Transparency International(UK)

Project PCOAT: “Preventing Corruption in the Official Arms Trade”

Arundel Conference

June 8 – 10, 2004

CONFERENCE PROCEEDINGS

Table of Contents

	Page
List of acronyms	3
Introduction	4
Session 1: Government perspectives on integrity in defence procurement	6
Session 2: Defence industry codes	10
Session 3: Integrity pacts and the experience so far	15
Session 4: Regulatory and parliamentary oversight of defence contracting	19
Session 5: Discussion Groups	24
Session 6: Discussion Groups: The Way Forward	30
Recommendations	32

Note
These conference proceedings are an amalgam of both oral presentations and written presentations of the speakers. This conference took place under the Chatman House rule. All names except those of the speakers have been removed.

Acknowledgements
Transparency International is particularly grateful to Lesley Richardson for her work as Conference Organiser.

List of acronyms

BPCB	Business Principles for Countering Bribery
COARM	Conventional Arms Exports Working Group
DFID	Department for International Development, U.K.
DII	Defence Industry Initiative (US)
DIP	Defence Integrity Pact
DIP	Direct Industrial Participation
ECA	Export Credit Agency
EDA	European Defence Agency
EITI	Extractive Industries Transparency Initiative
FCPA	Foreign Corrupt Practices Act
GSA	General Services Administration
IP	Integrity Pact
LMC	Lockheed Martin Corporation
MFA	Ministry of Foreign Affairs
MoD	Ministry of Defence
NAO	National Audit Office
NGO	Non-Governmental Organisation
NIP	National Industrial Participation
PCOAT	Preventing Corruption in the Official Arms Trade
TI	Transparency International
UNICE	Union of Industrial and Employer's Confederation of Europe

For further information on this project refer to the TI(UK) website www.transparency.org.U.K.

Introduction

The initiative to counter corruption in the official arms trade was developed over the period 2000-2003 in close association between TI(UK), with funding from DFID, and the Swedish Ministry for Foreign Affairs. The first phase of this project from January 2004 until July 2004, led by TI(UK), culminated in this conference at Arundel, Sussex, in June 2004. It brought together interested parties from defence companies, governments and NGOs to review the progress made in Phase 1 and to help chart the way ahead.

The objectives of the conference were:

- To bring together officers of European and US defence companies, representatives of governments and NGOs, to commence the development of a common framework for high quality standards of business conduct in international defence procurement

- To develop a common understanding across governments and companies of Integrity Pacts and to decide what modifications are needed so that they may be applied constructively by governments to international defence contracting

- To develop proposals as to how parliamentary and regulatory oversight of international defence contracting can best be strengthened

The conference was well attended with 6 defence companies, 5 governments and 6 NGOs represented from 14 countries. Day One comprised of presentations by speakers followed by discussion and on Day Two, participants spilt into working groups for themed discussions.

Day One: There were presentations given on the following:

Session One: *Government perspectives on integrity in defence procurement*
Steven Shaw, Deputy General Counsel, Contractor Responsibility, US Air Force
Air Vice Marshal David Hobart, Asst Chief of Defence Staff, MoD, U.K.
Anne Charlotte Wetterwik, Swedish Ministry for Foreign Affairs

Session Two: *Current defence industry codes: their strengths and weaknesses*
Dominique Lamoureux, General Secretary, Thales
Howard Weissman, Deputy General Counsel, Lockheed Martin
Simon Webley, Institute of Business Ethics
Susan Côté-Freeman, TI-Secretariat

Session Three: *Integrity Pacts and experiences so far*
Rosa Ines Ospina, Director, TI Colombia
Admiral Tahiliani, Chairman, TI India
Mark Pyman, Project leader, PCOAT project, TI (U.K.)

Session Four: *Regulatory and parliamentary oversight of defence contracting*
Roy Isbister, Saferworld
Professor Ravinder Pal Singh, Stockholm University
Judge Willem Heath, Heath Consulting

Day Two: There were working groups on the following:

Codes of conduct, parliamentary oversight and regulation, offsets, confidentiality & national security, Integrity Pacts, defence procurement and its reform and political pressure within the procurement process.

Opening Address

Peter Eigen, Chairman of Transparency International, opened the conference, welcoming participants from the many countries and organisations represented. He emphasised the importance of fighting corruption in the defence industry and of how this was also a proliferation issue: expanding the arms trade beyond what was necessary for a country's defence. The fight against corruption was also finding new frontiers to address with the development of international terrorism. He finds that there is a growing coalition against corruption, which has been given impetus by the signing of the UN Convention against corruption and the OECD Anti-Bribery Convention. Multilateral institutions were now much more active in this arena; the World Bank is now actively involved in the fight against corruption, and this work aligns with the work of TI. The World Bank announced in September 2003, for example, that they intend to use Integrity Pacts in its projects.

Welcome Speech

David Murray, Deputy Chairman of Transparency International (U.K.) and Chairman of the Strategy Committee for the PCOAT project, welcomed participants to the conference. He opened by stating that TI(U.K.)currently has four industry-focused projects: construction and engineering; extractive industries; money laundering (particularly in relation to London), and the arms trade. He added that TI in general and this conference takes as a starting point that defence is a valid industry and does not challenge the right of defence companies to exist and to conduct their business. Instead, what TI is looking for is an improvement in some areas of business conduct.

He thanked DFID as the sole source of funding for this project which has allowed it to be fully staffed at the TI(U.K.) London office. And mentioned that although the support from within defence industry for the project unfortunately is not unanimous, there are also companies that are supportive of the project's aims but are however, unable to be present. These are Boeing (US) and Rolls Royce.

Session One
Government Perspectives in Defence Procurement

Defence contracting is known to be an area where corruption has been particularly pervasive. Governments in a number of countries are taking measures to strengthen the integrity of the process, either in procurement processes or in oversight mechanisms. This session explored the main areas of focus from the government perspective.

U.S. Government Perspective by Steven Shaw, Deputy General Counsel, Contractor Responsibility, U.S. Air force

The tools of suspension and debarment protect the government from doing business with contractors that are not "responsible" and have the immediate effect of making the contractor ineligible for new contracts (and for many public subcontracts), or for federal assistance programmes with all Executive Branch departments and agencies. In addition to these measures, before the awarding of any new contract, the US contracting officer must verify that the contractor's name is not on the "GSA" list of all debarred companies and is available on the Internet.

Most suspensions are based on the commission of a crime or civil fraud, poor contract performance, or other contractor misconduct. Sanctions for irresponsible contractors include criminal penalties and imprisonment; civil penalties and restitution; termination of existing contracts; debarment and suspension. Debarment is for a specific period of time, generally no longer than three years. Civil penalties in government defence contracting amount to $300 million per annum.

In the U.S., contractors are encouraged to behave responsibly, principally through ethics programmes. This 'carrot' approach is considered to have a much greater impact than the 'stick' (incarceration). Companies can avoid being debarred or indicted for corrupt activities if they have such a system in place and misconduct will often be informally reviewed if it is disclosed by the contractor and administrative agreements signed in lieu of debarment. Documentation of remedial measures, improvements to and independent verification of a company's ethics programme and monthly reports to the U.S. Air Force are typical provisions in such an administrative agreement. The administrative agreement must be verified by an Ombudsman and be disclosed to the public. These procedures look similar to the draft of the DIP. However, ethics programmes should go beyond compliance and the single most important factor for the success of such a programme is that the message comes from CEO level.

A current example of this policy approach can be seen in the Boeing case. Boeing unlawfully took proprietary documents from Lockheed Martin in connection with the EELV Space Launch competition. As a result, three Boeing employees were indicted and the investigation of Boeing continues. In July 2003, Boeing was suspended from eligibility for future space-related contracts. In addition, Boeing had seven launch awards worth $1 billion terminated and was unable to compete for three further launches.

Sanctions can be applied to all parents, subsidiaries and divisions, regardless of location. However, information regarding past debarments in other countries is not easily obtained due to limited resources. The need for investigations to be broadened is recognised. If a subsidiary is found to have committed a corrupt activity and does not have an ethics system

in place, the parent company could be debarred. Misconduct can also be imputed: employees and owners who "should have known" of their employer's misconduct may be debarred and a contractor may be debarred for misconduct committed by employees.

An indictment constitutes adequate evidence for government to suspend a contractor (although this is not a prerequisite). Once a proposed debarment has been announced, the contractor has 30 days to respond and has the right to an evidentiary hearing if the material facts are disputed – a showing that has not once in the last seven years been made. A contractor can reduce sanctions by demonstrating responsibility, through for example; the existence of an effective ethics programme, voluntary disclosure of the act; full cooperation with the authorities; pleading guilty in a criminal case; disciplining employees; agreeing to implement remedial actions and management recognition of the problem.

U.K. Government Perspective by Air Vice Marshall David Hobart, Assistant Chief of Defence Staff, Ministry of Defence, U.K.

The U.K. public services are generally not predisposed to corruption. This is illustrated by Anthony Sampson's research which takes as starting point the absence of corruption in the U.K., and is mirrored in the work of the historian Peter Hennessy who also argues that corruption is not entrenched in the U.K.

A high level of oversight of the defence procurement and sales processes already exists in the U.K. through the National Audit Office (NAO) and the Ombudsman system as well as the strict export licensing controls, none of which are predisposed to corruption. Certainly, there are individual failures, but corruption is not institutionalised in the system. This is verified by the Nolan Report on Standards in Public Life which came to the same conclusion and is borne out by the lack of criticism the U.K. receives from its trading partners.

At the Ministry of Defence, corruption has not featured in any of the largest 50 programmes in the last few years. There is a clear separation between the officials who define requirements and capability and those who procure the equipment. There is no capability to proceed illegally. There are also strict procedures regarding the giving and receiving of hospitality

The forthcoming Freedom of Information Act will change working practices radically, further reducing the potential for any corrupt activity by reversing the burden of proof.

Swedish Government Perspective by Anne Charlotte Wetterwik, Swedish Ministry for Foreign Affairs

There are a number of guidelines and legal instruments available to governments for controlling the arms trade. For example, the EU Code of Conduct is constantly developing from a political commitment to a legally-binding document. However, the push for a new anti-corruption criterion in the EU Code has so far been unsuccessful. Industry is the key to the export control process, and the OECD Anti-Bribery Convention, UN Anti-Corruption Convention and Sweden's export control regime all have extensive outreach programmes to industry whose cooperation is essential. Therefore, existing tools must be used to boost links with companies and adherence to government guidelines. Within the national export licensing system, the need for anti-corruption control also for dual-use materials is recognised. National guidelines are the most effective place for controlling exports of defence equipment

and it is Sweden's intention to lead by example in this area. The Swedish government would like to promote and back a potential test case for a Defence Integrity Pact (DIP).

Real progress in export controls, requires a "sales pitch" by the seller countries, in addition to networking, awareness and alliance building (particularly in the EU setting), and tangible results on the DIP and the defence industry code. The Swedish Ministry for Foreign Affairs will spread the word on these initiatives nationally, within the EU (COARM), and internationally and will continue to work with TI and industry as partners in this.

SESSION ONE DISCUSSION

A number of questions were asked relating to debarment procedures in the US. For example, how public are debarments, what burden of proof is required to debar a company, are debarments from other jurisdictions considered, and post-debarment, what, if any special procedures are taken to improve company compliance?

The Representative explicated that debarments are public and that the names of debarred firms are listed on a website. Before a new contract is awarded, this site must be checked. Regarding burden of proof, present responsibility is the key issue and the intention is not to punish firms for offences committed in the distant past. Companies can be suspended on suspicion of wrongdoing and be debarred on reasonable cause. Debarment will happen based on the preponderance of evidence; that is if 51 per cent of evidence is convincing. If a contractor does not raise evidence to the contrary, then it is assumed that the act of bribery took place. There has not been a single hearing since the representative took office seven years ago. The pressure from government to debar companies has been increasing over this period. Sanctions are less severe if a company can show it has an ethics programme, if there is a code of conduct and if the perpetrators are fired. Post-debarment companies are taken off the Internet list when they agree to document the changes they have put in place in their systems; disciplinary procedures are implemented; hotlines set up; an independent in-house review has been set up that monitors procedures; there are external audits; and they have external verification by an independent ethics consultant to ensure effectiveness and thorough oversight. There is also a three-year period of probation. Debarment procedure is similar to the draft DIP.

The representative can only access debarment information relating to U.S. debarments – the information is not available for other companies. The department's limited resources constrict investigation efforts. For example, relating to an Asian deal, where a foreign agent of a large U.S. contractor was convicted of paying a bribe to secure the sale of helicopters, the U.S. representative could not obtain the information as there were insufficient resources to do so. It was accepted that investigations needs to be broader, but there remains the practical problem of obtaining information.

It was noted that after five years of debarment procedures, the number of debarments has not fallen, prompting the question to what extent the current stick programmes deter corruption?

One industry participant from Europe commented that more pressure needs to be put on those soliciting the bribes i.e. the governments of importing countries. This was partly in recognition that the OECD Anti-Bribery Convention only pressurises companies. A government official responded that progress could be made on existing control regimes which would flush out corruption, via the use of political statements, such as best practice documents and "statements of understanding". There was disagreement amongst participants as to whether the export control regimes possessed sufficient power to deal with anti-bribery

initiatives. Another participant added that UNICE could progress the anti-corruption agenda, as it entails a strong legally-binding commitment. However, searching for an appropriate political forum for this initiative should not deter from the fact that cooperating with industry in this area is key. Existing tools must be strengthened to boost links with companies.

Regarding the lack of criticism the U.K. receives from its trading partners, it was argued that a lack of peer pressure does not necessarily imply an absence of corrupt behaviour if all parties implicitly cover up for each other. Conceding this, it was suggested that this outcome is less likely to occur as overcapacity and the desire for competitive advantage become more pressing in the defence sector. It was emphasised that it is not in the U.K.'s interests to create an environment where companies win contracts unlawfully. This is being illustrated by the current U.K. caution towards obtaining contracts in Libya where there is still an EU arms embargo. One participant asked why the U.K. MoD repeatedly failed to follow up accusations of bribery in relation to U.K. firms. The response was that all allegations are followed up within the legal and administrative frameworks. Nothing is swept under the carpet. However, there is a constant drip-feed of allegations against U.K. companies and a variety of other 'mischief making' especially in the context of Gulf sales. The claim from one participant that U.K. companies are inadvertently encouraged to export corruption by excessive pressure to export was strongly refuted.

One participant asked how the DIP could be launched in COARM and whether EU countries should be targeted as buyers or sellers? In reply, initially the concept should be launched with the aim of persuading EU friends and partners to sign up to it. These countries should promote it to their companies as a good marketing tool. The next step would be for one country to adopt it and to lead by example.

It was asked whether there were analogous systems for debarment in the U.K. and Sweden. Currently in Sweden there is no debarment system, although developments within the UN system are being surveyed. Action will be taken against a company where there is sufficient evidence that it has breached the OECD Anti-Bribery Convention. Such cases could be investigated by the small parliamentary group that examine and provide counsel in forthcoming contracts and licences. Cases in the past, such as the Bofors case of the 80's, triggered the Swedish interest in the PCOAT project. However, it is difficult for a small country like Sweden to lead on such matters.

The issue of exceptionally close relations between government and their defence companies was raised as an area of concern. Reference was made to the current Boeing case in the U.S. which is an example of the revolving-door syndrome. It was added that U.K. government policy is not rigorously to investigate corruption allegations. For example, in the Al-Yamamah case, the government has not allowed questions to be asked in parliament or for the NAO report to be published and is therefore protecting BAe. However, there is a different industry view which complains that government does not give it enough support. The U.K. government relationship with BAe systems is not 'cosy' – viz the current semi-public arguments, and government is not complicit with industry.

Session Two: Defence Industry Codes

There is a common family of defence industry codes in the USA based around the Defense Industries Initiative, but there are different company-specific codes in Europe. Their effectiveness is not only in their content, but also in the way they are promulgated inside the company, their reach across the organisation and their interactions with government regulations and multilateral conventions. This session explored what elements would constitute a strong international framework or template, and how this framework could be developed.

Opening Comments by Laurence Cockcroft, Chairman of Transparency International U.K.

The Chairman opened by inviting participants to reply to a number of questions for example; are Codes for public relations purposes only? Are they effective only if the CEO and Board are committed to the process? Should companies that have Codes be treated more leniently?

In terms of the PCOAT project, can we envisage a global or regional code emerging? Can the TI business principles for countering bribery (BPCB) be used as a framework?

Perspective of one defence company by Dominique Lamoureux, General Secretary, Thales

Globalisation has been the catalyst for a changing regulatory framework, whilst Enron and September 11th have helped to shift the focus to a global and concerted fight against organised crime, money laundering, corruption, etc. As a result, corporate responsibilities are widening, linking international trade to respect for human rights and the fight against corruption. As the legal framework adjusts, greater transparency and traceability are required.

Changes in society make it necessary to develop high standards. In addition, there is a widening gap between legal and market requirements and the risk to corporate image that can be more damaging than criminal sanctions. An ethical approach for a company means assuming its economic, legal and social responsibilities. Globalisation places extra responsibilities on firms but does not offer a sufficiently comprehensive framework of regulations. Therefore, an international company must take on the task of producing rules to comply with existing regulations, to standardise the rules that apply to its employees and partners, and to define the highest standards. Regulatory pressures should be standardised across countries for reasons of fairness.

Adopting an ethical approach gives a company a competitive edge by, for example, reducing the risk of sanctions and enhancing a company's image and reputation. It can also strengthen company identity and staff motivation. Structures and procedures to guarantee strict compliance with the law include effective monitoring, audit mechanisms and sanctions. Structures and procedures to guarantee high standards include a code of ethics or conduct. Explicit commitment from management is essential, with no cosmetic buzz-words, to move from company ethics to an ethical company.

Lockheed Martin's FCPA Compliance Programme by Howard Weissman, Deputy General Counsel, Lockheed Martin

Lockheed Martin's FCPA compliance programme with the Foreign Corrupt Practices Act is embodied in two corporate policy statements, CPS-730: *Compliance with the FCPA* and CPS-704: *International Consultants*.

Lockheed Martin Corporation (LMC) policy applies directly to LMC, its wholly-owned subsidiaries, officers and employees. Policy applies by contractual requirements to distributors, agents, brokers, consultants, representatives, etc. who may have contact with a foreign customer and who are hired or retained to provide services directly related to obtaining, retaining, or facilitating business opportunities (including offsets). Affiliated (controlled but not wholly-owned) entities must adopt policies and procedures substantially similar to CPS-730 to assure compliance.

LMC has accounting and record-keeping controls as well as anti-bribery provisions. However, there are limited exceptions and affirmative defences of payments e.g. facilitating ("grease") payments. Operational directions include strict commitment to compliance, and prohibitions to make payments except under CPS-730. Ensuring compliance with financial and accounting directions is the responsibility of the Vice President and Controller. These directions prohibit for instance payments to anonymous or third party bank accounts.

It is the responsibility of each Responsible Officer (head of each LMC company or business element) to certify compliance with the FCPA and CPS-730. Reports are prepared to certify compliance with the FCPA and CPS-730 on an annual basis. Hospitality guidelines only apply to hospitality furnished to officials or employees of a foreign government or agency or instrumentality thereof and impose specific US dollar limits for meals and refreshments, limits on hospitality at air shows, roll-outs and trade shows.

LMC's due diligence process for international consultants under CPS-704 is designed to help ensure FCPA compliance. The process for retaining or renewing an international consultant includes references, disclaimer letters, ICP/Embassy check, legal opinion, etc. All employees involved in international business activities receive ethics training, including an FCPA compliance component. In addition, LMC's International Consultant Agreements contain a number of key provisions to promote FCPA compliance, such as that no payments or gifts have been or will be made, offered, or promised to improperly influence foreign officials and that the consultant agrees to comply with LMC's Code of Ethics and Business Conduct. The International Consultant Agreements also prohibits the consultant from subcontracting, delegating or assigning any of its rights or obligations under the agreement without LMC's prior written consent.

A Comparison of US and European Defence Company Codes of Conduct by Simon Webley, the Institute of Business Ethics

An evaluation of the following company codes of conduct was undertaken for the PCOAT project: Lockheed Martin, Raytheon, Boeing, General Dynamics, United Technologies, GE, Northrop Grumman, BAe Systems, Thales, Rolls Royce, EADS, Ericsson and Saab.

The results of a comparison of U.S. and European defence company codes of conduct revealed that US codes are considerably more compliance (rather than value) driven, are less user-friendly but are much more developed and detailed than their European counterparts. In

the U.S., Codes are driven by the Sarbanes-Oxley Act and the Securities and Exchange Commission. In the U.S., codes are taken very seriously and it is possible to have a fine reduced by up to 90 per cent if a company has such guidelines in place.

The embeddedness of the codes in the culture of their organisations is missing from both U.S. and European codes studied. Training, feedback and auditing are also conspicuous by their absence. All codes fell short on detail. Despite this, the European codes were thought to be harmonious with the requirements of the Defence Industry Initiative (DII). The DII has wide acceptance, (although or because), it not demanding and set at the level of lowest common denominator. Personal leadership from the top of the corporate structure and government encouragement are essential for the success of a code. Value based codes are considered superior to codes based on fear. It is considered worth the effort to develop a code.

Overall, codes are seen as an opportunity for management to show they take their business seriously. For example, 165 employees were fired from BP in 2003 due to fraud, theft and dishonesty.

The Transparency International-developed Business Principles for Countering Bribery were considered more detailed than most companies currently go into.

There were no references to standards on Israeli company websites. It is not known whether Russian companies make reference to standards.

The Business Principles for Countering Bribery (BPCB) by Susan Côté-Freeman, TI— Secretariat

The Business Principles for Countering Bribery (BPCB) (www.transparency.org) are a risk-management tool, set out in a generic document applicable to many sectors and usable by companies of all sizes. There are two main tenets to the BPCB: the enterprise shall prohibit bribery in any form, whether direct or indirect, and the enterprise shall commit to implementation of a programme to counter bribery. The BPCB apply to bribery of public officials and private-to-private transactions. Their purpose is to provide practical guidance for countering bribery, creating a level playing field and providing a long-term business advantage. It is a value (rather than compliance driven) driven document, purposely pitched at a level of good rather than best practice, and has been designed so that it can be embedded within an organisation.

The BPCB were inspired by the OECD Anti-Bribery Convention, where it was deemed that it would be helpful to create systems that would enable companies to fulfil their obligations. The focus is on the following areas: political contributions; charitable donations; hospitality; gifts; contractors and suppliers. TI is asking companies to adopt the BPCB or to use them as a benchmark against their own codes, and TI is currently talking to the larger players to put pressure on smaller firms to adopt the BPCB.

Business was involved in the development of the document and a Steering Committee has been formed which now has approximately 14 member companies, including some from the South. Limited consultations and field tests were carried out with Tata (India) and British Petroleum (Azerbaijan).

The BPCB were launched in 2002 and TI has now carried out 25 workshops in 15 countries. The scope has been intentionally limited to anti-bribery, where a gap had been identified in corporate policies. The BPCB are supported by a detailed guidance document and are

intended to be moderately static over time. The role of the CEO in anti-bribery policies, a light support structure and the absence of the involvement of a large number of lawyers are seen as crucial for the success of anti-bribery policies.

SESSION TWO DISCUSSION

A large part of the discussion focused on the purpose and efficacy of codes and the elements that are essential for their success.

Industry expressed the view that signing up to a code in itself is of little value. Creating confidence amongst the companies to be able to escape the prisoner's dilemma is imperative to the extent that if all the companies involved in a particular deal sense that there is corruption involved, all companies should be willing to withdraw. The formulation of an industry-wide DIP was viewed as one way to create this confidence.

No strong preference was expressed by participants as to whether a framework should be global or regional. Some participants suggested that the DII should be expanded to become a global initiative. Others preferred that a European equivalent focused on anti-corruption be developed in parallel with the DII. The DII was seen as a success in terms of interaction and cooperation even though the standard itself was not demanding, and thought easily adaptable to focus on anti-bribery.

When developing a code, it is necessary to design principles that are implementable and to bring the bodies within parliaments of exporting countries that oversee arms exports, more fully into the picture, thus creating a framework which will advance the practice in a legal way. Organisations like the Wassenaar Arrangement would be a suitable platform for this, but may require a redefinition of mandate. There is also the need to marry the principles of five or six main suppliers, secondary suppliers and the buyer countries. Another participant reiterated the importance of obtaining government support, particularly customer governments,. The participant added that 60-70 per cent of defence spending is within NATO, which is already developing a common procurement policy and so it may be possible to tag this initiative on to a common procurement policy. Another participant added that making a Code/IP a pre-qualification requirement for sales to NATO might help to resolve the problem of countries that refuse to sign up to ethical policies. A U.K. representative stated the importance of leading by example. By illustration, the example was given where the U.K., Canada and U.S. are currently helping Russia to dispose of weapon stocks. If Russian subcontractors don’t reach certain standards, then the U.K. will refuse to enter into a contract with them.

Many participants expressed the view that independent external monitoring was pivotal. One added that there is little evidence that codes have any impact on behaviour unless they are monitored, regardless of whether the code is industry-wide or not. To illustrate this point, it was stated that there are fifteen industry-specific codes of ethics: only one of these, the chemical industry, has proved itself to be effective as the companies are able to monitor each other.

The issue was raised as to who should be doing more to enforce the OECD Anti-Bribery Convention. In relation to the arms scandal in South Africa one participant expressed the view that companies should be doing more, but an industry participant refuted this, arguing for more pressure on governments. It was mentioned that the IP could be one way of ensuring the OECD Anti-Bribery Convention was being enforced. It was added that U.S. companies

can turn to the Department of Justice for help, which may explain why there has been more prosecution activity in the U.S. under the OECD Convention than anywhere else.

Regarding the U.S. compliance approach, it was opined that more independent thought within companies is required beyond the input of lawyers. One company representative noted that their company does impose additional controls, for example, through a code of ethics which stipulates that one must behave with honesty, integrity and follow foreign laws. To illustrate this point, despite the fact that facilitation payments are allowed under the FCPA, in that particular company, there is a general rule of no facilitation payments, and if the intention exists to make one, the request must go through the lawyer.

The important role of small companies in these initiatives was also raised as there is a tendency to focus on the prime contractors. The view was given that the large companies should use their market strength to encourage smaller ones, once they are on board themselves.

The point was also raised and noted that it would be beneficial for companies to provide information to their shareholders in the event that they had walked away from a potentially corrupt deal. They should also publish such information in their corporate reports, as Shell and BP have done on corruption incidents. Both these measures would help to gain wider support.

Session Three: Integrity Pacts and the experience so far

Integrity pacts are a promising tool for reducing corruption in major contracts and are thus of great interest for countries that place a priority on fighting corruption. This session will explore the experience of integrity pacts to date. The experience has been generally positive, but there are nevertheless issues. Features specific to the defence sector and their possible remedies were aired for discussion.

Opening Comments by Michael Wiehen, Chairman, Transparency International, Germany

IPs are already in existence in 16 or 17 countries. They were first used in Colombia, followed by other Latin American countries. European countries have begun experimenting with them. To date, civil works have proved a useful area for their application.

There are a number of possibilities for the development of an IP which includes the development of a company code with a structure for implementation and enforcement; the development of a sector wide code; or the development of a voluntary IP for the defence industry. The main advocates of the Integrity Pact (IP) should be business.

From experience, the execution phase of the IP is very important and this phase must also include agents. Arms' purchases must be made on competitive process not single-source process.

The Colombian Experience of Integrity Pacts by Rosa Ines Ospina Director, Transparency International, Colombia

The IP is not an antidote to corruption. However what they do is focus the discussion in the area of ethics in public contracting and they are also a good tool for transparency. Colombia has had an extensive and positive experience with IPs. Since 1999, there have been IPs in 77 public contracting procurements, with 50 different institutions in both central and local government, some 52 multinationals and 300 national companies have signed IPs over this time. Each IP helps to protect a massive sum of money. The important aspect of an IP is the process, not the document.

There are three main elements to the IP in Colombia. Firstly, the existence of a third party: a technical, independent expert that examines documents, ensuring that specifications do not already favour one bidder. Secondly, all bidding documents are made public. (The Colombia MoD puts most of the information relating to the bid on the Internet.) Bidders can sign a confidentiality agreement to see more sensitive information, which helps to build a risk map. Thirdly, it provides an ethical education and builds confidence.

Bidders' concerns are given great importance and they are encouraged to articulate the kind of behaviour that they would like to see in their competitors. They must also agree on sanctions. To fight corruption successfully, political pressure and facilitation payments must also be addressed. The procurement law has recently changed in Colombia whereby any

company wanting to deal with the government must have a set of business principles. These details are kept on a register.

Transparency International in Colombia has also recently carried out a detailed review of the application of a limited version of IPs in defence procurement in Colombia.

More detail of Colombia's experience with Integrity Pacts can be found in the summary of Integrity Pact experience so far at: www.transparency.org.U.K. and on the TI-Colombia website at: www.transparenciacolombia.org.co

The Indian Experience of Integrity Pacts by Admiral Tahiliani, Chairman, Transparency International, India

In 2001, Transparency International gave presentations in the Ministry of Defence on the subject of Integrity Pacts. The Ministry of Defence seemed earnest and promised to make this part of the revised procurement procedures which were being formulated then. However, the final procedures which promulgated a year later, omitted any reference to the subject of Integrity Pacts. With the change in Government in May, 2004, the opportunity to pursue this again is being taken up.

Integrity Pacts for Defence by Mark Pyman, Project Leader, PCOAT, Transparency International (U.K.)

Over the last five months, the PCOAT project has discussed key issues in relation to the IP with five governments: South Korea, Colombia, South Africa, the U.K. and the U.S. being examples of both exporting and importing countries. There have also been discussions with many companies and NGOs in those countries. Defence is different to other areas of business in a number of ways: the customer is almost invariably a government; the company is often indistinguishable from government; a high level of secrecy is employed; military hierarchies there exist; and agents are used extensively.

An important question needs to be addressed in whether Integrity Pacts for defence (DIP) can move forward with just importers, or just exporters, or just companies? As an importer, South Africa has shown an interest in DIPs. Exporting governments can push their companies to adopt DIPs and support their use, possibly through export credits or export controls. If 10-20 defence companies can commit to DIPs, this should be sufficient as there are far fewer companies in this sector than others.

The DIP has a number of salient features:

1. The need for an independent monitor
2. The specification of the amount of money an agent receives and how that is spent
3. The requirement that defence companies should implement a Code of Conduct. Two or three DIPs would galvanise companies into ensuring they have the necessary anti-bribery elements in their codes
4. Confidentiality and national security are particular to this industry. Negotiating this is difficult, but the Colombian MoD for example, was happy for TI and a lawyer to check through its accounts
5. Offsets are hugely open to corruption, as the recent case in South Africa illustrates and are not currently included in any defence industry codes or the DII

6. The need for the DIP to be applied to sub as well as prime contractors

There are other important questions that need to be addressed, for example does contract size matter? Should the DIP be a precursor to all government reforms? Should DIPs be aimed at large or small contracts? What is the correct content and process for getting DIPs into place?

The work done in this initiative has shown that Integrity Pacts should work well in defence and there is encouragement to see them applied for both importing and exporting governments.

A full report of the use of Integrity Pacts in defence is available at:
www.transparency.org.U.K. as part of Phase 1 of the PCOAT project.

SESSION THREE DISCUSSION

One participant from a developing country drew attention to the issue of political pressure from exporting nations and postulated that implementing an IP where *realpolitik* was at play would be an impossibility. Political parties are looking for money to contest elections and thus will solicit money whenever they can to this aim. Therefore, instead of an IP which focuses on one sector at a time, what is needed is a public sector integrity accord that covers all government departments. The only protection from government-to-government pressure is to keep discussions transparent and peer pressure from civil society is also crucial. The ability of political pressure to distort the market was raised by several participants.

National security and secrecy are further factors that will affect an IP in particular how bidding contracts are made public. In Sweden, industry was created out of the need for an independent defence industry to sustain national security during the Cold War. Companies have cutting edge technology that they want to keep secret. The Ministry of Defence in India themselves had admitted that secrecy was over-used for political reasons, and also partly to keep information from the opposition. Asking the military to share information even in the presence of a truly independent monitor was also noted as a potential difficulty.

The issue of how single-sourcing and the political nature of the defence market would affect IPs was raised, with the view being expressed that to some extent this was impossible to avoid, due to the unique features of this market. However, what must be avoided is deliberate single-sourcing. In the majority of cases, it is possible to stop this from happening. A broader definition/specification of product would encourage competition.

Regarding the independent monitor, the view was stated that the position would require constitutional authority. However, another participant thought that the independent monitor would not need constitutional authority as he/she does not make decisions but speaks and influences. If corruption was suspected, he/she will speak first to the main parties and if uncorrected, only then go public.

There are three models for independent monitor:
1. Team consisting of a lawyer, a technical expert and an NGO representative
2. An auditor, (similar to an single qualified assessor)
3. Independent monitor
4. Committee for example the U.K.'s NAO or the Comptroller and Auditor General (CAG) in India, that would include an Ombudsman and nominated members of the Defence Committee

The general opinion of the conference was that DIPs should best be applied by the encouragement of exporting governments as sellers. It was also seen to be in the interests of industry to promote them. Secondly, DIPs should initially be aimed at the prime contractors who would then use their market strength to encourage smaller companies to adopt them.

Session Four:
Regulatory and Parliamentary Oversight

Defence contracts pose special challenges both for regulators and for parliaments. They are often large relative to other procurements; they are cloaked in secrecy, sometimes justifiably, sometimes not; defence companies are aggressive and competitive in an oversupplied market. This session discussed whether these issues are being addressed sufficiently and if not, which are the measures that would have the greatest beneficial effects? The issue of where do company codes and Integrity Pacts fit into the tapestry of oversight was also debated.

U.K. Arms Export Controls by Roy Isbister, Project Co-Ordinator, Arms Export Controls, Saferworld

There is much room for improvement in both domestic procurement and in export controls in the U.K. to ensure that they are free from corruption. One suggestion for this has been that corruption could become a 9th criterion in the EU Code of Conduct, but feedback shows limited appetite for this at present. However, it should be possible to elaborate on criterion 8 – the sustainable development criterion – to include anti-corruption wording. In criterion 8, there could be a requirement to examine whether defence expenditure is on or off budget; a reference made to corruption indices; examination of whether there is an ethics and compliance code in place or whether DIPs are in use (in the future). Criterion 8 should be used to pre-empt corruption and it should be explicit that licences will be refused where government has reason to believe there has been corrupt activity. This said, criterion 8 is seen as the 'poor relation' of the criteria as very seldom is it used to justify a denial notification.

Another suggestion is for export licenses to require an explicit anti-corruption statement, for example, by requesting a personal sign-off letter by a senior executive of the exporting company. If the only cost for a company of corrupt activity is that an export licence is turned down, it does not pose much of a risk for a company and thus follow-on sanctions are also necessary.

A third requirement is for transparency to be enhanced by the publishing of annual reports and a fourth suggestion is for increased parliamentary oversight that would enhance accountability with a more proactive commitment to investigating rumours of corruption. These details should be published, particularly when corruption has occurred. Credit should be withdrawn from the export credit agencies if there is any corrupt activity discovered and agents' fees should be published which would raise the burden of proof.

Parliamentary oversight and the positive impact that Integrity Pacts can make on defence contracting by Professor Ravinder Pal Singh, Centre for Pacific and Asian Studies, Stockholm University

There are a number of democratic reforms including improving parliamentary oversight of the defence procurement processes which would increase the military's accountability to the public and reduce possibilities for corruption.

Confidentiality is an impediment to accountability

Secrecy can allow corruption, fraud and abuse to creep into the system, which can encourage interested parties to enhance secrecy even further, creating a vicious circle. Secrecy can also lead to security apprehensions in the region leading to an action-reaction spiral of arms procurement decisions. A lack of accountability can, for instance, generate threat assessments that exaggerate demands for military equipment, which in turn can lead to insecurity in neighbouring countries.

To remedy this, public understanding of the military's decision-making processes will enhance public confidence and professional scrutiny by agencies other than those who have an "interest" in the decision will benefit the military's decision-making outputs. Parliamentary oversight of arms procurement processes would address only a small element of the larger problem – the building up of awareness in civil society of its fundamental right to know how the state is planning and developing policies for its security. Therefore, it is essential to build a political culture which accepts democratic control of the armed forces as the norm.

Accountability of defence budgeting processes

National parliaments have a constitutional role and duty to monitor and scrutinise public expenditures and financial demands of the government. Defence budget-making must develop a professionally accountable financial accounting system. As the security sector is entirely financed from public tax, the governments are obliged to explain to the tax payers its processes for organising security of the society.

Accountability and transparency of defence budget process and financial expenditure must be ensured. This can be achieved by clearly documenting the defence management process for evaluation and audit, and legislating processes for parliamentary review of defence budget allocations. Parliaments should harmonise competing requirements of confidentiality of military related information and legislate the requirement of accountability of public funds allocated to the defence budget. Defence budget proposals could be broken down to different levels of security classification, with one level being classified expenditures which could be scrutinised by a bi-partisan sub-committee on defence budget and military expenditures.

Processes and methods for auditing defence expenditure

The most important part of security sector accountability process is the obligation of the executive and the armed forces to render the accounts on a timely basis. Auditing is fundamental to accountability. Parliamentary audit or accounts committees should ensure that the statutory audit authority functions according to the constitutional provisions, achieves the best international standards, introduces legislations in the parliament which enhance its professional oversight capacities, and ensure that an external audit of the statutory audit authority is carried out by preferably an agency in the private sector.

Corruption: a product of unverified military confidentiality

The military leadership's efforts to make their decision-making processes accountable for professional and financial probity would be the primary requirement for creating an environment in which corruption is neither accepted nor condoned.

What can be done at parliamentary levels to check corruption in arms transfers?

Considering the need to harmonise legitimate requirements of military confidentiality with valid needs of public accountability to check corruption and fraud in arms transfers. The need is to develop a resource with following criteria: i) enables scientific verification; ii) a professionally qualified body, iii) which should be constitutionally legitimate; and iv) should have an independent statutory authority. A commission based on these criteria could be formed as and when a statement of intent for arms acquisition is announced by an arms buying government (or it issues a request for proposal).

In the case arms buying countries, such a commission should function under the aegis of bi-partisan members of parliamentary committee on defence. It should comprise of representatives from the statutory audit authority; corruption vigilance departments; parliamentary ombudsman.. It should examine experts from anti-corruption watch dog agencies, arms procurement offices and intelligence services responsible for confidentiality of documents.

Once an arms supplying company or a country responds to arms procurement request, parliamentary committee for foreign affairs in the supplying country should organize a similar commission to monitor corruption prevention processes which should include: former representatives from arms sales promotion offices; export licensing authority, corruption vigilance departments; parliamentary ombudsman and one/two bi-partisan members from related parliamentary committees.

These two commissions should verify corruption prevention steps being taken at all the stages of arms sales and procurement process. Findings of such a commission should be sent to the cabinet as well as the leader of the opposition. If correective action is not taken then the findings should be resented to defence committee of the parliament.

Democracy and the Arms Deal in South Africa by Judge Willem Heath, Heath Associates

In a democracy the Legislature is accountable to oversight committees in the parliament and the Executive should act with integrity, representing the interests of the population: if this does not occur, the government does not have a mandate to rule.

In the recent arms deals in South Africa, there were serious irregularities in the procurement and conclusion of contracts. The deal lacked integrity, politicians were ignorant of the actions of the Executive and companies were overcome by greed. The principles of democracy failed. The call by the oversight committee for an in-depth investigation by objective experts was never undertaken. This lack of adherence to parliamentary recommendations is the reason why controversy still looms despite the contracts being signed some time ago.

The only way to serve the electorate is through democracy. Once minds have been re-orientated towards more democratic practices, IPs will follow naturally. A government is obliged to practise integrity: it is not a question of choice.

This conference is an expression of a desire on the side of interested parties who are known to promote integrity. It is exciting to see companies who share this desire forming part of the debate to lay down guidelines for future defence contracts.

Integrity is the key word. From South African and other experiences, it will be an uphill battle to promote integrity. However, there are reasons to be positive about the promotion of integrity.

To combat bribery and corruption in arms deals, total transparency in the procurement of arms is required. In other words, the public should have a right to decide whether government should spend public funds to purchase arms instead of increasing budgets for social development. What sets the arms industry apart is the extent of secrecy, which breeds corruption and which has clouded aspects of South Africa's arms deal. Legitimate needs for secrecy, such as national security, are necessary, but often helps to cover up inappropriate aspects of the defence contracts. The balance of government control and transparency needs to be addressed carefully.

The key element emerging from most arms deals is the concentration of decision-making power in the hands of a few officials, often leading to bribery and corruption. To what extent should decision-makers be required to explain the choices they make?

In addressing these questions, arms procurement decision-making processes should not be seen as technical issues separate from political matters.

There is a need for two different types of accountability - political accountability and administrative accountability. Political accountability is required to avoid government policies and programmes that do not correspond to public preferences and interests. Administrative accountability is required to reduce the level of waste, corruption, fraud and abuse to a minimum. Accountability needs both internal and external control systems. In both, the control systems need to be based on laws that establish right to information.

In South Africa, a law, namely the Promotion of Access to Information Act, was published in 2000. Under this act, one of the South African contractors who tendered for the arms deal but who was not awarded the tender, won a court decision against top ranking government officials and agencies to force them to hand over information regarding the arms deal tendering process to him. This was a landmark case and this law should be implemented in all countries in a similar form to aid transparency.

Corruption inflates the price of purchased equipment and increases the tax burden on citizens. For poor people this is an unforgivable betrayal of public trust. This was evident in the South African arms deal, the value of which was inflated.

SESSION FOUR DISCUSSION

The discussion mainly focused on whether anti-corruption criteria should be added onto export control regimes, or whether it would better to focus attention on encouraging the enforcement of existing legislation. One industry representative expressed the view that anti-corruption criteria in the export control process would put an added administrative burden in an already over-burdened area. If there is meaningful legislation prohibiting corruption, then efforts should be focused there. If violations are found, a group of sanctions, including civil and criminal fines, debarments and suspension of export licences should be considered. It would be more effective to focus on existing EU laws and the OECD Anti-Bribery Convention rather than trying to create new ones.

It was mentioned that there are already internal guidelines within DFID to consider levels of transparency and accountability in the importing country under criterion 8. It would therefore be possible to ask staff on the country desks to also consider parliamentary scrutiny, budget allocation and other such measures when granting a licence and DFID would be willing to encourage other member states to look at the possibility of introducing the corruption issue into criterion 8. Another government representative added that whilst the review of the Code is ongoing, a trend towards a more formalised version may entail a more open interpretation of the criteria. However, including anti-corruption wording in criterion 8 would have a better chance of success than pushing for a new, 9th criterion. A different U.K. government representative doubted that even reasonable belief of corruption in criterion 8 could bar an export from going ahead as some competitors can create rumours of false and corrupt payments.

One participant noted that in the past there were a greater number of export licences and it would be possible to insert anti-corruption criteria here. A different participant proposed that it is more a question of practicality: how a government would like to organise its own oversight. Explicit guarantees should be requested by ECAs, for example requiring the signature of managers, whereby if corruption is found, insurance cover would be void. There is a strong argument that at any point in the financing of credit for arms exports, extra tools are needed. The idea of introducing an anti-corruption component (either as a process or statement) into the export licensing is to pre-empt trouble.

Regarding agents' commissions, one participant stated that disclosure of commissions by buyers would be welcomed at export license stage but argued that norms needed to be established as to what is an acceptable amount to pay. A government representative retorted that setting a percentage of contract amount was problematic and that the acceptable amount of commissions would need to be worked out on a case by case basis. It was noted that an NGO called TRACE has developed standards of due diligence in this area.

A further comment was made that the regulatory approach should not be limited to markets and bureaucracies. Parliamentary scrutiny should play an early role and this would help to reduce threat inflation. However, a large and possibly an increasing number of defence purchases are made off-budget and therefore purchases do not necessarily go to parliaments for scrutiny. Parliaments are trying to become more assertive and are trying to address this problem of need to know in order to enhance public accountability. For example, the budget committee of the parliament in South Korea functions in three different ways, which includes, producing a budget and presenting it to parliament, looking at classified elements of the budget (having been sworn to secrecy) and scrutiny of the budget by a cross-party committee. However, the view was also expressed that since it is a politically controlled market, even with more parliamentary oversight, politicians can protect the executive depending on the internal balance of power. In this sense, political will is the key.

Session Five
Working Group Offsets

Two groups tackled the issue of offsets. Questions were addressed such as: How widespread is their use? What are the pros and cons? Where do the principal risks for corruption lie? How should offsets best be managed?

Much of the discussion focused around the offsets deal in the recent arms scandal in South Africa. The representatives from South Africa outlined the major issues with respect to the deal. The initial value of offsets indicated by the government was more than three times the contract value of 32 billion Rand, in the order of 104 billion Rand. Among a number of problems associated with this deal, were that the offset agreement itself did not legally specify that the money be spent in South Africa and companies were seldom seen to comply with their offset commitments. The perception in South Africa was that the money would have been much better spent on social needs such as housing, health and education.

Some industry representatives argued that as offsets create an extra burden for companies and do not allow for a level playing field, they should be banned. This view was countered by a representative from another defence company who argued that in commercial terms, European firms can gain a competitive advantage using offsets, and thus to abolish them would put European firms at a disadvantage. U.S. companies are able to benefit from economies of scale and the enormous political influence of their government abroad. His view was also that it is unfair to label offsets as a corrupt area and this was seconded by a civil society representative, who added that it is not only corruption that drives offsets: they are often linked to presidential 'pet' projects.

One company representative explained that within his own company, offsets are divided into two main groups: DIP (direct industrial participation) which are easier to quantify; and NIP (national industrial participation) which are harder to quantify. He added that DIPs involve investments and all payments are clearly linked to milestones in the offset delivery. No payment is made to the company until these offset milestones are reached. The volume of NIP is much higher and programmes last for many years. Overall, it was judged too early to predict the final outcome of the various offset arrangements in South Africa.

One industry representative stated that offsets are considered an essential part of any major defence contract as countries must be given the skills, training and technical knowledge to run the products and systems that they purchase. U.S. government policy is not to propose specific offsets and government-to-government sales do not include them. The government, however, does not intervene if U.S. companies chooses to include them in their defence sales packages.

The advantages and disadvantages for both companies and countries that are associated with offsets were also discussed. For example, on the country side, advantages include technology transfer and local production while the disadvantages include distortion of the bid through inflated pricing and the ongoing risk of corruption throughout the process. On the company side, advantages would include a stronger bidding position and the opportunity to gain a comparative advantage in this area, while disadvantages are giving work away and the distraction from the company’s core business. Overall, it was surmised that the confusion and

opacity surrounding the application of offsets make it not only easy to hide corruption, but also endanger the ability of the market to operate efficiently and transparently.

The most critical issue was thought to be how to manage offsets, not only from an anti-corruption perspective, but also throughout the process. The key areas of due diligence of both agents and those involved in the process, systematic monitoring of implementation, penalties for non-delivery and ownership of 'sub-sub contractors' were identified as being central to creating a better system. The need for flexibility was also addressed as many offset stipulations are initially vague and can vary as importing government change their minds on their requirements as the contract progresses. One channel of corruption was the award of offset contracts to companies close to the government and/or a country's head of state. If the exporting company is not familiar with the location, there will be little time to verify whether the companies bidding for offsets are bona-fide or not. Additionally, in a situation where there is little indigenous industry, most, if not all companies may in fact be connected to the government, making it potentially difficult to intervene in this area.

Working Group:
Codes

The two groups on codes addressed the following questions: how to develop an industry-wide code? Should it be European or global? Would a code or framework similar to the DII be more suitable? Who should be involved in the process? How should the process be started?

One view expressed was that the concept of an over-riding code for the defence industry would need to be developed globally. It was thought that it may be better to start from the beginning (thereby scrapping the DII in the process) as there could be resistance for cultural reasons to the expansion of the DII into a global initiative. A second undertaking would be to construct a 'Statement of Principles' as a key feature of a model framework - a list of 5-10 key features which would be acceptable to all as a minimum standard. Each company could then reword these Principles to fit the codes of their own organisation. The third proposition made was that implementation of the essential features of an ethics compliance programme could be converted into company-wide best practice, to be used as required across the defence sector.

However, a second set of opinions thought that the DII works well and thus would be a useful starting point for a defence industry code. The six principles of the DII should be taken and adapted to focus more broadly on anti-bribery and other moral issues.

The code should be generated by the key companies themselves as ownership is essential. The code should not be imposed by governments, although they too are important stakeholders in the process.

One cause for concern with the DII was that currently there is no external monitoring mechanism and this would need to be to be addressed if the DII was to be adapted. The example of the chemical industry code in Canada which includes provisions for external monitoring was offered as a possible model on which to base the new code. Overall, developing a framework approach for the whole industry, bound around principles similar to the DII, but focused on anti-corruption was seen as the best way forward.

Working Group: Parliamentary and Regulatory Oversight

Discussion included: Which regulatory change offers the best scope for anti-corruption requirements? What are the priorities or actions needed to develop parliamentary oversight in defence?

There were two sets of views were given. One, that effort should be focused on ensuring that proper enforcement of existing regulatory frameworks and this should take priority over adding anti-corruption criteria to export controls. However, a second set of opinions was that specific corruption could reasonably be included in export control regimes at the national and international level which could relate to both importers and exporters.

There should be more parliamentary oversight of and involvement in export decisions and proper investigation into past corrupt activities.

The debarment mechanism in the export control process was seen as an important tool for government and participants agreed that it should become more widespread and active in countries other than the U.S. It should also be seen as a preventative measure rather than just punitive.

The U.S. system of sophisticated regulation (compliance, codes, practices) offers a good model and transparency throughout the process should be the rule rather than the exception, particularly regarding agents fees. There was no common agreement on possible criteria for agent disclosure.

A Statement of Understanding, with specific anti-corruption wording, should be sought at a high political level to show willing which would give more bite to enforcement of current regulations. It should ensure that the new Freedom of Information Act does not make exceptions for the defence sector.

Working Group: Defence Procurement and its Reform

Questions considered included: Whether there is a reform textbook for change? What are the priorities for reform and how should progress be made?

For exporting countries, it was deemed that progression towards mechanisms which resemble the bureaucracy-heavy system in the U.S. is probably inevitable and may offer the best way forward. Such a system would allow for example, clear limits to be set on agent fees. It was also agreed that greater transparency at all stages of an importing country's analysis, combined with increased parliamentary oversight of the subsequent process was highly desirable.

The suggestion was made that more countries could get involved in sending teams out to help importing countries with their procurement practices and this would serve the additional purpose of addressing the current mistrust of individual exporting country motives in sending out such teams.

It was thought that the idea of creating a survey of vulnerability of a country's defence procurement processes should be explored by TI. Such indices have been used for comparison of municipal bodies in some countries and have a significant impact.

The huge variation in the standards and methods of arms procurement practices across countries was commented on and that one of the main priorities for reform should be a clear articulation of best practices within the overall process. This would include, inter alia, value for money, accountability and transparency, a clear legal framework and checks and balances for the separation of key procurement functions for example definition of requirements and the acquisition itself.

As for TI's role in this reform, it should be to gain a country's confidence by acting with credibility and competence. TI could participate in capacity building and the sharing of ideas amongst procuring nations to develop expertise in this area. However, it needs to be kept in mind that there is no 'reform textbook' which would impose an externally generated generic approach onto importing countries. A good entry point for TI is often a change of government or a scandal which has created the political will to tackle the problem of corruption or malpractice.

Working Group:
Defence Integrity Pact (DIP)

Discussions included: What are the priorities in facilitating adoption by governments? Who should be involved? And what is the best way to make progress?

The main goals of a DIP were seen as being to promote competition, obtain value for money by getting prices right, ensure efficiency, increase transparency for accountability and reduce corruption. The onus for establishing a DIP should be on the buyer country, and political will is crucial in this process. The DIP can be applicable for single-source as well as open-bids. Confidentiality agreements could be implemented where essential. The need for DIPs to be applied early on and for the duration of the contract was explicated. The corruption-risks from offsets and secondary contracts were viewed as extremely high, and the result of political pressure is to skew the process further.

National security, secrecy and a lack of impartiality were the initial problems identified in defence contracting. The point was made that traditions and practices in different parts of the world vary. For example, there is still a residue of ideologically and "bloc" motivated countries in the global marketplace. Therefore the country-specific DIP needs to be tailored for specific country needs. An independent monitor was deemed crucial to the process and more important than public scrutiny. He/she would need to sign a confidentiality agreement. The importance of involving all stakeholders in mapping the risks was emphasised. Finally, the parliamentary defence committee scrutiny process in the importing country should be able to complement a DIP once the political decision to proceed has been taken.

Working Group: National Security

Discussion included: What problems does secrecy pose for the defence industry? Can secrecy can categorised? How much information 'should' be published?

The discussion focused on secrecy, the abuses of it and how corruption thrives on it. The rationale for secrecy should always be open to scrutiny and DIPs could be one way of making more information known. This is not to ignore the fact that technical knowledge should be safeguarded, although, in practice it does not actually need to stay 'secret' for long. Pressure from governments to maintain secrecy was also noted, and this was often because they don't want neighbouring countries to know about their own defence procurement. Different categories of secrets were noted: technological secrets; commercial secrets (revealing this information might affect a firm's competitiveness); and strategic confidentiality (to conceal the defence capability).

The opinion was expressed that as a rule, information should be published: secrecy should be the exception. Specification criteria should be published, but this need not include the key technical details. A further point was made that if all information on the details of all monetary transactions involved in a contract were published, even without exact technical details, there would be less scope for corruption. It was suggested that an expanded DII may be one way of forcing firms to reveal information. However, buying governments would also need to agree to reveal the details of their expenditure, subject to parliamentary oversight.

Working Group: Political Pressure

Discussions included: What constitutes political pressure? Is political pressure itself a form of corruption? How can it be countered?

Political pressure, both from within and from exporting countries was recognised as one of the most distinguishing features of large defence contracts. Different motives for and types of political pressure were identified. It was noted that political pressure can vary in intensity and can be either external or internal. Political pressure may be motivated by the desire to create an economic linkage through offsets and/or licensed production or to maintain one's own natural industry. Political prestige may also play a part e.g. the desire to execute a "pet presidential" project. Political pressure may also be the result of strategic pressure e.g. the desire to be part of an alliance/ club or be motivated by fear of sanctions and/or political repercussions. Corporate pressure by "national champions" on governments may also encourage governments to pressurise other governments.

Possible solutions to political pressure were discussed. A strong, widely respected procurement process was probably the best, albeit partial solution. There was the suggestion of holding a transparency audit or attempting to debunk some of the myths of the benefits of defence procurement in particular relation to political benefits and offsets. The idea of a TI

country procurement vulnerability survey could be researched. Attempting to reduce demand for defence equipment by, for instance, using NGOs and media to ensure the existence of an external oversight mechanism and initiating a collective agreement among (NATO) states were further ideas put forward for this.

Discussion Groups: The Way Forward

This final session split into three groups, each focusing on what is achievable in the PCOAT project over the next eighteen months.

Defence Integrity Pacts

The suggestion of a DIP across the industry was promoted. The sector agreement was thought essential if firms are to have an interest in and take ownership of this project.

The priority was now to do some real applications of the DIP. The importance of finding a test case where the risk of failure is low is paramount and will facilitate the project being adopted in the first instance. Hence, a market should be sought out where there are near monopoly conditions. This pilot scheme is likely to be imperfect but the DIP can be modified as a result and the benefits of the learning process publicised.

The group did not think it necessary to choose a country where an IP already exists. In terms of location, one southern and one northern country should be selected at a minimum. Colombia, India and South Africa are potential southern candidate countries. South Africa may be particularly interested and has a forthcoming procurement in the near future. It may also have more robust political will following the recent arms import scandal.

Sweden, U.K., Latvia were cited as potential northern countries to pilot a DIP. The MoD was thought to be the main hurdle in the U.K., although there was willingness to pursue the idea. The same problem was raised in relation to Sweden, there are also fewer large contracts in question at this point in time. Latvia may be willing to implement a DIP. Latvia is currently building up its defence base and there national concern that corruption will increase as a result of the procurement process of being overwhelmed by large defence companies.

Industry Framework/Anti-Corruption Code

This group focused on processes for the establishment of an anti-bribery code of conduct or framework for the defence industry.

This group believed that although codes only take care of part of the problem of corruption, it was well worth progressing with one in this initiative. It was agreed that a framework set of principles as in the DII was the best way to start, focused on anti-corruption. One of the principles should be the adoption of the TI Business Principles for Countering Bribery. The DII could be expanded for this aim. Since support from the top is pivotal in the success of any code, the recommendation was made that CEOs of corporations should be contacted directly in relation to this. Monitoring of the code was thought essential and debarment was seen as an essentially useful tool.

The need for importing governments also to raise their standards was noted. One way for this to be done might be for NATO countries to establish a code of compliance that could apply to NATO-country companies. In this vein, if NATO could be persuaded to make a code part of

their procurement processes, it could also then be extended to apply when operating outside of the NATO area.

A final suggestion was made that a website detailing information on issues such as integrity in defence procurement, a debate of a way forward, the listing of each company's code of conduct and past infringements could be set up.

Regulatory Oversight and Procurement Reforms

To begin with, this group believed that TI should identify broad procurement principles that are consistent with broader principles of best practice and then, from this, develop a definition of a good practice.

A further recommendation was that TI should engage in capacity-building initiatives with importing countries. This would require a multi-sector steering group which might involve the NATO parliamentary assembly as a testing ground.

A Statement of Understanding from high political levels to include buyers and sellers should be requested that would support anti-corruption proposals and would help TI make entries into ministries of defence across various countries.

TI should work with those involved in arms export control regimes at both national and international levels, to make anti-corruption more explicit in the regulations. The role of the export credit agencies (ECAs) could further be explored.

The development of a vulnerability survey that examines the vulnerability for corruption should be explored. Finally, defence procurement could become the topic of the TI essay competition to celebrate Anti-Corruption Day on December 9th.

Recommendations

A number of recommendations were distilled from the conference proceedings. In addition, TI(UK) has developed a suite of proposed actions to address each of these.

1. Implementing Defence Integrity Pacts

The Conference recommended that Defence Integrity Pacts (DIP) now be applied in real situations. Initially, it is recommended that two early applications be identified, one in a buyer country and one in a seller country. Potential countries are South Africa, Colombia or India as southern countries and Latvia, U.K., and Sweden as northern countries. The DIP should be tailored to suit individual country needs, applied early and for the duration of the contract.

Proposed Actions:

i. Actively engage exporting governments on the merits of supporting DIPs, suggesting that the DIP could be launched in fora such as COARM, NATO, the Wassenaar Arrangement and maybe other export control regimes. This, in some cases, may require a redefinition of mandate

ii. Publicise DIPs widely and particularly to importing governments:
   - Produce a smart, formal booklet on anti-corruption in defence contracting and the use of DIPs
   - Speak at relevant conferences about DIPs, and provide articles for publication

iii. Work closely with TI chapters to promote the application of DIPs in their governments

iv. Discuss with multilateral institutions on ways to fund the DIP independent monitors

v. Establish firm links with interested governments, through personal visits similar to those undertaken in Phase 1

vi. Discuss with interested governments whether they might act as the sponsor of an inter-governmental initiative in reducing corruption in defence procurement; for example, using the Extractive Industries Transparency Initiative (EITI), sponsored by the U.K. Government, as a possible starting point model

2. Developing a Framework Code of Conduct for the Defence Industry

A critical mass of defence companies should come together, with the support of TI(UK), to develop a strong framework code of anti-bribery and corruption measures for the entire industry. The use of a framework, based around a modest number of principles, as in the DII approach in the U.S., would serve as a good basis for bringing the whole industry on board. Signatory companies can later align their own organisations to this framework.

Proposed Actions:

i. Build on the energy of the major players in Phase 1 of the PCOAT project, to rally the defence industry to develop a European and a global framework, facilitated by TI (U.K.) as required.

ii. Work with a few European exporting governments and their national companies, to develop a strong European position that is fully supported by the governments: possibly the U.K., France and Sweden in the first instance

iii. Approach the CEOs of major European defence companies to make a statement of intent at an appropriate public forum. One possible forum to make public the existence of this initiative could be the Paris Air Show in July 2005

iv. Encourage the G8 countries to take a clear position in combating corruption and improving transparency in defence procurement. This could be done by a statement at next year's G8 summit, and through appropriate preparatory work with government in advance of that

v. Develop a more detailed understanding of 'who owns who' in the defence industry and the composition of typical consortia

3. Exporting Country encouragement of their industry

The conference recommended that exporting countries be strongly associated with this initiative given the importance of their role. TI should work with European exporting Defence Ministries and their export support organisations to promote strong anti-corruption practices as an important platform for the common competitiveness of European companies.

Proposed actions:

i. Work with the U.K. Government, particularly the Ministry of Defence and others to bring all large U.K. based exporting companies into the fold of companies supporting a global industry framework. The U.K. is an important exporter, and it hurts both the U.K. and the global credibility of the defence sector if U.K. companies are not fully involved

ii. Approach the 'Letter of Intent' group of countries and companies in Europe (France, U.K., Sweden, Italy, Spain, Germany), to propose the establishment of a sub group devoted to establishing and maintaining a strong framework of anti-corruption standards across this group

iii. In co-operation with national ministries of defence, meet with defence companies and the defence industry associations to discuss the implications of the changing laws on bribery and corruption and the opportunities this may create for competitive advantage

4. Strengthening anti-corruption measures in regulatory requirements

The conference debated moves to place anti-corruption assurance more centrally in the arms control regimes, both at national and international level, providing they were

carefully targeted, rather than generally adding to the bureaucratic burden. Although there were mixed views, TI concluded that this was an important area to develop further into practical proposals. The conference supported the need for OECD Anti-Bribery Convention signatories to enforce the Convention more energetically.

Proposed actions:

i. Work with COARM and POLARM to strengthen anti-corruption measures in EU arms control regimes

ii. Stimulate OECD Anti-Bribery Convention signatory countries to investigate credible allegations of wrongdoing by defence companies and enforce as required.

iii. Maintain pressure on the regulatory environment around arms exports, notably to strengthen the EU Code of Conduct in respect of anti-corruption measures, preferably in the form of a 9th criterion

5. Reforming Defence Organisations and Processes

The Conference supported moves to strengthen anti-corruption measures and reform initiatives in defence procurement processes.

Proposed Actions:

i. Enter into discussions with the NATO Secretariat and the European Defence Agency on improving transparency and anti-corruption measures in NATO and EU procurement processes

ii. Assist groups that provide assistance on defence procurement reform (for example the Defence Advisory Teams based in the U.K.), with advice on the anti-corruption requirement of such reform

iii. Develop a set of principles related to procurement processes which would embody a definition of best practice

iv. Explore the development of a defence vulnerability survey for countries which focuses on the vulnerabilities to corruption