

Exporting Corruption: How Rich Country Export Credit Agencies Facilitate Corruption in the Global South

An interview with The Corner House
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The Corner House is a small UK-based research and advocacy organization. Since its founding in 1997, The Corner House has aimed to support democratic and community movements for environmental and social justice. Its current staff are Nicholas Hildyard, Susan Hawley, Larry Lohmann and Sarah Sexton. The Corner House has been a leader in documenting how rich country institutions, especially export credit agencies, promote or contribute to corruption in developing countries, and in documenting the effects. The Corner House has also played a key role in advocating for reforms in the UK and other rich countries to combat corruption around the globe.

Multinational Monitor: What are Export Credit Agencies (ECAs)? What is the rationale for their existence?

The Corner House: The mission of ECAs is to promote national exports. ECAs are public or state organizations that use taxpayers' money to insure companies operating or trading abroad against commercial and political risks. These "country risks" include violence or war, nationalization and expropriation, foreign exchange shortages, the buyer being unable or unwilling to pay, the importing government interfering, the company's deal or project not being completed or not being commercially viable, a moratorium on external debt and a break-off in trade relations.

An exporter takes out insurance — an export credit guarantee — with an ECA, which undertakes to pay the exporter for the exported goods and services if the importer defaults on payment. The financial liabilities of ECAs are underwritten by national governments, although ECAs that are part of the OECD [the Organization of Economic Cooperation and Development, made up of the world's industrialized countries] are required to cover any losses from the premiums they charge.

ECAs not only insure against risks that commercial insurers won't; they typically do so at lower premiums. ECA insurance provides the political backing of national governments that can enforce contracts or ensure that companies get paid.

For companies and the banks that finance them, wrote Rupert Wright in *EuroMoney* nearly a decade ago, "What could be nicer in times of turmoil than having the risk picked up by the taxpayer."

MM: How economically substantial are ECAs?

The Corner House: ECAs are the largest source of public finance for private sector projects in the world. They underwrite 10 percent of global exports from large industrial countries. ECAs provide 80 percent of gross capital market financing from private sources for developing countries, according to World Bank data. Between 1998 and 2002, ECAs' support averaged \$85 billion a year in medium and long-term credits, compared to some \$67 billion lent annually by the World Bank and other multi-lateral development banks, according to the International Monetary Fund (IMF). Between 1995 and 2002, according to the IMF, every major commitment over \$20 million made by a Western bank to companies operating in or trading with poorer countries had some form of official public guarantee.

MM: Does ECA activity change what projects multinationals will invest in? Would they make the same investments even in the absence of ECA support?

The Corner House: Few companies will operate in developing countries without ECA support. In particular, private financial markets will not invest in large extractive or extractive-related infrastructure projects without ECA backing — the risks are considered too high. ECA involvement assures would-be investors that a project has the backing of institutions with sufficient political muscle to ensure that debts and contracts will be honored by the host country.

MM: Do ECAs provide funds to cover the cost of bribes? Is this done knowingly?

The Corner House: Export credit agencies can be complicit in corruption in several ways, most directly when commissions hiding bribes are involved. A company often pays a commission to a local agent or “fixer” to help win a contract for a project or deal. A legitimate commission would be 2 to 3 percent of the total cost of a project and paid into a local bank account of a respected local businessman who had no personal ties to contract decision-makers. A dubious commission containing a bribe might be 10 to 20 percent, paid into an offshore account or secret trust, or paid to a minister or official involved in decision-making on the contract to be awarded.

When ECAs insure a company’s contracts against the risk of not being paid or the project being cancelled, they have usually included these commissions in the overall sum underwritten. Underwriting commissions is thus “an indirect encouragement to bribe,” according to former European Union Director-General for Development Dieter Frisch.

ECAs have also paid out insurance claims to companies when Southern governments have cancelled their contracts because the company allegedly paid bribes. In July 1998, Canada’s export credit agency reimbursed BC Hydro after the Pakistani government cancelled its contract for a power plant project because it had allegedly paid bribes to government officials.

MM: Do ECAs provide insurance for companies engaged in corrupt activity? Is this done knowingly?

The Corner House: Even though bribery is difficult, increasingly sophisticated and potentially expensive to prove, ECAs have a long history of turning a blind eye to graft. They regularly back deals that are obtained corruptly. Many ECAs do not require the contracts they back to have been won through competitive tender, which can be a sure way for buying or importing countries to ensure they get value for money. When allegations of corruption do arise, ECAs have often merely asked the companies they insure for assurances that no wrongdoing took place and have not investigated further.

MM: A key function of ECAs is their public nature and ability to apply political muscle against developing countries. How do they employ this muscle, and how does this relate to the corruption issue?

The Corner House: ECAs have encouraged developing countries to overlook corruption and pressured governments to drop corruption investigations. In 1998, various Western countries pressured the Pakistani government to abandon its corruption investigations into the Hubco power plant, built in 1997 and backed by the ECAs of France, Italy and Japan.

MM: What was the role of ECAs in supporting Enron’s energy project in India (and other Enron projects)?

The Corner House: Enron received an estimated \$7.2 billion in public funds for 38 projects in 29 countries, according to estimates by the Washington, D.C.-based Sustainable Energy and Economy Network. Of this, OPIC — the Overseas Private Investment Corporation, a U.S. government agency offering investment insurance — approved over \$2.6 billion in risk insurance for 14 projects. Over 10 years, the U.S. Export-Import Bank provided \$825 million in support of five Enron-related projects around the world. Enron officials served on the Bank's advisory committee. Non-U.S. ECAs also financed Enron heavily.

At least five ECAs, including those of the United States, Britain and Belgium, funded Enron's Dabhol Power Plant in the Indian state of Maharashtra. The project was agreed to in haste without transparency or competitive tendering, and was surrounded by corruption allegations from the outset. In June 2001, the Dabhol Power Company shut down the plant after the Maharashtra State Electricity Board decided not to buy any more power from it. Dabhol power was four times more expensive than that from domestic power producers. Maharashtra was spending more on power from Dabhol than its entire budget for primary and secondary education. Despite the shutdown, Enron continued to bill the Electricity Board \$21 million a month. In September 2001, Enron demanded that the Indian government pay it \$2.3 billion for its investment and debts on the project.

After Enron's collapse in December 2001, Dabhol was put up for sale. Foreign investors claimed that it had been effectively expropriated by the Indian government, and international court battles ensued. Many investors have now been compensated via their national ECAs, which will seek to recover their pay-outs from the Indian government. The Indian government, and ultimately the Indian people, face a huge bill for that "white elephant." Both foreign investors, and the ECAs that backed them, were extremely negligent in assessing Dabhol's risks and should accept mutual responsibility for the aftermath.

But the U.S. government, represented by Vice President Dick Cheney, reportedly threatened to withdraw aid from India and warned that the dispute would "spell death to potential investment in India" unless the Indian government came up with a solution that benefited Enron and protected U.S. taxpayers' money.

MM: How did ECAs facilitate corruption during the Suharto regime in Indonesia, and what did they do after Suharto's exit?

The Corner House: During the Suharto era, it was an open secret that many deals were tainted with bribery. Yet Indonesia was a major recipient of ECA funding. After Suharto's fall in 1998, ECAs continue to turn a blind eye to corruption. An Indonesian state audit report in September 2002 revealed that 4.2 billion rupiahs (£280,000/\$550,000) of foreign funding intended as export credit facilities for the Indonesian defense ministry, armed forces and national police were missing because of corruption.

ECAs have opposed Indonesian government action to cancel Suharto-era contracts if investigators found evidence of corruption. In July 1999, the ECAs of Japan, Germany, Switzerland and the U.S. pressured the post-Suharto government to honor such contracts awarded to Western companies to supply power. These contracts cost, on average, over one-third more than they should have; were not won through competitive tender; and were strongly suspected of being infused with corruption. The Indonesian people paid for that possible corruption in the form of higher power tariffs.

MM: What is the role of ECAs in the defense sector, and how does this relate to concerns about corruption?

The Corner House: ECAs have historically been major supporters of the arms industry (with the exception of U.S. Ex-Im, which does not finance arms sales, because the Pentagon has its

own export credit service). In the 1990s, the British ECA used 30 percent of its budget to cover military exports. During the same period, roughly one-fifth of the contracts concluded by the French ECA were for military purposes, according to recent research by the European Network Against Arms Trade.

Bribery is an acknowledged and well-entrenched feature of the arms trade. According to the American Chamber of Commerce, 50 percent of the bribes paid worldwide between 1994 and 1999 are related to the arms trade. The CIA estimates 40 to 45 percent. Yet the arms trade accounts for just 1 percent of world trade.

MM: Is it fair to blame ECAs for their entanglement with corruption? Isn't this how megadeals are done throughout much of the developing world? Can the ECAs realistically stay out of these deals, if that's where the action is?

The Corner House: There isn't a country where there are not laws against corruption. ECAs are public institutions and are bound by the law. So it isn't a question of being "fair" or "unfair:" it is a question of honoring the law.

Corruption cannot be excused on the racist grounds that it is normal "business practice" in developing countries. Focusing on developing countries instead of industrialized ones — on bribe-takers, not bribe givers — obscures the close connection between the institutional culture, bureaucratic practices and priorities of public and private institutions in the North, and corruption in the South. It also obscures the long history of anti-corruption movements in the South, which dispel the claim that corruption is a "cultural norm" in the South. It was Lesotho — not the Northern countries — which initiated lawsuits against the multinationals subsequently found guilty of bribery in the notorious Lesotho Highland Water Project.

And one should always remember that corruption is not a "victimless crime." In poorer countries, corruption has a more devastating and immediate impact on its victims. It diverts expenditure away from health and education, where bribery returns are small, to more lucrative sectors such as construction, defense, and oil and gas. The poor are most affected by "white elephant" projects such as power plants or dams that have been arranged in corrupt circumstances, fail to meet their stated objectives, dislocate local communities and cause environmental damage. In the energy sector, contracts awarded in dubious circumstances have locked governments into paying high rates for electricity, which are passed on to the consumer in the form of higher tariffs.

The people of Southern countries can also end up paying for corrupt and unproductive projects when export credit agencies pay compensation to companies and then recover the amount directly from Southern governments or add this amount to a country's official debt.

MM: Are there meaningful differences among ECAs, in terms of their attitudes toward and policies on corruption?

The Corner House: Different ECAs are forging ahead (and lagging behind) in tackling corruption in various areas.

Official information may not be reliable. Analysis by a trade union anti-corruption group, UNICORN, of a September 2005 OECD survey of ECAs' use of anti-bribery measures puts Greece at the top with a score of 12 out of a maximum 16.5, followed by Austria, Italy and Australia. With the exception of Italy, G7-country ECAs performed poorly. Germany was bottom of the G7 group with a score of 6.67, and in twenty-seventh position overall, the U.S. was second bottom and twenty-fifth overall. However these results in all likelihood reflect how the ECAs filled in the OECD's questionnaires rather than actual practice.

In March 2006, Britain's ECA — under pressure from parliamentarians and NGOs — reinstated anti-bribery measures that it had earlier scrapped as a result of corporate lobbying. These are likely to put Britain now well ahead of other ECAs.

MM: What do ECAs demand from importing countries by way of guarantees?

The Corner House: When ECAs give insurance to a company or bank doing business abroad, they almost always require the importing country to offer a counter-guarantee. In the event of a default, such as a contracting party not paying up or the project proving unviable, the importing government must compensate the ECA concerned. If it does not do so, the amount is added to the importing country's official debt as a bilateral (government-to-government) debt.

MM: How significant is developing country debt related to ECA-backed deals? Is there any way to estimate how much of this figure was siphoned off in corrupt deals?

The Corner House: The debts owed to ECAs are huge — export credits represented some 34 percent of the \$1 trillion in external indebtedness of developing countries in 2002. Export credit debt is charged at commercial rates of interest, not the lower rates incurred by bilateral or multilateral loans. Export credit debt is therefore particularly onerous for poorer countries.

This build-up of debt owed by Southern countries to ECAs has been exacerbated by the “moral hazard” that lies at the heart of the export credit process. Companies know that they will be rescued by ECAs from “the consequences of their own decisions” — they will be bailed out by the public purse with few questions asked if things go wrong with their business decisions. They may not, therefore, be as prudent in their investment decisions or as cautious in their risk assessments as they might otherwise be, particularly if they do not have to consider fully whether a project is commercially viable or not because of ECA insurance. The substantial debt owed to ECAs suggests that this has indeed been the case.

No audits have been conducted of the debt owed by ECAs — so it is impossible to know for certain how much is debt incurred as a result of corruption. It is likely to be high, however.

MM: Can developing countries reasonably refuse to provide the guarantees that ECAs seek to extract?

The Corner House: Not if the ECAs are to fund companies operating in their countries.

MM: Are ECA policies and practices related to corruption improving? If so, how? What are strengths and weaknesses of those policies and practices?

The Corner House: ECAs have dragged their feet on strengthening their anti-corruption procedures. In 2006, however, the ECAs of the OECD agreed on strengthened measures aimed at avoiding giving taxpayer support to export contracts tainted by bribery.

These provide for greater disclosure by ECA applicants. They are now required to inform the ECA if they have been charged or convicted of bribing a foreign public official in the five years preceding the application. They are also required to disclose their agents' identities, and the size and purpose of agents' fees and commissions “upon demand.”

OECD ECAs are now obliged to routinely check whether an applicant appears on any publicly available list of the international financial institutions, such as the World Bank, debaring it from being awarded public contracts. If an applicant is listed, or has disclosed violations of national anti-bribery laws, the ECA must scrutinize the project further before proceeding with its application.

If there is ‘credible evidence’ of bribery before credit is approved, OECD ECAs are now required to suspend the application while they carry out further investigations.

But there are still major loopholes. There is no automatic requirement for an applicant to disclose the identities of agents or the amount and purpose of commission. The applicant is not required to disclose information on the corruption track record of a subsidiary, joint venture or consortium partner. ECAs are not required to debar companies that have convictions for foreign bribery offenses, even when the applicant appears on a publicly available list, has been debarred by a national court, or is the subject of multiple corruption convictions. ECAs are required to report only credible evidence of bribery to their national law enforcement agencies, not suspicions of bribery.

MM: Are the new ECA rules on corruption likely to meaningfully impact the level of corruption in the developing world and the conduct of multinationals?

The Corner House: The new procedures for OECD ECAs are a step in the right direction. But everything will depend on the loopholes being plugged and the rules being enforced.

OECD law enforcement agencies still assume that bribe-giving companies are the victims of greedy foreigners demanding bribes — or that bribery is just the way of doing business abroad.

Corruption cases are complex. If Western governments are serious about tackling bribery carried out by their companies, they have to provide sufficient resources to their law enforcement agencies to prioritize and pursue bribery allegations. National initiatives to combat money-laundering so as to counter terrorism should theoretically provide governments and law enforcement agencies with greater access to information about bribes and other corrupt payments. But it is not yet clear that such information is leading to more investigations into or convictions for bribery.

The U.S. has had legislation since 1977 criminalizing the payment of bribes to foreign government officials and political parties by U.S. businesses and individuals, and requiring companies to keep accurate and detailed accounts reflecting all transactions. Yet until recently the U.S. courts have barely pursued companies paying bribes outside the U.S. As of 2003, there had been just 32 criminal prosecutions and 14 civil enforcement actions under the Foreign Corrupt Practices Act (FCPA), with 21 convictions — an average of one conviction a year. Lack of funds for proper enforcement, high standards for initiating prosecutions, the self-regulation approach of the U.S. Securities and Exchange Commission, and fluctuating political will have variously been cited as explanations.

Thus, despite the legislation, World Bank research shows that 42 percent of U.S. companies pay kickbacks to gain government contracts in former Soviet Union countries. U.S. companies are perceived as more likely to bribe than French, Spanish, German or British companies, using middlemen, such as agents, joint venture partners or foreign subsidiaries, to get around the FCPA. Since 2000, there has been a much higher level of FCPA enforcement activity (investigation and prosecution) and over the past two years record fines have been imposed, signaling “a heightened degree of scrutiny of and graver consequences for FCPA violators in the future.”

MM: What are the best solutions, or key elements of solutions, to disentangle ECAs from corrupt practices? How important should be the role of debarment, and is debarment politically feasible?

The Corner House: The most effective measure to tackle corporate bribery is refusing ECA support for a set period of time to companies convicted of corrupt business practices. The World Bank and some other international financial institutions already use debarment as an anti-corruption tool. All EU member states are now obliged to exclude from public procurement contracts companies that have been convicted by final judgment of corruption offenses.

The OECD has suggested debarment as an economic disincentive against corporate bribery. The ECAs of Belgium, Denmark, Greece, Hungary, Luxembourg and Switzerland say that it is their practice, though not a required practice, to deny official support where there has been a conviction for corruption.

Anti-corruption groups are also pushing for mandatory rules that would obligate ECAs to: require companies to disclose the names of their agents; introduce a ceiling on commission payments; withhold support where there are detailed and credible suspicions of bribery and where an official investigation has been opened; have in place rigorous anti-corruption due diligence procedures and audit procedures that will allow spot checks on customer documentation; inform national investigative authorities of suspicions or evidence of bribery as a matter of routine and required practice, and put in place appropriate whistleblower procedures to enable people both within the Export Credit Agency and outside it to raise concerns about corruption in projects supported by the ECA; and refuse cover to companies who have, or whose senior executives have, been convicted of corruption or bribery.

Several ECAs have already adopted some of these procedures.

MM: Should ECAs be shut down, and the insurance role left to the private sector? Would this harm developing countries?

The Corner House: ECAs were set up to subsidize Northern companies, not to benefit developing countries. Most ECAs have been “captured” by the richest of the rich corporations, (although banks also like them because they remove the risk from their loans.)

It is these corporations that would miss publicly funded ECAs the most. For people in the South, the end of ECAs would mean fewer bad projects since many of them would not go ahead. Although some ECAs are seeking to recast themselves by adopting a “sustainable development” mandate, ECAs are not sustainable development agencies — they lack the necessary expertise, approach and culture.

Privatizing ECAs would not necessarily resolve the problems.

Deprived of the “comfort blanket” that ECAs currently provide, the corporate sector would quickly seek to evolve new mechanisms to pass their risks on to the public sector. Privatized ECAs would not be subject to the same oversight or rules as public sector ECAs — and would not be bound even by the (albeit minimal) environmental, human rights or other standards under which official ECAs now increasingly operate.

In this respect, ECAs are a symptom of a much wider malaise.

The issue is how to reclaim development finance for the public good — rather than for the benefit of a small minority. Who should decide on investment policy? How might decision-making, at project and policy levels, be democratized? These are the prior questions that need to be addressed before asking the question of whether or not ECAs have a place in development.