

ANTICORRUPTION POLICY

PROPOSED CLARIFICATIONS AND RELATED CHANGES TO CONSULTING AND PROCUREMENT GUIDELINES

I. INTRODUCTION

1. The Anticorruption Policy¹ designated the Office of the Auditor General (OAG) as the point of contact for allegations of fraud and corruption in Asian Development Bank (ADB) projects and among staff. In September 1999, ADB established an Anticorruption Unit (OAGA) within OAG to deal with such allegations. With the experience gained in addressing such concerns since then, OAGA has concluded it is now appropriate to clarify certain aspects of the Policy by clarifying and strengthening the fraud and corruption-related terms, and applying sanctions to more than just the award of new contracts.

2. This paper addresses critical issues that affect the daily activities of OAGA and its ability to assure and promote the ethical standards required by the Policy. The current fraud and corruption terms are narrowly defined, and focus on procurement issues. This constrains OAGA investigations. Also, OAGA has found fraud and corruption in ADB-financed activities are not limited to procurement. In addition, the Policy effectively limits remedial actions primarily to ineligibility to be awarded ADB-financed contracts. OAGA has concluded this constraint may place ADB in a position where parties that ADB has found not to have maintained the highest ethical standards may find ways to participate in ADB-financed activities other than being awarded contracts. For example, such a party may be a subcontractor or supplier without being awarded an ADB-financed contract, or may actively participate in an ADB-financed seminar.

3. This paper is not intended as a comprehensive review of the implementation of the Policy. The Policy requires the Management to circulate to the Board a paper analyzing ADB's experience with the Policy.² The Governance and Regional Cooperation Division of the Regional and Sustainable Development Department (RSGR) has begun such a review, and is currently starting a consultation process. However, deferring action on this paper's issues will extend the constraints on OAGA investigations and effective remedial actions. Therefore, OAG has concluded immediate changes are prudent to minimize ADB's reputational risk. This paper was coordinated with RSGR, and does not conflict with its efforts to assess implementation of the Governance and Anticorruption Policies.

II. BACKGROUND AND ISSUES

A. Update Terms and Broaden Definitions

4. Recognizing that there is no universal or comprehensive definition of corrupt behavior, the Policy defined corruption as "the abuse of public or private office for personal gain" and included a more comprehensive definition.³ In an effort to harmonize ADB procurement standards, the Policy detailed the World Bank's definitions of corrupt and fraudulent practices from 1996 so that ADB could adopt those definitions.⁴ The Policy further illustrated corruption and fraudulent practices, but did not specifically define other terms.

¹ ADB. 1998. *Anticorruption Policy*. Manila.

² *Ibid.*, para. 79.

³ *Ibid.*, para. 17.

⁴ *Ibid.*, para. 19.

5. As a result, ADB's *Guidelines for Procurement Under Asian Development Bank Loans and Guidelines on the Use of Consultants by Asian Development Bank and Its Borrowers* (hereinafter collectively referred to as Guidelines) detailed fraud and corruption-related terms similar to the way the World Bank did. In ADB's Guidelines, corrupt practices are "behavior on the part of officials in the public or private sectors⁵ by which they improperly and unlawfully enrich themselves...by misusing the position in which they are placed, and it includes the offering, giving, receiving, or soliciting of any thing of value to influence the action of any such official in the procurement process or in contract execution." Fraudulent practices are "a misrepresentation of facts in or to influence a procurement process or the execution of a contract to the detriment of the Borrower, and includes collusive practices among bidders...designed to establish bid prices at artificial, noncompetitive levels and to deprive the Borrower of the benefits of free and open competition."

6. In May 2004, the World Bank gave new definitions of fraud and corruption-related practices associated with procurement. Appendix 1 is an excerpt of the World Bank's Procurement Guidelines detailing those revised terms. Although the World Bank acted unilaterally, it is appropriate for ADB to consider the World Bank's changes in fraud and corruption-related terms in the context of ADB's own definitions.

7. The World Bank's new definitions focus specifically on procurement. While OAGA has found that many fraud and corruption concerns relate to procurement, limiting the application of the Policy to procurement does not completely fulfill an explicit objective of the Policy: ensuring ADB projects and staff adhere to the highest ethical standards.⁶ Therefore, ADB's fraud and corruption-related definitions should not be limited to procurement issues. OAGA proposes to adopt the same terms introduced recently by the World Bank, but to modify the specific definitions to remove the limitation to procurement so that ADB can best fulfill its Policy objective.

8. OAGA has reviewed numerous concerns related to conflicts of interest, and acknowledges that understanding what constitutes a conflict of interest may vary. Although conflicts of interest may not necessarily constitute fraudulent practices or corruption, they clearly relate to maintaining high ethical standards. To permit ADB to effectively assess and manage conflicts of interest among its projects and staff, ADB should establish a single, consistent standard to form a basis against which all parties to ADB-financed activity can address concerns of conflicts of interest. Therefore, in addition to the terms used by the World Bank, based on OAGA experience, it is necessary for ADB to establish a definition of "conflict of interest" in conjunction with other terms defined pursuant to the Anticorruption Policy.

B. Update Operations Manual and Guidelines

9. ADB's Operations Manual Section C5 articulates the Policy's definition of corruption and explanation of fraudulent practices, and definitions pursuant to the Policy are specified in the Guidelines. Changes to terms and definitions pursuant to the Policy will necessitate updating those documents.

⁵ Inclusion of the private sector is the only difference between the World Bank definitions and ADB's.

⁶ ADB. *Anticorruption Policy*. paras. 53-73.

C. Reinforce the Policy's Objective

10. The Policy provided specific text, detailed in Appendix 2 of this paper,⁷ that was incorporated into ADB's Guidelines. That text limited to ineligibility for awards of ADB-financed contracts the action against entities found to have violated the Policy. Ineligibility for awards of ADB-financed contracts does not address numerous situations in which debarred entities may be involved in ADB-financed projects or other activities.

11. To ensure that ADB operations fulfill the need to assure and promote highest ethical standards, ADB should have sufficient latitude to respond to situations where debarred entities may become subcontractors, or may be involved in projects involving ADB funds, but where a borrower or another development institution (through a parallel financing agreement) exclusively finances a particular contract or activity. In addition, it would be appropriate for ADB to have latitude to assess whether debarred entities or their representatives should be allowed to participate in ADB activities other than contracts, such as conferences or workshops.

12. In outlining administrative changes for ADB, the Policy referred to alleged incidences of corruption among ADB projects and staff.⁸ In translating the Policy to an operational practice, ADB's anticorruption procedures⁹ limit OAGA to investigating concerns of fraud and corruption specifically related to an ADB-financed activity. However, ADB may find itself in situations where entities otherwise eligible to be involved in some capacity in an ADB-financed activity do not meet the highest ethical standards that the Policy demands, examples are entities that other international financial institutions have debarred for serious fraud or corruption, or reliable courts have found guilty of serious crimes. In such cases, ADB could jeopardize its reputation and integrity if it does not have the means to prevent such entities from participating in ADB activities or having access to ADB premises.

13. To fulfill the Policy's explicit objective to maintain the highest ethical standards in all aspects of ADB activity, it would be more appropriate if ADB, through its established anticorruption procedures,¹⁰ had the latitude to apply ineligibility to all aspects of an ADB-financed activity.

III. PROPOSED CLARIFICATIONS AND CHANGES

14. Pursuant to ADB's Anticorruption Policy, ADB will define

- (i) corrupt practice as the offering, giving, receiving, or soliciting, directly or indirectly, anything of value to improperly influence the actions of another party;
- (ii) fraudulent practice as any action, including misrepresentation, to obtain a financial or other benefit or avoid an obligation by deception;

⁷ ADB. *Anticorruption Policy*. Appendix 2.

⁸ *Ibid.*, para. 77(ii).

⁹ Formerly Guidelines on Operational Procedures, Section 55; now Audit Manual, Chapter 800, which may be found at <http://adb.org/anticorruption/anticorruptionprocedures.pdf>.

¹⁰ Audit Manual, Chapter 800 (<http://www.adb.org/anticorruption/anticorruptionprocedures.pdf>). ADB's Oversight Committee on Anticorruption determines remedial actions under the Anticorruption Policy.

- (iii) collusive practice as an arrangement between two or more entities without the knowledge, but designed to improperly influence the actions, of another party;
- (iv) coercive practice as impairing or harming, or threatening to impair or harm, directly or indirectly, any party or its property, or persons closely related to a party, to improperly influence the actions of that party;

and will consider all existing references to corrupt and fraudulent practices in the context of ADB's Anticorruption Policy, including references in ADB's Ordinary and Special Operations Loan Regulations,¹¹ to comprise those four terms.

15. Recognizing that there is no universal definition of conflict of interest, and further recognizing a need to provide a consistent basis for ADB to evaluate potential conflict situations pursuant to the Policy, ADB will define conflict of interest as a situation in which a party has interests that could improperly influence that party's performance of official duties or responsibilities, contractual obligations, or compliance with applicable laws and regulations.

16. ADB will update its *Guidelines for Procurement Under Asian Development Bank Loans* as outlined in Appendix 3 to refer to such definitions, and will update similar provisions in ADB's *Guidelines on the Use of Consultants by Asian Development Bank and Its Borrowers*.

17. ADB will amend its anticorruption procedures so as to have latitude to impose sanctions where ADB determines that an entity eligible to participate in an ADB activity has not maintained the highest ethical standards, even if the activity that demonstrates the failure to maintain such high ethical standards is not related to an ADB activity, and those sanctions may apply to any ADB activity or situation.

IV. RECOMMENDATION

18. To ensure that ADB can fulfill its responsibilities to ensure that all ADB projects and staff maintain the highest ethical standards, the President recommends that the Board approve

- (i) the fraud and corruption-related terms and definitions detailed in paras. 14 and 15;
- (ii) updating ADB's *Guidelines for Procurement Under Asian Development Bank Loans*, and *Guidelines on the Use of Consultants by Asian Development Bank and Its Borrowers*, as noted in para. 16; and
- (iii) amending ADB's anticorruption procedures as detailed in para. 17.

¹¹ As established by ADB, *Anticorruption Policy*, para. 75 and Appendix 3, Section 8.03 of those regulations refer to "corrupt or fraudulent practices."

**EXCERPT FROM
GUIDELINES FOR PROCUREMENT UNDER IBRD LOANS AND IDA CREDITS
(Effective 1 May 2004)**

Fraud and Corruption

1.14 It is the Bank's policy to require that Borrowers (including beneficiaries of Bank loans), as well as bidders, suppliers, and contractors under Bank-financed contracts, observe the highest standard of ethics during the procurement and execution of such contracts. In pursuance of this policy, the Bank:

- (a) defines, for the purposes of this provision, the terms set forth below as follows:
 - (i) "corrupt practice" means the offering, giving, receiving, or soliciting, directly or indirectly, of any thing of value to influence the action of a public official¹ in the procurement process or in contract execution;
 - (ii) "fraudulent practice" means a misrepresentation or omission of facts in order to influence a procurement process or the execution of a contract;
 - (iii) "collusive practices" means a scheme or arrangement between two or more bidders, with or without the knowledge of the Borrower, designed to establish bid prices at artificial, non-competitive levels;
 - (iv) "coercive practices" means harming or threatening to harm, directly or indirectly, persons, or their property to influence their participation in a procurement process, or affect the execution of a contract;
- (b) will reject a proposal for award if it determines that the bidder recommended for award has, directly or through an agent, engaged in corrupt, fraudulent, collusive, or coercive practices in competing for the contract in question;
- (c) will cancel the portion of the loan allocated to a contract if it determines at any time that representatives of the Borrower or of a beneficiary of the loan engaged in corrupt, fraudulent, collusive, or coercive practices during the procurement or the execution of that contract, without the Borrower having taken timely and appropriate action satisfactory to the Bank to remedy the situation;
- (d) will sanction a firm or individual, including declaring ineligible, either indefinitely or for a stated period of time, to be awarded a Bank-financed contract if it at any time determines that the firm has, directly or through an agent, engaged in corrupt, fraudulent, collusive, or coercive practices in competing for, or in executing, a Bank-financed contract; and
- (e) will have the right to require that a provision be included in bidding documents and in contracts financed by a Bank loan, a provision be included requiring bidders, suppliers and contractors to permit the Bank to inspect their accounts and records and other documents relating to the bid submission and contract performance and to have them audited by auditors appointed by the Bank.

¹ Includes World Bank staff and employees of other organizations taking or reviewing procurement decisions.

1.15. With the specific agreement of the Bank, a Borrower may introduce, into bid forms for large contracts financed by the Bank, an undertaking of the bidder to observe, in competing for and executing a contract, the country's laws against fraud and corruption (including bribery), as listed in the bidding documents.² The Bank will accept the introduction of such undertaking at the request of the Borrowing country, provided the arrangements governing such undertaking are satisfactory to the Bank.

² As an example, such an undertaking might read as follows: "We undertake that, in competing for (and, if the award is made to us, in executing) the above contract, we will strictly observe the laws against fraud and corruption in force in the country of the [Purchaser] [Employer], as such laws have been listed by the [Purchaser] [Employer] in the bidding documents for this contract."

**EXCERPT FROM BOARD PAPER R89-98:
POLICY-DIRECTED REVISIONS TO ADB'S GUIDELINES
FOR PROCUREMENT RELATED TO ANTICORRUPTION¹**

In keeping with evolving best practice among multilateral development banks, Sections 2.14, 2.15, and 2.16 of the Bank's *Guidelines for Procurement* will be modified as follows:

Fraud and Corruption

- 2.14 It is the Bank's policy to require that borrowers (including beneficiaries of Bank loans), as well as bidders/suppliers/contractors under Bank-financed contracts, observe the highest standard of ethics during the procurement and execution of such contracts. In pursuance of this policy, the Bank:
- (a) defines, for the purposes of this provision, the terms set forth below as follows:
 - (i) "corrupt practice" means behavior on the part of officials in the public or private sectors by which they improperly and unlawfully enrich themselves and/or those close to them, or induce others to do so, by misusing the position in which they are placed, and it includes the offering, giving, receiving or soliciting of any thing of value to influence the action of any such official in the procurement process or in contract execution; and
 - (ii) "fraudulent practice" means a misrepresentation of facts in order to influence a procurement process or the execution of a contract to the detriment of the borrower, and includes collusive practices among bidders (prior to or after bid submission) designed to establish bid prices at artificial, noncompetitive levels and to deprive the borrower of the benefits of free and open competition;
 - (b) will reject a proposal for award if it determines that the bidder recommended for award has engaged in corrupt or fraudulent practices in competing for the contracts in question;
 - (c) will cancel the portion of the loan allocated to a contract for goods or works if it at any time determines that corrupt or fraudulent practices were engaged in by representatives of the borrower or of a beneficiary of the loan during the procurement or the execution of that contract, without the borrower having taken timely and appropriate action satisfactory to the Bank to remedy the situation;
 - (d) will declare a firm ineligible, either indefinitely or for a stated period of time, to be awarded a Bank-financed contract if it at any time determines that the firm has engaged in corrupt or fraudulent practices in competing for, or in executing, a Bank-financed contract; and
 - (e) will have the right to require that, in contracts financed by a Bank loan, a provision be included requiring Suppliers and Contractors to permit the Bank to

¹ Similar provisions will be inserted into the Bank's *Guidelines on the Use of Consultants by Asian Development Bank and Its Borrowers*.

inspect their accounts and records relating to the performance of the contract and to have them audited by auditors appointed by the Bank.

- 2.15 With the specific agreement of the Bank, a borrower may introduce, into bid forms for large contracts financed by the Bank, an undertaking of the bidder to observe, in competing for and executing a contract, the country's laws against fraud and corruption (including bribery), as listed in the bidding documents. A footnote should also be inserted into documents where such a pledge has been inserted noting that it has been placed there at the request of the borrower.
- 2.16 When the contract is to be financed wholly or partly by the Bank, the contract documents shall include an undertaking by the contractor that no fees, gratuities, rebates, gifts, commissions or other payments, other than those shown in the bid, have been given or received in connection with the procurement process or in the contract execution.

**PROPOSED UPDATE TO ASIAN DEVELOPMENT BANK'S GUIDELINES FOR
PROCUREMENT RELATED TO ANTICORRUPTION**

In keeping with evolving best practice among multilateral development banks, Sections 1.06, 1.07, and 1.08 of ADB's *Guidelines for Procurement Under Asian Development Bank Loans* will be modified and Section 1.09 will be added as follows (similar provisions will be inserted into ADB's *Guidelines on the Use of Consultants by Asian Development and Its Borrowers*):

Fraud and Corruption

- 1.06 The Bank's Anticorruption Policy requires Borrowers (including beneficiaries of Bank-financed activity), as well as bidders, suppliers, and contractors under Bank-financed contracts, observe the highest standard of ethics during the procurement and execution of such contracts. In pursuance of this policy, in the context of these guidelines, the Bank:
- (a) defines, for the purposes of this provision, the terms set forth below as follows:
 - (i) "corrupt practice" means the offering, giving, receiving, or soliciting, directly or indirectly, of any thing of value to influence the action of any party in the procurement process or the execution of a contract;
 - (ii) "fraudulent practice" means a misrepresentation or omission of facts in order to influence a procurement process or the execution of a contract;
 - (iii) "collusive practices" means a scheme or arrangement between two or more bidders, with or without the knowledge of the Borrower, designed to influence the action of any party in a procurement process or the execution of a contract;
 - (iv) "coercive practices" means harming or threatening to harm, directly or indirectly, persons, or their property to influence their participation in a procurement process, or affect the execution of a contract;
 - (b) will reject a proposal for award if it determines that the bidder recommended for award has, directly or through an agent, engaged in corrupt, fraudulent, collusive, or coercive practices in competing for the contract in question;
 - (c) will cancel the portion of the financing allocated to a contract if it determines at any time that representatives of the Borrower or of a beneficiary of the Bank-financing engaged in corrupt, fraudulent, collusive, or coercive practices during the procurement or the execution of that contract, without the Borrower having taken timely and appropriate action satisfactory to the Bank to remedy the situation;
 - (d) will sanction a party or its successor, including declaring ineligible, either indefinitely or for a stated period of time, to participate in Bank-financed activities if it at any time determines that the firm has, directly or through an agent, engaged in corrupt, fraudulent, collusive, or coercive practices in competing for, or in executing, a Bank-financed contract; and

- (e) will have the right to require that a provision be included in bidding documents and in contracts financed by the Bank, requiring bidders, suppliers and contractors to permit the Bank or its representative to inspect their accounts and records and other documents relating to the bid submission and contract performance and to have them audited by auditors appointed by the Bank.
- 1.07 With the specific agreement of the Bank, a beneficiary of Bank-financing may introduce an undertaking of the bidder to observe, in competing for and executing a contract, the country's laws against fraud and corruption (including bribery), as listed in the bidding documents. The Bank will accept the introduction of such undertaking at the request of the Borrowing country, provided the arrangements governing such undertaking are satisfactory to the Bank.
- 1.08 When the contract is to be financed wholly or partly by the Bank, the contract documents shall include an undertaking by the contractor that no fees, gratuities, rebates, gifts, commissions, or other payments, except those shown in the bid, have been given or received in connection with the procurement process or in contract execution.
- 1.09 The Bank considers a conflict of interest to be a situation in which a party has interests that could improperly influence that party's performance of official duties or responsibilities, contractual obligations, or compliance with applicable laws and regulations, and that such conflict of interest may contribute to or constitute a prohibited practice under the Anticorruption Policy. In pursuance of the Anticorruption Policy's requirement that Borrowers (including beneficiaries of Bank-financed activity), as well as bidders, suppliers, and contractors under Bank-financed contracts, observe the highest standard of ethics, the Bank will take appropriate actions to manage such conflicts of interest or may reject a proposal for award if it determines that a conflict of interest has flawed the integrity of any procurement process.