

PRESS RELEASE

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FOR PRESS: to request a review copy of the *Global Corruption Report 2005* or to view the report electronically, contact gcr@transparency.org or visit www.globalcorruptionreport.org. For interview requests please contact press@transparency.org

Highlights from the Transparency International *Global Corruption Report 2005*

Corruption in the construction sector

The nature and scale of the problem

Surveys repeatedly reveal corruption to be greater in construction than in any other sector of the economy.ⁱ The scale of corruption is magnified by the size and scope of the sector, which ranges from transport infrastructure and power stations to domestic housing. Corruption affects both private and public players as they vie for their share of the global construction market of around US \$3,200 billion per year. This market represents 5–7 per cent of GDP in developed and advanced developing countries and around 2–3 per cent of GDP in lower-income developing countries.ⁱⁱ

Corrupt practices are found at every phase in construction projects. Some projects would not have passed the planning stage without the motivation of corruption; the awarding of construction contracts is too often tainted with corruption as are the operation and maintenance of projects after construction is finished. The tender process may be corrupted by international pressure. Through offers of arms or aid the government of a developed country may influence a developing country to make sure that a company from the developed country is awarded a project, even if it is not the cheapest or best option.

Certain characteristics make the construction sector prone to corruption: the fierce competition for 'make or break' contracts; the numerous levels of official approvals and permits; the uniqueness of many projects, which makes it difficult to compare pricing; the opportunities for delays and overruns; and the fact that the quality of work is rapidly concealed by concrete, plaster and cladding. Projects are executed by dozens, sometimes hundreds, of small-scale subcontractors creating a maze of transactions that are difficult to monitor.

Corruption in construction also has a direct cost in lives. Sub-standard construction projects, tainted by bribery, injure and kill when they are built in earthquake zones. The corrupt are all too often willing to put their personal gain before the welfare of others, as is no more clearly demonstrated than by TI Integrity Awards 2004 winner Satyendra Dubey, who was killed shortly after communicating his concerns about corrupt practices within the National Highways Authority of India.

The role of international finance

Some US \$250 billion is spent annually on infrastructure in the developing world alone. Much of this money comes from commercial banks and multilateral development banks (MDBs) such as the World Bank, while privately invested (but government-sponsored) export credit agencies (ECAs) often underwrite large scale projects. The impact that all these groups can have on corruption is enormous and the influence of MDBs goes beyond the vast sums of money they actually invest (the World Bank plans to spend US \$7 billion on infrastructure projects in 2005)

since they act as a catalyst for further financial support from the private sector and help set developing countries' policy on infrastructure. While MDBs have begun the process of blacklisting companies that have been proven to engage in corrupt behaviour, MDB involvement in a project is no guarantee that it will be free of corruption. ECAs have shown even less inclination to tackle corruption, often failing to apply with any diligence anti-corruption measures even in the rare instances where such measures exist.

Major strides in recognising the problem of corruption have been taken by both MDBs and ECAs – partly as a result of external pressure from NGOs. Measures taken include debarment of companies found guilty of fraud and corruption, stricter procurement guidelines, and improved financial management and oversight. There is considerable room for improvement, however. Supervision needs to be increased, safe channels for whistleblowers are needed, disclosure and transparency should be improved and public participation needs to be promoted.

Companies that bribe to win international business should risk punishment and blacklisting, irrespective of where they commit the crime. Even where the international and national legal architecture is in place to prosecute bribery, companies have escaped prosecution. The tenacity with which prosecutors in the impoverished African country of Lesotho have challenged large Western companies for paying bribes for contracts to build a US \$8 billion hydroelectricity plant has bucked that trend. Following a court case conducted in Lesotho, the World Bank reversed an earlier decision not to debar one of the companies involved, Canadian engineering firm Acres International, and may respond with similar debarment proceedings against other companies that are now facing prosecution, including the German company Lahmeyer, Spie Batignolles of France and Impregilo of Italy.

The costs of corruption

Corruption in the construction sector not only plunders economies, it shapes them. Recognising the problem of corruption in the construction sector, budget decision-makers may skew spending away from the sector to avoid losses. Alternatively, if the decision-makers are themselves corrupt, they may decide to spend more on infrastructure in order to increase opportunities for personal gain. At the installation stage, corruption lowers expenditure on infrastructure and reduces the productivity of that expenditure. Corruption also raises the operating cost of infrastructure services, and reduces the quality of services and access to them, especially for the poor.

The costs of corruption in the construction and engineering sector are not limited to money. The damage caused by natural disasters such as earthquakes is magnified in places where corrupt building practices flourish, such as where inspectors are bribed to ignore building and planning regulations. The result, when poorly built homes collapse, is that lives are lost and thousands are injured.

Corruption in the construction sector also ravages the environment. Many projects have progressed only because bribes were paid to ignore environmental and social hazards, often with the collusion of consultants who risk forfeiting future projects if they fail to endorse their clients' interest in promoting new greenfield investments. Projects subject to allegations of bribery include:

- The Yacyretá hydropower project on the border of **Argentina** and **Paraguay**, built with World Bank support, which is flooding the Ibera Marshes. Due to cost overruns, the power generated by Yacyretá is not economic and needs to be subsidised by the government. According to the head of Paraguay's General Accounting Office, US\$1.87 billion in expenditures for the project 'lack the legal and administrative support documentation to justify the expenditures'.
- The Jatigede dam on the Cimanuk River, **Indonesia**, which will submerge a land area of 49 km², drown 30 villages and displace around 41,000 people. Construction is expected to start this year. Environmental experts argue that the Jatigede dam is not needed.
- The reservoir of the Bakun dam in Sarawak, **Malaysia**, which will submerge 700 km² of tropical rain forest. The mandate to develop the project went to a timber contractor and friend of Sarawak's governor. The provincial government of Sarawak is still looking for customers to consume the power to be generated by the project.
- The Bataan nuclear power plant in the **Philippines**, which was built at a cost of more than US \$2 billion. The contractor, Westinghouse, admitted paying US \$17 million in

commissions to a friend of former president Marcos. The reactor sits on an active fault line, creating a major risk of nuclear contamination if the power plant ever becomes operational.

- The Bujagali dam in **Uganda**, which is currently being investigated for corruption by the World Bank and four different governments after a British subsidiary of the Norwegian construction company, Veidekke, admitted paying a bribe to a senior Ugandan civil servant. The cumulative environmental impacts of Bujagali and other dams on the Nile have never been assessed.

Corruption and post-conflict reconstruction

The challenges faced by conflict-affected countries are formidable. The need for anti-corruption measures is particularly acute in the first years after war. One of the main dangers corruption poses is that infrastructure projects may be designed according to the needs of empowered officials and institutions, rather than of needy populations. This risk is particularly high with bilateral assistance, when major projects are sought to maximise capital return to the donor country through the use of construction companies from the donor country.

The adverse affects of corruption on the reconstruction process go beyond the physical rebuilding of a country. Less corruption in post-conflict reconstruction means not only better-targeted, higher quality, and more efficient assistance, but also a greater contribution to the transformation of the local political economy, as well as the consolidation of more effective state institutions and legitimate political parties. Less corruption can help build a stronger peace.

Corruption in many cases figures among the factors that triggered political unrest or facilitated conflict escalation in the first place. In Cambodia, for example, the corruption of local and regional authorities as well as the participation of ordinary people in the logging sector benefited the Khmer Rouge, helping to sustain the conflict for several years.

The lack of a systematic commitment to transparency in the reconstruction process has put **Iraq** at risk of corruption on a massive scale as aid money floods in unrestrained by institutional safeguards or even simple inventory systems at ministries and state companies. Another factor is the legacy of corruption left by the former regime's control over the economy and the speed at which new economic policy is being introduced. Rapid privatisation, if enforced by the IMF and the Paris Club of official creditors as a condition for reducing and rescheduling some US \$120 billion of foreign debt, could magnify opportunities for corruption.

The credibility of the international community to play a role in curbing corruption in Iraq has been dented by the 'oil-for-food' scandal, and the secrecy surrounding the allocation of lucrative contracts by the US government. Contracts have been 'bundled' such that smaller companies cannot compete; many lucrative deals have gone to companies such as Halliburton and Bechtel with close links to individuals in government; and there have been suggestions of excessive profiting by the prime US contractors who subcontract jobs to local firms at a fraction of the price they themselves are paid.

Corruption around the world

Africa

There were significant setbacks in the fight against corruption in certain countries in Africa, and many challenges remain for the continent. The African Union Convention on Preventing and Combating Corruption is still eight ratifications short of the 15 needed for it to enter into force.

The credibility of **Kenya's** coalition government to make good on its anti-corruption campaign was dented by a series of high-profile scandals in 2004 including an alleged US \$10 million stashed in bank accounts by a cabinet minister and US \$24 million reportedly overpaid to Anglo-Leasing to upgrade passports. The donor community's confidence in the government's strategy to fight corruption through a series of laws and offices has been severely damaged by the scandals.

Zimbabwe's chaotic land reform process has crippled the agricultural economy and stripped the country of basic commodities such as fuel and food, as well as foreign currency. Informal markets have emerged to satisfy the need for basic items and foreign currency. Few people, businesses or even government institutions can survive without recourse to these illegal

markets. More positively, new powers and a new governor at the reserve bank appear to be making headway in cleaning up the financial sector.

Institutional, legal and judicial reforms are urgently needed in the **Democratic Republic of the Congo**, but will be difficult to achieve given the precarious post-war political situation. Many of the leaders of today's transition government have been accused of embezzlement to fund the conflict. A key area for reform is government contracting. Anti-corruption measures are applied to contracts funded by international donors but only 3 per cent of contracts entered into by the Congolese authorities involve a tendering process.

The creation of **Burkina Faso's** new High Commission for the Coordination of Anti-corruption Activities was met with optimism, and the success of the country's broader anti-corruption strategy is closely tied to the ability of this new body to take on high-profile corruption cases and ensure that its work is visible. The insistence by the commission on publicising progress reports on corruption cases is positive, as is the national anti-corruption policy it released in April 2004.

Studies by various international organisations into corruption in **Cameroon's forestry industry** prompted the government to create a new unit to fight corruption in the sector. However, the fact that the unit was created within the under resourced forestry ministry – the very site of many of the alleged corrupt acts – has dented expectations that the new team will be effective. **Police** corruption continued to be a major concern in the period under review. In March 2004 taxi drivers went on strike, denouncing police harassment and demanding that the state-defined rate set for fines be respected.

Asia/Pacific

Corruption in **elections** was a concern in several countries of the region. At national elections held in July 2003 in **Cambodia**, there were reports of widespread vote buying, violence and intimidation by all contesting parties, particularly in rural areas. The ruling Cambodian People's Party accounted for the larger share of these allegations. The elections interrupted protracted discussions over an anti-corruption law, a key demand of civil society, though the draft currently under debate is weak and falls well short of the requirements of the UN Convention against Corruption.

Vote buying was also a problem in **Indonesia's** July 2004 presidential elections, according to reports by the general election supervisory committee and watchdogs such as Transparency International Indonesia. The weak campaign finance law of 2003, which lacks sanctions for failing to present accounts or disclose donors, did little to deter parties from attempting to bribe the electorate. There is evidence that corruption has been decentralised along with power since the end of the Suharto administration in 1998.

Independent monitoring of election spending in **Sri Lanka** uncovered a multitude of irregularities at the April 2004 ballot, including the abuse of state resources – particularly state media – for campaign purposes.

In **India**, state parliamentary elections in November 2003 provided the first extensive test of a requirement for all candidates contesting elections to declare their educational levels, criminal records, assets and financial liabilities. The information was widely publicised by the media and monitored by NGOs.

Political instability and an apparent lack of concern by the electorate about the criminal history of aspirants to elected positions have contributed to high levels of corruption and **impunity** in **Vanuatu**. Former prime minister Barak Sope was sentenced in 2002 to three years' imprisonment for forging government guarantees, yet a year later he was elected in a by-election. President Alfred Maseng Nalo was elected in 2004 as he was serving a two-year suspended sentence for corruption.

Several countries issued **whistleblower** regulations in 2003–04. The **Indian** government issued a resolution on whistleblowers in April 2004, which, though welcome, is weaker than the draft law written by the Indian Law Commission and currently under examination by the government. Whistleblower protection was also approved in **Japan** in June 2004 and will come into force by 2006.

The **judiciary** came under scrutiny in **Sri Lanka**, where a survey of acting and retired judges carried out by the Marga Institute gave substance to the public perception that corruption is widespread in the judiciary. Of 50 judges questioned, 41 reported 226 incidents of bribery within the judiciary. There have been two attempts to impeach chief justice Sarath Nanda Silva

on charges including obstruction of justice, violation of the constitution and abuse of power. On both occasions the president dissolved parliament before proceedings could be completed.

The **Vietnamese** government has repeatedly affirmed its determination to tackle corruption and, as evidence that it is serious about this goal, has prosecuted several prominent figures. With tight state control over the media, there is little independent investigation into the wrongdoing of senior officials, however, compounding the risk that investigations will remain selective rather than comprehensive.

An anti-corruption commission was created in **Bangladesh** in 2004 to replace the discredited anti-corruption bureau. The commission has wide-ranging investigative powers, but its autonomy is limited. The commissioner is appointed by the president and the government controls its budget. New **procurement** regulations that promote transparency and accountability were introduced at the ministry of planning, but, significantly, exceptions are allowed on matters of state security, including military spending.

A new presidential decree on public procurement was issued in **Indonesia** in December 2003, creating a national oversight office and requiring full disclosure of all bidding information.

New guidelines on procurement were also introduced in **China** in line with the 2003 Government Procurement Law. A key area of concern is corruption in the construction sector, especially given the massive spending on infrastructure for the 2008 Olympic Games. An auditing and supervision department has been set up by the Beijing government and the organising committee for the Games to oversee an estimated US \$16 billion of business opportunities for domestic and foreign investors.

Europe

Corruption was a trigger for **political change** in parts of Central and Eastern Europe. **Georgian** president Mikhail Saakashvili swept to power in January 2004 with a promise to tackle corruption as his first priority. Tough action against five high-ranking officials of the Shevardnadze government won the confidence of the general public and the international community leading to the renewal of some international loans to the country. Civil society has also voiced concern, however, that civil and human rights have been undermined by the zealous anti-corruption campaign.

In **Russia**, President Vladimir Putin's crackdown on corruption came under fire for selectively targeting his political opponents, most notably Mikhail Khordorkovsky, chief executive of oil giant Yukos. A new presidential commission has been set up to tackle corruption, but has little power to do more than merely advise the president on anti-graft measures. Civil servants' salaries were substantially raised in 2004 in an effort to curb extortion of bribes for administrative services.

Several countries introduced wide-ranging **anti-corruption laws** in the period in question. **Azerbaijan's** new anti-corruption law came into effect in January 2005, against a backdrop of scepticism about whether it will translate into concrete actions to curb corruption, given the flaws in the law itself and a track record of poor law enforcement in the country. The law creates new anti-corruption bodies, but makes them dependent on the executive.

Britain continues to debate its draft anti-corruption bill, which was published in March 2003, but the future of the law remains uncertain. It is criticised for failing to provide a clear definition of corruption and terms that will be easily understood by enforcement agencies and the public at large.

A number of regulatory initiatives attempted to curb **corruption in politics**. A series of new laws adopted by the **Romanian** parliament aim to limit the abuse of political office. These included the restricting of parliamentary immunity, new asset disclosure requirements on candidates for political office and a code of conduct for civil servants.

Amendments to **Latvia's** political party finance law were adopted in February 2004 setting limits on spending, prohibiting corporate donations and providing for comprehensive reporting requirements and control mechanisms. The law is one of the most progressive in the region.

Serbia adopted a new law on political party financing, which introduced public funding for political parties. Loopholes in the law and ambiguous wording about the state's commitment to provide funds to parties limited its impact in the June 2004 presidential elections, however, and the electoral commission lacks the resources to verify campaign finance reports.

Slovakia introduced a new conflict of interest law, under the impetus of a civil society coalition, Alliance – Stop Conflicts of Interest. The law that was eventually adopted in May 2004

is significantly weaker than the version proposed by NGOs and the minister of justice. Implementation mechanisms are weighted in favour of public officials, and many sectors of government as well as important state-controlled companies fall outside the scope of the law.

In **Croatia** civil society lobbying efforts bore fruit in October 2003 when the Right of Access to Information Act and the Conflicts of Interest in the Exercise of Public Office Act were passed. Both acts are weaker than the versions supported by civil society. More worryingly, there are indications that the laws are not being respected. Public authorities failed in the first year of implementation to publish their annual reports of activities, while the commission charged with monitoring conflicts of interest has not been given a budget and has yet to be legally constituted.

Independence of the **judiciary** continues to be a problem in several countries and could prove a stumbling block as **Romania** prepares to join the EU in 2007. Lawmakers appear especially unwilling to grant the judiciary financial independence. In the **Czech Republic** the judiciary came under scrutiny for colluding with administrators of bankruptcy proceedings with whom they allegedly shared assets skimmed from lucrative bankruptcy cases.

Private sector corruption was never far from the headlines. One in four business leaders in **Norway** say that corruption exists in their industry sector, and one in 10 admitted that it affects their company, according to a survey by Norway's largest insurance firm, Gjensidige NOR. The survey followed press coverage of a series of cases involving price fixing, collusive tendering, embezzlement, tax, fraud, false accounting and solicitation of bribes.

In **Poland**, investigations into Rywingate – the attempt by a film producer to bribe MPs to vote against a media ownership bill – drew to a close, but not before prompting investigations into other allegations of bribery by private lobbying groups, in particular from the pharmaceutical, bio-fuel and mobile telephone sectors.

Bribes were allegedly paid for contracts to build a new football stadium in Munich that will stage the opening match of **Germany's** 2006 World Cup. The Austrian company Alpine was said to have paid 2.8 million euros for classified information leading to its winning the contract. Politicians renewed calls for a national blacklist of companies convicted of corruption, though the proposal has yet to be seriously debated at federal level.

In **Ireland**, the official probes into the influence of business over politics set up in the 1990s continued to unravel complex networks of covert financial payments to politicians and public officials. The inquiry into bribery of planning officials in Dublin continues.

Turning to the **finance sector**, **Britain** continues to demonstrate a double standard between corruption at home and abroad. It is unclear whether new anti-corruption controls for the Export Credit Guarantee Department, to which 95 per cent of all debt from developing countries to Britain is actually owed, will be applied with the rigour needed to prevent lending to lucrative projects that are plagued by corruption.

Turkey adopted new laws criminalising false reporting by banks and improving banking supervision after it was revealed that some of the country's largest banks were embezzling deposits or using them to obtain credit. In the past seven years the state has had to take over 22 banks whose owners and senior officials are on trial for embezzlement at a cost to the public purse of US \$42 billion.

Americas

Canada's relatively 'clean' image was shaken by a scandal involving massive misappropriation and misuse of public funds in the department of public works. Money intended to create a more positive perception of the federal government in Quebec following the narrow defeat of the 1995 sovereignty referendum was funnelled to advertising firms – some with political connections to the government – through schemes involving over-billing, artificial invoices and fictitious contracts. As a result, a series of institutional reforms including improved whistleblower protection and new appointment procedures for executives of state companies was introduced.

Elections were held in Argentina and Panama. The new **Argentine** political finance law was put to the test for the first time in April 2003, but the results of an analysis of financial reports and parallel monitoring efforts shows that while it is positive that parties have to disclose financial reports, these reports often bear little relation to reality.

Corruption was centre stage in the May 2004 **Panamanian** elections, with all four candidates promising concerted action to fight graft. It remains to be seen whether the winner, President Torrijos, has the political will to translate his promises into actions. High levels of voter

fraud and accusations of irregularities in the financing of the 2004 electoral campaigns have pushed electoral reform high on the public agenda.

The **judiciary** was a topic of concern in several countries. In **Nicaragua**, despite pressure from the G8, the main political forces failed to approve a new law that would introduce transparent and competitive recruitment procedures and would require the supreme court to relinquish its current powers to administer appointments and salaries.

In 2002 **Argentinean** president Néstor Kirchner had spearheaded the impeachment of judges who had been handpicked by former president Carlos Menem. In 2003-04 the new procedures for the appointment of supreme court judges were applied. To wide public acclaim these new procedures gave the legal, academic and civil society communities the opportunity to raise objections to supreme court nominees.

The weakness of the judiciary relative to the executive and legislative branches of government was evident in **Bolivia** where parliamentary immunity and a compliant congressional commission responsible for investigating high-profile corruption cases allowed five-year old allegations of corruption against former defence minister Fernando Kieffer to continue to stall. Also in **Bolivia** the misuse of state funds was evident at various levels of government. An accusation that a government minister had embezzled ministerial funds prompted a debate over a new law that would give the auditor general and a legislative commission oversight over the use of the funds.

Corruption at local level was the focus of initiatives in **Colombia**. Governors and mayors were asked to sign transparency pacts with civil society organisations in an effort to tackle corruption at the regional and sub-regional levels. Success of the scheme has been limited, however, because the terms of the pact are too vague for compliance to be effectively monitored.

In **Peru**, corruption at local level also came into focus as the central government set in train its process of devolution of power to the regions. The speed with which the operation was implemented, however, meant there was no time to put control mechanisms in place to supervise the new local government institutions, and a year later eight of the 25 regional presidents had been investigated for corruption and one had been deposed for bribery and embezzlement. Failure of the new institutions to provide watchdog bodies and their constituents with information about their operations is a major failing.

The **Brazilian** government's fight against corruption continued to be characterised by knee-jerk reactions to scandals rather than a concerted effort to tackle the problem branch and root. Corruption in gambling and football was a big topic in the period under review, which saw the president of the Brazilian Football Confederation and a former coach of the national team under investigation for embezzling fraud and misappropriation of funds.

Corruption scandals in **Costa Rica** served to underscore the importance of independent monitoring of government contracting. The social security administration was accused of accepting bribes for the award of a lucrative medical equipment contract, which prompted the legislature to revive discussions over a six-year-old anti-corruption bill. One effective oversight agency, an academic institute charged with overseeing the highway agency, was hampered by a lack of financial independence.

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ⁱ See Transparency International's 2002 Bribe Payers Index, and Control Risks Group's 'Facing Up to Corruption', summarised in the *Global Corruption Report 2003* and *2004*, respectively.

ⁱⁱ UNCTAD, *Regulation and Liberalization in the Construction Services Sector and its Contribution to the Development of Developing Countries* (UNCTAD, 2000), available at www.unctad.org/en/docs/clem12d2.en.pdf