so the Nigerian Government began expensive civil proceedings. The Nigerian

Government's UK solicitor notes that the UK has now frozen some \$40 million, but this has not yet been repatriated¹⁷⁴.

The legal complexity of repatriating funds and wrangles over what those funds will then be used for have delayed progress in several countries. In the UK responsibility for freezing assets and their repatriation could be made clearer and possibly streamlined. The Assets Recovery Agency concentrates on domestic crime, the proceeds of international organised drugs crime and terrorist financing. It has no earmarked resources to work on repatriating the proceeds of foreign corruption. In some cases overseas authorities conducting prosecutions in their own jurisdictions liaise with the CPS regarding asset confiscation¹⁷⁵.

The AAPPG is pleased to note that the CPS is currently enforcing three confiscation orders, though none of these relate to Africa or the proceeds of corruption¹⁷⁶.

A Commonwealth Working Group on Asset Repatriation identified common problems in asset repatriation in a number of countries. Most significant were proper funding of relevant agencies and proper enforcement of legislation. It also emphasised the importance of mutual legal assistance and peer review.

The AAPPG believes that these complications can and should be tackled and reminds the UK Government of its commitments to repatriation of funds in the 2005 G8 Communiqué and in the recommendations of the Commission for Africa.

In his recent speech on combating terrorist financing the Chancellor made a commitment to strengthen the pre-emptive asset freezing regime and to review whether an office for asset freezing is also required in 2007. We welcome these commitments and the resources deployed to implement them, but we want to see the same commitments made to the proceeds of corruption.

Prevention

Proper enforcement of a robust anti-money laundering legal framework including legal and civil sanctions, is an important part of prevention. Also necessary is an information campaign for the whole regulated sector, particularly those sectors – such as auctioneers and casinos – less accustomed to performing due diligence checks on customers.

Progress on enforcement

The AAPPG notes that in September 2005 a Nigerian state governor was charged in London with three counts of money laundering and that police seized £1 million in cash in the governor's London house¹⁷⁷. Despite the unfortunate fact that Governor Alamieyeseigha managed to illegally leave the UK without facing

trial, the charge was an important step and showed that the UK law enforcement agencies are trying to implement the commitments the UK has made on this issue.

The UK's Crown Dependencies and Overseas Territories

The UK is responsible for the Crown Dependencies (CDs) of the Isle of Mann, the Bailiwick of Jersey and the Bailiwick of Guernsey. It has a further 14 Overseas Territories (OTs) which include famous offshore financial centres such as Bermuda, the British Virgin Islands and the Cayman Islands¹⁷⁸.

The CDs are self-supporting and are not part of the UK, but nor are they colonies. As they do not have sovereign status they cannot sign international agreements in their own right. However they do have some international autonomy, or specific arrangements. For example Jersey is not a member of the EU, though it is treated as part of the European Community in terms of free trade of goods.¹⁷⁹

As non-sovereign states and because the Crown, through the Privy Council and therefore the UK Government¹⁸⁰, is ultimately responsible for the good government of the CDs, we make recommendations relevant to the CDs to the UK Government. We will also be conveying our recommendations to the governments of the CDs.

In some instances the UK has signed up CDs to international agreements, in others it has extended agreements to them at their request. Documents from the UK's Corruption Overseas Committee indicate that there have been significant problems in persuading all of the CDs of the advantages of signing up to and implementing a number of agreements. For example neither Jersey or Guernsey had agreed to the extension of any of the UK's Mutual Legal Assistance Treaties (MLATs) and with some issues prefer to negotiate their own agreements. Meanwhile Jersey has apparently not been forthcoming in providing assistance to the Assets Recovery Agency¹⁸¹.

The AAPPG notes the important work already underway to help CDs and OTs diversify their economies, to reduce their reliance on offshore banking. The UK Government must improve its working relationship with the CDs and ensure that all relevant international agreements are fully extended to them, in particular the UN Convention Against Corruption and the EU Third Directive on Money Laundering. Legislation within the CDs is needed to implement these directives. The complex constitutional relationship between the UK and the CDs is unclear. Many might see poor cooperation and implementation by the CDs and OTs on corruption issues reflecting badly on the UK. Indeed some accuse the UK of allowing banking secrecy in CDs and OTs to continue because it financially benefits the UK as well as the CDs and OTs.

Policy Coherence

As stated in section 4 the AAPPG recommends the appointment on an anti-corruption champion to coordinate policy coherence and implementation across Whitehall. The brief must explicitly include issues relating to money laundering.

Headline Recommendations to tackle money laundering

A full list of recommendation made by the AAPPG is given in section 2. Below are those recommendations most relevant to tackling money laundering.

Rigorously enforce existing laws against international bribery, corruption and money laundering.

Fully implement the Third EU Money Laundering Directive as soon as possible and well before the December 2007 deadline.

Ensure that Crown Dependencies and Overseas Territories deal with corruption and money laundering as robustly as the UK.

Appoint an Anti-Corruption champion for a two year period to coordinate policy coherence and implementation across Whitehall and to work with devolved executives, Crown Dependencies, Overseas Territories and international partners.

Further Recommendations

A. Investigations

Work to improve inter-agency coordination and ensure there is clarity on who is ultimately responsible for money laundering investigations.

Give a high priority to investigations into the laundering of the proceeds of corruption, and to tracing, freezing and repatriating these funds where possible. These activities should have earmarked funds to ensure they are not sidelined by the focus of investigative and enforcement agencies on drugs and anti-terrorism.

B. Closing the loopholes

Include within the Company Law Reform Bill a requirement for UK registered companies to declare beneficial ownership and end the practice of directors of registered companies being themselves companies, unless beneficial ownership can be shown. Encourage the UK's Crown Dependencies and Overseas Territories to introduce similar legislation where they have not done so already.

C. The Third EU Money Laundering Directive

In implementing the Third EU Money Laundering Directive, clearly identify corruption within the working definition of a serious crime and highlight the relevance of offshore transactions as a sign of possible corrupt activity.

In the run up to the implementation of the EU directive engage in an information campaign targeting all UK businesses that may be affected to ensure they are aware of their responsibilities regarding due diligence checks, politically exposed persons and suspicious activity reports and what signs they should look out for.

Work closely with the EU on ensuring continental implementation of the Third EU Money Laundering Directive.

Encourage Crown Dependencies and Overseas Territories to introduce legislation along similar lines to the Third EU Money Laundering Directive and the recommendations of the Financial Action Task Force (FATF) where they have not done so already.

6. Aid and Corruption

Corruption is a major problem in some countries to which the UK Government contributes overseas development assistance (aid), either bilaterally or through multilateral channels. This chapter considers the links between aid and corruption. It looks at ways in which aid may be undermined by corruption and also how aid may in turn impact on corruption – for better or worse. It looks specifically at UK aid, including budget support.

Corruption's Impact on Aid

Corruption can undermine aid by reducing its effectiveness. Aid money can be misappropriated and final outcomes of aid reduced or simply not delivered. Corruption can take place at various stages of the aid cycle. It can also create cynicism about aid among the electorate in donor countries.

Corruption can affect aid in various ways. Opportunities for corruption may exist during the selection of an aid project and in its design, procurement, implementation, as well as in the financial management and evaluation of the project.¹⁸² Where there is direct *budget* support, the risks may be greater still and opportunities for corruption exist throughout the budgetary cycle – from formulation through execution to evaluation.¹⁸³

As discussed in detail in Section 3, corruption undermines development efforts and this includes those funded by overseas aid. World Bank aid to Africa over the last 40 years is in the region of US\$54 billion, and yet in the same period many indicators suggest the continent's economic situation has worsened.¹⁸⁴ Misuse of aid is a major contributing factor to the poor results from these financial inputs, and corruption is a significant part of the misuse of aid.

Aid's Impact on Corruption

For many years, however, the international community turned a blind eye to corruption, even kleptomania, in 'friendly' developing countries. The World Bank only began to openly discuss the importance of corruption in the mid nineties¹⁸⁵. The experience recounted by the founder of Transparency International of the World Bank's reluctance to deal with corruption is a case in point. Evidence exists from numerous countries of some donors' wilful ignorance of corruption and even of blatant misuse of their funds, in countries in which they operate.

In some cases aid was misused by corrupt governments not simply for personal financial gain but to maintain their hold on power through extensive systems of patronage. This undermined development, democracy and often human rights. In the infamous example of Mobutu in Zaire, the IMF was long aware that hundreds

of millions of dollars were being misappropriated, but chose to continue lending to the country until the early nineties. Such enormous losses, mainly to the state mining company's accounts, were apparently referred to in IMF reports as 'uncompensated sales' or leakages.¹⁸⁶

Thus in the past aid has actually been misused in such a way as to directly undermine its stated developmental aims and in the worst cases has exacerbated the scale of corruption and the tenure and gall of corrupt leaders. This has led some pundits to describe aid as part of the problem rather than part of the solution. Geo-political changes coupled with the realisation of just how damaging corruption has been have changed that and all donors are now taking corruption more seriously. However, evidence to the US Senate Foreign Relations Committee suggests ongoing 'leakage' amongst the multilateral development banks including the World Bank, the Asian and African Development Banks and others, could still be as high as 20% - 30%¹⁸⁷. If this figure is correct it is not leakage, it is a major outflow and it is not acceptable.

Unintended side effects of specific aid policies must also be considered. For example in the 1980s and early 1990s the rush to reduce the role of the state in developing countries, some of which were corrupt, led to ill-planned and ill-monitored privatisations. Uganda's privatisation programme began in 1992 and the sale of 142 state owned enterprises was expected to generate 900 billion Ugandan Shillings. However, by 1999 only 3.7 billion Ugandan Shillings had been banked, indicating the possible existence and scale of discount sales to government cronies at the expense of the national treasury.¹⁸⁸

Attempts at reducing government expenditure by cutting public sector wages may also have contributed to petty corruption by poorly paid officials.¹⁸⁹

Donors and policy makers now broadly admit these side effects and have redesigned some policies in response. DFID, for example, has gradually increased its capacity building programmes for key public sector areas and has funded anti-corruption machinery. Some aid programmes now support public sector wages.

Furthermore, aid agencies, governmental and non governmental, are not immune to the same pressures as businesses in corrupt environments. Clearly in some cases they face very difficult decisions, particularly in humanitarian emergencies where speedy delivery of life-saving items can be hampered by solicitations for bribes. All aid agencies must avoid taking part in corruption, and learn from, rather than hide, the mistakes of the past.

From a UK Perspective

The UK is a major international donor, spending £4,823 million on development in 2004-05¹⁹⁰. The UK Department for International Development, through which

80%¹⁹¹ of this money is channelled, is at the vanguard of progressive donor policies in many respects. It has committed to increase predictability of aid and donor harmonisation and has ended tied aid. DFID has also demonstrated its commitment to address non-aid issues which are slowing development including unfair trade and corruption. One of the policies seen as progressive is the move away from project aid towards increased budget support, but this carries its own risks.

Corruption and Projects or Budgets?

In response to issues of the unpredictability of aid, high transaction costs, a lack of national ownership and undermining of national state structures, DFID has steadily increased its use of budget support. Budget support can be made to general budgets or to specific sectors or ministries and within DFID is known as Poverty Reduction Budget Support (PRBS). DFID's 2005 Annual Report stated that it planned to significantly increase PRBS to 30% of its bilateral aid in 2005-06. If the UK is to double its aid to Africa by 2010 the majority of additional funding will be deployed as some sort of budget support because the UK does not have the capacity to manage significantly more projects.

Budget support is seen by many as at greater risk of misappropriation than project support because financial management and implementation are not directly under the control of the donor. However, as discussed above and in Section 3 the aid 'project', be it the building of a new road or delivery of medicines, is by no means free from the risk of corruption and it brings with it its own problems. For example excessive investment in projects parallel to state structures can undermine the state and lead to duplication and poor coordination. It also raises fundamental issues of accountability. Ideally, the people should be able to hold their government accountable for the services provided. But there are no lines of accountability between ordinary poor people and international donors whether international institutions, donor countries or international non-governmental organisations. Nevertheless, projects are an essential component of the aid system, and indeed are the only appropriate form of aid in some contexts. They can also address problems not prioritised in national strategies and are extremely important in responses to humanitarian emergencies.

DFID only provides PRBS where 'circumstances are appropriate'. In making this judgement DFID takes into account broad governance issues, budget priorities, commitment to robust financial systems and the specific local effectiveness of PRBS. Consideration also includes a: "thorough evaluation of public financial management and accountability systems, and associated risks"¹⁹². The risk evaluation for all budget support, looking at each of these dimensions, is vital and must be robust and constantly under review.

PRBS has great potential for supporting the development of the state, rather than investing in parallel structures and displacing accountability. Use of PRBS will

only reap results in contexts where there is a well functioning public financial management, good levels of transparency and financial reporting. Where its use is contingent on a higher level of government accounting and transparency across the national budget it also has the potential to be an effective tool to tackle corruption in the public sector and catalyse more effective financial management. It should also be linked to broader governance concerns, such as protection of human and democratic rights. The aim is for this support to contribute to virtuous circles of transparency, governance and poverty reduction. The fear is that if not well monitored it may be misused and contribute to vicious circles of increasing corruption instead.

It is also necessary to consider whether giving PRBS, even where directed at one sector where it is accounted for within a particular ministry, can allow other government funds to be displaced for nefarious purposes;¹⁹³ or whether it might allow theft, governance or human rights abuses to take place outside of that particular sector, overlooked by assessors¹⁹⁴. Partly for this reason sector budget support needs the same level of accountability and transparency as general budget support.

The Utstein Group, an anti-corruption research group of which the UK is a member, suggests that budget support can be damaging in fractionalised societies, increasing rent seeking and shifting the political balance¹⁹⁵. Clearly, these non-fiscal potential problems should be examined very seriously when a country's suitability for budget support is assessed.

If DFID is to increase aid via budget support it must ensure that this contributes to a virtuous rather than vicious circle and realises the potential for increasing ownership, accountability, dialogue and development¹⁹⁶. Where this does not take place, backing for budget support, despite its theoretical advantages, will wither.

DFID's approach appears to be to straddle an apparent contradiction in which increased national ownership of development spending priorities coincides with increased donor input into budget discussions:

*"The other thing that giving budget support gives you is the opportunity to... be part of the discussion about what the country is going to do for itself to tackle corruption: reform public financial management; set up corruption commissions; prosecute people; track public expenditure; provide information about the money that should be coming to the school governors, the school board; the drugs that should be turning up at the clinic. Then the public opinion, civil society, can get to work within the politics of the country and start calling people to account if the money does not turn up."*¹⁹⁷

Thus the precise design, implementation and monitoring of budget support determine its potential to set in motion the virtuous circles, which are theoretically then propelled by an active civil society.

In the last six months alone DFID has had to make difficult decisions about the use of budget support in a number of African countries where governance, human rights and democratic concerns have meant that the integrity of aid could not be assured, including in some countries previously heralded as examples of improving governance and prime targets for budgetary support. DFID is learning lessons regarding budget support and these must lead to changes in details in the implementation and monitoring of the policy. Despite the interest in increasing the amount of aid delivered by budget support and its apparent progressive advantages DFID must not turn a blind eye to corruption, major governance, electoral, constitutional and human rights abuses. While the AAPPG heartily commends the UK's increases in aid budgets, pressure to disperse must never undermine the effectiveness and integrity of aid. DFID should not hesitate to freeze budget support where necessary and find other methods to fight poverty.

Recent Budget Support and Sector Support Decisions

DFID provides sector specific budget support in Kenya to the Ministry of Education, which until recently was headed by one of the politicians most caught up in allegations surrounding the Goldenberg scandal (allegations which relate to his service under a previous administration)¹⁹⁸. While not doubting for a moment that education in Kenya should be a top priority for UK development assistance, it is imperative that sector specific funding is protected, just as general budget support is protected. It is also essential that direct support for this government ministry does not send the signal to the Kenyan Government that the UK does not take corruption seriously. This is particularly important given the recent revelations of the Githongo dossier of corruption in previous and present Kenyan Governments¹⁹⁹.

However, the AAPPG is aware that DFID does take allegations of corruption in Kenya, as elsewhere, very seriously and notes that DFID chairs the Development partners' Anti-Corruption Group in Kenya²⁰⁰.

In its 2005 Departmental Report DFID estimated that in 2005-2006 97% of its country programme in Ethiopia would be made up of PRBS, with the lion's share not being earmarked. In January 2006 the Secretary of State stopped general budget support for Ethiopia, despite previous high hopes for improvements in Ethiopia's governance – particularly human rights concerns. This followed the election-related disturbances in 2005 and the resultant deaths of demonstrators and large scale arrests. DFID has had to find other ways to channel and safeguard its aid as it continues to direct money at poverty reduction in Ethiopia.

The report also estimated that the country programme for Uganda would be 70% PRBS in 2005-06, with none of the funds earmarked.²⁰¹ Uganda was also used as an example demonstrating the benefits of budget support, which DFID credited with gains in the management of the budget process, improved

effectiveness of state institutions and government accountability to its citizens.²⁰² In December 2005, however, DFID chose to reduce budget support by £15-20 million, re-directing the aid to humanitarian relief in the north. Thus in the space of less than 10 months Uganda had fallen from the example of a country where budget support was appropriate to one whose lack of commitment to the independence of the judiciary, arrest of opposition leaders, state financing for the government party and a significant budget overrun meant that support was cut²⁰³. In the case of Uganda, DFID has pinpointed governance concerns other than corruption for the cut.

In contrast, a group of donors working together, including the UK, are hopeful that virtuous circles of budget support and financial accountability are beginning to turn in Ghana. Here donors, who share the view that the Ghanaian Government's financial reporting system is adequate to account for direct budget support, pool funding to be spent by various Ministries. The Ghanaian Government now receives most of its aid through multi-donor budget support. As much as US\$5 billion may be made available to the Ghanaian Government in this way between 2006-2009, pending its implementation of a plan to make information about budget support more transparent to its citizens.²⁰⁴

Multilateral organisations and the UK

Nearly 40% of DFID expenditure is channelled through multilateral organisations and it is vital that those organisations apply equally robust procedures to prevent corruption. The main multilateral organisations the UK contributes to are the EU, the World Bank and the United Nations (see table 6.1).

Table 6.1

Source: Statistics on International Development: 2005 Edition²⁰⁵

<u>UK Aid Type</u>	<u>Amount in 2004-05</u>
Bilateral	£2,145 million
Bilateral to Sub-Saharan Africa	£825 million
Bilateral via UK civil society orgs.	£233 million
Multilateral	£1,504 million
European Community's Development Programme	£898 million
World Bank	£206 million
United Nations	£194 million

The World Bank spends roughly half of its total assistance through budget support²⁰⁶ and therefore faces similar risks. With DFID the Bank has been at the forefront of research into how best to assure the integrity of such aid, setting up a research unit looking specifically at corruption. It is also ahead of DFID and many other donors in terms of its procurement in so far as it debars companies

convicted of corruption from World Bank contracts and makes this information public. It also provides a hotline for people to report suspicions of corruption relating to World Bank funding. However, as with many large organisations, the progressive anti-corruption work taking place in one unit does not always seem to impact on every decision made across the organisation. The recent decision to announce further direct budget support to Kenya was delivered while one of the country's biggest corruption scandals was being exposed. It was only after a scathing attack by former British High Commissioner to Kenya, Sir Edward Clay, that the World Bank decided to freeze this funding until the situation could be resolved. The former diplomat pointed out that to agree the funding in the midst of a huge corruption scandal not only left the integrity of the funds in doubt, it also sent a signal to the Kenyan Government and people that corruption was not a major issue for donors.

While the 'message' sent by international donors' decisions may sound of little consequence, they are in fact a very important aspect of our assistance. The history of international aid being used to prop up despots is not a distant memory in many parts of Africa. If civil society activists see that a corrupt government is losing financial backing, they will feel empowered to call for action on corruption. On the other hand if funds still flow in despite allegations of massive corruption at the highest level, civil society will feel those in power are protected and untouchable. The impunity of leaders disempowers civil society.

The HIV/AIDS crisis has been acknowledged a major catastrophe for Africa. This has led to increased - and much needed - funding, both bilateral and multilateral. The Global Fund to Fight AIDS TB and Malaria has channelled some of these funds to countries via Country Coordination Mechanisms (CCMs). Unfortunately, some of this money has been misappropriated. However, the Global Fund took action and froze funding in some countries. In Uganda some of the money was stolen within the Project Management Unit, and grants were then frozen. Funds have since been released following an agreement between the CCM, the Ugandan Ministry of Finance and the Global Fund, and will be overseen by an external management company.²⁰⁷ The abuse was spotted and dealt with, but the Global Fund must now implement the lessons learned and implement better safeguards in future programmes.

There is an important role for parliamentarians in both donor and recipient countries in terms of debating and scrutinising development aid channelled through multilateral organisations. The MDBs and other multi-lateral funding organisations should be encouraged to facilitate such involvement.

The European Union has been criticised in the past for poor accountability, disbursement and targeting of aid but improvements have been made. The recently published 'EU Strategy for Africa' makes a number of progressive points and suggests an increase in general and sectoral budget support. The same standards discussed above must be applied to EU budget support. The EU

strategy also explicitly backs the African Peer Review Mechanism. The AAPPG calls on the UK Government to push for the highest anti-corruption standards and a focus on anti-corruption projects in EU aid programmes. It believes that anti-corruption should be a main focus of the EU's strategy. The EU should also annually report back to the European Parliament on the effectiveness, transparency and accountability of its aid programmes.

Non Governmental Organisations and Corruption

In 2004-05 £233 million of the UK's bilateral aid was channelled through civil society groups. Such groups are not more immune to corruption than any other. High standards should also be sought in terms of anti-corruption planning, financial transparency and accounting. The priority of supporting grassroots organisations or small international NGOs should not weaken the need for financial accountability within such organisations.

While no one expects small local NGOs to have the same accounting capacity as government departments or multilateral institutions, there are basic anti-corruption procedures and accounting procedures that all organisations can and should implement. NGOs should be asked to follow these if they wish to receive UK taxpayers' support. The larger international non-governmental organisations are in some cases as big as African government departments²⁰⁸ and there is no reason why they should not follow the same high standards in respect of anti-corruption procedures, financial accounting, barring corrupt contractors and refusing to pay bribes. The AAPPG suggests that DFID collaborates with other major international donors to work with NGOs to improve their anti-corruption procedures.

Aid tailored to fight corruption

As well as *protecting* aid from corruption, aid should also be used specifically to *fight* corruption. Existing anti-corruption and governance initiatives include support for anti-corruption programmes within governments, anti-corruption commissions and national audit offices and these should be provided with technical and financial support by DFID as they have been in Uganda, Sierra Leone, Malawi and Zambia.²⁰⁹ Such programmes must tackle embedded networks of corruption and patronage which can extend beyond single administrations. This area of work is a vital component of aid if it is to be effective.

Broader capacity building for public financial management is also central and should be a fundamental pillar of any budget support. It can also be used where budget support is not necessarily used. Such capacity building can benefit from external expertise but the capacity to monitor and account must be built and sustained locally. Revenue collection and full accounting is also central, this can

also help deter capital flight and connected money laundering. Investment in the financial sector can also help deter capital flight.

Good financial management not only increases transparency for donors and civil society but can also help governments themselves identify leakages and take necessary action. For example, financial tracking in Sierra Leone with DFID support revealed that 90% of drugs could not be accounted for or did not reach their final destination. Identifying the problem meant that action could be taken so that by the second tracking survey the figure had gone down to 30%.²¹⁰

The UK Government can also make an impact by encouraging African partner governments to ratify and fully implement the UN Convention Against Corruption and the African Union Convention on Preventing and Combating Corruption. They can do this, for example, through supporting capacity to ensure the necessary domestic legislation is drawn up and enacted and that enforcement authorities are established and resourced within a short timescale.

The integrity of the judiciary is also central and programmes to support anti-corruption efforts within the legal system are an important component of any broader anti-corruption strategy. Similarly Parliamentarians should monitor their governments and scrutinise government budgets in detail²¹¹. Capacity building for parliamentarians to fulfil these fundamental roles is also needed, for example, by increasing their access to independent sources of comparative information so they can better take part in debates and supporting public accounts or other cross party scrutiny committees. DFID and other donors can help increase transparency by asking recipient governments to involve parliament in approving aid budgets and priorities and ending significant off-budget spending.

Support should also be given to civil society organisations that hold governments to account. In particular the media is vital as an effective exposé and monitor of corruption, as the recent media coverage of the Anglo Leasing scandal in Kenya has demonstrated. Supporting the capacity of the media to retain their independence in the face of government pressure and to carry out investigative work, for example through sharing journalistic best practice, is worthy of support. Donors should take into account any government attempts to curtail the independence of the media when considering budget support.

The AAPPG commends DFID and some of the multilateral organisations for already funding many of these priorities. But if the battle against corruption is not to be lost these priorities must be mainstreamed, not looked at as additions. The resources should be increased significantly, as success in this area will also improve the effectiveness of all aid contributions in reaching national poverty reduction targets.

Looking Forward

The AAPPG supports budget support where democratic and human rights are observed and full financial accountability can be assured. It supports DFID in making difficult decisions about cutting or freezing budget support where the full integrity of UK aid is not assured. The AAPPG would like the same high standards to be applied to both general and sector specific budget support.

With regards project aid, being a project does not of itself assure transparency and corruption presents a risk throughout the phases of a project cycle. The highest standards are required in financial accountability of aid projects funded by UK taxpayers' money, whether bilaterally, through multilateral agencies or non-governmental organisations.

The AAPPG supports the private member's International Development (Reporting and Transparency) Bill. If passed it would require the Secretary of State for International Development to report annually to Parliament on expenditure on development assistance as well as on effectiveness and transparency. The AAPPG suggests that the Secretary of State includes within that report to Parliament, where possible, an account of estimated leakages and of DFID's attempts to ensure transparency and accountability for UK taxpayers' overseas aid. Mutual accountability is imperative.

Box 6.1 **The Lugar Bill**

In late 2005 the US President signed the Multilateral Development Bank Law, also known as the Lugar Bill. This followed a series of hearings, Chaired by Senator Richard Lugar, about multilateral development banks (MDBs) in which serious concerns about corruption were raised.

The law makes it US policy to call on MDBs to implement anti-corruption procedures making clear the circumstances for barring, grants or guarantees and the annual disclosure of the financial interests of MDB staff and to follow high standard anti-corruption guidelines in all procurement in any project which is wholly or partially funded by the MDBs.

The rationale behind the law was that given a significant proportion of US aid is channelled through multilateral development banks, the USA has an interest in ensuring that delivery is not threatened by corruption.

The Senate hearing also highlighted other issues such as harmonisation of anti-corruption policies, ensuring staff have incentives to uncover and report rather than cover up corruption in their projects and the need for MDBs to provide more support to anti-corruption units and for prosecuting corruption. Action on all these findings is essential.

In the USA, fears about the effectiveness of US tax payers' money being channelled through multilateral development banks has led to enactment of the Lugar Bill (see box 6.1) calling on Multilateral Development Banks to which the

USA financially contributes to implement anti-corruption programmes which include debarment and disclosure of financial interests. This indicates that similar levels of transparency are possible throughout the multilateral organisations.

The AAPPG suggests that the UK should be making similar calls on multilateral organisations and non-governmental organisations which receive UK tax payers' money and that progress on full accountability in all sectors be included in the Secretary of State's annual report to Parliament, following enactment of the International Development (Reporting and Transparency) Bill. Should the bill fail to be enacted the Secretary of State should consider utilising government time to re-introduce the proposal to Parliament.

While the UK is at the forefront of many progressive policies, including donor coordination and more recently policy coherence; the UK must also learn from other donors. For example the World Bank's list of companies barred from procurement is an important tool to fight corruption across different aid types, as is their anti-corruption hotline.

The AAPPG commends the work done by the New Partnership for Africa's Development in setting up the African Peer Review Mechanism. The APRM is an example of African leadership in improving governance and accountability. The UK has repeatedly expressed its support for the APRM. The AAPPG asks DFID to both continue this support and to take the results of country reviews into account explicitly when it examines the appropriateness of budget support or gives aid to a particular country. For the APRM to be meaningful its results must be respected and used by donors as well as African governments. Donors such as the UK can provide incentives to undergo the APR process and, achieve good results and implement recommended changes²¹². Meanwhile many governments across Africa are establishing effective anti-corruption strategies, campaigns and institutions and these efforts should be commended and supported.

We hope that a central pillar of DFID's new White Paper on development due out later this year will be the protection of aid from corruption and safeguards that ensure aid does not facilitate, contribute to or hide corruption, but rather is used explicitly to support domestic efforts to fight the problem.

Headline Recommendations on Aid and Corruption

A full list of the AAPPG's recommendations is given in section 2. Below are those most relevant to aid.

Report to Parliament annually on international development spending with a particular focus on transparency, effectiveness and details of support for anti-corruption priorities and strategies.

Appoint an Anti-Corruption champion for a two year period to coordinate policy coherence and implementation across Whitehall and to work with devolved executives, Crown Dependencies, Overseas Territories and international partners.

Further Recommendations

A. Safeguarding Aid

Apply the highest levels of financial reporting and accountability to *both* general and sectoral forms of direct budget support in Africa; ensure design of UK budget support contributes to increases in financial transparency and broader governance improvements across recipient governments.

Continue to freeze budget support where its integrity can no longer be assured and ensure such decisions send a clear message that the donors no longer turn a blind eye to corruption.

In assessing suitability for budget support take into account any results from the African Peer Review Mechanism and encourage prospective recipients of UK aid to take part in the process.

Work with multilateral organisations to ensure that anti-corruption strategies, including financial accountability and management, are implemented in all programmes. Ensure increased support for anti-corruption projects and systems that support transparency and accountability.

Work with the other major donors to assist the non governmental sector to improve transparency and ensure anti-corruption strategies are mainstreamed throughout their work.

B. Mutual Transparency

By the end of 2007 create a list of companies, individuals and organisations convicted of corruption or where overwhelming evidence exists, and debar them from DFID (and all UK Government) programmes and contracts. Provide an anonymous anti-corruption hotline or e-mail, accessible from any country.

Encourage the EU to report back to the EU Parliament annually on international development spending with a particular focus on transparency and effectiveness. Include where possible estimates of leakage through corruption and details of the EU's efforts to minimise leakage and utilise aid to increase transparency and ensure effectiveness.

Encourage the multilateral development banks and other multi-lateral organisations to increase the involvement of parliamentarians in both donor and recipient countries in discussing developmental priorities and improving scrutiny and transparency.

C. Aid to fight corruption

Prioritise support for anti-corruption programmes in Africa including anti-corruption commissions, audit offices and programmes to improve the management of public finances, revenue collection and management. Encourage the ratification and implementation of UN and AU conventions relating to corruption. Increase the resources available for such programmes and encourage multi-lateral and other bilateral donors to do the same.

Significantly increase support for systems and projects which contribute to the domestic-led fight against corruption in recipient countries. These include support for:

- **The development of independent media**
- **Civil society organisations working on anti-corruption and transparency**
- **Anti-corruption schemes within the judiciary**
- **Parliamentarians in their role as monitors of the executive and scrutinisers of government budgets, particularly public accounts committees**
- **National audit offices**

Annexes

Annex 1: The Africa All Party Parliamentary Group

The Africa APPG was established in January 2003.

The Current Officers of the Group are as follows:

President: Lord Hughes of Woodside

Vice Presidents: Lord Avebury and Baroness Chalker of Wallasey

Chair: Hugh Bayley MP

Vice Chairs: John Bercow MP, Lord Chidgey, Lord Lea of Crondall

Secretary: Sally Keeble MP

Treasurer: Lord Freeman

The Africa APPG also has an executive committee comprised of officers of the Group and a further 25 members.

Total membership of the Africa APPG is 170, including members from both Houses of Parliament.

The administration costs for the Africa APPG are covered by the Royal African Society. Specific funding for this report was received from KPMG and Deloitte, as declared on the Register of All Party Groups.

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Annex 2: The Corruption and Money Laundering Inquiry

The Africa APPG decided to embark on this inquiry following its 2005 report *“The UK and Africa in 2005: How Joined up is Whitehall?”* and correspondence with members of the African Diaspora in the UK.

A call for written evidence was sent out in July 2005, with a deadline of October 2005. A full list of written evidence submissions is available on request. Four oral evidence sessions took place in December 2005-January 2006, as follows:

Session	Date	Witnesses
Session 1: NGOs	Thursday the 8 th December 2005	Mr Graham Rodmell and Mr David Murray, Transparency International UK Dr Sue Hawley, The Corner House Mr Alex Yearsley and Ms Sarah Wykes, Global Witness
Session 2: UK Government	Wednesday the 11 th January 2006	Rt Hon Hilary Benn MP, Secretary of State for International Development, Lord Triesman of Tottenham, Parliamentary Under Secretary of State, Foreign and Commonwealth Office, Paul Goggins MP, Parliamentary Under Secretary of State, Home Office
Session 3: Business	Wednesday the 18 th January 2006	Mr Nelson Ogushakin, The Association for Consultancy and Engineering, Mr Graham Hand, British Consultants and Construction Bureau Mr Hamish Goldie Scot, Scot Wilson Consulting Engineers Mr Neil Stansbury, the UK Anti-Corruption Forum. Mr Peter Brew, International Business Leaders Forum Mr Simon Gilbert, De Beers Group
Session 4: Money laundering	Thursday the 19 th of January 2006	Mr Raymond Baker, Guest Scholar, the Brookings Institution, Prof. Prem Sikka, University of Essex, Mr Richard Murphy, Tax Justice Network.

Full transcripts of the oral evidence sessions are available on request.

The Following Parliamentarians took part in all or some of the oral evidence sessions, steering committee meetings:

Lord Brett
Lord Chidgey
Baroness Flather
Lord Freeman
Lord Lea of Crondall
Baroness Northover
Lord Paul
Baroness Whitaker

John Bercow MP
Hugh Bayley MP
Lyn Brown MP
Russell Brown MP
David Drew MP
James Duddridge MP
Mike Gapes MP
Sally Keeble MP
Chris Mullin MP
Derek Wyatt MP

Decisions regarding the inquiry were made by the Steering Committee. The Steering Committee was made up of the AAPPG Executive, other interested AAPPG members and the following external experts who were invited to contribute:

Mr Laurence Cockroft (Transparency International UK)
Mr Richard Dowden (Royal African Society)
Mr John Githongo (Former Kenyan anti-corruption tsar)
Dr Sue Hawley (The Corner House)
Mr Gavin Hayman (Global Witness)

Three steering committee meetings took place on the 12th of October 2005, the 26th of January 2006, the 16th of March 2006 and the 22nd of March 2006. Consultation also took place by e-mail.

Representatives from the two funding organisations were also invited to attend the October 2005 planning meeting. One representative from Deloitte attended, the first meeting. No representatives from the two funders attended any further meetings or had sight of any draft of the report. The report was drafted by the AAPPG's secretariat in consultation with the Executive and the Steering Committees. The final report was approved by parliamentarians alone.

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¹¹⁷ Global Witness written evidence to the AAPPG Page 3

¹¹⁸ "Time for Transparency: Coming clean on oil mining and gas revenues" 2004 Global Witness Page 31

¹¹⁹ "The Riddle of the Sphinx: Where has Congo's oil money gone?" December 2005 Global Witness. Page 12 and David Pallister in the Guardian 01.06.05
<http://business.guardian.co.uk/story/0,,1496275,00.html> Accessed on 20.03.06

¹²⁰ Global Witness in both written and oral evidence to the AAPPG

¹²¹ For example one UK lender tried to take the ROC government to court for defaulting on loans

¹²² See Annex 2 for further information about written evidence submissions

¹²³ Transparency international Bribe Payer's Index 2002 see <http://www.transparency.org>

¹²⁴ Peter Brew, IBLF in oral evidence to the AAPPG 18.02.06 Page 18

¹²⁵ *ibid* Page 24

¹²⁶ FTSE Press Release 22.02.06 http://www.ftse.com/Media_Centre/index.jsp Accessed 22.02.06

¹²⁷ Elizabeth Lort-Phillips and Vanessa Herringshaw "Beyond the rhetoric: measuring transparency in the oil and gas industry." In the Global Corruption Report 2006

¹²⁸ "Extracting Transparency: The need for an International Financial Reporting Standard for the Extractive Industries" Published by Global Witness 2005

¹²⁹ Simon Gilbert, De Beers in oral evidence to the AAPPG 18.01.06 Page 24

¹³⁰ See for Example Early Day Motion number 1283 and the open letter to Gordon Brown from SustainAbility dated 14.12.05

¹³¹ This includes non corporate organisations such as Amnesty International

¹³² Simon Gilbert, De Beers in oral evidence to the AAPPG 18.01.06 Page 17

¹³³ By 'new ECGD guidelines' the AAPPG means those agreed in the Government's final response to the consultation, issued on 16.03.06 to come into force in July 2006.

¹³⁴ Today Programme Friday 27th May 2005

¹³⁵ Raymond Baker in oral evidence to the AAPPG 19.01.06. Page 1

¹³⁶ The Progressive Policy Institute
http://www.ppionline.org/ppi_ci.cfm?knlgAreaID=108&subsecID=900003&contentID=253413. Accessed on 28.02.06

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- ¹³⁷ See for example "Corruption and Money Laundering in the UK: One Problem, Two Standards" Report on the Regulation of Trusts and Company Service Providers October 2004 Transparency International (UK) Policy Research Paper 003
- ¹³⁸ See for example
http://www.kirkbytimes.co.uk/news_items/2004_news/liverpool_fc_sell_off.html
<http://www.chelseablog.com/2005/10/28/can-we-please-hate-chelsea-for-all-the-right-and-irrational-reasons/> Both accessed 01.03.06
- ¹³⁹ "A Message to World Leaders: What about the Damage we do to Africa?" June 2005 The Royal African Society. Page 2
- ¹⁴⁰ FSA written evidence to the AAPPG Page 2
- ¹⁴¹ FSA written evidence to the AAPPG Page 3
- ¹⁴² FSA written evidence to the AAPPG Page 4
- ¹⁴³ Restricted Whitehall Note of Corruption Overseas Meeting on 22nd September No 0262. Made available by freedom of information act request by Dr S Hawley.
- ¹⁴⁴ Kendall Freeman Solicitors in a letter to the AAPPG dated 10.02.06
- ¹⁴⁵ Geoffrey Wood, "Business and Politics in a Criminal State: The Case of Equatorial Guinea" African Affairs Vol 103, no 413, Oct 2004
- ¹⁴⁶ "Time For Transparency: Coming Clean on oil, mining and gas revenues" 2004 Global Witness. Page 55
- ¹⁴⁷ *ibid*
- ¹⁴⁸ "Money Laundering and foreign corruption: Enforcement and effectiveness of the Patriot Act. A Case study involving Riggs Bank" July 2004 Minority Staff of the permanent sub-committee on investigations.
- ¹⁴⁹ Global Witness written evidence to the AAPPG Page 7
- ¹⁵⁰ Financial Action Task Force on Money Laundering Report on Money Laundering Typologies 2003-2004. Page 19
- ¹⁵¹ FSA written evidence to the AAPPG Page 2
- ¹⁵² E-mail from Assets Recovery Agency 03.03.06
- ¹⁵³ "Corruption and Money Laundering in the UK: One Problem, Two Standards" Report on the Regulation of Trusts and Company Service Providers October 2004 Transparency International (UK) Policy Research Paper 003
- ¹⁵⁴ Global Witness in written evidence to the AAPPG
- ¹⁵⁵ Global Witness in written evidence to the AAPPG
- ¹⁵⁶ The Third Money Laundering Directive: Regulatory Impact Assessment HM Treasury 2004
- ¹⁵⁷ F.T. 17.03.06, Ellen Kelleher, "Revenue widens its scrutiny of offshore funds."
- ¹⁵⁸ See www.ukincorp.co.uk (accessed 08.03.06)
- ¹⁵⁹ See www.companyservices.warnerlow.com (accessed 08.03.06)
- ¹⁶⁰ "Recovering the proceeds of crime" June 2000 Report by the Policy Innovation Unit Page 85
- ¹⁶¹ According to press reports a UK accountant working for Liverpool firm acted as agents for a Swiss registered company owned by a UK resident and sister of one of those currently under investigation in Kenya (see for example David Pallister in The Guardian 20.03.06 "Britain urged to investigate UK link to Kenya scandal." This report also lists two other companies registered in the UK that John Githongo would like the UK authorities to investigate: Silverson in Cambridge and LBA Systems in Fyfe.
- ¹⁶² *ibid* page 86
- ¹⁶³ "Investigation urged into west African oil deals" 20.12.05 David Leigh and David Pallister The Guardian
- ¹⁶⁴ "The Riddle of the Sphinx: Where has Congo's oil money gone?" December 2005 Global Witness
- ¹⁶⁵ KPMG report 2003, cited in Jimmy Burnsard and Peter Thal Larson 01.12.05 Financial Times
- ¹⁶⁶ MH Fleming June 2005 "UK Law enforcement agency use and management of SARS"
- ¹⁶⁷ "Recovering the proceeds of crime" June 2000 Report by Policy and Innovation Unit, Cabinet Office
- ¹⁶⁸ Tim Daniel of Kendall Freeman Solicitors in writing to the AAPPG Page 4
- ¹⁶⁹ MH Fleming June 2005 "UK Law enforcement agency use and management of SARS" Page v

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- ¹⁷⁰ MH Fleming June 2005 "UK Law enforcement agency use and management of SARS"
- ¹⁷¹ MH Fleming June 2005 "UK Law enforcement agency use and management of SARS" Page vi
- ¹⁷² Rt. Hon Gordon Brown MP, in a Speech at RUSI, London, 13.02.06
- ¹⁷³ Indeed a number of African scholars are calling for a change in language used to describe grand corruption. See for example Kofele-Kale, Ndiva; "Partimonicide: The International Economic Crime of Indigenous Spoilation" in Vanderbilt Journal of Transnational Law, vol.28, no.45, 1995, pp.45-118; who claims that massive corruption and presidential graft can and should be named "patrimonicide" (along with "genocide").
- ¹⁷⁴ Kendall Freeman Solicitors in a letter to the AAPPG dated 10.02.06
- ¹⁷⁵ E-mail from Assets Recovery Agency dated 03.03.06
- ¹⁷⁶ Letter from Paul Goggins dated 18.01.06 to Hugh Bayley MP, House of Commons
- ¹⁷⁷ Reported by Reuters on the 30th September 2005
- ¹⁷⁸ FCO website at:
<http://www.fco.gov.uk/servlet/Front?pagename=OpenMarket/Xcelerate/ShowPage&c=Page&cid=1044360168291> accessed on 28.02.06
- ¹⁷⁹ States of Jersey website: <http://www.gov.je/ChiefMinister/International+Relations/> accessed on 28.02.06
- ¹⁸⁰ "Collaboration with the Crown Dependencies on Stolen Assets" a document of the Corruption Overseas Committee (undated) obtained by Freedom of Information request by Dr S Hawley
- ¹⁸¹ "Collaboration with the Crown Dependencies on Stolen Assets" a document of the Corruption Overseas Committee (undated) Obtained by Freedom of Information request by Dr S Hawley
- ¹⁸² U4 Utstein Anti-Corruption Resource Centre Website at:
<http://www.u4.no/helpdesk/helpdesk/queries/query76.cfm> Accessed on 24.02.06
- ¹⁸³ *ibid*
- ¹⁸⁴ Shakut Hassan "Corruption and the Development Challenge", Journal of Development Policy and Practice
- ¹⁸⁵ *ibid*
- ¹⁸⁶ Michela Wrong "In the Footsteps of Mr Kurtz: Living on the Brink of Disaster in the Congo" 2000 Fourth Estate London
- ¹⁸⁷ Bruce Rich "Bank Heist" The Environmental Forum Sep/Oct 2005 Note in fairness such a figure has to be a guestimate.
- ¹⁸⁸ George Ayittey in Evidence to the Senate Foreign relations Committee 28.09.04
- ¹⁸⁹ "How Northern Donors Promote Corruption: Tales from the new Mozambique" The Corner House Briefing 33. October 2004
- ¹⁹⁰ Statistics on International Development: 2005 Edition Key statistics. Available at www.dfid.gov.uk
- ¹⁹¹ *ibid*
- ¹⁹² "Poverty Reduction Budget Support" DFID Policy Paper May 2004. Available at: <http://www.dfid.gov.uk/pubs/files/prbspaper.pdf>
- ¹⁹³ Chris Mullin MP in questioning Rt. Hon Hilary Benn 11.01.06 Page 4
- ¹⁹⁴ One estimate suggests that leakage from aid into military spending may be around 11%, given the volume aid and relative small size of African militaries, the researchers suggest as much as 40% of military budgets may be inadvertently supported by aid; Collier and Hoeffler forthcoming "Unintended consequences: Does aid promote arms races" in Oxford Bulletin on Economics and Statistics
- ¹⁹⁵ *ibid*
- ¹⁹⁶ "Direct Budget Support and Corruption" Ivar Kolstad Utstein Anti-Corruption Resource Centre U4 Issue 1 2005
- ¹⁹⁷ Rt. Hon Hilary Benn MP, in oral evidence to the AAPPG 11.01.06 Page 3
- ¹⁹⁸ The Goldenberg scandal is said to have cost Kenya as much as US\$1 billion (see note 33) and was carried out through abuse of export compensation, in which the government tried to encourage exports through compensating Kenyan exporters costs. The abuse took place in that export compensation was given where no exports had taken place.

¹⁹⁹ A written statement made by John Githongo, the former anti-corruption chief in Kenya, to the Kenyan President in November 2005 is now publicly available.

²⁰⁰ E-mail from DFID dated 22.03.06

²⁰¹ DFID Departmental Report 2005 Page 116

²⁰² *ibid* page 117

²⁰³ DFID Press Release 20.12.05

²⁰⁴ "Budget Support in Ghana: reducing poverty through partnership." DFID News available at: <http://www.dfid.gov.uk/news/files/countries/africa/ghana-mdbs.asp> Accessed on 02.03.06

²⁰⁵ Key Statistics section available at <http://www.dfid.gov.uk/pubs/files/sid2005/contents.asp> Accessed on 02.03.06

²⁰⁶ Ivar Kolstad "Direct Budget Support and Corruption" Utstein Anti-Corruption Resource Centre U4 Issue 1 2005

²⁰⁷ Global Fund Press Release 10.11.05 and 24.08.05

²⁰⁸ For example total charitable expenditure by UK NGO Oxfam in 2004-05 was £154.4 million Oxfam Annual Report and Account 2004-05 available at: http://www.oxfam.org.uk/about_us/downloads/report2005.pdf Similarly Niger's Central Government Budget was US\$320 million in 2005 according to the US Department of State, see: <http://www.state.gov/r/pa/ei/bgn/5474.htm> Accessed on 16.03.06. It is also worth noting that such charities are looking at these issues as Oxfam's suspension of aid in Aceh pending investigation into 'financial irregularities' shows. See Shawn Donnan in Financial Times 16.03.06 "Oxfam Probes 'irregular' Aceh tsunami spending"

²⁰⁹ Rt. Hon Hilary Benn in answer to Parliamentary Question 13.06.2005 Column 1W

²¹⁰ Rt. Hon Hilary Benn in oral evidence to the AAPP 11.01.06

²¹¹ As UK Parliamentarians we are also asking for more details about the effectiveness and volume of the UK's aid spending, see recommendation number 5.

²¹² For example Trevor Manuel MP, Minister of Finance in South Africa is widely quoted as having said "If I was a donor, I would not give a cent to a country that had not signed up to the APRM; moreover if I was an investor I would not invest in any country that had not signed up." For example see comments by Myles Wickstead at the EPC "Governance - Made in Africa Conference" 25th July 2005 and the RAS "Delivering the G8 Goods" seminar on 17th October 2005.

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