

Contribution to the Discussion Workshop “Corruption and the role of tax havens”

Hiding proceeds of corruption through the abuse of Law The extractive industries example

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April 2016

I- Context

“We have no more business nor in grey countries or in non-cooperative countries”, stated the CEO of a French Bank before the French Senate in April 2012.² With the scandal of the Panama papers, this sentence takes another twist. Over the last decades, the Bank would have helped creating hundreds of shell companies registered in Panama and/or in other tax havens.³ The public opinion was deeply moved by this exposure which has led the French authorities, in particular the Senate, to call for a new audition of the CEO and ask for accountability.⁴ However, at the time of the hearing in 2012, Panama was neither on the French non-cooperative list of countries⁵ nor listed as a grey country by the OECD.⁶ This situation illustrates very well some economic actors’ practices: playing with words and legal terms and abusing the Law.

This recent example is one among numerous others revealed thanks to whistleblowers (e.g. Stéphanie Gibaud from UBS) or the work of investigative journalists (e.g. Swissleaks, Luxleaks, The Bribe Factory, etc.) and civil society organisations highlighting the issue of using tax havens to hide proceeds of corruption or evade taxation.

II- The issue at stake

Illicit financial flows, defined as money illicitly earned, transferred or utilized, range from corruption to tax evasion or money laundering. They represent billions of dollars lost in revenues for countries all over the world. For Africa, it would be equivalent to the average annual development aid and assistance dedicated each year.⁷ Moreover, they dramatically reduce the amount of resources available for essential public services such as education or health.

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² Comptes rendus de la Commission d’enquête d’évasion des capitaux, audition de Mr. Frédéric Oudéa, président-directeur général du groupe Société générale, président de la Fédération bancaire française, 17 avril 2012, available at http://www.senat.fr/compte-rendu-commissions/20120416/ce_evasion.html#toc3.

³ Le monde, « Panama papers » : les 979 sociétés offshore créées par la Société générale via Mossack Fonseca, 8 avril 2016.

⁴ <http://www.publicsenat.fr/lcp/politique/panama-papers-senat-auditionnera-publiquement-frederic-oudea-dg-societe-generale-mois->

⁵ Arrêté du 4 avril 2012 pris en application du 2 de l'article 238-0 A du code général des impôts – Panama was removed from the French non-cooperative list of countries on 1st January 2012, available at https://www.legifrance.gouv.fr/affichTexte.do;jsessionid=36FF204A4378361B2A19FD10BFE24CF7.tpdila16v_3?cidTexte=JORFTEXT000025673403&dateTexte=&oldAction=rechJO&categorieLien=id&idJO=JORFCONT000025673084.

⁶ Panama was removed from the OECD grey list in 2011.

⁷ UNECA, Report of the High Level Panel on Illicit Financial Flows from Africa, 2015, available at http://www.uneca.org/sites/default/files/PublicationFiles/iff_main_report_26feb_en.pdf.

Recognising the negative impacts of illicit financial flows, the international community has undertaken various actions and initiatives over the last decades. International instruments to combat corruption were adopted (e.g. the OECD Anti-Bribery Convention or the United Nations Convention against Corruption) and commitments were made to automatically exchange tax information (e.g. OECD BEPS Action Plan).

Despite these efforts, illicit financial flows are still occurring, mainly because of an enabling environment. Gaps, inconsistencies and weaknesses of international, regional and national legal frameworks are indeed key in providing space to hide illicit financial flows, and corruption in particular. These loopholes lead economic actors to be creative, innovative and play with the discrepancies. A statement made by a multinational corporation's CEO over suspicions of tax avoidance and corruption is instructive in that regard: "*what we did was not illegal vis-à-vis the national legal system (...), it was in compliance with the law*". In relation to these aspects, one can wonder whether Law can foresee, anticipate and/or adapt to all unintended or unexpected effects of the regulations.

III- The abuse of Law to hide proceeds of corruption: the extractive industries example

Over the last decades, globalisation has led to the abolition of internal borders, a deregulation of financial markets, an increased ease of communication means as well as interdependence and interconnection among actors. Economic actors, notably multinational corporations, have also been playing a greater role in this new global area. Nevertheless, globalisation has had unforeseen impacts such as weakening the role of States and the development of a gray area between legality and illegality but also between licit and illicit. It has enabled actors to use and benefit from the different legal systems around the world with regulations being done at the national level rather than at the global level. Moreover, gaps or lacks of legislations in specific areas has contributed to this phenomenon. Hence, this has created opportunities for developing new and innovative techniques to conceal corruption, particularly through the use of legal tools. Understandably economic actors are aiming for those jurisdictions that offer them what they consider to be the best arrangements.⁸ They maximise options available to them and creatively use and interpret the Law in their favour. Furthermore, they often contribute to the design and crafting of legislations. Some authors refer this situation as "business illegalism", i.e. the possibility for specific actors to use, manipulate, and write the law in order to play with boundaries of legality, leading to a sense of impunity.⁹

Every sector in our economy can be affected by this illegalism; the extractive sector is no exception. According to OECD, the extractive industries sector is the most prone to foreign bribery.¹⁰ It can be explained by the involvement of multiple actors (public officials, corporations, intermediaries, etc.), destinations, scales which makes it complex to regulate. Corruption within the extractive sector can take the form of petty bribe, grand corruption, extortion, undue-influence, embezzlement, etc. in

⁸ Ronen Palan, Tax Havens and the Commercialization of State Sovereignty, International Organization 56.1, 2002, 151-176, available at <http://muse.jhu.edu/article/14309>.

⁹ For example, see Pierre Lascoumes, Les Affaires ou l'Art de l'ombre : Les délinquances économiques et financières et leur contrôle, 1986.

¹⁰ OECD, OECD Foreign Bribery Report, 2014, available at <http://www.oecd.org/corruption/oecd-foreign-bribery-report-9789264226616-en.htm>.

order to obtain favours, to take profit from unclear rules or manipulate the law or turn a blind eye on illegal activities. Corruption takes place at all stages of the value chain: from allocation of licences, negotiation of contracts or procurement of goods and services to revenue collection and monitoring of operations. It is made possible through numerous mechanisms and systems including the use of tax havens, secrecy jurisdictions and legal/regulatory heavens.

The following sections look at cases in the extractive industries sector in which legal entities were misused from their original purpose and laws manipulated to hide proceeds of corruption.

Case study 1: Corporate vehicles diverted to hide corruption

Among the mechanisms provided by the various national legal frameworks, corporate entities or vehicles, such as shell or offshore companies, trusts and foundations are the most favoured to hide proceeds from corruption. They are not illegal in themselves. They can be a logical choice for some business transactions and may have a legitimate purpose, e.g. for mergers and acquisitions or estate.¹¹ It is the way they are used that makes them illegitimate and illicit. Having recourse to nominee shareholders or directors, to bank accounts abroad and to complex ownership and control structures do not breach national laws. However, in most cases, these vehicles and mechanisms are being diverted from their original purpose to conceal proceeds of corruption.

In the extractive industries sector, complex layers of corporate structures, shell companies, offshore transactions are used to disguise illegal payments and dilute corporate or individual liability.¹² Shell companies can be established in order to conceal the award of contracts to companies in which public officials or their proxies hold interests. Part of signature bonuses could be assigned to a bank account in a secrecy jurisdiction. Charity foundations or social development projects can be used as channels for corruption.¹³ In each of these cases, solely legal corporate entities have been used but to a different purpose.

Example 1: Shell companies and real estates from Nigeria to France

An Oil Minister in Nigeria under Sani Abacha opened a series of bank accounts in Switzerland under his brother's name and a false identity. He also created a network of shell companies in the British Virgin Islands supported by banks in Gibraltar, Switzerland and London. In Paris, a Société civile immobilière – a company managing real estate – was created to purchase real estates and goods under the company's name: a mansion, a castle Boulay Morin, a speed boat, a yacht and various art objects and antiques.¹⁴ In other words, profits generated from corruption in Nigeria with the award of oil licences led to launder funds through the various bank accounts and the purchase of real estates and goods in France.

¹¹ FATF, The misuse of corporate vehicles, including trusts and company service providers, 2006.

¹² OECD, Typology on Corruption Risks in Extractives with Mitigation Measures and Incentives, 2015, to be published.

¹³ NewsinEnglish, More queries over Statoil in Angola, 2016, available at <http://www.newsinenglish.no/2016/02/08/more-queries-over-statoil-in-angola/>.

¹⁴ Rue 89, Un ex-ministre nigérian du Pétrole condamné en France, 2007, available at <http://rue89.nouvelobs.com/2007/11/22/un-ex-ministre-nigerian-du-petrole-condamne-en-france-4266>.

A Société civile immobilière is a legal corporate entity created to manage assets in a flexible manner. It is a common corporate vehicle in France. However, in various corruption cases, this type of company has been used to conceal the identity of the estate's real owners and launder money.

Case study 2: Local content requirements misused to perpetuate corruption and elite capture

Over the last few years, many resource-rich countries have introduced local content requirements into their regulatory frameworks. The objective is to create jobs, promote enterprise development and accelerate the transfer of skills and technologies at the national and local level.¹⁵ These rules can include an obligation to award a percentage of procurement of goods and services to local companies or enter into joint ventures with local partners in order to operate in the country.¹⁶ Although local content regulations were designed to shape and strengthen economic development, in various instances they have been misused and manipulated to generate corruption, elite capture and rent-seeking.¹⁷ The literature highlights cases where public officials encouraged, or even imposed, companies to enter partnerships with specifically designated companies if they wished to operate in the country. These companies were eventually revealed to be shell companies with disguised ownership or in which their proxies hold interests.¹⁸ Other examples include foreign companies establishing a consortium with local companies ultimately owned by government officials to win a bidding process for licenses as well as local content legislations being drafted in order to favour legal entities with close connection to public officials.

Example: Cobalt International Energy and local content requirements in Angola

Angola adopted local content regulations to develop its oil sector. As a result Cobalt International Energy partnered with local companies for two oil Blocks in Angola: Nazaki Oil and Gas and Alper Oil – which hold respectively 30 per cent and 10 per cent in the blocks. Cobalt had not previously worked with neither of them and was unfamiliar with them.¹⁹ According to Cobalt, these companies were assigned as local partners by the Angolan government. It was disclosed that Nazaki Oil and Gas is partly owned by Aquattro, a company linked to Angolan officials. The former head of Sonangol (the Angolan State-owned oil company) and generals associated with the President would have shares in Aquattro.²⁰ Alper Oil's owners remain undisclosed so far.

The Department of Justice in the USA is currently conducting an investigation into Cobalt International Energy's operations in Angola under the Foreign Corrupt Practices Act.

¹⁵ IPIECA, Local content strategy: a guidance document for the oil and gas industry, 2011.

¹⁶ World Bank, Local content policies in the oil and gas sector, 2013.

¹⁷ OECD, Typology on Corruption Risks in Extractives with Mitigation Measures and Incentives, 2015, to be published.

¹⁸ Maira Martini, Local content policies and corruption in the oil and gas industry, Transparency International, U4 Expert Answer, 2014, 2014:15.

¹⁹ Tom Burgis, US to probe Cobalt oil links in Angola, Financial Times, 2012.

²⁰ Tom Burgis, SEC drops corruption probe into Cobalt, Financial Times, 2015.

Case study 3: Abuse of bidding processes

In the extractive industries sector, bidding processes have been put in place in order to reduce the risk of collusion and corruption caused by direct allocation of licenses and permits. They aim at introducing transparent processes and promoting competition among companies. Nevertheless, examples show that in some circumstances, bidding processes can be diverted to favour companies linked to public officials and hide proceeds of corruption. A classic scenario is when a bidding company winning the call for tenders turns out to be a shell company controlled by a public official with no demonstrated ability to perform in the sector or when evaluation criteria were designed to favour a company with undisclosed owners. One sees that although the legislation was adopted to avoid corruption, it can still be misused to continue “business as usual”.

Example: Kinross Gold Corporation and suspicious bidding process

Kinross Gold Corporation is a Canadian mining company under investigation by the US Security Exchange Commission for allegations of bribery in Mauritania. The Canadian authorities have also been urged by civil society organisations to investigate.

Kinross Gold Corporation is said to have close ties with governmental officials in Mauritania. A whistleblower has revealed practices within the mining company. It is suspected to have selected service providers connected to the President, funded the local police' offices, hired influential persons among the company's staff and concluded contracts with agents / middle men through its Las Palmas office. Furthermore, in 2013, Kinross Gold Corporation launched a bidding process to provide services related to logistics within the mine. Maurilog, a local company with undisclosed beneficial ownership, was rewarded the procurement contract while its offer was at a higher price than its competitor and it had no demonstrated expertise in the area.²¹ One of its shareholders would be connected to the President of Mauritania.

This case highlights how a transparent bidding process can be used to conceal corruption.

Case study 4: Using intermediaries

Hiding proceeds of corruption would not be possible without the support of a wide range of actors that set up corporate vehicles, bank accounts, and influence or obtain favours from decision-makers. These intermediaries can be a law firm, an audit or accountancy firm, a financial institution, a middle-man / big man, commercial agent, etc. National and international legislations combating corruption have been strengthened in the recent years to take into account some of these practices. The US Foreign Corrupt Practices Act and the UK Bribery Act are among the most ambitious regulations against corruption with extraterritorial competences. Nevertheless, economic actors have developed legal “tricks” in order to avoid being subjected to these mandatory rules, such as concluding contracts with service providers under another national legal framework than the US or UK

²¹ Le monde, Kinross, en Mauritanie, la malédiction de la mine d'or de Tasiast, 2015, available at http://www.lemonde.fr/afrique/article/2015/11/13/kinross-en-mauritanie-la-malediction-de-la-mine-d-or-de-tasiast_4809432_3212.html.

jurisdiction, paying services in currency other than US Dollars, or having recourse to commercial agents with shadow activities.²²

⇒ I suppose this point on intermediaries will be discussed in greater details by other speakers.

Example: BSGR, Guinea and intermediaries

In 2008, Guinea's government would have stripped Rio Tinto half of its rights to Simandou's mine.²³ BSG Resources, a mining company based in Guernsey, a subsidiary of the Beny Steinmetz Group whose owner is Israeli diamond magnate Beny Steinmetz, bought the rights.²⁴ BSG Resources invested around 160 million USD and sold 51 per cent of its stake to Vale for 2.5 billion USD two years later. The profit on the sale is said to be equivalent to 2.4 times Guinea's entire national budget in 2011.²⁵

In 2013, the FBI began to investigate the deal. Mamadie Touré, the wife of former Guinean President, would have received payments into US-held bank accounts, from Frederic Cilins, an agent for BSG Resources in Guinea through an offshore company, Pentler Holdings Ltd.²⁶ During a meeting in Florida at Jacksonville airport, he would have repeatedly offered her millions of dollars to destroy evidence showing that the rights to the Simandou mine had been won after bribes were paid to Guinea government officials.²⁷ According to Global Witness, a French transcript of that conversation would show that Frederic Cilins was acting on direct orders from Beny Steinmetz himself.

IV- Preliminary concluding remarks

- Every legal provision can be a tool for economic actors, being it a multinational corporation, a bank, a governmental official, to conceal corruption by diverting it from its original purpose and manipulating it.
- In each corruption case, tax havens have been used. Nevertheless, the way Law is interpreted and analysed is a main issue to consider and look at.
- One needs to take into account that actors adapt quickly to legal reforms (always a step ahead) and change jurisdictions accordingly.
- A matter of how legal frameworks are enforced.
- Even the best law can be misused. Is it the role of Law to regulate, anticipate and respond to all flaws?
- What next?

²² See for example the Alstom case, available at <https://www.justice.gov/opa/pr/alstom-pleads-guilty-and-agrees-pay-772-million-criminal-penalty-resolve-foreign-bribery>.

²³ African Progress Panel, Equity in extractives, 2013, available at http://app-cdn.acwupload.co.uk/wp-content/uploads/2013/08/2013_APR_Equity_in_Extractives_25062013_ENG_HR.pdf.

²⁴ The independent, The corruption deal of the century: How Guinea lost billions of pounds in Simandou mining licensing, 2013, available at <http://www.independent.co.uk/news/world/africa/the-corruption-deal-of-the-century-how-guinea-lost-billions-of-pounds-in-simandou-mining-licensing-8662534.html>.

²⁵ African Progress Panel, *ibid*.

²⁶ Global Witness, New evidence ties BSGR to company behind Guinea mine bribery, 2013, available at <https://www.globalwitness.org/fr/archive/new-evidence-ties-bsgr-company-behind-guinea-mine-bribery/>.

²⁷ Global Witness, Guinea's "Deal of the Century", 2014, available at <https://www.globalwitness.org/fr/reports/guineas-deal-century/>.