



Licence to bribe?

Reducing corruption risks around the
use of agents in defence procurement

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Licence to bribe?

Reducing corruption risks around the use of agents in defence procurement

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1. An enduring problem

Defence procurement has produced some of the biggest international corruption scandals. Last year, South Korea indicted 63 individuals, including 10 current or former military generals and a former vice minister, over an investigation into alleged defence procurement corruption.¹ The US Navy is currently at the centre of a high-profile scandal relating to its 25-year relationship with Glenn Defense Marine Asia (GDMA). As of March 2016, nine individuals had pleaded guilty and a US Navy captain sentenced to four years imprisonment over bribes paid to Navy officials.² The Scorpene scandal, which involved suspicious payments to Malaysian defence officials in the 2002 sale of French submarines, has recently resulted in a first indictment against the former head of DCNS. The contract, worth USD 1.25 billion, was reportedly the most expensive military procurement by Malaysia to date.³

Corruption in defence procurement is about more than inflated commissions on sales and the waste of public money. By draining state funds, corruption degrades a nation's ability to provide security and essential services such as health, education, and infrastructure. It can result in soldiers operating with equipment that doesn't work or with no equipment at all. Corruption has the potential to damage relations between countries⁴ and can drive instability even in seemingly stable and prosperous countries. For states exporting to regions where defence institutions lack transparency and accountability, the risk of diversion is high and there is increasing evidence of arms from a wide range of countries reaching non-state actors such as the Houthis in Yemen and ISIS.⁵

Agents have played a key role in defence procurement for decades and many cases of procurement corruption have involved agents. They are widely recognised as one

of the highest risk factors for corruption across the sector but, despite recent changes to the regulatory environment, the risks are as difficult to manage as ever. In 2013, more than 90 per cent of reported US Foreign Corrupt Practices Act (FCPA) cases were found to have involved third party intermediaries.⁶ A global survey of compliance officers published in 2016 found the main reasons behind increases in company bribery and corruption risks were perceived to be increases in the number of third party relationships, as well as global expansion, and increased enforcement of regulations.⁷

The defence contracting environment exacerbates these risks. The defence market is moving away from traditional buyers in Europe and North America. This decline can be partly attributed to the drawdown in Afghanistan and reduction in armed conflict in Iraq, as well as budgetary concerns and an increased focus on domestic economic priorities. At the same time, global economic power is shifting towards emerging economies like China, India, Brazil, Mexico, Russia, Indonesia, and Turkey. By 2030, the collective size of these economies is likely to be larger than that of the G7, while Colombia, Peru, Nigeria, Morocco, Vietnam, Bangladesh, and the Philippines will have become huge consumer markets.⁸ Competition for contracts is intensifying but many of the markets where companies are looking to make up the shortfall in sales are precisely where corruption risks are higher. These markets are often characterised by opacity in the defence sector and companies frequently rely on local agents to participate in bidding and carry out contracts, either due to legal requirements or realities on the ground. Many of these jurisdictions also require companies to undertake countertrade or offset agreements alongside the main contract and these opaque mechanisms create further opportunities for agent activity.⁹

Major exporting governments, such as the UK in its 2015 National Security Strategy and Strategic Defence and Security Review, recognise corruption as a driver of instability and acknowledge the risks posed to national security by instability abroad.¹⁰ Yet there is far less recognition that exporting arms to jurisdictions with high vulnerability to corruption could be undermining national security strategy. Governments have an interest in reducing procurement risks in their primary markets, but also a responsibility for ensuring that defence exports do not contribute to regional and global inequality, poverty, and insecurity. As the defence market continues to evolve, there is a growing discord between processes in exporting nations and those in emerging import markets. Companies are operating in more challenging jurisdictions, often with government encouragement, while also being expected to comply with the extraterritorial requirements of anti-bribery legislation in their home countries.

Companies have a clear role to play in managing the agents they work with. Companies should not only have full oversight of agent activities but also maintain the right to audit their financial accounts. Unless companies are prepared to follow the money, the use of agents will continue to pose high risks. But change is not going to happen by company action alone. In order to reduce opportunities for corruption and the risk of instability abroad, governments need to raise international standards in defence procurement, and create space for civil society to provide independent oversight of defence contracting.

The concentrated nature of the defence industry provides a potential transformative opportunity. Countries share the same small set of global suppliers for major defence items and the top ten arms-importing governments account for 49 per cent of all purchases.¹¹ Impact would be felt at a global level if even a small number of major exporting governments took steps to strengthen export controls and required importing governments to implement basic defence budget transparency and independent oversight as a condition of export. Licensing criteria and controls like the EU Common Position on arms export control already exist but are not adequately implemented. Many exporting governments are turning a blind eye to the destructive impact of their defence export policies.

Similarly, if several importing governments were to introduce stronger transparency requirements around the use of agents on companies tendering for their business, it is likely that all major companies would adapt to changes, so as not to lose out in the competitive process. This may in turn encourage other governments to rise to equivalent standards of transparency, particularly as companies become more sensitive to the risks of contracting in jurisdictions that are highly vulnerable to corruption. Ultimately this change would lead to stronger defence sectors, more efficient public spending, and greater public trust across the board.

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Recommendations

COMPANIES

Implement ethics and anti-corruption programmes that minimise the corruption risks posed by agents:

- Conduct due diligence when selecting and reappointing agents.
- Maintain procedures and contractual rights for the full monitoring, control, and audit of agents.
- Ensure that ethics and anti-corruption policies are adopted by agents.
- Deliver risk-based anti-corruption training.

Ensure that agent incentive structures are centralised, accountable, and transparent:

- Fees should be justified in writing and regularly reviewed.
- Contracts should include clear statements of work with stage payments.
- Payments should be paid into local bank accounts.
- Remuneration should be in accordance with local law.

Make greater demands of governments:

- Request guidance and clarity on procurement processes.
- Seek support from home governments for influencing the way business is conducted abroad.
- Use government mechanisms to report corrupt activity.
- Deal directly with customers.

IMPORTING GOVERNMENTS

Increase clarity and transparency in procurement:

- Ensure that embassies and procurement officials are well-equipped to provide guidance on procurement processes.
- Review procurement processes and implement systems that increase transparency and reduce interaction with government officials.

Establish ethics and anti-corruption requirements for all bidding companies:

- Require that companies have ethics and anti-corruption programmes that apply to their agents.
- Require that companies register agents and declare all forms of remuneration.
- Require that agents receive payments into local bank accounts and that company contracts outline the right to audit agent financial accounts by government agencies.

Strengthen oversight and enforcement:

- Establish mechanisms for reporting corruption in procurement.
- Strengthen domestic oversight of procurement, as well as international collaboration on oversight and enforcement.
- Prosecute those found guilty of committing corrupt acts.
- Allow civil society to independently monitor defence contracting.

EXPORTING GOVERNMENTS

Review arms export strategies and strengthen export controls:

- Review arms export strategy and strengthen the application of export licensing criteria, including by requiring basic transparency and oversight mechanisms over public spending as a condition of export.
- Establish enforceable licensing and disclosure requirements for national defence companies, and work with other governments to implement similar standards.
- Require that national defence companies have ethics and anti-corruption programmes that apply to their agents.
- Empower national crime agencies to monitor, investigate, and prosecute corrupt acts.

Support companies facing demands for corrupt behaviour:

- Request support from, or apply pressure on, importing governments.
- Provide support to companies operating in challenging environments.

CIVIL SOCIETY

- Demand more information from governments on how public money is spent in the defence sector.
- Monitor defence procurement and publish information on defence contracts.
- Conduct research into agent ethics and anti-corruption programmes.
- Discuss the risks around the use of agents with national defence establishments and export credit agencies, and provide advice for reducing these risks.
- Advocate for greater disclosure around the use of agents by defence companies.
- Advocate for governments to require companies to have ethics and anti-corruption programmes that apply to their agents as a condition of bidding for MoD contracts.
- Establish independent reporting mechanisms to collect allegations of malfeasance.

The research for this project drew predominantly on four sources:

Transparency International Defence and Security's Defence Companies Anti-Corruption Index (CI). The CI assesses the transparency and quality of defence company ethics and anti-corruption programmes. In 2015, 163 companies from 47 countries were assessed using publicly available information and against a questionnaire of 41 indicators. companies.defenceindex.org

Transparency International Defence and Security's Government Defence Anti-Corruption Index (GI). The GI assesses the existence, effectiveness and enforcement of institutional and informal controls to manage the risk of corruption in defence and security institutions. Evidence was drawn from sources and interviewees across 77 indicators to provide detailed assessments of national defence institutions. government.defenceindex.org

In-depth conversations with industry, government, and civil society stakeholders held between September 2015 and March 2016. The majority of these were conducted on a confidential basis.

Publicly available information, in particular on regulatory controls and enforcement.

2. Agents

Companies work with all kinds of third parties, from distributors to consultants, lawyers, and estate agents, and many use different terminology when referring to these roles. In this report, agents are defined as individuals or entities authorised to act for, or on behalf of, a company to further its business interests, for example in sales or marketing, and in, or with, a foreign country or foreign entity. The corruption risks discussed here are applicable to other types of intermediaries, but agents pose distinct risks because they are authorised to act on the company's behalf, often with a high level of discretion and minimal oversight, and their activities usually involve close interaction with public officials. The terms agent and broker are often used interchangeably, but brokers tend to operate as independent intermediaries in arranging and facilitating arms deals, rather than company representatives.

Agents often play a vital role in defence transactions and perform a range of legitimate functions. These can include: building relationships with public officials and decision-makers; exploring business opportunities in new regions, particularly where a market is difficult to penetrate without advice on local priorities and practices; complying with local law that requires representation by an agent; expanding an in-country presence on a temporary or flexible basis; or assisting with logistics, language expertise, licensing, and legal advice. In some cases, an agent may be able to provide advice on how a company can avoid corrupt practices and individuals. The tasks undertaken by agents are viewed as commercially sensitive by companies and an agent can be regarded as one of a company's key competitive advantages in a sales campaign.

CORRUPTION RISKS

Despite the legitimate functions carried out by agents, there is substantial evidence that some act illegally: the OECD's analysis of 427 cases of foreign bribery between 1999 and 2014 found that intermediaries were involved in three out of four foreign bribery cases and in the majority of cases, "bribes were paid to obtain public procurement contracts".¹² In 2013, law firm Latham & Watkins noted that "[o]ver half of all aerospace and defense industry enforcement actions involve bribe payments by third-party agents working on behalf of aerospace and defense companies."¹³ Many well-known corruption scandals have allegedly involved agents:

- UK and US investigations into bribery allegations on the part of BAE Systems (BAE), which closed in 2010, tracked payments across more than 15 jurisdictions and relationships with over 100 agents and intermediaries.¹⁴
- According to a leaked report by Debevoise & Plimpton, who had been commissioned by German manufacturer Ferrostaal to conduct a compliance investigation, EUR 1.18 billion in "questionable payments" were made to agents in jurisdictions such as Portugal, Greece, South Korea, and Indonesia for contracts between 1999 and 2010.¹⁵
- In 2014, Hewlett-Packard agreed to pay USD 108 million for violating the FCPA. Payments made by a subsidiary through agents and shell companies to a Russian public official allegedly totalled more than USD 2 million, while in Poland a public official received bribes which were said to be worth more than USD 600,000.¹⁶

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The characteristics of the defence sector increase corruption risks in contracting:

- **National security** provides a ready, and sometimes legitimate, excuse for opacity and secrecy;
- **Supply chains** are frequently long and globally integrated;
- **Contracts** are usually large and can take years to negotiate and complete;
- Many products are highly technical and require specific expertise; and
- **Governments** are often closely involved.

The entire contracting cycle is vulnerable and corruption risks may take various forms.

Subversion or manipulation of procurement decisions

An agent may be able to act independently and according to their own interests. They may bypass government procurement officers and liaise directly with the end-user in order to create opportunities or influence decision-making. An agent may also attempt to subvert the procurement process by steering a procurement official or end-user to procure from a particular company.

In Indonesia, agents and brokers are frequently consulted by government procurement officials during the development of technical specifications for required equipment. This creates the risk that agents and brokers are able to manipulate the process by ensuring that specifications favour their clients' products.¹⁷

Conflicts of interest

The process of identifying an agent is often informal. Governments and companies can direct business to acquaintances or relatives. Indeed, some governments designate specific agents through which companies are required to work. Agents are often former military or public officials and many have close connections with national defence establishments. In some jurisdictions, it can be virtually impossible to find a local partner that does not present a conflict of interest.

In 2013, the Indian Central Bureau of Investigation (CBI) filed charges against the son of former Indian National Congress party leader and Member of Parliament, Shrikant Verma. The charges alleged that Rheinmetall Air Defence paid USD 530,000 to Abhishek Verma in order to avoid being backlisted by the Indian government.¹⁸ More recently, former Korean Minister of Patriots and Veterans Affairs Kim Yang was found guilty of accepting USD 1.22 million in return for helping AgustaWestland win a helicopter contract.¹⁹

Offsets and after-sales²⁰

An agent's services can be retained after the main contract has concluded, and extended to after-sales and offset contracts, which may not be subject to the same level of scrutiny. Where the main contract is clean, after-sales contracts may be used as conduits for bribes. An offset contract can be more vulnerable to corruption, particularly in the case of indirect offsets where the offset investment is not necessarily related to the underlying defence contract. Projects can take a variety of forms and may require a large number of third parties and partners to structure the transaction and implement the project.

The 2004 EUR 1 billion Portuguese purchase of two submarines from German contractors, Howaldtswerke-Deutsche Werft, MAN Ferrostaal, and Thyssen Nordseewerk, (jointly the German Submarine Consortium), has been dogged by allegations of corruption around the main deal and the offset package, valued at EUR 1.21 billion. German executives were accused of "paying their Portuguese counterparts EUR 1 million to disguise old investments as new ones as they sought to fulfil the offset obligations".²¹ The scheme is alleged to have cost the Portuguese government EUR 34 million.

Corrupt incentives driving decisions to appoint an agent

An agent may be hired covertly or overtly by a company to facilitate corrupt payments, in order to win contracts. Agents may be paid for legitimate services openly and for illegal activity by alternative means, or companies may hire agents entirely off the books and set up offshore companies to obscure payments.

In 1999, BAE sold a USD 39.97 million air traffic control system to the Tanzanian government. Investigations into allegations of corruption revealed that two companies under the control of BAE agent, Shailesh Vithlani, received one per cent and 30 per cent of the contract price. In sentencing, the Judge took the view that BAE had concealed from the auditors and the public that they were making payments to Vithlani, "with the intention that he should have free rein to make such payments to such people as he thought fit in order to secure the contract for BAE."²²

Agents

Legitimate services masking corrupt behaviour

An agent may be involved in illegal activity alongside legitimate work, which may or may not be known by the company. Payments made by agents from their own accounts are rarely subject to scrutiny. According to the US DoJ FCPA Resource Guide, the US Congress anticipated the use of agents in bribery schemes and defined the term “knowing” to prevent the “head-in-the sand”²³ problem. Companies and their employees cannot avoid liability purely by arguing that they did not know that their agents paid bribes.

“This is a wake-up call for small and medium-size businesses that want to enter into high-risk markets and expand their international sales”

Kara Brockmeyer, Chief of the US SEC Enforcement Division’s FCPA Unit.

The case of Smith & Wesson provides an illustration of the risks facing companies of all sizes. In 2014, the US Securities and Exchange Commission (SEC) charged Smith & Wesson Holding Corporation with violating the US FCPA. According to the SEC order, when seeking to break into new markets between 2007 and 2010, the company retained third party agents in multiple jurisdictions and paid improper payments through these agents to government officials. Smith & Wesson agreed to pay USD 2 million to settle the charges. In addition to terminating its entire international sales staff, the company has committed to reporting to the SEC on its FCPA compliance efforts for a period of two years.²⁴

WHY DO AGENTS ENGAGE IN CORRUPT ACTIVITIES?

Agents can act as vehicles for complicit corporate bribery, or they can engage in corrupt behaviour of their own volition. There are a number of reasons for the former:

Elimination of uncertainty

Due to their expertise and knowledge of the corrupt system, an agent may know to whom and how much to bribe, be able to guarantee the enforcement of an illegal contract, and reduce the risk that bribery is detected. By charging fees in exchange for services, agents may also generate the belief that their services are neither illegal nor socially condemned. This belief may be reinforced by the fact that the supplier does not directly engage in bribery, and the notion that companies are protected by strong compliance procedures.²⁵

Creation of distance from corrupt activity

Companies have highlighted tensions between those working for business units and central compliance departments. Companies can face significant compliance challenges when operating in international jurisdictions, particularly where bribery is seen as common and necessary for engaging in those markets. Using agents to pay bribes can be seen as a way to remain competitive while distancing the company from corrupt activity.

From an agent's perspective, the incentives for corruption may differ from those motivating companies.

Pressure to close a deal

Sales campaigns can last for several years and an agent may only receive payment if and when a contract has been awarded. Both wins and losses are substantial: given the size of many defence contracts, a relatively low success fee could still constitute millions of dollars. By incentivising success, companies may also be incentivising malfeasance as a means of increasing the likelihood of success.

Sense of impunity

A number of companies have suggested that contractual requirements and compliance procedures for agents are sufficient deterrents to corrupt behaviour. However, such measures may create a false sense of security. For agents, a perceived lack of scrutiny, particularly with regard to their financial accounts, and successful prosecutions for corrupt activity may sit in stark contrast to the reputational and financial risks for the companies that employ them.

Unwillingness to sacrifice a contract

Agents are employed for their ability to win contracts and success is not only crucial for the contract at stake but also for strengthening an agent's credibility. An agent may be unwilling to sacrifice a contract if only a small bribe is the price of winning. This may be compounded in markets where bribery is common, the practice is perceived as normal, and there may be the illusion that there are no victims.

Fear of damaging relationships

Agents are often employed for their contacts. Refusal to engage in bribery may damage existing and long-standing relationships. On the other hand, successful deals enhance an agent's reputation both in the eyes of the buyer and the seller.

3. Defence companies and agents

Following the introduction of the US Foreign Corrupt Practices Act in 1977, the OECD Convention on Combating Bribery in 1999, the UN Convention against Corruption in 2005, and the UK Bribery Act in 2011, all of which explicitly cover bribery through third parties, compliance and anti-bribery have become part of the business lexicon. Defence companies have started to collaborate on industry-wide initiatives²⁶ and there exists a wealth of guidance on managing third party risks.²⁷ Many companies are paying closer attention to corruption risks, as is evident in the improvement by a number of companies in the second edition of the Defence Companies Anti-Corruption Index (CI).²⁸ This may be linked to the introduction of more stringent regulations globally, in particular ‘failure to prevent’ clauses.

Improvement may also be a product of the ‘burning platform’ where high-profile allegations of corruption, such as those relating to BAE’s Al-Yamamah contract with Saudi Arabia, have driven reform. Shortly following the allegations, in 2007, BAE appointed an independent committee to make recommendations on ethical business practice and, three years later, the company engaged an external independent committee to assess progress in meeting these recommendations. The findings were published on BAE’s website.²⁹ Alongside tone from the top and shareholder pressure, companies have indicated to us that experiencing an investigation first hand or seeing a peer go through such an investigation are powerful drivers of change.

The US Foreign Corrupt Practices Act (FCPA) prohibits “indirect bribes” through third parties or intermediaries. It covers payments made to “any person, while knowing that all or a portion of such money or a thing of value will be offered, given, or promised, directly or indirectly” to a foreign official or other prohibited recipient. “Knowing” includes being aware of a high probability of bribery. *Section 30A(a) of the Securities & Exchange Act, 15 United States Code § 78dd-1(a).*

The OECD Convention on Combating Bribery requires that all parties criminalise bribery, both direct and through intermediaries, to foreign public officials. *OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, 1997, Article 1 (1).*

The UN Convention against Corruption (UNCAC) requires that all parties criminalise both direct and indirect bribery of foreign public officials, both direct and indirect. Bribery of any person who directs or works for a private sector entity is also prohibited. *United Nations Convention against Corruption, 2003, Articles 16, 18, 21.*

The UK Bribery Act prohibits passive and active bribery, and applies to all “associated persons”: individuals who perform services for or on behalf of an organisation. Organisations are liable if they fail to prevent bribery from occurring, obviating the defence that agents acted of their own volition. Burden of proof is placed on companies to demonstrate that they have in place “adequate procedures” to prevent bribery. *UK Bribery Act 2010, Section 7.*

DEFENCE COMPANIES ANTI-CORRUPTION INDEX (CI)

Transparency International's Defence Companies Anti-Corruption Index measures the transparency and quality of defence company ethics and anti-corruption programmes. Conversations held with companies for the 2015 Companies Index revealed broad awareness of the risks around the use of agents, as well as company liability for their behaviour. However, the results demonstrate that the management and control of agents continues to be a key area of vulnerability. Only eight per cent of companies provided good public evidence of regular diligence processes for agents, and only 12 per cent published strong evidence of contractual rights and processes for the behaviour, monitoring, control, and audit of agents. These were some of the lowest scoring areas in the Companies Index. Many companies indicated to us that they are aware of the demands placed on individuals in sensitive positions. However, according to publicly available evidence, only 13 per cent provide tailored training to employees in sensitive positions, such as those in business development, sales and marketing, in-country project management and government relations.

The Companies Index did reveal some examples of good practice relating to stringent due diligence procedures, anti-bribery and corruption risk assessment, limited term contracts, and mandatory repeat due diligence prior to extending contracts or reappointing agents. There was also evidence of clear anti-corruption clauses within agent contracts, regular audit and monitoring procedures, and disciplinary measures in cases of contract breaches. Overall, companies received better scores for promoting their ethics and anti-corruption programmes to agents. Just under 50 per cent of companies ensure that their ethics and anti-corruption policy is widely available.

The Defence Companies Anti-Corruption Index (CI) provides a tool for companies to identify weaknesses in their ethics and anti-corruption programmes. As the CI is based on publicly available evidence, examples of good practice are available for other companies to refer to.

For example, one company provides public evidence that business divisions are required to keep a record of who proposed an agent appointment, why, due diligence undertaken, whether there were any red flags and, if there were, how they were resolved, and the signature of the approver. Agents are reviewed annually as part of the anti-bribery and corruption risk assessment process, and agency arrangements are renewed at least every two years. Agents are defined broadly and all appointments require approval from the Chief Executive.

Another company publishes a clause contained within all agent contracts that commits the agent to the following:

- certifying that they are familiar with the US FCPA, the UK Bribery Act, and the company's anti-bribery policy, and that they will comply with these;
- notifying the company of any violation of anti-bribery laws;
- certifying that no officer, employee or family member is or has become a public official;
- certifying that there has been no change in ownership of the company;
- certifying that, unless prior authorisation has been received, the agent has not engaged or paid any third party to assist in their performance of the contract;
- allowing for reasonable access to the agent's books and records and periodic audit of these; and
- agreeing that noncompliance with any provision set forth or false certification is a basis for the withholding of payment and immediate termination of the agreement.

Full company reports are available at companies.defenceindex.org

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INCENTIVE STRUCTURES

While an essential step, compliance is not a panacea. Despite efforts to ensure that policies and procedures are stringent, companies tell us they fear agents may operate outside the law of their own volition. What is critical here is the way that agency relationships and incentives are structured.

Our research indicates that agents are generally paid by commission, retainer, or a combination of the two. Companies have told us they tend to prefer commission payments because this shares business risk with the agent. However, requiring agents to work on a 'no win, no fee' basis, often for several years, creates powerful incentives to ensure the closure of a contract by any means necessary. Commission arrangements are also high risk because they typically involve a significant degree of discretion and can take into account the expected effort of an agent, previous experience, expected resource outlay, and

rates for similar contracts. Commission rates vary enormously – in one jurisdiction they have reportedly been as high as 40 per cent of the contract³⁰ – and this can make it difficult to determine what is reasonable and fair, and easier to disguise illegal payments. Payments usually cross jurisdictions and agents may maintain banking facilities in countries that are known tax havens and secrecy jurisdictions, making it more difficult to identify and investigate suspicious activity. It is also rare that companies or importing governments have contractual rights to audit agent financial accounts, which make it impossible for either to track adequately where payments are going. Retainer arrangements are not necessarily more accountable if they are not regularly reviewed, and the reasonableness of remuneration well-evidenced. Where a combination of commission and retainer is used, the retainer is often recouped out of the end commission but, in such cases, the commission can still be regarded as a bonus or success fee.

3.1 Recommendations for defence companies

ETHICS AND ANTI-CORRUPTION PROGRAMMES

What is crucial to the effectiveness of an ethics and anti-corruption programme is ensuring a clear understanding of the rationale behind policies and procedures, as well as the risks they are designed to mitigate.

- **Where resources permit, conduct thorough in-house due diligence when selecting and reappointing agents.** Due diligence should be conducted by individuals who do not have a vested interest in agent appointments, such as central compliance teams. Face-to-face interviews could be conducted in the presence of a lawyer. Due diligence should be risk-based and refreshed at least every three years, as well as when there is a significant change in the business relationship or the nature of the agency.
- **Maintain formal procedures and contractual rights for the monitoring, control, and audit of agents with respect to countering corruption.** Well-trained agreement monitors within business units can ensure that agent activities are monitored against realistic objectives and expectations. Agent activities and agreement monitors should also be subject to periodic centralised audit. Contracts should include the right to audit all agent financial accounts by the company or an independent auditor, and the relevant government agency.
- **Ensure that ethics and anti-corruption policies are understood and adopted by agents.** Policies should be clear and understandable, and breaches of policy should constitute a contract-terminable offence.
- **Deliver risk-based training, which explicitly covers anti-corruption, to agents as well as the staff that manage them.** The needs of agents and employees in sensitive positions should be assessed and training tailored to meet these needs. Companies should identify ways to assess the effectiveness of training to ensure that it is up-to-date and fit-for-purpose.

INCENTIVE STRUCTURES

Remuneration arrangements for agents should be centralised, accountable, and transparent.

- **Fee levels should be justified in writing** by referencing objective criteria, such as the prevailing market rate, past performance, reputation and expertise, the complexity and duration of the work and resources required, risks borne by the agent, and proportionality with the value of the overall contract.³¹ This information, as well as payments themselves, should be monitored on an ongoing basis and subject to periodic centralised audit.
- **Contracts should include clear statements of work with measurable outcomes and milestones with stage payments where possible.** Contracts should be subject to periodic centralised audit.
- **Remuneration should be paid into local bank accounts.** It is good practice to pay the agent only in the country where he or she performs the services, or in the country where the agent regularly conducts business. At a minimum, agent banking facilities should be registered in countries that are not known tax havens or secrecy jurisdictions.

- **Remuneration arrangements should be in accordance with local law.**

Where advice on local requirements is provided by an agent or other third party, companies should seek to verify this information with embassies and governments themselves.

GOVERNMENT SUPPORT

Company practice is changing beyond the creation, extension, and implementation of ethics and anti-corruption programmes. Some of the largest companies, as well as those that operate in niche areas, tell us that they are moving away from working with agents where regulations permit. Companies with the resources to do so are choosing to open local offices instead of working with agents and, in some cases, turning down business in high-risk jurisdictions. A recent survey of senior legal and compliance officials found that 30 per cent of respondents decided not to conduct business in a particular country because of the perceived risk of corruption. Another 41 per cent reported that the risk of corruption was the primary reason for pulling out of a deal on which they had already spent time and money.³² However, this approach to managing the risks is clearly not scalable. While some companies may be in a position to refuse business, this may serve to push contracts to companies that are not well-equipped to deal with corrupt practices,³³ and to those operating in jurisdictions where controls are weak.

Governments play a role here. Many are highly protective of their defence industries, and regard an independent defence capability as a fundamental element of national security. However, many domestic markets may be too small for the necessary

economies of scale and it may not be possible for defence companies to survive without a significant export business. Many companies end up in an untenable situation where their governments are encouraging them to venture into some of the most challenging markets in the world, but where the nature of the operating environment creates powerful incentives to break the law.

Companies should make greater demands of both importing and exporting governments.

- **Request guidance from importing governments** on local procurement processes, regulations, and customs, and on remuneration requirements and acceptable commission rates.
- **Seek support from home governments for influencing the way business is conducted.** Collectively apply pressure on importing governments to adopt the same standards that are required in home countries.
- **Use government mechanisms to report corrupt activity.** Report malpractice to home government embassies overseas, and work with companies at all levels of the supply chain as well as other bidding companies to request support from importing governments.
- **Deal directly with customers.** Communicating directly with the end-customer and ensuring transparency throughout the process can minimise opportunities for manipulation by agents.

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4. Governments and agents

India attempted to prohibit the use of agents in defence procurement in 1989 but reports of agent activity continued to surface. In an attempt to regain control over agent activities, in 2001, the Central Vigilance Commission, Central Bureau of Investigation, and Comptroller and Auditor General recommended that agents be permitted and registered. However the registration requirements were so stringent that no agents registered. Subsequent efforts to limit the use of agents appear to have been similarly unsuccessful. The upcoming revisions to the Defence Procurement Procedure (DPP) are expected to, once again, change the government's stance on agents.

Governments are very often aware of the risks associated with agent activity. In some cases, it is the end-customer that has identified malpractice, not the supplier, and defence ministers have been known to instruct companies to deal directly with them in an attempt to reduce the influence of agents. However, the attitudes of governments towards agents vary significantly, are often contradictory, and there are frequently regulatory barriers to reducing corruption risks.

The Government Defence Anti-Corruption Index (GI) assesses the existence, effectiveness and enforcement of institutional and informal controls to manage the risk of corruption in defence and security institutions. The 2015 results provide a stark illustration of the risk environment that defence companies are operating in. Of 113 countries, almost three-quarters were assessed to have a high to critical level of corruption risk in procurement.³⁴ Another 69 per cent of the countries assessed were found to have low transparency and/or weak government controls relating to the use of agents and intermediaries in procurement. More than half of the top 15 importing markets fall within this group.³⁵

ATTEMPTS TO BAN AGENTS

A number of jurisdictions have at various times banned or attempted to ban the use of agents in selected or all aspects of military procurement,³⁶ suggesting at least a general awareness of the associated risks. Yet in such cases, the use of agents has remained prevalent as the underlying reasons for using an agent had not been addressed.

Prohibiting access to agent services can put a company at a significant disadvantage when operating in certain markets. Complex procurement procedures may require navigation by local experts, legal counsel, or individuals with language expertise. Some markets may be particularly difficult to penetrate without an entry-point. Where agents are intentionally employed to act as vehicles for corrupt transactions, public officials may have a vested interest in perpetuating these complexities. Given such strong incentives for contracting the services of an agent, instead of preventing corrupt behaviour, prohibitions can reduce oversight by pushing activity underground.

Prohibitions on agent activity have also typically been weak, easy to circumvent and, at times, contradictory. In the UAE, for example, a formal directive instructs companies seeking contracts with the Armed Forces not to enter into a deal with an agent. However, in order to bid on government contracts, foreign manufacturers are required to be represented by a commercial agent, incorporate a Limited Liability Company, or establish a local branch,³⁷ and external guidance published by UK Trade & Investment DSO confirms that agents operate in the sector.³⁸ In Saudi Arabia, Royal Decree M/2 (1978) mandated the use of domestic Saudi agents by foreign firms, while prohibiting agents in defence-related sales. This law was repealed in 2001. However, Council of Ministers Resolution No. 1275 (1975) also bans the use of agents in defence-related agreements with the Saudi government, and this has not been repealed. In practice, it appears that the use of agents is widespread.³⁹

ENCOURAGING OR MANDATING LOCAL PARTNERSHIPS

Policies governing the use of agents can also be driven by industrial and economic considerations. A number of governments actively encourage local investment by foreign companies – for example, establishing local branch offices, forming local investment partnerships, ensuring that local companies are awarded elements of production, or hiring a local agent - as a condition of participation in military procurement. This may or may not be as part of an offset contract.

If the process for appointing an agent is fair and their activities are transparent and accountable, there can be benefits to local partnership requirements. Local agents are likely to have an established presence in-country, use a local bank account, and provide services that are subject to local taxation and financial regulation. Oversight is likely to be higher than in jurisdictions where there are no controls at all. However, the process of identifying and hiring an agent is rarely transparent and can be subject to government influence. Governments can apply restrictions on who can act as an agent, such as in Iraq where agents must be Iraqi nationals and resident in-country. A number of governments designate specific agents that companies must interact with, or suggest a limited selection for companies to choose from. Funneling transactions through a small number of agents who may have been selected for unknown reasons, and who already have close relationships with the government, can encourage and sustain corrupt relationships. Companies have told us that mandatory requirements to use a local agent can result in them having to work in ways they are not comfortable with.

REGULATING COMMISSIONS

Governments are clearly aware of the risks surrounding commission payments, as previously discussed, and a number have attempted to ban commissions altogether. In Saudi Arabia, Resolution 1275 states that any company with a defence contract with the government is prohibited from paying any commission to any sales agent. However, court cases heard outside of Saudi Arabia indicate that this is rarely, if ever, enforced.⁴⁰ The OECD Working Group on Bribery in International Business Transactions has outlined good practice for companies on reducing corruption risks in remuneration,⁴¹ but there is a distinct lack of detailed guidance from national governments on acceptable payment structures and practice within different jurisdictions.

LEGISLATIVE CONTROLS

140 countries have signed the UN Convention against Corruption and 41 have adopted the OECD Convention on Combating Bribery. Despite these commitments, both of which cover bribery through third parties, few countries have adopted robust national anti-corruption regulations that specifically cover offences committed by agents. Even where there is recognition that companies should be liable for the behaviour of their agents, legal regulations have not necessarily been updated to reflect this. In precedents involving domestic public officials in South Korea, courts have recognised that corrupt payments may be made via third parties, but the US Foreign Bribery Prevention Act has not been extended to specifically cover them.⁴²

There are examples of anti-bribery and anti-corruption regulations that do cover agents: the Kenyan Anti-Corruption and Economic Crimes Act prohibits the offering of a bribe by an agent; the Australian Criminal Code outlines both individual and corporate liability for the actions of an agent; the Brazilian “Clean Company Act” prohibits the use of third parties to conceal

interests and covers agents acting on a company’s behalf; and both the Singaporean Prevention of Corruption Act and Turkish Criminal Code apply to the use of intermediaries in bribery. However, even where legislation exists, there are challenges in how these controls can address the corruption risks posed by agents.

Language loopholes

Agents perform a range of functions and operate under a variety of names; sales agents, marketing advisors, and consultants, to name a few. Formal controls can often be circumvented with terminology. For example, the Saudi Arabian Government Tenders and Procurement Law states that no intermediaries are allowed. However “agents authorised by original producers shall not be deemed intermediaries”.⁴³ In India, there appear to be ways in which the government is able to bypass the provisions of the Defence Procurement Procedure, while companies may be able to circumvent integrity pact⁴⁴ requirements by working with ‘consultants’ rather than ‘agents’.

Defence exceptionalism

Defence procurement is commonly governed by different regulations to other forms of procurement. In Brazil, defence procurement is subject to supplementary controls in addition to the general procurement regime. In Egypt, commercial agents are prohibited from military tenders but often form a mandatory requirement in other types of public procurement. In other countries, defence offers higher levels of secrecy and flexibility. In China, military procurement is exempt from the Government Procurement Law. Differing standards for defence procurement can increase confusion and drive the perceived need for agents.

Extraterritoriality

Agents can be internationally mobile, which makes monitoring, investigation, and prosecution of corrupt activity more difficult. National controls relating to bribery are rarely extraterritorial and often make a distinction between ‘domestic’ and ‘foreign’. In the UAE and India, domestic laws that prohibit bribery of public officials do not apply to foreign officials. When an agent is intentionally employed to facilitate bribery, it becomes relatively easy to identify and exploit the jurisdictional limits of legislation.

Enforcement

Even where legislation covers corrupt acts committed abroad, enforcement is dependent on international cooperation. In Indonesia, bribery involving an Indonesian public official is punishable regardless of the jurisdiction. However, if a person outside Indonesia was suspected of breaking the Anti-Corruption Law, investigation and enforcement would rely on mutual legal assistance agreements with the relevant country.⁴⁵ Recent years have seen an increase in enforcement actions against companies for bribing foreign officials.⁴⁶ However, agent involvement in corruption continues to make headlines and in many cases enforcement and prosecution in this area remains weak. Since the Bofors Howitzer scandal in 1987,⁴⁷ India has investigated numerous allegations of defence corruption involving intermediaries but no agent has been prosecuted.

Liability

Legislation differs on who can, and should, be held liable for corrupt behaviour. Many statutes outline company liability for bribery conducted through an agent. Fear of individual prosecution can drive change, particularly if employees feel that their company cannot protect them. The 2015 US Department of Justice Yates Memo suggested that; *“one of the most effective ways to combat corporate misconduct is by seeking accountability from the individuals who perpetrated the wrongdoing. Such accountability is important for several reasons: it deters future illegal activity, it incentivizes change in corporate behaviour, it ensures that the proper parties are held responsible for their actions, and it promotes the public’s confidence in our justice system”*.⁴⁸ A challenge to this approach is that, in large corporations, it can be difficult to determine if an individual possessed the knowledge and criminal intent to establish their guilt beyond a reasonable doubt. Agents themselves may face liability for their actions. The Malaysian Anti-Corruption Commission and Penal Code outline liability for an intermediary if he or she abets or is engaged in the bribery of a foreign official. Under the Czech Criminal Code, an intermediary can be punishable as an accomplice or accessory to bribery. However, these types of clauses are rare and there is little public evidence of effective enforcement.

4.1. Recommendations for importing governments

In jurisdictions where corruption risks involving agents are high, some governments are looking to government-to-government sales, such as US Foreign Military Sales (FMS), and single-source procurement.

In **FMS**, instead of the purchaser dealing directly with the contractor, the US Defense Security Cooperation Agency acts as an intermediary. A number of companies are choosing to operate through this programme rather than direct commercial sales, and some countries only procure through FMS. FMS enables a government to take a more active role in procurement but it comes with its own limitations. Common complaints from companies involved in FMS relate to the length of time and money it costs to go through the process, export licensing requirements, and a perceived lack of transparency. From a government's perspective, direct commercial sales typically offer greater flexibility.

Single-source procurement may be necessary for certain defence purchases but, where possible and practical, an open and competitive procurement process can drive cost savings, improve quality of the product or service, and ensure the best value for money. Crucially, open competition is the only way to hold the government to account for its procurement.⁴⁹ The fact that uncompetitive procurement is being seen as the best solution for reducing the influence of agents is evidence that something more fundamental in defence procurement needs to change.

As the principal buyers of defence equipment and arms, importing governments have the power to dictate the terms of procurement and make demands of those selling to them. The first step in managing the risks posed by agents is establishing a robust procurement framework. For example, an openly published national security strategy from which a clear acquisition plan is drawn would reduce the opportunity for agents to manipulate procurement requirements, particularly if decisions are likely to be reviewed against the acquisition plan by a competent national audit office, parliamentary select committee, or well informed public. Similarly, the prospect of effective tender board audits could reduce the risk that conflicts of interest by individual officials will be acted on.

Transparency International's Government Defence Anti-Corruption Index outlines the fundamental elements of a robust procurement framework, and the implementation of its recommendations would go a long way to improving procurement systems.⁵⁰ However, even where systems appear to be strong, companies have told us that procurement processes can lack clarity and even government customers may not understand what is required. In order to raise standards in defence procurement, governments need to work with companies to reduce opportunities for undue influence, increase transparency and accountability, and make illegitimate activity easier to detect and prosecute.

PROVIDE GUIDANCE AND CLARITY

Procurement regulations can be opaque, confusing, or contradictory, and there can be a lack of clarity on acceptable commission rates, as well as local laws and customs. In jurisdictions like Indonesia and Pakistan, companies are finding that even local procurement officials are unclear on what is formally required to participate in procurement. This can be a reason for the government designating an agent with specific knowledge or expertise for a company to work with.

To be effective, regulations need to be fully understood by both buying and selling parties, and consistent with other local and international controls.

- **Ensure that procurement officials understand their own procurement policies and processes**, thus reducing government and company dependency on agents.
- **Ensure that embassies and procurement officials are able to provide accurate advice** to companies and exporting governments on controls relating to remuneration. To the extent that it is possible, embassies and procurement officials could support bidding companies by sharing verified information on corrupt activity involving agents.
- **Ensure that procurement officials are trained and well-equipped to deal with issues** and queries from industry and other governments. Procurement officials should be knowledgeable of supplier obligations and empowered to ensure that contractors meet these obligations.

REDUCE COMPLEXITY AND INCREASE TRANSPARENCY

Where agents are not banned, procurement procedures require updating and streamlining in order to reduce the need for agents and opportunities for manipulation. In India, excessive bureaucracy and 'red tape' has proliferated the number of 'touchpoints' with government, each of which presents an opportunity for corruption. In Canada, the government has recently formed an Ad Hoc Cabinet Committee⁵¹ to oversee major defence purchases, like the F-35, in an attempt to reduce lengthy delays and cost overruns, and in response to a perceived lack of accountability in some of its major weapons purchases.⁵²

Procurement procedures need to be fit for purpose and as transparent as possible.

- **Regularly review procurement processes** and request feedback from bidding companies.
- **Implement systems that reduce interaction with public officials and make processes simpler and more transparent.** E-procurement has already been successfully adopted by many governments to varying extents and, while this may not be appropriate for every tender, electronic systems can be introduced for parts of the process or particular types of procurement. The entire competitive process, along with assessment criteria, should be fair and transparent.

ANTI-CORRUPTION REQUIREMENTS FOR BIDDING COMPANIES

As previously discussed, having a strong ethics and anti-corruption programme can help companies to manage the risks posed by agents. In the 2015 Government Index, Japan was the only country to receive the maximum score for its requirements of bidding companies in terms of compliance and business conduct programmes and procedures.⁵³ Companies are required to demonstrate to the Japanese Ministry of Defence that they have a formal and publicly declared compliance programme, and an ethical supply chain. The Ministry of Defence also calls for adherence to a set of guidelines for bidding and contracts.⁵⁴

Integrity and anti-corruption requirements should set clear expectations for bidding companies.

- **Require that all bidding companies have effective ethics and anti-corruption programmes**, that these programmes are made public, and that they apply to all agents. Monitoring mechanisms must be in place to ensure these are enforced. Companies should also maintain contractual rights to audit their agents' accounts.
- **Consider using pre-contract integrity pacts** or similar mechanisms to establish binding obligations that relate to the use of agents on both the buying and selling parties.

LICENSING AND DISCLOSURE REQUIREMENTS FOR BIDDING COMPANIES

Licensing and disclosure requirements for agents can provide a minimum level of oversight. There are numerous examples of this in practice. In Indonesia, agents must be registered with the Directorate of Business Development and Company Registration. Registration is subject to the provision of extensive documentation and certificates are valid for a maximum of two years. In Saudi Arabia, agents are required to register contractual agreements on the Agents and Distributors Register. In Pakistan, the Directorate General of Defence Purchase requires that foreign companies declare the percentage or amount of commission paid to an agent, while agents are required to provide information relating to their employment as well as personal data, and certification from their foreign principals' embassy certifying the legitimacy of the principal.

While such mechanisms are not guaranteed to reduce corruption, if an agent is required to disclose to the government its identity, financial information, and information relating to each contract and commission, it may deter malfeasance and can provide evidence for any future investigations. Registration requirements can also increase oversight. For example, if a registered agent is required to run their local business with significant equity or a bank guarantee, the agent's assets are at risk of confiscation in case of misconduct. Regulation may stipulate that agents cannot refer to a legal professional privilege, forcing them to testify against principals in court and disclose otherwise confidential information. Registration could also foster a sense of competition if unregistered agents are denied legal recourse or prohibited from operation, or the number of registered agents is limited.⁵⁵ However, it should be noted that there are also risks to excessive regulatory burdens. In India, licensing is conducted on a local rather than centralised

basis. The lack of standardisation across provinces proliferates opportunities for undue influence and corrupt behaviour.

Effective oversight relies on good practice in licensing and disclosure.

- **Require that all bidding companies register their agents with the defence procurement agency or ministry of defence, and declare all agents used in a contract.** This should be done for the main contract and any offset and after-sales arrangements. Monitoring mechanisms must also be implemented to ensure that these requirements are adhered to, and use of undisclosed agents should be a contract-terminable offence.
- **Require that bidding companies declare the principal aspects of all financing packages. This should include commissions paid to any agents and payment timelines.** This information should be public but, at a minimum, declarations should be made to the defence procurement oversight agency or ministry of defence for purposes of monitoring and investigation. Monitoring mechanisms must also be implemented to ensure that these requirements are adhered to.
- **Require that all registered agents receive payments into local bank accounts.** At a minimum, agent banking facilities should be registered in countries that are not known tax havens or secrecy jurisdictions. Defence procurement oversight agencies or ministries of defence should have the right to audit agent accounts and track all payments with reference to particular contracts. These requirements should be written into contracts with all companies.

MECHANISMS FOR REPORTING CORRUPTION

Few governments operate effective mechanisms to facilitate the reporting of perceived malpractice in defence procurement. Even where these exist, for example in the Czech Republic, it has been suggested that proving a complaint can be difficult and companies fear retribution in the form of exclusion from future procurement. Reporting mechanisms that effectively deter retaliation or misuse can be difficult to implement, but there are examples of good practice. The Taiwanese Government Procurement Act outlines a complaint mechanism for companies. The results of disputes are available on the website of Public Construction Commission and the high frequency of complaints by local shipyards suggests that the mechanism functions well. Singapore has an e-procurement website where companies can request information on procurement decisions and submit complaints. There is an extensive legal framework outlining the complainant's protection.⁵⁶

- **Establish formal mechanisms that allow companies to report perceived malpractice in procurement.** For genuine (non-malicious) complaints, companies must be well protected against discrimination in future procurement, and corrupt suppliers must be appropriately punished.

OVERSIGHT AND ENFORCEMENT

Importing governments need to strengthen internal and external oversight of procurement. National anti-corruption institutions such as Nazaha in Saudi Arabia, the Inspector General in Iraq, and the Supreme National Agency for Combatting Corruption and General Inspectorate in Yemen, could be expanded to perform oversight and audit functions across all stages of defence procurement. Such institutions must be empowered by law and in practice to operate free from political interference. Governments

could also form coalitions or work within existing international structures, such as the Association of Southeast Asian Nations (ASEAN), to conduct audits of agent remuneration, for example. This kind of collaboration could help to address issues relating to extraterritoriality and create additional encouragement for importing governments to change their practices. Importing governments should allow, and where possible support, civil society organisations to independently monitor and audit defence contracting.

Effective oversight and enforcement can and should take multiple forms.

- **Strengthen institutional oversight of procurement.** Ensure that the relevant bodies are independent, adequately resourced, and empowered to perform these functions. Punitive sanctions should be adopted to provide a credible deterrent against corrupt activity.
- **Form coalitions or work within existing international structures to increase oversight of agent activities** and strengthen enforcement of regulatory controls.
- **Investigate and prosecute individuals and entities that are found to have committed corrupt acts.** Agents should be held liable for their actions, as well as the companies they work for. Oversight bodies and national crime agencies should be responsible for and empowered to investigate and prosecute corrupt behaviour.
- **Allow and support civil society to independently monitor and audit defence contracting.** This should include both formal measures to allow for civil society participation, as well as long-term efforts to change attitudes towards civil society engagement where relevant.

4.2. Recommendations for exporting governments

Governments should take more responsibility for ensuring they are not simply encouraging companies to venture into the most corruption prone markets in the world, while demanding compliance with anti-bribery legislation at home. At the very least, governments should be offering more support to companies operating in markets where governance, transparency, and accountability in procurement is weak. In such jurisdictions, agents pose particularly high corruption risks. Yet these are precisely the markets where governments are encouraging their national defence companies to seek business. Corruption is increasingly recognised by government as a driver of instability. It is explicitly identified as a cause of conflict in the UK's 2015 National Security Strategy and Strategic Defence and Security Review, which goes on to state that "instability, conflict and state failure overseas pose an increasingly direct threat to the UK... It is firmly in [the UK's] national security interests to tackle the causes and to mitigate the effects of conflict".⁵⁷ Given the potential of defence exports to fuel corruption and instability in environments where levels of accountability and transparency are already low, governments might ask more searching questions of their export policy.

EXPORT CONTROLS

Many exporting governments already have a clear obligation to address the underlying issues of transparency and accountability. For example, criterion eight in the EU Common Position on arms export control commits exporters to consider a recipient country's relative levels of military and social expenditure, taking into account the desirability that states should achieve their legitimate needs of security and defence with the least diversion for armaments of human and economic resources. When budgets are opaque, purchases are not linked to strategy, and the public are not involved in meaningful debate over defence

policy, it is difficult to determine what constitutes a legitimate security need. Greater transparency and accountability is a pre-requisite for making this judgement.⁵⁸ There is a strong case for a more rigorous application of export licensing criteria to include an evaluation of the transparency and accountability provisions of the end user, including basic defence budget transparency as well as effective and independent oversight over public spending.

DISCLOSURE REQUIREMENTS

The US appears to be the only major exporter of arms with controls that specifically apply to payments made to agents. Part 129 of the International Traffic in Arms Regulations (ITAR) requires that persons engaged in "brokering activities" involving "defence articles and defence services controlled for the purposes of export on the US Munitions List" must register and receive a licence prior to engaging in such activities. These regulations apply to any US persons located inside or outside the US or foreign persons located in the US or outside the US when "owned or controlled by a US person".⁵⁹ Although the regulations name brokers specifically, the regulations define "*brokering activities*" broadly, meaning that "any action on behalf of another to facilitate the manufacture, export, permanent import, transfer, reexport, or retransfer of a US or foreign defense article or defense service, regardless of its origin". Actions specifically include "soliciting, promoting, negotiating, contracting for, arranging, or otherwise assisting in the purchase, sale, transfer, loan, or lease of a defense article or defense service".⁶⁰

Part 130 of the ITAR requires that any person who applies to the Directorate of Defense Trade Controls for an export licence for defense articles or services valued at USD500,000 or more must declare "fees or commissions in an aggregate amount of \$100,000 or more".

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International Traffic in Arms Regulations (ITAR), §130.10 (excerpt) ⁶¹

(a) Every person required under § 130.9 to furnish information specified in this section in respect to any sale must furnish to the Office of Defense Trade Controls:

- (1) The total contract price of the sale to the foreign purchaser;
- (2) The name, nationality, address and principal place of business of the applicant or supplier, as the case may be, and, if applicable, the employer and title;
- (3) The name, nationality, address and principal place of business, and if applicable, employer and title of each foreign purchaser, including the ultimate end-user involved in the sale;
- (4) Except as provided in paragraph (c) of this section, a statement setting forth with respect to such sale:
 - (i) The amount of each political contribution paid, or offered or agreed to be paid, or the amount of each fee or commission paid, or offered or agreed to be paid;
 - (ii) The date or dates on which each reported amount was paid, or offered or agreed to be paid;
 - (iii) The recipient of each such amount paid, or intended recipient if not yet paid;
 - (iv) The person who paid, or offered or agreed to pay such amount; and
 - (v) The aggregate amounts of political contributions and of fees or commission, respectively, which shall have been reported.

(b) In responding to paragraph (a)(4) of this section, the statement must:

- (1) With respect to each payment reported, state whether such payment was in cash or in kind. If in kind, it must include a description and valuation thereof. Where precise amounts are not available because a payment has not yet been made, an estimate of the amount offered or agreed to be paid must be provided;
- (2) With respect to each recipient, state:
 - (i) Its name;
 - (ii) Its nationality;
 - (iii) Its address and principal place of business;
 - (iv) Its employer and title; and
 - (v) Its relationship, if any, to applicant, supplier, or vendor, and to any foreign purchaser or end-user. [...]

Companies have long argued that commercial sensitivities prevent them from publicly disclosing information relating to agents and agents' commissions.⁶⁴ Others have suggested that, in certain jurisdictions, legal considerations prevent this kind of disclosure. However, a number of companies already declare details of commission payments to financial authorities in their own countries. In South Korea companies are required to declare to the government who

the agent is and how much they are being paid. This information could be audited periodically and used in investigations.

A responsible export policy should complement national security strategy, and include robust export licensing controls as well as disclosure and integrity requirements for companies, and effective enforcement of these.

A number of **export credit agencies** place disclosure requirements relating to agents on companies seeking export credit.

In order to apply for financial support from UK Export Finance (UKEF), customers are currently required to provide information about all agents used in export transactions. For each agent, their name and address, a description of services, the amount or value of remuneration payable to them, and the country/countries of payment are required. Customers are asked to declare if any agent has been engaged in corrupt activity or been convicted or blacklisted for being involved in corruption.⁶² In April 2016, UK authorities froze Airbus export credit financing after the company reported that it had failed to notify UKEF about its use of agents. Although French and German export credit agencies do not require the same level of disclosure, both governments have also suspended export credit facilities.⁶³

Australia's Export Credit Agency (EFIC) has recently amended its procedures to request the name and address of any agents used in connection with a contract. EFIC conducts due diligence on all agent commission fees, regardless of value.

- **Review arms export strategy in conjunction with national security strategy, and strengthen export licensing procedures** to ensure that criteria relating to agents and corruption risks are stringent and rigorously applied.
- **Strengthen or establish disclosure requirements for national defence companies.** At a minimum, companies should be required to declare to a government authority the amount of commission paid to agents and details of the recipients. These should be accompanied by monitoring mechanisms to ensure that requirements are adhered to. Export licences and export credit should be contingent on these requirements.
- **Work with other governments to implement similar standards.** This could alleviate concerns relating to fairness, and assist with enforcement.
- **Require that national defence companies have effective ethics and anti-corruption programmes in place** and that these apply to the use of agents. Export licences and export credit should be dependent on this requirement.
- **Strengthen national crime agencies to ensure they are adequately resourced and empowered to monitor, investigate, and prosecute corrupt acts.** Laws and regulations only work if they are well enforced. These agencies should themselves be subject to independent external audit.

PROVIDE SUPPORT TO COMPANIES

The US government provides a service to assist US companies by interviewing local agents and conducting due diligence.⁶⁵ While liability for the behaviour of agents remains with the company, government involvement may provide a useful indicator for companies, and more importantly reflects the responsibility governments have for their exports. Governments can help defence companies to avoid corrupt practices by providing guidance on local practices and laws, like US embassy in-country profile reports, and tools for reducing corruption risk, such as template agreements, model clauses and policies, and training modules. Governments should also provide practical advice and support to companies facing demands for corrupt behaviour overseas.

- **Support defence companies in avoiding and dealing with corrupt behaviour.** This could involve applying pressure on importing governments, or providing practical advice and guidance to companies.

5. Recommendations for civil society

Integrity Pacts are agreements between governments and companies that they will abstain from bribery and corrupt practices for the extent of the contract. Even for these voluntary agreements, accountability must be ensured by a monitoring system, typically led by civil society groups.⁶⁶

Another example of a tool that requires collaboration with civil society is the **High Level Reporting Mechanism (HLRM)**.⁶⁷ An HLRM is a prevention-oriented reporting channel that companies could use to report corrupt behaviour during a public process. Their use may deter potential perpetrators and increase public trust in procurement, particularly in jurisdictions where criminal law enforcement may be perceived to be unduly influenced by politics.

As in all public-private interactions, company and government reform is not enough to drive meaningful change. In particular, government controls such as registers of agents and reporting channels may still be vulnerable to exploitation. In a number of jurisdictions, civil society organisations face significant obstacles to engaging in the defence sector. They may be actively excluded from participation by governments and industry, or they may lack technical expertise and knowledge. However, civil society can play a crucial role in overseeing procurement, holding governments to account, and raising public awareness where public systems and processes are failing.

In order to establish credibility and build trust between stakeholders, there needs to be inclusive mechanisms that allow for independent oversight and bind government, industry, and civil society into reform.

- **Monitor defence procurement and collaborate with parliamentarians, journalists, research institutions and others to gather and publish information on defence contracting.** Even where technical expertise is lacking, apply and build on existing knowledge of government spending and oversight, as well as business integrity.
- **Conduct research into the transparency and quality of agent ethics and anti-corruption programmes.**⁶⁸ It is in the interests of agents to demonstrate that they have transparent and high-quality ethics and anti-corruption principles. Use this information to engage with the defence establishment, the media, and citizens.
- **Engage with defence and security establishments and export credit agencies.** Discuss what measures are being taken to reduce risks around the use of agents. Provide practical advice on further reform and tools for reducing corruption risks.
- **Advocate for greater disclosure around the use of agents by defence companies.** This could include government requirements to register all agents used, and/or to disclose the identities of agents used in defence procurement as well as commissions paid to them.
- **Advocate for governments to require that companies have effective ethics and anti-corruption programmes that apply to their agents as a condition for bidding on ministry of defence contracts.**
- **Establish independent reporting mechanisms** to collect allegations of malfeasance involving agents, and catalyse action based on their reports. These mechanisms require industry and government support, and should be empowered to regulate defence procurement.

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44. Integrity Pacts are agreements between governments and companies that they will abstain from bribery and corrupt practices for the extent of the contract. They can require bidding companies to declare any agents used and payments made to them in connection with the award of the contract.

45. D. Sidharta & W. Ratna, 'Indonesia', in Homer E Moyer Jr (ed) *Getting the Deal Through. Anti-Corruption Regulation in 43 jurisdictions worldwide*. (London: Law Business Research Ltd, 2015), p.90.

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50. Further information is available in Annex 2. The full GI and scoring criteria is available at <http://government.defenceindex.org>

51. Office of the Prime Minister, Canada, 'Cabinet Committee Mandate and Membership', 22 March 2016. Available online: http://pm.gc.ca/sites/pm/files/docs/Cab_committee-comite.pdf [accessed April 2016].

52. The NATO Association of Canada, 'The New Ad Hoc Cabinet Committee on Defence Procurement', 26 February 2016. Available online: <http://natoassociation.ca/the-new-ad-hoc-cabinet-committee-on-defence-procurement/> [accessed April 2016].

53. Governments that require companies to show that they have a formal and publicly declared compliance programme in order to bid for defence work score a minimum of 3 on Question 61 of the GI. Bulgaria, Greece, Norway, and the U.S. all scored 3.

54. Transparency International Defence and Security, *Government Defence Anti-Corruption Index*, 2015. Japan assessment. Available online: <http://government.defenceindex.org/countries/japan/> [accessed April 2016].

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57. HM Government, *National Security Strategy and Strategic Defence and Security Review 2015*. Available online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/478936/52309_Cm_9161_NSS_SD_Review_PRINT_only.pdf

58. EU adopted Council Common Position 2008/944/CFSP, 8 December 2008. Available online: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:335:0099:0103:EN:PDF>. Criterion four requires consideration of the likelihood of armed conflict, the possibility that equipment would be used for purposes other than national security and defence, as well as the impact on regional stability - taking into account the balance of forces and their relative expenditure on defence. All of these factors are impossible to evaluate when the recipient state has in place no transparency and accountability provisions over their defence budget or security strategy. Similarly, a lack of institutional oversight in recipient states makes it difficult to be sure that criterion six on the commitment to non-proliferation would be met. Criterion seven relates to the risk of diversion or onward transfer. Evidence of strong anti-corruption controls should be part of evaluating a state's ability to exert effective export controls. Criterion eight commits exporters to consider a recipient country's relative levels of military and social expenditure, taking into account the desirability that states should achieve their legitimate needs of security and defence with the least diversion for armaments of human and economic resources.

59. *International Traffic in Arms Regulations (ITAR), Part 129 – Registration and Licensing of Brokers* (U.S. Department of State). Available online: https://www.pmdtc.state.gov/regulations_laws/documents/official_itar/2014/ITAR_Part_129.pdf [accessed April 2016].

60. We note that the text of Part 129 was amended in April 2016. “Brokering activities” were previously defined as acting “as an agent for others in negotiating or arranging contracts, purchases, sales or transfers of defense articles or defense services in return for a fee, commission, or other consideration”.

61. *International Traffic in Arms Regulations (ITAR), Part 130: 22 U.S. Code § 2779 - Fees of military sales agents* (U.S. Department of State). Available online: https://www.pmddtc.state.gov/regulations_laws/itar.html [accessed April 2016].

62. In 2015, the UK Export Finance held a consultation on proposed changes to their Anti-Bribery and Corruption Policy. The proposed changes include the removal of declarations or enquiries about agents. The outcome of this consultation is available online: <https://www.gov.uk/government/consultations/uk-export-finances-anti-bribery-and-corruption-policy> [accessed April 2016].

63. ‘Airbus Export Credit Misstep Referred to U.K. Serious Fraud Office’, *The Wall Street Journal*, 4 April 2016. Available online: <http://www.wsj.com/articles/airbus-export-credit-misstep-referred-to-u-k-serious-fraud-office-1459769913> [accessed April 2016].

‘UK freezes Airbus export support’, *BBC News*, 4 April 2016. Available online: <http://www.bbc.co.uk/news/business-35959828> [accessed April 2016].

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64. For one example, see *Final Statement by the UK National Contact Point (NCP) for the OECD Guidelines for Multinational Enterprises, Complaint from Corner House against BAE Systems plc*, 5 November 2010. Available online: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31746/10-1265-final-statement-ncp-corner-house-bae-systems.pdf [accessed April 2016].

65. Export.gov, *The Gold Key Matching Service* (2009). Available online: http://www.export.gov/salesandmarketing/eg_main_018195.asp [accessed March 2016].

66. For more information, see Transparency International, ‘Tools: Integrity Pacts’, available at: https://www.transparency.org/whatwedo/tools/integrity_pacts/3/

67. For more information, see B20 Collective Action Hub, ‘High Level Reporting Mechanism (HLRM)’, available at: <http://www.collective-action.com/initiatives/hlrm>

68. The CI methodology could be used as the basis for assessment, although this would need to be adjusted depending on the agent’s business. For more information, see: <http://companies.defenceindex.org/methodology/>

Annexe 1: Agents and third parties in the 2015 Defence Companies Anti-Corruption Index

The CI 2015 assesses the transparency and quality of ethics and anti-corruption programmes of 163 defence companies from 47 countries. Five pillars of corruption risk form the basis of the questionnaire. The CI asks two targeted questions about agents within the risk management pillar, and additional questions that touch on the company's interaction with management of agents within the company policies & codes and training pillars.

LEADERSHIP, GOVERNANCE & ORGANISATION	RISK MANAGEMENT	COMPANY POLICIES & CODES
LEADERSHIP, GOVERNANCE & ORGANISATION	RISK ASSESSMENT	POLICIES
EXTERNAL MANAGEMENT	PARTNERS & AGENTS	GIFTS & HOSPITALITY
STRUCTURE & ORGANISATION	OFFSETS	FACILITATION PAYMENTS
MONITORING & EVALUATION	PERSONNEL & HELPLINES	POLITICAL & CHARITABLE INSTITUTIONS
TRAINING	PERSONNEL & DISCIPLINE	
GENERAL TRAINING	HELPLINES & WHISTLEBLOWERS	
SPECIALIST TRAINING		

RISK MANAGEMENT

A11: Does the company conduct due diligence that minimises corruption risk when selecting or reappointing its agents?

The assessor is looking for evidence that due diligence has been conducted on all its current agents and is conducted as a matter of policy on all new agents. The assessor will also look for evidence that the company has a policy to refresh the due diligence at least every 3 years, and when there is a significant change in the business relationship or the nature of the agency. "Agents" are the agents, advisors or other third party intermediaries authorised to act for or on behalf of the company to further its business interests.

2: The company has formal procedures in place, and refreshes the due diligence at least every 3 years and when there is a significant change in the business relationship.

1: The company has formal procedures but there is no evidence that the company refreshes the due diligence at least every 3 years and / or when there is a significant change in the business relationship.

0: There is no evidence of such a procedure or its provision is so weak as to be ineffective.

A12: Does the company have contractual rights and processes for the behaviour, monitoring, control, and audit of agents with respect to countering corruption?

The assessor is looking for evidence that the company has insight into the agent's activities with regard to the alignment of the intermediary's ethics and anti-corruption agenda with that of its own programme and has in place the contractual rights and formal processes to prevent or deal with the occurrence of any violations, through correction or termination / disclosure to regulatory authorities.

2: The company has formal procedures and contractual rights in place, such as monitoring by the business unit, internal or external audit by an assessor independent of the relevant business unit, and termination of contract if corrupt activities are found.

1: The company has formal procedures and contractual rights in place, but falls short in some way; for example there is no evidence of monitoring.

0: There is no evidence of such a procedure or its provision is so weak as to be ineffective.

COMPANY POLICIES & CODES

A17: Is the company's anti-corruption policy easily accessible to Board members, employees, contracted staff and any other organisations acting with or on behalf of the company?

The assessor is looking for evidence of easy availability to any person requiring access. This could include translated into multiple languages (at least the main geographies that the company operates in) and publication of the policy in an intranet or publicly available site.

2: The company's policy is easily available for all employees, contracted staff, and affiliated organisations.

1: The company's policy is not easily available in some way—available in limited languages, or not accessible to contracted staff, for example.

0: There is no evidence that the company has an anti-corruption policy.

A17a: Is the company's anti-corruption policy easily understandable and clear to Board members, employees and third parties?

The assessor is looking for evidence that the anti-corruption policy is written in clear, understandable terms for all audiences and not couched in dense, legal terms. The

policy should be easily understood by a new employee or third party who has not worked in the sector before, and is unfamiliar with the corruption risks. Note that whereas this question refers to ease of understanding, the previous question, A17, refers to ease of access.

2: The policy is written in accessible, comprehensible language.

1: The company's policy is not easily understandable to employees and third parties; for example, it is not easily understood by a non-legal audience.

0: There is no evidence that the company has an anti-corruption policy.

TRAINING

A27 Does the company have a training programme that explicitly covers anti-corruption?

Anti-corruption training that is focused, and grounded by assessment of where corruption risk is highest, is a crucial part of a company's efforts to promote integrity.

Yet often, anti-corruption training is contained within a larger corporate compliance or Code of Ethics training programme. The assessor is looking for evidence that anti-corruption training is either explicitly provided as a separate training programme or is a module that is part of the company's larger ethics training programme.

2: The company has an explicit anti-corruption module as part of its ethics and compliance training programme.

1: The company has a training programme on its ethics and compliance systems (which include an anti-corruption policy) but it is not clear if there is a specific anticorruption training module.

0: There is no evidence such training exists.

A28: Is anti-corruption training provided in all countries where the company operates or has company sites?

2: Training is provided in all countries where the company operates or has company sites.

1: Training is provided in the principal countries where the company operates or has company sites.

0: Training is poorly represented across the countries where the company operates or has company sites.

A30: Does the company provide tailored ethics and anti-corruption training for employees in sensitive positions?

The assessor is looking for evidence that the company has assessed the training needs of employees in sensitive positions and provides tailored ethics and anti-

corruption training. Sensitive positions are those that will expose an employee to potentially corrupt situations at a greater frequency than other staff and / or to more specific forms of corruption. Functions that have high risk can include marketing, government relations, contracting, in-country project management, sales, etc.

2: The company tailors its ethics and anti-corruption training programme for employees facing different levels of risk.

1: The company has a varied ethics and anti-corruption training programme but this is either not comprehensive or not targeted at all high risk positions.

0: There is no evidence of such training being delivered.

Annexe 2: Procurement in the 2015/16 Government Defence Anti-Corruption Index

The GI assesses the existence, effectiveness and enforcement of institutional and informal controls to manage the risk of corruption in defence and security institutions. The research is carried out using a questionnaire of 77 indicators based around five risk areas: political, finance, personnel, operations, and procurement.

For the purposes of this report, questions 70-72, relating to offset contracting, have been excluded from the scoring criteria provided below.

GOVERNMENT POLICY

Corruption risk will be particularly high where legislation exempts or ineffectively governs defence and security procurement, and where scrutiny is lacking. Government policy may be conducive to corruption where there exist privileged defence relations, questionable defence budgets, or external financing with improper payback terms

57. Does the country have legislation covering defence and security procurement with clauses specific to corruption risks, and are any items exempt from these laws?

4. The country has long established and well-tried legislation covering defence and security procurement. As far as can be determined, no items are exempt from these laws, OR any exempt items have a particular national importance or sensitivity and are subject to other forms of independent scrutiny. This legislation has clauses specific to corruption risks.

3. The country has legislation covering defence and security procurement. As far as can be determined, no items are exempt from these laws, OR any exempt items have a particular national importance or sensitivity and are subject to other forms of independent scrutiny.

2. The country has legislation covering defence and security procurement. There is

evidence that this legislation is largely enforced and exempt procurement is generally independently scrutinised.

1. The country has legislation covering defence and security procurement. There is evidence that this legislation is often by-passed and exempt procurement is not independently scrutinised.

0. The country has no legislation covering defence and security procurement.

58. Is the defence procurement cycle process, from assessment of needs, through contract implementation and sign-off, all the way to asset disposal, disclosed to the public?

4. The defence procurement cycle is disclosed in detail.

3. Some elements of the defence procurement cycle are disclosed in detail; other elements, though openly disclosed, are only summarised or are otherwise less clear.

2. The defence procurement cycle is openly disclosed in summary form only.

1. The defence procurement cycle is disclosed only in a very abbreviated or general way.

0. There is no evidence that the defence procurement cycle is disclosed. It is, indeed, unlikely to have been formalised at all.

59. Are defence procurement oversight mechanisms in place and are these oversight mechanisms active and transparent?

4. Procurement oversight mechanisms are in place. They are independent formalised processes and they are transparent. There is evidence to demonstrate that they are highly active, and that this activity spans changes in governments.

3. Oversight mechanisms are in place and there is evidence that they are generally active and transparent. However, it is not clear that they are entirely independent of government and there may be shortcomings in levels of transparency.

2. Oversight mechanisms are formally in place and there is evidence that they are active. However, there is evidence that their activity may not be consistent or effective. The results of oversight activity are unlikely to be transparent.

1. Oversight mechanisms formally exist, but they are highly inactive and lack transparency.

0. There is no evidence of procurement oversight mechanisms, OR such mechanisms exist, but they are entirely non-transparent and there is no evidence that they are active.

60. Are actual and potential defence purchases made public?

4. There is a policy to disclose defence purchases and this is made clear through annual audits. The government also publishes the plans for defence purchases for at least the next few years. (Note: Exemptions for security restricted items is an acceptable reason, but only where it is clear that the bulk of defence purchases are disclosed and this restriction is therefore credible.)

3. There is a policy to disclose defence purchases. There may be some information on forward purchase plans but this is not extensive. (Note: Exemptions for security restricted items is an acceptable reason, but only where it is clear that the bulk of defence purchases are disclosed and this restriction is therefore credible.)

2. There is evidence that many defence purchases are not made public. Security or confidentiality is often given as a reason for such secrecy but evidence suggests that this is partly, but not fully, justified.

1. There is evidence that many defence purchases are not made public and there is no security justification as to why this information is withheld.

0. Defence purchases are not made public in any sort of detail, even though an aggregate total spend may be disclosed.

61. What procedures and standards are companies required to have – such as compliance programmes and business conduct programmes – in order to be able to bid for work for the Ministry of Defence or armed forces?

4. Companies are required to show that they have a formal and publicly declared compliance programme and that they insist upon a supply chain that itself upholds ethical standards in order to bid for defence work. Companies with prosecutions for corrupt activities may be partially or totally barred from bidding.

3. Companies are required to show that they have a formal and publicly declared compliance programme in order to bid for defence work.

2. Companies are required to sign 'no-corruption' (or equivalent) clauses in all contracts with the government, but are not required to have compliance programmes in place.

1. No requirements are placed on companies beyond what is generally in company law. During the bidding process, the government does, however, make at least some reference to the need for companies to avoid corruption.

0. No requirements are placed on companies beyond what is generally in company law; no discrimination is made between companies on the grounds of integrity.

CAPABILITY GAP AND REQUIREMENTS DEFINITION

Where requirements are backed by a solid, transparent strategy, and where openly published security classifications are applied to defence procurement, we may be more comfortable that corruption prompted by exaggerated and inaccurate 'requirements' will be averted.

62. Are procurement requirements derived from an open, well-audited national defence and security strategy?

4. Procurement requirements are derived from a national defence and security strategy. The strategy is openly published; there is logical flow down from strategy to individual procurements; and government audits give confidence that this is followed.

3. Procurement requirements are largely derived from a national defence and security strategy. The strategy is openly published, but there is no audit verification that this is what really happens.

2. Procurement requirements are in part derived from a national defence and security strategy. However, there is still a significant element of procurement outside of the national strategy.

1. Procurement requirements are at least formally derived from a national defence and security strategy. However, there is a large element of procurement outside of the national strategy or through opportunistic purchases.

0. There is no national strategy guiding the formulation of procurement requirements. Evidence suggests that procurement is often opportunistic.

63. Are defence purchases based on clearly identified and quantified requirements?

4. There is evidence that the Ministry of Defence and Armed Forces systematically base their purchases on clearly identified requirements. Work is undertaken to define and quantify the need for all significant purchases before the purchase procedure commences.

3. There is evidence that the Ministry of Defence and Armed Forces do base most of their purchases on clearly identified requirements. However, this is not always followed and there are occasionally opportunistic and unplanned purchases.

2. There is evidence that the Ministry of Defence and Armed Forces do base at least their major purchases on clearly identified

requirements. However, this is not always followed and there are also opportunistic and unplanned purchases.

1. There is a formal procedure in place for defining purchase requirements. However, this is not routinely followed in practice and it is rare for there to be formal analysis of requirements.

0. Purchases are not based on quantification of requirements. They are often opportunistic in nature.

TENDER SOLICITATION, ASSESSMENT AND CONTRACT AWARD

Corruption risk is increased where there is lack of open competition for procurement awards, where bidders are in any way favoured, and where assessment criteria are not objective or fair. Collusion between bidders poses a further risk.

64. Is defence procurement generally conducted as open competition or is there a significant element of single-sourcing?

4. All defence procurement is conducted as open competition, except in clearly defined and limited circumstances. There is a relatively small component (say, 10% or less) of single-sourcing, which has to be justified to scrutinisers.

3. Defence procurement is conducted as open competition, though a significant minority of the value of contracts (say, 30%) are single-sourced, sometimes without clear justification.

2. Defence procurement is conducted in principle as open competition, though a significant percentage of the value of contracts—up to 50%—are single-sourced, sometimes without clear justification. (Note: based on a multi-country study in 2006, the average defence single-source procurement percentage was 50%).

1. Defence procurement is in principle conducted as open competition, but in practice a majority of defence contract value is purchased single-source.

0. There is little open competition, with

most contracts being single-sourced.

65. Are tender boards subject to regulations and codes of conduct and are their decisions subject to independent audit to ensure due process and fairness?

4. Tender boards are subject to regulations and codes of conduct that are transparent. The country has an independent auditing function which audits tender board decisions and reports the results of these audits openly.

3. Tender boards are subject to regulations and codes of conduct that are transparent. The country has an independent auditing function which audits tender board decisions, though its reports and results are not always seen as independent and the results may not be automatically published.

2. Tender boards are understood to be subject to regulations and codes of conduct, though these are not particularly transparent. Auditing takes place when cases are contested though the results are not particularly transparent.

1. Tender boards are understood to be subject to regulations and codes of conduct, though these are not publicly available. Audits of tender board decisions are not routinely undertaken.

0. There is no transparency of tender board procedure and practice. Audits are not normally undertaken of tender boards, OR the country does not conduct competitive tenders.

66. Does the country have legislation in place to discourage and punish collusion between bidders for defence and security contracts?

4. Laws and procedures are in place that strongly disallow collusion. As a result, it is almost unknown in the country. An offence can result in prosecution, debarment from current and future competitions, or other sanctions.

3. Collusion is actively discouraged by

the government and there is evidence of offending companies facing punishment. However, there are occasionally cases in the press where collusion is strongly suspected.

2. Collusion is actively discouraged by the government and there is evidence of offending companies facing punishment. However, there is evidence that sanctions are often not robustly applied when collusion is evident.

1. There are national laws outlawing collusion, but no legislation specific to defence. Enforcement of measures to punish colluding companies is likely to be only weakly enforced.

0. There is no legislation specific to the defence sector, nor wider national legislation, that outlaws collusion.

CONTRACT DELIVERY AND IN-SERVICE SUPPORT

Where procurement staff are knowledgeable of suppliers' obligations in procurement contracts, and corrupt suppliers are appropriately punished, we can be more confident that procurement officials themselves are likely to be clean. This is enhanced where companies are given protection to complain about corrupt activity. It is also important that there is scrutiny of money flows during the in-service performance of equipment: corrupt exchanges may occur when payment is made for modifications and repairs.

67. Are procurement staff, in particular project and contract managers, specifically trained and empowered to ensure that defence contractors meet their obligations on reporting and delivery?

4. Procurement staff are trained and empowered to ensure that defence contractors meet their obligations.

3. Procurement staff are trained and empowered to ensure that defence contractors meet their obligations. However,

there may be minor shortcomings in the department's ability to fulfil its obligations, such as limited staff shortages.

2. Procurement staff are expected to ensure that defence contractors meet their obligations, but there is limited training and staff are rotated in and out from other functions. There are likely to be significant staff shortages.

1. Procurement staff are expected to ensure that defence contractors meet their obligations, but there is limited training and staff are rotated in and out from other functions. There are likely to be significant staff shortages. There may be evidence of undue influence from higher grades within the organisation.

0. Defence procurement staff are not organised into a professional staff department. There are likely to be significant staff shortages. There is little control or oversight of defence contractors by procurement staff, and there is likely to be evidence of undue influence from higher grades within the organisation.

68. Are there mechanisms in place to allow companies to complain about perceived malpractice in procurement, and are companies protected from discrimination when they use these mechanisms?

4. Formal mechanisms are in place to allow companies to complain about perceived malpractice in procurement. For genuine (non-malicious) complaints, companies are well protected against discrimination in future procurements.

3. Formal mechanisms are in place to allow companies to complain about perceived malpractice in procurement. However, these are only partially used as some companies believe it would be disadvantageous to complain.

2. Formal mechanisms are in place to allow companies to complain about perceived malpractice in procurement. However, these are rarely used as companies see it as dangerous to complain.

1. No formal mechanisms are in place to allow companies to complain about perceived malpractice in procurement. It is likely, though not certain, that companies are disadvantaged in future procurements if they attempt to complain.

0. No formal mechanisms are in place to allow companies to complain about perceived malpractice in procurement and there is evidence of companies that have attempted to complain being unfairly disadvantaged or debarred from future procurements.

69. What sanctions are used to punish the corrupt activities of a supplier?

4. A range of sanctions are available, from procurement executive-imposed debarment to legal sanctions, including heavy fines or imprisonment. There is evidence that such sanctions are consistently applied in practice.

3. Sanctions by the procurement executive, such as prosecution or debarment, are available and such sanctions are quite regularly applied in practice.

2. Sanctions by the procurement executive, such as prosecution or debarment, are available but such sanctions are only sometimes applied in practice.

1. Sanctions by the procurement executive, such as prosecution or debarment, formally exist but are almost never applied in practice.

0. There is no evidence of any sanctions existing.

AGENTS AND BROKERS

73. How strongly does the government control the company's use of agents and intermediaries in the procurement cycle?

Of key interest here is whether there is a policy on their usage and whether they are subject to vetting and scrutiny; if they are forbidden, is this law strictly enforced?

4. Agents and intermediaries are strongly controlled and limited. They may be forbidden by the government. Where they are forbidden, there are controls to ensure the law is not circumvented. Where they are not forbidden, there is a clear policy on their usage, and they are subject to scrutiny. These controls are public and well known to companies.

3. Agents and intermediaries are controlled or limited. Where they are limited, there are controls to ensure the law is not circumvented. There is a policy on their usage, and they are subject to some degree of scrutiny.

2. Agents and intermediaries are used in the procurement cycle. There is some control over their usage, though probably no clear policy.

1. Agents and intermediaries are used in the procurement cycle, and although there is some degree of control over their usage, there is evidence that is frequently not enforced effectively, or not obeyed.

0. The government imposes no restrictions on the use of agents and intermediaries, or provides controls that are entirely ineffective.

FINANCING PACKAGE

Complex and secretive financing packages, where payment timelines, rates, and terms and conditions are poorly defined, pose a clear corruption risk. In many cases the main defence contract has a high level of scrutiny, but the same is very rarely true of

the financing package.

74. Are the principal aspects of the financing package surrounding major arms deals, (such as payment timelines, interest rates, commercial loans or export credit agreements) made publicly available prior to the signing of contracts?

4. Principal aspects of the financing package surrounding major arms deals are comprehensively detailed and made publicly available prior to the signing of the contracts.

3. Most details of the financing package are made publicly available prior to the signing of the contract, though some aspects of the package are less precisely detailed than other aspects.

2. Some details of the financing package are made publicly available, and key elements such as the sums involved and the payment deadlines are included. However details on matters such as interest rates and rules and regulations surrounding default penalties are likely to be limited.

1. The existence of a financing package and the identity of the provider are normally made public, but no further details are likely to be available.

0. Details of the financing package are not publicly available. There may be no information on whether a financing package exists at all.

SUB-CONTRACTORS

Large defence contracts involve many layers of sub-contractors. The compliance programmes of sub-contractors are usually significantly weaker than those of the platform-makers, which leads to additional potential for corruption. To ensure propriety it is prudent for a government to not only conduct appropriate due diligence on the main defence contractor, but to ensure that the main contractor conducts comparable due diligence on the sub-contractors it employs.

75. Does the government formally require that the main contractor ensures subsidiaries and sub-contractors adopt anti-corruption programmes, and is there evidence that this is enforced?

The main contractor will contract some elements of the work to be done to other companies, known as sub-contractors. They in turn can further contract work out. Such 'chains' of contractors are very common in the defence industry.

4. The government formally requires the main contractor to ensure that its subsidiaries and sub-contractors adopt anti-corruption programmes. There is evidence that this is enforced.

3. The government formally requires the main contractor to ensure that its subsidiaries and sub-contractors adopt anti-corruption programmes. There is, however, evidence that there are shortcomings in enforcement.

2. The government formally requires the main contractor to ensure that its subsidiaries and sub-contractors adopt anti-corruption programmes, but there is no evidence that this is enforced.

1. The government encourages but does not formally require the main contractor to ensure that its subsidiaries and sub-contractors adopt anti-corruption programmes.

0. There is no evidence of the government formally requiring the main contractor to ensure that its subsidiaries and sub-contractors adopt anti-corruption programmes, nor is there evidence of the government encouraging this informally.

SELLER INFLUENCE

When procuring defence and security equipment and services, international political deals and arm-twisting can mean that the contract is awarded to a company because of its nationality, rather than its bid. To avoid corruption, it is important that the government bases procurement decisions on legitimate need, and is not

pressured into purchases by sellers.

76. How common is it for defence acquisition decisions to be based on political influence by selling nations?

This is inevitably a difficult question. Media stories may provide a guide. Political influence by the selling nation is a common characteristic of large defence deals. Yet many governments manage to keep the decision based on technical or capability grounds.

4. Almost no acquisitions are granted as a result of political influence. There is consistent evidence that the government purchases according to military need, and this is validated by independent assessments or statements by the media that identify this specific need.

3. The bulk of evidence suggests that acquisitions are independent of political influence, yet some evidence points towards occasional incidences or small-scale purchasing that has a political element.

2. Some acquisitions are granted as a result of political influence by seller nations. Where expenditure is justified by reference to military need, there is likely to be uncertainty over how pressing this military need is.

1. Although the government may sometimes justify purchases by referring to military need, the bulk of evidence suggests that purchases are driven by political influence by seller nations.

0. Evidence suggests that it is extremely common for defence decisions to be driven by political influence by seller nations. The government is unlikely to justify military procurement by referring to military need, and may not justify its defence and security expenditure at all.

EMBARGOED

