

Transparency International (UK)

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

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## **Project Summary (Phase 1)**

1. Introduction – drivers for change
2. This initiative
3. Outputs
4. Conclusions and next steps
5. List of recommendations
6. Contacts and enquiries

**July 2004**



## **1. Introduction – drivers for change**

Corruption in the arms trade continues to flourish. TI's bribe payers Index in 2002 ranks the arms industry in the top 3 most corruption prone industries worldwide. In the other two 'top 3' industries – oil and public works+construction – major international initiatives are underway to address corruption, involving the whole industry and many governments. Yet in arms, no such impetus exists.

People put forward different reasons for this. Some say it is because the arms industry and defence ministries have always been intimately entwined and remain so today. Others ascribe it variously to public indifference, lack of public data on arms spending, the pressure generated by overwhelming military threats, and the difficulty of knowing where to start.

But this is beginning to change. Many countries are much more aware of the damage that corruption does to their economy, their institutions and their development if not controlled, and that military spending is one of the biggest spenders in public contracting. There is a growing body of knowledge on how corruption in military procurement leads not only to inefficient buying of the wrong product, but also to far greater spending than is really justified by the threats. In this way, corruption in military procurement actively diverts resources from investments to develop the country and challenge poverty.

Within the defence companies too there are changes. Defence suppliers have had to look outside the military field since the fall of the Berlin wall: consequently they have a much higher percentage of civil work, and staff unused to military contracting. This is leading to a change of culture, one less tolerant of old ways of working. The legal environment is now tougher, with better anti-corruption laws, notably the OECD convention doing for the rest of the world what the FCPA has long done in the USA. Export Credit guidelines are at last getting tougher, with the UK leading the way. The market has changed too. The largest export market by far is now the USA, and non-US companies know that they must be at the very least in line with FCPA requirements if they are to do business in the US. In addition, the US makes it clear to foreign defence contractors that if they wish to compete in the US they need to be seen to operate cleanly in their operations elsewhere in the world.

These are real pressures, and many people in companies and in governments are responding to them.

## **2. This initiative**

Transparency International, as an international NGO dedicated to the eradication of corruption, has long been keen to see the prevention of corruption in this industry. Since 2001, TI (UK) has been bringing together governments, company representatives and civil society to explore constructive measures that can be taken. Conferences were held in Cambridge, England in April 2001 and Stockholm in February 2002, supported by the Swedish Ministry for Foreign Affairs and Trade. Twelve recommendations were made: for the reform of defence exporting processes, of importing procurement processes, and for the reform of trading rules to remove exemptions for arms companies.

Since the beginning of 2004, the UK Government, through the Department for International Trade and Development, has provided support to Transparency International (UK) to take

these recommendations forward, and to build an international coalition that together can combat corruption in the official arms trade.

### **Phase 1 – the road to Arundel**

In the first phase of this work, Transparency International(UK) has worked on two of these recommendations:

- the defence industry should develop a framework, or ‘meta-code, containing strong anti-corruption provisions, drawing on the experience of the Defence Industry Initiative in the USA, for individual implementation by defence companies globally
- importing countries should use Integrity Pacts in defence contracting, and also be encouraged to do so by exporting countries and governments

TI (UK) has developed these priorities in Phase 1 through the following activities:

- i. talking with governments in three arms importing countries and with civil society organisations in those countries, including the national TI chapter, about how Integrity Pacts can assist them and how they may need to be modified for defence contracting. The three countries were South Africa, South Korea and Colombia
- ii. talking with three exporting governments about the measures that they were taking and measures that could be considered to strengthen anti-corruption measures and to encourage their national industry to promote anti-corruption approaches in their export sales activities. The exporting countries were Sweden, the UK and the USA.
- iii. talking with defence contracting companies about how the industry might come together as a sector to promote stronger anti-corruption codes and promotion of Defence Integrity Pacts.
- iv. comparing defence company codes of conduct, and comparing them also with the requirements of the US Defence Industries Initiative and the TI principles for Countering Bribery
- v. reviewing the vulnerabilities to corruption at each step of the defence procurement process
- vi. carrying out an examination of how cut-down versions of Integrity Pacts have operated to date in defence contracting in importing country governments in South Korea and Colombia

The work done was reviewed at a conference at Arundel, Sussex, England, June 8 – 10, 2004, at which progress to date was discussed by representatives of companies, governments and civil society.

### 3. Outputs

TI has produced eight reports from this phase of the work:

1. A short project summary – this document
2. Defence Integrity Pacts – a tool for combating corruption in defence contracting
3. The defence procurement process and its vulnerabilities
4. Summary of the Arundel Conference
5. A comparison of the anti-bribery and corruption provisions of defence company codes, produced by the Institute of Business Ethics in the UK
6. Regulatory update
7. Detailed proceedings of the Arundel conference
8. A summary of Integrity Pact experience outside of the defence sector, being a condensed version of extensive documentation on the TI website

These reports are available on the TI(UK) website: [www.transparency.org.uk](http://www.transparency.org.uk). In addition, a number of other detailed presentations and reports are also available on the website.

### 4. Conclusions and next steps

This first phase has resulted in four broad conclusions:

1. Defence Integrity Pacts, proven in other sectors, can be a robust tool for reducing corruption risks in defence contracting. To be effective, however, it is essential that the independent monitor role is strengthened and made more professional. Importing governments find the concept appealing.
2. Defence companies increasingly see benefit in an industry wide approach to anti-corruption measures. This can be based on the DII type of framework, suitably strengthened.
3. Each of the four major groups of players – exporting governments, importing governments, defence companies and financing institutions – can make progress on their own. The nature of the defence business – global and with a political dimension – and the lack of a current industry mechanism for discussing such issues, argue for a forum in which all these groups can address anti-corruption issues together, and for a neutral organisation such as TI to facilitate such discussions.
4. There is great scope for reducing the risk for corruption through more transparent and better procurement processes in importing countries

These conclusions have been developed into recommendations and a set of proposed actions to advance each of them: see Section 5 below.

TI is now working with the UK Government at present on how to make best progress in Phase 2. Broadly, TI expects to carry on the same path as at present, working with companies, governments and civil society to build practical coalitions, to help importing countries put Defence Integrity Pacts in place, and to work with the defence industry in

getting to a global, or at least European, framework of conduct, and to work with exporting country governments on strengthening their support for, and oversight of, defence company standards of conduct.

## **5. List of 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 southern country and one in a northern 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 a forum such as CO-ARM, NATO, the Wassenaar Arrangement and the Australia Group. 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 UK 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 USA, 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 COAT project, to rally the defence industry to develop a European and a global framework; facilitated by TI (UK) 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 UK, 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 UK Government, particularly the Ministry of Defence and others to bring all large UK based exporting companies into the fold of companies supporting a global industry framework. The UK is an important exporter, and it hurts both the UK and the global credibility of the defence sector if UK companies are not fully involved.
- ii) Approach the 'Letter of Intent' group of countries and companies in Europe (France, UK, 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 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 9<sup>th</sup> 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 UK), 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 procurement index for countries which focuses on the vulnerabilities to corruption.

## 6. Contacts and enquiries

For further information, contact Carolyn Hodder at Transparency International UK on 0207 981 0344 or at [Carolyn.hodder@transparency.org.uk](mailto:Carolyn.hodder@transparency.org.uk), or project leader Mark Pyman at [markpyman@transparency.org.uk](mailto:markpyman@transparency.org.uk).

**Transparency International (TI)** has been at the forefront of the anti-corruption movement since it was formed in 1993. TI is a non-profit making, independent, non-governmental organisation, dedicated to increasing government accountability and curbing both international and national corruption.

TI(UK), also formed in 1993, is one of a network of 90 national chapters carrying out the TI mission around the world. TI works in a non-confrontational way with governments, companies, development agencies, NGOs and international organisations to seek a consensus to combat corruption. The UK chapter has worked on a slim staffing structure, and draws heavily for its work on the pro bono contribution of time by senior professionals in relevant fields such as law, banking, accountancy, diplomacy, corporate ethics and economics.

TI(UK) does not seek to expose individual case of corruption, but rather seeks to promote remedies for its underlying causes. Recent projects have included a heavy involvement in work to increase transparency in the extractive industries, including membership of the “Publish What You Pay” coalition of NGOs and contribution to the UK Government’s “Extractive Industries Transparency Initiative” (EITI), and also the production of a major report on money laundering in the City of London.