

# Corrupt but legal:

## Institutionalised corruption and development finance

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I want to talk this morning about corruption in development finance.

But those expecting a Hollywood-style exposé of sleazy officials, brown paper envelopes stuffed with cash or secret bank accounts will be disappointed.

For the corruption I want to talk about is the corruption that has no need to hide in the shadows because it is perfectly legal.

So the focus is not on bribes or money laundering or fraud – important as these are to expose – but on lawful, routine, accepted practices that decay, debase or otherwise deteriorate democratic politics.

This sense of corruption-as-decay has longer history than the relatively recent equation of corruption simply with bribery, money laundering and fraud.

Reclaiming this older usage, I want to argue, is critical if corruption is to be recognised for what it is: a form of politics without which modern capitalism could not flourish.

So let's begin with a simple fact: most corruption today is entirely lawful. Some corruption is certainly criminalised. The bribery of foreign officials is now universally outlawed, even in countries, such as Germany, where until twenty years ago it was legal.

Bribes are also no longer tax deductible, a practice that was also legal in many European countries until the mid-1990s.

Fraud, extortion and money laundering are unlawful in all jurisdictions, although not a single US bank has ever been prosecuted for the crime of money laundering.

But bribery, money laundering and fraud are not the be-all-and-end-all of corruption.

Indeed a narrow focus on such crimes (vital as it is to investigate and prosecute them) hides many perfectly legal practices that the general public often rightly regards as corrupt.

Cue the steady stream of heads of industry, ex-Ministers and government officials that pass back and forth (quite legally) through the revolving doors between politics and business.

Cue the partly tax deductible fine (yes, the public pays, not the company) that Goldman Sachs negotiated when it was charged with selling worthless packages of subprime mortgages.

Cue the "immaculate" corruption that sees companies pleading guilty to criminal charges but no individual being indicted.

Cue the self-interested policy-making that, through privatisation, outsourcing and public-private partnerships, has transformed the provision of public services into publicly-guaranteed get-rich-quick for private investors and financiers.

Cue the “take, not make” playground that has been created for rent-seeking financiers, with the public picking up the tab through enforced austerity – in effect, the theft of workers’ wages – when things go wrong.

Many of these perfectly legal but nonetheless corrupt practices are not only routine within government and companies: they frequently pass for “good governance”.

Some may even be deemed duties of office; and many – privatisation, for example – are the stated mission of public bodies.

Something is clearly “rotten in the state of Denmark”.

It is not just that the law is unequally applied.

The decay goes deeper: the very policies and laws that overtly serve to combat corruption are now themselves a shield to the corrupt.

### **Neoliberalism’s corruption**

Take the definition of corruption employed by the World Bank, namely, “the abuse of public office for private gain”.

The first thing to note is that the definition to exclude whole swathes of corrupt practice from scrutiny

For starters, corruption is cast exclusively as a pathology of the public sector – “the abuse of public office for private gain”.

The definition thus renders “uncorrupt” (and legal) a range of corrupting forms of power-mongering, one example being political contributions by companies.

The focus on *individual* “private gain” made by *individual* “office holders” likewise obscures institutionalised forms of corruption that benefit groups or classes without rewarding any particular “office holder” directly or at all.

The fetishising of public sector corruption also hides the many collusions between “public” and “private” that make most corruption possible.

Instead it casts the “public” (interpreted as “the state” or “bloated bureaucracy” or “regulators”) as a perpetually grasping hand and the “private” (interpreted as “the private sector”) as its victim.

For a neoliberal institution such as the Bank, the political advantages of such a one-side, slanted view of corruption are clear.

Anti-corruption policies can be readily enlisted (as they are) to the cause of rolling back the state, privatising state assets and giving the private sector a greater say in decision-making.

The “fight against corruption” becomes a means of reconfiguring what the Bank defines as “the public” and harnessing it to the interests of a supposedly “clean” private.

Critically, the intended outcome is not to banish the “private” from the “public”, but rather to make certain private-regarding interests acceptable and normal within the sphere of government decision-making, while outlawing others.

## **Beyond the public/private divide**

Is there anything we can rescue from the Bank's definition?

I think not.

And the reason is that the public/private divide is a dangerous distraction.

It relies on what historian of corruption Peter Bratsis has called the "fantasy" that the "public" and "private" can be treated as fixed, coherent and neatly bounded spheres.

They aren't and never will be.

And reducing corruption to a technical debate on where to set the entirely fictional boundaries between public and private misses what is most important about corruption.

Private gain at public expense, for example, is not automatically corrupt: every public sector employee in a sense scores private gains at the public's expense.

But *anti-social* gain – that is, gain at the expense of the common good – is, by any standard, corrupt.

A bribe is not necessarily corrupt: it may be entirely legitimate if it works to circumvent despotic authority.

But a bribe that circumvents democratic decision-making is corrupt.

Impunity from justice may not be corrupt, where (for example) juries refuse to convict in resistance to an unjust law.

But impunity that places those with power and wealth above the law simply by dint of their status is corrupt.

Undermining trust in an institution – a company that avoids taxes, for example – may also be key to delegitimising and challenging abusive power.

But undermining trust in the law through gaming regulations in the interests of accumulation rots the “good society”.

### **Corruption and the “good society”**

And here we come to the nub of the issue.

Corruption can only be understood in terms of its opposite: in terms, that is, of what is *not* impure, deviant, debased, tainted, disreputable, unscrupulous, venal, wicked, or any of the other common synonyms for “corruption”.

And that, of necessity, requires some shared understanding of what constitutes the “good society” and the “common good”.

Both of these concepts are far broader than that of the “public interest” (I mean, give us a break: what public agency, after all, does not automatically claim to be acting in the public interest?).

In effect, corruption – if it is to be properly identified and challenged – forces us to focus on the good society.

What does the “good society” imply for relations of political and economic power? Who decides? And through what processes? Whose voice counts?

It is precisely this political debate that is missing from current discussions of corruption.

Yet without the conversation, there can be no legitimate public sense of what does or does not constitute corruption.

Preventing the conversation or undermining the political processes through which it might occur should thus, arguably, be recognised as the ultimate form of corruption.

Indeed the common thread that runs between all forms of corrupt practice – from bribery to revolving doors – is the capturing or bypassing of democratic forms of deliberation through which a common understanding of the common good can be reached.

It is this broader impact on society as a whole, rather than illicit private gain per se, that makes an action corrupt.

A bribe does not simply put money into the hands of a politician: it excludes all but the politician and the briber from a say in a decision that affects the broader public, whose interests should be paramount.

The gaming of the law ensures that the scope, applicability and implications of legislation are changed not through democratic deliberation but through legal fora in which the public may not even have standing (arbitration courts for example).

And revolving doors between companies and government ensure that those around the decision-making table share a common, partial view of the world.

And through such “democracy grabs”, the body politic is gradually subverted.

It is rendered “morally unsound, rotten, infected” – it has become, in the Oxford English Dictionary definition, “corrupt”.

Private-regarding behaviour at society’s expense –*anti-social* gain - becomes the new normal, corrupting institutions and individuals alike.

This older sense of “corruption”, which dates back to Aristotle, is alive and well within the public at large.

Building on that older usage may therefore assist in breaking out of the anti-bribery cul-de-sac into which many anti-corruption campaigns have been driven by modern definitions.

Here I would like to explore some examples of corrupt practice that are legal, routine and central to the workings of contemporary politics and commerce.

### **The European Investment Bank: institutionally corrupt?**

One area that I have been researching is that of development finance – and particularly the practices of the European Investment Bank (EIB), one of the largest development finance institutions in the world.

So what EIB practices might arguably fall into the category of institutionally corrupt – that is rotten, corrosive of democracy, anti-social?

One area of concern is the EIB’s support for public-private partnerships (PPPs).

There is no doubt that such support has yielded huge profits for private companies – returns can be as high as 25% a year.

But has this private gain been achieved at the expense of democracy – the key test of institutional corruption?

Some salient features of the ways in which PPPs have been promoted and negotiated are pertinent.

One is that the legislative changes needed to enable PPPs, particularly in the global South, have often been imposed on governments, generally

as loan conditions agreed through behind-closed-door negotiations from which the public is excluded.

This is corrupt.

Another is the one-sided advice that the EIB provides on how PPP legislation should be structured.

The EIB-funded European PPP Expertise Centre (EPEC), for example, is staffed by advisors drawn from the EIB itself or staff on secondment mainly from the private sector.

Not a single trade unionist, human rights defender or environmental activist appears to be involved.

Instead the advisors are drawn from a pool that reflects a limited set of social, economic and political interests.

As such, the public cannot trust that their advice reflects “the common good”.

And, without such trust, the public arguably cannot have a sense of inclusion in the decisions that are made.

And that is potentially corrupting.

There is concern too over the PPP contracts that are negotiated.

Because democracy suffers when publicly-supported contracts are negotiated entirely in secret.

It suffers when “commercial confidentiality” is used to deny access to the contracts.

And it suffers when public institutions fetter democratic decision-making by “freezing” environmental and social legislation for PPP operators – an issue I will explore in more detail this afternoon.

And it suffers when contracts are used to lock in profits but lockout democracy.

And because democracy suffers, the EIB's support for PPPs may be said to be "institutionally corrupt".

No laws are broken, no regulations flouted. But that is precisely the point: the corruption is entirely legal – but no less corrupt for that.

### **Intermediated finance and corruption**

Many of the same forms of corruption would appear to characterise EIB funding for the private sector via so-called financial intermediaries, notably private equity funds.

Here the financial support provided is not direct but indirect: a private sector fund manager is provided with funds by the EIB that are then invested on its behalf.

As with PPPs, there is little doubt that the EIB's investments enable private gain to be made at public expense.

But public investments in private equity funds come at a huge cost to democratic accountability.

Like PPPs, private equity fund contracts are negotiated in secret and rarely disclosed. The public is not therefore able to scrutinise their terms.

But some details have emerged from leaked contracts.

Typically, the contracts give investors only "limited rights" to the accounts and records of fund managers.

The investors generally have no rights whatsoever to withdraw from an investee company (even where it has concerns about its operations).

The investors have no rights to carry out anti-money laundering checks on the companies in a private equity fund's portfolio.

In effect, the channelling of public investments through private equity funds not only hands decision-making power to the funds, but effectively places those decisions largely beyond scrutiny.

The direction of travel is profoundly corrupt. Corrupt because the private gains at public expense rests on the systematic erosion of democratic accountability.

### **Revolving Doors**

A third area of concern is the EIB's rules relating to conflicts of interest.

Under its current rules, EIB board members must report potential conflicts to an ethics committee, which then rules on whether they are problematic.

Where a conflict is identified, the rules give the discretion to individual board members as to whether or not they should abstain on votes. This is hardly reassuring.

As the European Ombudsman argues, it should be "the responsibility of the relevant EU institution, and *not the individual in question*, to determine whether there is a conflict of interest.

The mere appearance of such conflicts, the Ombudsman stresses, is problematic – and should be prevented.

Rightly so, for appearances are critical to maintaining public trust. And without trust, the public cannot be "included" (albeit by proxy) in decision-making.

The appearance of corruption is thus an important standard for judging institutional corruption:

To deny such a standard is, in the words of US academic Dennis Thompson, “tantamount to denying democratic accountability” since “appearances are often the only window that citizens have on official conduct”.

The EIB does not deny that appearances count, but claims that it does not have the staff to take a proactive role in scrutinising all the affiliations of board members.

But, in the minds of many people, relying on self-reporting and self-identifying by those who should be scrutinised renders corrupt a screening system overtly intended to avoid corruption.

The arbitrary rules governing the “cooling off” period between serving on the EIB’s board and being able to lobby the EIB are also problematic.

For example, members of the EIB’s Board of Directors must wait just six months before they are permitted to lobby. Why six months? What makes six months and a day ethical but six months less a day unethical? For that matter, what makes six months ethical?

And why does no cooling off period apparently exist for the eight independent experts who sit on the Investment Committee of the EIB’s European Fund for Strategic Investments?

Is it really credible that some might not wish to lobby for the companies they work for or have worked for? Companies which, to judge from the experts’ published declarations of interest, have in three cases received EIB funds.

The very arbitrariness of the rules only serves to underscore the conflicts of interest that are present and the incoherence of the “public/private” divide as a means of identifying corruption.

Many are left with the impression – and impressions count – of an elaborate, ritualistic ballet dance of integrity, in which “holy water” is poured on certain practices either by sanctioning them through weakly drawn codes of conduct.

The cooling off rules, for example, only mention “lobbying” as a prohibited activity. They do not appear to prevent former senior executives of EIB from taking jobs with companies who have benefited from EIB loans during their period in office, either inside or outside the “purdah” period.

What is at issue here is not the individual behaviour of those who act according to the rules but the rules themselves – and whether or not they allow for practices that the public consider corrupt.

And it is the public’s perception – rooted in a non-legalistic view of corruption – that matters here.

Revolving doors are viewed as cronyism: a self-referential and self-serving system which allows private interests both to influence and to benefit from policy making.

Cronyism is poison to the body politic: and it is this that makes revolving doors corrupt.

The ripples wash through the entire system.

The public sector comes to be managed increasingly as a private company

This is a world where regulators seeking to tighten financial regulation are told (and I am not making this up): “You shouldn't be listening to government lawyers: you should be listening to private lawyers”.

A world where government agencies deem it appropriate that companies receiving public support should “self-assess” their compliance with the environmental and social safeguard policies on which that public support has been conditioned.

A world in which the first instinct of officials confronted with allegations of wrong doing is not to call the police but to email the accused wrong doer.

For this is a world in which “pockets of impunity” are created through a cosily-defined common purpose between the public and private sectors, and a myopic blindness to its conflicts.

A world that is, in a word, “corrupt”.

## **Beyond Bribery**

What might one conclude from this brief foray into institutionalised corruption?

That PPPs are an institutionally corrupt form of public service delivery?

Absolutely!

That intermediated public finance corrupts democratic accountability?

For sure.

That the EIB is shot through with rules that ferment practices that the public views as corrupt? That too.

But this should not surprise.

For the distinctions between legal and illegal corruption or between public and private graft hide a simple truth.

To be blunt: corruption-as-social-decay is not as an aberration of the market but an inevitable outcome of profit-making activities.

Recognising this, will surely be essential if strategies and alliances are to emerge that can genuinely unsettle corruption.

For the task we face is nothing less than rebuilding the now decayed processes that would allow the “common good” to be defined through democratic politics, not those seeking political or financial gain.