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A REVIEW OF THE ANTICORRUPTION STRATEGIES OF THE AFRICAN DEVELOPMENT BANK, ASIAN DEVELOPMENT BANK, AND EUROPEAN BANK ON RECONSTRUCTION AND DEVELOPMENT

HEARING

BEFORE THE

COMMITTEE ON FOREIGN RELATIONS UNITED STATES SENATE

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A REVIEW OF THE ANTICORRUPTION STRATEGIES OF THE AFRICAN DEVELOPMENT BANK, ASIAN DEVELOPMENT BANK, AND EUROPEAN BANK ON RECONSTRUCTION AND DEVELOPMENT

THURSDAY, APRIL 21, 2005

U.S. SENATE,
FOREIGN RELATIONS COMMITTEE,
Washington, DC.

The committee met, pursuant to notice, at 9:30 a.m., in room SD–419, Dirksen Senate Office Building, Hon. Richard G. Lugar, chairman of the committee, presiding.

Present: Senators Lugar and Martinez.

OPENING STATEMENT OF HON. RICHARD G. LUGAR, U.S. SENATOR FROM INDIANA

The CHAIRMAN. This meeting is called to order.

The Foreign Relations Committee meets to continue our review of U.S. policy toward the multilateral development banks. This hearing is the fourth in an ongoing series examining ways that the U.S. Congress and our Government can contribute to anticorruption and antifraud efforts at the multilateral development banks. The committee's work aimed at the MDBs is being conducted on multiple fronts. In addition to holding hearings, I have directed letters of inquiry on individual projects and policies to the respective banks. Committee staff members have visited overseas projects and conducted interviews with bank employees, nongovernmental organization representatives, academies, and others.

Building on this oversight effort, at the request of the Bush administration, I will soon introduce authorization legislation replenishing funds for the subsidized windows of the World Bank, Asian Development Bank, and African Development Bank. This legislation will include reform proposals to bring about more transparency and accountability in the operations of all five multilateral development banks.

Today, we are especially pleased to be joined by Ambassador Paul Speltz, U.S. Executive Director of the Asian Development Bank, and Mr. Mark Sullivan, U.S. Executive Director of the European Bank for Reconstruction and Development. We look forward to their testimony regarding the anticorruption strategies of the banks to which they are assigned. We also look forward to the testimony of Hemantha Withanage, Executive Director of the Center

for Environmental Justice in Sri Lanka and Tom Devine, Legal Director of the Government Accountability Project.

In addition, the committee invited two other witnesses to testify—Ambassador Cynthia Perry, the U.S. Executive Director to the African Development Bank, and Akie Hart, President of the Mangrove Forest Conservation Society of Nigeria. Both were unable to be with us due to unavoidable conflicts. They have provided us with written testimony, which we are very pleased to include in the record.

The United States has strong national security and humanitarian interests in alleviating poverty and promoting development around the world. The MDBs leverage the resources that we can devote to these goals. Since 1960, the United States has provided more that $42 billion in direct contributions to the MDBs. But we must ensure that our contributions are managed well and that the mission of the MDBs is not undercut by corruption.

The U.S. Senate is not alone in its inquiry into development bank financing. The Parliament of the United Kingdom has undertaken its own inquiry. In addition, the Italian Senate issued an Order of the Day last September referencing our committee's MDB hearings and calling for anticorruption reforms. We will include a copy of the Italian order in the hearing record.

[EDITOR'S NOTE.—The Italian Order mentioned is included in the Additional Statements and Other Material Submitted for the Record section.]

Corruption impedes development efforts in many ways. Bribes can influence important bank decisions on projects and contractors. Misuse of funds can inflate project costs, deny needed assistance to the poor, and cause projects to fail. Stolen money may prop up dictatorships and finance human rights abuses. Moreover, when developing countries lose development bank funds through corruption, the taxpayers in those poor countries are obligated to repay the development banks. So, not only are the impoverished cheated out of the development benefits, they are left to repay the resulting debts to the banks.

At our May 13, 2004, hearing, we learned that the MDBs have been taking steps to curb corruption, but much more needs to be done. Our witnesses provided clear recommendations about how the MDBs can minimize leakage in development financing. They recommended changing the incentives at the MDB, so that staff would have less pressure to lend. Witnesses also recommended that the MDBs focus more actively on supervision and auditing of MDB lending. They argued for more transparency in MDB operations, and an MDB requirement that borrowers improve transparency within their governments.

In our July 21 hearing, we learned that the United States Treasury Department does encourage anticorruption efforts at the MDBs, and reviews all MDB loans. The Treasury, however, has limited ability to investigate the misuse of MDB funds. According to Under Secretary John Taylor, and I quote, "The first line of attack, if our staff hears about issues like this, is to work through our Executive Directors at the institutions."

During our July hearing, we also learned the government of Lesotho was strained financially during its prosecution of corruption

relating to a World Bank-financed project. Unfortunately, there is no mechanism to assist poor countries that want to prosecute corruption related to their loans. It was suggested the MDBs harmonize anticorruption policies, and mutually recognize blacklists. As it now stands, a company that is debarred from the World Bank can still receive contracts from the other MDBs.

The testimony that we will hear today will further inform our efforts to develop reauthorization legislation that I will introduce shortly. The challenge of preventing waste, fraud, and corruption at the MDBs must be tackled with vigor. We welcome our distinguished witnesses, and look forward to their insights and their counsel.

It is indeed a privilege to have both of you gentlemen in our first panel. As I have mentioned earlier, we will have a second panel to follow your testimony. Before that, we will pose questions to you. At the time the distinguished ranking member joins our hearing, I will recognize him for an opening statement. But for the moment we will proceed with testimony in the order that I introduced you, and that would mean, first of all, the Honorable Paul Speltz, and then the Honorable Mark Sullivan.

Mr. Speltz.

STATEMENT OF HON. PAUL SPELTZ, U.S. EXECUTIVE DIRECTOR, ASIAN DEVELOPMENT BANK, MANILA, PHILIPPINES

Mr. SPELTZ. Thank you, Mr. Chairman. First of all, a personal comment. Ambassador Cynthia Perry, who is a close friend of all of ours, Representative to the African Bank, her husband is extremely ill, dying, and she was here right up with us until yesterday, and had to fly down to Houston last night to be with her husband.

The CHAIRMAN. Our thoughts will be with her and we appreciate the testimony that she has submitted. It will be a part of our record.

Mr. SPELTZ. Thank you. I'm also pleased to be here with my colleague, Mark Sullivan. The last time we were together, we were going through Senate confirmation hearings, and sitting in the same chairs, so it's a pleasure to be with him.

With your permission, I'd like to give a short statement, and provide my full statement for the record.

The CHAIRMAN. Your written statement will be published in full, and that is true also for Mr. Sullivan, so that you may summarize and utilize the time effectively here.

Mr. SPELTZ. Thank you.

Mr. Chairman, members of the committee, I thank you for your invitation to come and speak with the committee today on a subject that is fundamental to poverty reduction in Asia, and at the very core of sustainable development. Corruption is illegal, unethical, and inefficient. The Asian Development Bank must call corruption by its name, and take steps to prevent it and punish those who perpetrate it.

In an environment of scarcity, every dollar lost to waste, fraud, and poor governance, is a dollar not invested in health care, clean water, education, critical infrastructure, and other essential services. My goal is to make the Asian Development Bank a more re-

sults-driven and accountable institution. This means not only rewarding countries for good performance, but ensuring that the ADB makes the most efficient possible use of donor resources. This means full transparency, and protecting the shareholders of this institution, and the contributions they've made to it.

Since becoming U.S. Executive Director to the ADB in 2002, I have made internal governance reform, and fighting corruption top priorities. This committee may recall in my confirmation testimony here in June 2002, in which, when asked by Senator Sarbanes, even before I relocated to Manila, I stressed the importance of anticorruption efforts at the Asian Development Bank. That effort continues to this day. I have also made frequent visits to Capitol Hill to meet with congressional staff on anticorruption issues, and I hope to continue this dialog for as long as I am in my current position.

I was also pleased to host, at ADB last summer, a senior staff from this committee who was looking into these issues, and today, I again extend the invitation to any others who want to visit the ADB in Manila.

In the past few years, the ADB has made significant progress in opening its operations to outside scrutiny, strengthening its anticorruption capability, and promoting good governance in borrowing countries. Lending for Good Governance grew 50 percent last year, and the weight given to governance in the country allocation formula for the Asian Development Fund was substantially increased. A growing number of bank projects and country papers specifically address the risk of corruption and government's ability and willingness to deal with it. In 2004, the Bank halted disbursement on two loans for Indonesia because of corruption concerns. But these actions, while positive, are only the first steps in the right direction.

My Office has been, and will continue to be, at the forefront of advancing these reforms. At the institution level, we hope the ADBs Integrity Division, which was formerly called the Anti-Corruption Unit, become even more proactive in addressing allegations of fraud and abuse.

In the next few days, the Bank will begin implementation of a new, public communication policy that fundamentally changes the types of information made available about ADB operations, and how that information is made available and useful to all stakeholders. The new public communication policy will require full disclosure of the ADB budget, Board minutes, and Board schedule, and will continue the practice of publishing an annual report on corruption investigations. This new policy also satisfies many other elements of transparency language in section 581 of the 2004 appropriations legislation, which this committee crafted.

While this is another step in the right direction, the United States will continue to press for even greater transparency in the years ahead. At the project level, we would like anticorruption safeguards built into more project documents, stricter sanctions for those who violate them, and more spot procurement audits out in the field. Projects recently approved by the Asian Development Bank Board in response to the tsunami disaster, contain the most sweeping and most advanced safeguards to date. However, these

safeguards need further integration into all of the Bank's operation.

Internally, the ADB has bolstered the resources and staff available to its Integrity Division, which investigates corruption, and has doubled the number of procurement audits. As a result of U.S. advocacy, the 2005 budget for the Auditor's General Office was increased by 19 percent. As part of these efforts, I have served on the Audit Committee of the Board of Directors for the last 2½ years, and have helped turn that Committee into a more effective instrument for oversight. The Committee meets more frequently—once a month on average—as opposed to three times per year, when I first arrived, and when appropriate, without the participation of Bank management.

It reviews the audit report of the Bank's external auditors, and monitors management's implementations of its recommendations. The Committee works very closely with the Office of the Auditor General, of which the Integrity Division is a part, and it has helped that Office become a more active agent for promoting internal governance. Recently, the Office began a review of internal procurement rules, and it has sponsored regular corruption and fraud awareness workshops for all new incoming staff at headquarters, and for staff, a selective resident missions which, for example, in the year 2004, included instructions in Bangladesh, Pakistan, and Uzbekistan.

All of these elements are critical, but we believe much more can be done. We would like to see a more proactive and powerful role for ADB's Integrity Division, including a further increase in the number of procurement audits. This will require more resources, but it is an investment that will yield significant dividends.

Whistleblower protections also need to be strengthened to encourage staff to continue to report allegations of fraud. ADB can, and should, establish an important deterrent by publishing the names of debarred firms and individuals, and by automatically disqualifying those firms debarred by other financial institutions. We would like ADB to work with other MDBs, in the future, on a set of tough, uniform anticorruption standards.

At the country level, we hope to see assistance for good governance and anticorruption expanded, and at the project level, a greater willingness to cancel loans when corruption is detected.

Mr. Chairman, to reiterate and to close, I am fully committed to this agenda, and will continue to exercise the leadership and the influence of the United States to ensure success. Thank you for your time and consideration this morning.

[The prepared statement of Hon. Speltz follows:]

PREPARED STATEMENT OF PAUL W. SPELTZ, U.S. EXECUTIVE DIRECTOR, ASIAN DEVELOPMENT BANK (ADB), MANILA, PHILIPPINES

INTRODUCTION

Mr. Chairman, Ranking Member Biden, members of the committee, I thank you for your invitation to come and speak with the committee today on a subject that is fundamental to poverty reduction in Asia and is at the very core of sustainable development.

The goal of my office has been, and continues to be, to make the Asian Development Bank a more results-driven institution. This means not only rewarding countries for good performance, but ensuring that the ADB makes the most efficient pos-

sible use of its resources. This means full transparency and protecting the shareholders of this institution and the investments they have made in it. Corruption is illegal, unethical, and inefficient. In an environment of scarcity, every dollar lost to waste, fraud, and misgovernance is a dollar not invested in health care, clean water, education, critical infrastructure, and other essential services. This a human tragedy for the intended recipients in developing countries and a waste of taxpayer money in shareholder countries.

Since becoming U.S. Executive Director of the ADB in 2002, I have made internal governance reform and fighting corruption top priorities. The committee will recall my confirmation testimony here in June 2002 in which, when asked by Senator Sarbanes, even before I relocated to Manila, I stressed the importance of anticorruption efforts at the ADB. I have also enjoyed my frequent consultations with congressional staff on anticorruption issues and hope to continue this dialog for as long as I am the U.S. Executive Director. A senior staffer from the Senate Foreign Relations Committee, Jay Branegan, visited my office in August 2004, and I would be happy to extend an invitation to others that might wish to visit the Bank in Manila.

The ADB has made significant progress in opening its operations to outside scrutiny, strengthening its anticorruption capability, and promoting good governance in borrowing countries. But these actions, while positive, are only first steps. My office has been, and will continue to be, at the forefront of advancing these reforms. At the institutional level, we expect that the ADB's Integrity Division (formerly Anticorruption Unit) will become even more proactive in addressing allegations of fraud and abuse. The Bank's new public communications policy is a step in the right direction, and we will continue to press for even greater transparency. At the project level, we would like anticorruption safeguards built into more project documents, stricter sanctions for those who violate them, more "spot" procurement audits, and a greater willingness to cancel loans where corruption is detected. And at the country level, we want to see lending for good governance expanded.

Let me be more specific.

INSTITUTIONAL EFFORTS

Over the last year, the Bank has made significant strides toward becoming more open and accountable at the institutional level.

As a result of U.S. encouragement, the Audit Committee of the Board of Directors is now a more effective instrument for oversight. The Committee meets more frequently—once a month as opposed to three times per year—and, when appropriate, without the participation of Bank management. It reviews audit reports from the Bank's external auditors and monitors management's implementation of their recommendations. The United States has led efforts to make the Office of Auditor General a more active agent for improving internal governance. Recently, the Office began a review of internal purchasing rules and it has sponsored regular corruption and fraud awareness workshops for incoming staff at headquarters and for staff at selected resident missions, which in 2004 included Bangladesh, Pakistan, and Uzbekistan.

To combat corruption and thwart possible misuse of resources, the ADB recently elevated the status of its Anticorruption Unit to an independent Integrity Division within the Auditor General's Office. The Integrity Division serves as the initial point of contact for allegations of fraud and corruption in ADB-financed projects or ADB staff. It also conducts training seminars in forensic accounting and other investigative techniques to ensure ADB-funded activities and staff adhere to the highest standards of ethical conduct and recently launched a series of mandatory code of ethics seminars for all staff. The United States is encouraging the Integrity Division to increase the number and scope of its procurement audits and corruption investigations and is working closely with management to ensure that there are adequate resources for the Integrity Division to carry out its expanding responsibilities. As a result of U.S. advocacy, the 2005 budget for the Auditor General's Office was increased 19 percent. The ADB was the first MDB to post on its Web site an annual report summarizing corruption investigations.

The Bank recently decided to debar corrupt firms from all ADB-sponsored activities, not just procurement, and we will press for further enhancements in the months ahead. The ADB should also move toward publishing a list of debarred firms. We will continue to urge the ADB to work with other MDBs on a uniform set of "state-of-the-art" standards encompassing ethics, procurement, and anticorruption.

Progress is also being made on creating an institutional culture that promotes transparency. As a result of strong U.S. advocacy, the ADB has drafted a new public communications policy that substantially increases the presumption of disclosure

and includes several of the objectives from the transparency language in section 581 of Division D of the FY 2004 Consolidated Appropriations Act, which this committee helped to craft. Among other things, the ADB's new policy will make public the minutes of Board discussions and summaries of Board discussions of policy and strategy papers. But it also goes much further. The public will also have access to a rolling, 3-week schedule of Board of Directors' meetings, country performance ratings, and a full version of the ADB budget.

Those affected by ADB policies should have a strong voice in the policy process. In this light, we are pleased the Bank has taken significant steps to become more responsive to the concerns of civil society. In 2004, the ADB established a new inspection mechanism to address the concerns of persons affected by ADB projects. The new mechanism consists of a Special Project Facilitator who will focus on informal problem-solving and a Compliance Review Panel, which will focus on investigating alleged violations of the ADB's operational policies and procedures. The Compliance Review Panel reports directly to the Board of Directors. In 2004, the Compliance Review Panel initiated new investigations of two projects and monitored implementation of remedial measures for affected populations on a third project. The 2005 ADB budget includes a 12-percent increase in funding for the Compliance Review Panel.

Accountability is also promoted through the Operations Evaluation Department or OED. The OED evaluates the effectiveness of the Bank's operations at the project, sector, and country level, and assesses the contribution of those resources to a country's overall development. As a result of strong U.S. advocacy, a number of important reforms were made last year in the operation of the OED. The OED now reports directly to the Board rather than through the President and the appointment of the head of the OED is a decision of the board, upon nomination by the President. The OED's work program is subject to Board approval and the OED has unfettered access to all information and individuals it deems necessary to fulfill its work program.

PROJECT-LEVEL EFFORTS

The ADB has a number of tools to reduce the risk of corruption in project design and implementation.

On the prevention side, we would like staff to take greater advantage of their consultations with executing agencies and local contractors to address corruption head-on and recommend improvements in design that mitigate fraud. An increasing number of projects include strict anticorruption safeguards including, most recently, the subregional transport facilitation project in Nepal, the Sri Lanka tsunami rehabilitation project, and the Bangladesh independent anticorruption commission project. We would like to see more.

We encourage project staff to be more proactive in reporting allegations of corruption to the Auditor General. The Bank uses an array of measures to protect the identity and confidentiality of whistleblowers including the use of a special telephone line to report allegations of corruption and secure fax lines and e-mail addresses for staff from the Integrity Division. These protections are helpful, but we would like to see ADB management do more to encourage staff to come forward with claims of fraud and corruption and to guarantee that those who do will be protected. The Auditor General's Office is revising its Terms of Reference to further strengthen these protections.

Encouraging ethical behavior in staff also requires the right incentives. The ADB is increasingly using specific targets in project documents to measure development outputs and it is our goal that these be incorporated in every set of project documents as soon as possible. To ensure that results are actually achieved, the United States and other major shareholders have pushed strongly for a system that rewards staff for the quality, not the quantity, of their work. As part of this, staff should not only be assessed on achievement of development outcomes, but also on how well they comply with ethical guidelines. We will press for these standards to be implemented in the new human resources policy.

Related to this, the ADB has been actively implementing its administrative sanctions policy. Under this policy, the Bank rejects a proposal for award of contract where corrupt or fraudulent practices were used by the bidder, cancels the financing allocated to a contract if ADB determines that the beneficiary has engaged in corrupt practices, and debars the individual or firm from doing business with the ADB in the future. As a result of strong advocacy by my office and the Treasury Department, the ADB agreed to add two new professional staff to the Office of Auditor General in 2005 to strengthen its anticorruption oversight and to double the number of "spot" project procurement audits. In 2004, the Bank halted disbursement on two

loans for Indonesia because of corruption concerns. We hope to see a similar aggressiveness in investigating allegations of corruption in other countries.

Finally, ADB resident missions in each borrowing country play a critical role in providing oversight for project implementation. Our goal is to ensure they have adequate resources to provide ongoing project supervision and fiduciary oversight over procurement processes.

COUNTRY-LEVEL EFFORTS

Goverance assessments are an integral part of every ADB Country Strategy and Program. These assessments measure government performance against an array of benchmarks including anticorruption efforts, institutional strength, public administration, government interference in the economy, and transparency. Recently, there have been greater efforts to cooperate with and harmonize these assessments with those of the World Bank. During 2004, new assessments were initiated for Azerbaijan, Uzbekistan, Nepal, Laos, Afghanistan, India, and Sri Lanka.

The ADB is providing substantial amounts of assistance to help build accountable public-sector institutions and develop national anticorruption efforts at the country level. In 2004, lending for good governance increased 56 percent from $450 million to $700 million, and we expect further growth this year. Let me elaborate on a few of the Bank's most notable programs.

An ADB initiative in Balochistan Province, Pakistan, is designed to reduce corruption by mandating third-party assessment of all projects and independent audits of district accounts. In Bangladesh, the ADB helped the national government to establish an independent Anticorruption Commission to investigate and prosecute cases of corruption and fraud. The ADB is helping the Government of Vietnam to develop a grievance mechanism for handling complaints about corruption and to strengthen the oversight role of the National Assembly. Technical assistance to Indonesia, Micronesia, Thailand, and Bangladesh has helped these countries privatize state-owned enterprises, reducing the corruption that often accompanies such companies.

At the regional level, 23 countries have endorsed and drafted action plans as part of an ADB–OECD Anticorruption Initiative for Asia and the Pacific. The ADB and OECD are also working with the United Nations to help participating countries in Asia and the Pacific to ratify the U.N. Convention Against Corruption. In November 2004, the ADB provided $250,000 in technical assistance to help regional countries comply with the terms of the initiative.

At the 2003 APEC Summit in Bangkok, leaders supported a proposal by the United States to establish a Cooperation Fund for Regional Trade and Financial Security Initiative. To date, Australia, Japan, and the United States have each committed $1 million to the trust fund, which is run out of the ADB and will support technical assistance for antimoney laundering, customs modernization, and port security in developing member countries. Treasury's Office of Technical Assistance has secunded an expert who is working with the ADB to implement the trust fund and provide expertise for other Bank programs. These efforts will reduce the likelihood that public and private funds will be appropriated for illicit purposes.

Finally, to ensure that countries with good governance are commensurately rewarded, the United States and other ADB donors agreed last year to substantially increase the weight given to good governance—which includes anticorruption—in the performance-based allocation system for the Asian Development Fund. This system provides a clear incentive for countries to tackle governance issues in order to receive greater resources. The ADF allocations that result from the performance-based allocation system are made public.

CONCLUSION

To conclude, Mr. Chairman, let me say how seriously I take the threat corruption poses to the effective development of poor countries. The ADB has undertaken some important initial reforms but the proof of success is sustained effort. Reform is needed both within the Bank, to ensure that the ADB establishes a zero tolerance culture for corruption, and in the Bank's dealings with borrowing countries. The ADB must be more willing to call corruption by its name, and punish those who perpetrate it. This will require greater ownership from borrowing countries and stricter sanctions for those who violate the public trust, whether they are ADB staff, consultants, or employees of executing agencies. The United States is fully committed to this agenda and will continue to exercise our leadership and influence to ensure its success.

Thank you.

The CHAIRMAN. Well, thank you, Mr. Speltz, for your testimony. I now call upon the Honorable Mark Sullivan.

STATEMENT OF HON. MARK SULLIVAN III, U.S. EXECUTIVE DIRECTOR, EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT, LONDON, UNITED KINGDOM

Mr. SULLIVAN. Thank you, Mr. Chairman. I welcome your invitation to appear before you today to report on the efforts of the European Bank for Reconstruction and Development to combat corruption.

I share your belief in the importance of this issue, and have made it a priority for the U.S. Executive Director's Office. Financing for MDBs comes from the taxpayers' of their shareholder countries, and those taxpayers are entitled to the assurance that the MDBs will use their money in an appropriate and efficient manner.

My testimony today will focus on what was accomplished in 2004, and what we are pursuing this year. The EBRD's purpose is to foster transition of its countries of operation toward open market-oriented economies. The Bank currently conducts its investment activities in 27 countries that were formerly either a part of the Soviet Union, or the Soviet Bloc. Their histories have left them with a challenge when it comes to addressing and dealing with corruption.

For reasons set out more extensively in my written testimony, the EBRD does not have the leverage with the governments that other multilateral development banks, which lend directly to governments, have. The major reason is that the charger of the EBRD provides that at least 60 percent of the EBRD's investment activities must be in the private sector. In 2004, 86 percent of all signed projects were in the private sector.

Now, notwithstanding its relative lack of leverage, the EBRD actively uses its resources to address the burdens placed by corruption on the economies of the region. The Bank maintains an active policy dialog with the governments of its countries of operations. It publicizes the levels of corruption in each country by working with the World Bank on surveys, which assess the quality of the business environment in each of our countries of operations, and by focusing on that business environment, in our country's strategies—which are adopted every other year—and in which we focus on the level of corruption and on integrity concerns.

The EBRD also seeks to assist the creation of an investor friendly, transparent, and predictable legal environment through its legal transition program. In addition, the EBRD contributed to the establishment in 2003 of the Business Principles for Countering Bribery, and joined with the other multilateral development banks last December, on the anniversary of the U.N. Convention Against Corruption, and reaffirming their shared commitment to the fight against corruption.

In the context of its projects, the Bank requires covenants by all of its borrowers relating to compliance with applicable laws concerning financial crime and corruption, and the maintenance of associated records. Failure to comply with the anticorruption covenants is a material breach which will be penalized as vigorously as the breach of any financial covenant. Urged strongly by the

United States, the Audit Committee of the Board of Directors has been increasingly involved in the process of assessing the systems in place for ensuring compliance with those covenants. One result of this effort is now, the EBRD must inform the Board of any waiver of a material condition of a loan or equity investment agreement with the borrower or investee.

To promote good governance effectively in its countries of operation, the EBRD must make sure that its own operations are consistent with best practices, and we have seen progress on that front. In April of last year, the Board of Directors strengthened the Audit Committee with a revised Terms of Reference that formally established the Committee responsibilities with respect to the integrity of the EBRD's financial statements, the soundness of its internal controls, the status and performance of its internal functions of compliance, internal audit, project evaluation and risk management, and the independence, qualifications, and performance of the Bank's external auditor.

While the independence of the internal functions was materially enhanced by the new Audit Committee Terms of Reference, the question of full independence remains to be resolved. But on a positive note, the EBRD's President now supports independence of that evaluation function. Where the Bank's practices lag the other MDBs, we anticipate the Board will approve a change in 2005. We've had two meetings on that already, there will be a meeting this Friday, tomorrow.

In my September 20, 2004, letter to you, I wrote that the EBRD's existing code of conduct is outdated, and that we would work for the adoption of a new, revised version. The Board is now in the process of a new code, we anticipate its adoption in 2005.

The EBRD has a new Chief Compliance Officer who has considerable experience with FATF and anticorruption NGOs, and she has been engaged in integrating the compliance function into the every day work of the EBRD. We have proposed, and the Bank's President supports, increased involvement by the Chief Compliance Officer in project preparation process, and is committed to making the necessary resources available to the CCO.

My Office worked with other Directors to develop an integrity certification that is required in every project document that comes to the Board. The EBRD maintains their telephone hotline, and a compliance inbox on its Web site for the reporting of allegations of fraud, corruption, and misconduct in the Bank's activities, or in its projects. To inform the public of its findings, the EBRD management has approved, in principle, the publication of an anticorruption report, the first of which is expected to be published next fall, I have given copies directly to the President of the World Banks and the ADBs annual reports, and we would hope that we will have, using them as a guide, a better reporting than we have to date on those issues.

The CCO believes the EBRD has in place a viable whistleblower protection mechanism. She's made recommendations for improvements, and has posted whistleblower information on the EBRD's Internet and public Web sites. We've had meetings before the Audit Committee on this particular matter, and in the next few months

the Board, as a whole, will review the existing procedures, and will consider areas for improvement.

With respect to efforts to combat money laundering and the financing of terrorism, the EBRD has enhanced its integrity procedures by adding checks against the Office of Foreign Assets Control, and other U.S. Government lists as a part of its due diligence process, and EBRD now has mandatory training in this area for Bank staff, and has initiated training for bankers and regulators in its countries of operations.

Beginning in 2003, we urged the Bank to adopt a COSO system of internal controls. In May of last year, prior to the annual meeting, management agreed to do so and has subsequently delivered on its promise. The internal controls are in effect for the Bank's 2004 financial statements, and as a part of this project, the Bank has also completed an operational risk self-assessment exercise, and established a framework for the continued development of operational risk identification measure mitigation and management capacity. I should also note that reputational risk, Mr. Chairman, is part of the operational risk review and implementation, and finally, the Bank is in the process of hiring an operational risk manager.

The EBRD's public sector operations frequently involve the procurement of goods, civil works, and services by governmental entities. The EBRD, with the assistance of outside consultants, has developed training for new staff in the basic principles of public sector procurement. Last month, the EBRD also took additional steps to strengthen oversight of its public procurement through a greater involvement of the Chief Compliance Officer, and through expanded reviews.

Since my arrival, the U.S. Director's Office has made improvements in EBRD governance and anticorruption measures the top priority. In the past year we've seen progress, and we think there's a foundation in place for further progress this year. We intend to push for greater independence of the internal functions, increased resources to enable them to take on more responsibility, and a continued focus at all levels on integrity issues.

Mr. Chairman, our goal is, and has been, for the EBRD to have a corporate culture and environment that features enhanced corporate governance, internal controls and compliance, and that promotes good governance in its countries of operations. My office is committed to continuing our efforts to that end. Thank you, Mr. Chairman.

[The prepared statement of Hon. Sullivan follows:]

PREPARED STATEMENT OF MARK SULLIVAN III, U.S. EXECUTIVE DIRECTOR, EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT, LONDON, UNITED KINGDOM

Mr. Chairman, Ranking Member Biden, members of the committee, I welcome your invitation to appear before you today to report on the efforts of the European Bank for Reconstruction and Development ("EBRD") to combat corruption. I share your belief in the importance of combating corruption in the international development system and have made this issue a priority for the Office of the U.S. Executive Director at the EBRD.

The Under Secretary of the Treasury for International Affairs, John B. Taylor, testified before this committee on July 21, 2004, that the administration takes very seriously the fight against corruption and that we all have an obligation to help ensure that the multilateral development banks (MDBs) undertake effective

anticorruption efforts. The capital comes from the taxpayers of their shareholder countries, and those taxpayers are entitled to the assurance that the MDBs will use those moneys in an appropriate and efficient manner. As Under Secretary Taylor noted in his testimony, the U.S. Treasury and the U.S. Director's Office at the EBRD work together to promote anticorruption measures at the Bank. Our Office is committed to advancing integrity, anticorruption, and transparency efforts at the EBRD.

The EBRD's President, Jean Lemierre, sent a July 16, 2004, letter to the committee describing the EBRD's anticorruption initiatives. My September 20, 2004, letter to the chairman also described some of those efforts and reaffirmed our continuing support for the EBRD's efforts to combat corruption. My testimony today will touch upon matters referred to in my and President Lemierre's letters, focusing on what was accomplished in this important area in 2004 and what my Office is pursuing this year.

Our goal is, and has been, for the EBRD to have a corporate culture and environment that features enhanced corporate governance, internal controls, and compliance and that promotes good governance in its countries of operations. While there was progress toward that goal in 2004, it is clear that there is more that we and the EBRD can do.

THE EBRD'S OPERATIONS

The EBRD currently conducts its investment activities in 27 countries that formerly were either a part of the former Soviet Union or of the Soviet bloc. The Agreement Establishing the European Bank for Reconstruction and Development requires that it apply sound banking principles in all its operations, and the Bank makes no concessional loans. The agreement also requires that at least 60 percent of the EBRD's investment activities be in the private sector. Over the 14-year life of the Bank, 72 percent of its signed agreements for debt and equity financing have been in the private sector, and in 2004, the figure was 86 percent.

The EBRD's purpose is to foster the transition of its countries of operation toward open market oriented economies. Eight of the EBRD's countries have such economies and are now members of the European Union. An additional two countries with open market oriented economies are expected to join the EU in 2007, and a third country may join in 2008. Their histories, and those of the 16 other countries of operation have left all the EBRD's countries of operation with a challenge when it comes to addressing and dealing with corruption issues.

Unlike those MDBs that lend regularly to governments and that have the option of extending structural or sectoral adjustment loans, the EBRD does not have significant leverage with the governments of its countries of operation. In addition, some of the countries do not engage in sovereign borrowing at this time because of IMF assessments of debt sustainability. In other cases, the EBRD's financial operations have been restricted to private sector projects only as a result of the countries' lack of commitment to the economic and political principles set forth in the Agreement Establishing the European Bank for Reconstruction and Development. And, of course, there is the Bank's unique approach to transition through private sector investment which limits direct leverage with the governments of all of the EBRD's countries of operations.

EBRD Governance and Anticorruption Efforts at the Country Level

Notwithstanding its lack of leverage with the governments of its countries of operation relative to that of the other IFIs, the EBRD uses its resources to work with those governments to address the burdens placed by corruption on their economies and the transition process. It is the EBRD's view that corruption and fraud cripple progress and poison the investment climate and that a corrupted investment climate limits the effectiveness of the EBRD's private sector focus on transition. Consequently, the EBRD maintains an active policy dialog on the subject with the governments of its countries of operation and supports that dialog in a variety of ways.

One method of support comes from publicizing the levels of corruption in each country. The EBRD and the World Bank created the Business Environment and Enterprise Performance Survey ("BEEPS"), which is designed to generate comparative measurements of a range of interactions between business entities and the state including corruption political influence, and regulation. The initial BEEPS in 1999 interviewed 4,000 firms in 22 transition countries. By 2002, the number of firms interviewed was 6,000, and the BEEPS covered all of the EBRD's countries of operation other than Turkmenistan. In 2005, the EBRD and the World Bank will conduct a third round of BEEPS that will include interviews of 8,000 firms in all of the EBRD's countries of operation. This latest round is intended to focus on the poorest countries of operation. The results of the BEEPS can be found on the Web

sites of the EBRD and the World Bank. Following the two earlier reports, the EBRD analyzed the results in its annual Transition Report, which included a table on the frequency and extent of the "bribe tax" in each country of operation.

Additional focus on the problem of corruption resulted from the 2003 establishment of Business Principles for Countering Bribery. The EBRD, working with Transparency International and Social Accountability International, other NGOs, business groups and trade unions, led the effort to establish the Principles. On the anniversary of the United Nations Convention against Corruption in December of last year, the EBRD joined with the other MDBs in reaffirming their shared commitment to the fight against corruption in their respective operations and projects.

Every other year, the EBRD adopts a Country Strategy for each country of operation, which contains a business environment section that describes, among other things, the state of corruption and levels of governance. The EBRD posts each strategy on the Bank's Web site, and in 2004 had the strategies translated into the official native language of 14 countries of operation.

The EBRD continues to operate its Legal Transition Program, which addresses corruption and good governance issues and which seeks to assist the creation of an investor-friendly, transparent and predictable legal environment to improve the investment climate in the Bank's countries of operations. By advancing improvements in governance and regulatory frameworks, the EBRD helps its countries of operations to reduce the opportunities for corruption.

The EBRD developed and has conducted its Corporate Governance Sector Assessment Project since 1999. It assesses the quality of corporate governance legislation vis-a-vis the standards set by the OECD's Principles of Corporate Governance. The assessment is conducted every other year, and the Bank will conduct its third survey this year and will publish it in 2006. Country specific reports can be accessed from the EBRD's Web site. Good legislation is one thing, and implementation is another. Therefore, since 1995, the Bank has annually evaluated implementation of these laws in its Legal Indicator Survey. This information can be accessed on the Web site. The Legal Transition effort extends to a judicial capacity initiative in the early transition countries. This year there will be a focus on building judicial capacity in Georgia.

Program activities in 2004 included:

- Hosting a Legal Roundtable on Promoting Fair Competition during its April 2004 Annual Meeting. The roundtable stressed the importance of sound competition policies and institutions to facilitate transition to the market economy and attract foreign investment;
- Publication in April 2004 of the EBRD's annual report, Law in Transition, which focused on competition law and policy; and
- Publication in the autumn of 2004 of an online supplement to Law in Transition, LiT online, which focused on how to establish a favorable legal environment in the early transition countries in the region, namely Azerbaijan, Armenia, Georgia, Moldova, Kyrgyzstan, Tajikistan, and Uzbekistan.

THE EBRD'S INSTITUTIONAL GOVERNANCE

To promote good governance effectively in its countries of operation the EBRD must make sure that its own operations are consistent with best practices, and 2004 saw progress on the governance and anticorruption fronts. In April, the Board of Directors approved new terms of reference for the Audit Committee for the first time in a decade. The effect of this approach was to strengthen Audit Committee authority and responsibility. The United States took a leading role in the effort to modernize the terms of reference on the grounds that an unregulated institution using taxpayer dollars has a special responsibility to examine the state of its own governance measures on a regular basis in light of best private sector practices and to adopt those practices in the conduct of its own affairs.

The Audit Committee Terms of Reference formally set out for the first time a number of Committee responsibilities relating to:

- The integrity of the EBRD's financial statements and its accounting, financial reporting, and disclosure policies and practices;
- The soundness of its internal controls regarding finance and accounting measures and their effective implementation;
- The status and performance of the Bank's compliance, internal audit, project evaluation and risk management functions, and their ability to perform their duties independently; and
- The independence, qualifications, and performance of the Bank's external auditor.

Today, the Audit Committee has the explicit authority to take a range of actions with respect to the external auditors, from participation in the selection process and compensation to the scope of each year's proposed audit and the review of the accuracy and integrity of the Bank's financial statements and other key financial disclosures prior to their release. The Committee is to be a participant in the discussion and resolution of any disagreements between management and the external auditors. To date, none have arisen. The Terms of Reference formally codify the Committee's right to meet with the external auditor, the Internal Auditor, the Chief Compliance Officer ("CCO") and the Director of the Project Evaluation Department without management being present, and it has exercised that right on a regular basis.

The Audit Committee must periodically review and evaluate Internal Audit, Project Evaluation and the Chief Compliance Officer (collectively, along with Risk Management, the "Internal Functions") to assess whether: Their roles are appropriate for the Bank's purposes and needs; their policies, procedures, methodologies, budgets, and staffing resources are adequate for them to perform their roles; and they are performing to expectations. The Committee must be consulted prior to the engagement of the heads of the Internal Functions (except the head of Risk Management), and the Bank's President can remove them only in accordance with the guidance of the Board of Directors given in executive session.

INDEPENDENCE AND COORDINATION OF INTERNAL FUNCTIONS

While the independence of the Internal Functions has been enhanced by the new Audit Committee Terms of Reference, the question of actual independence remains to be fully resolved. This is especially the case of the EBRD's evaluation function where the Bank lags behind members of its peer group which have the function reporting diectly to directors who make the decisions as to hiring and removal and the function's budget. Then Deputy Secretary of the Treasury, Samuel W. Bodman, pointed out in his address to the Governors at the EBRD's 2004 annual meeting:

> The Bank's promotion of improved legal structures and good corporate governance contributes to improvements in the business environments of its countries of operation. It seems logical—and, we would argue, is required—that the EBRD itself should adhere to the highest standards of corporate governance. The EBRD, like other international financial institutions, is a steward of the taxes paid by the citizens of its members and, as such has significant and serious responsibilities to its shareholder nations.
>
> And so, we are pleased that the Bank has committed to establish a strong framework of internal controls and assessment procedures for the 2004 financial statements and beyond. This commitment will serve as a powerful example to other international financial institutions.
>
> Yet our work is not done. More progress is needed, particularly on the independence of key individuals and the improvement of transparency and disclosure policies.

My Office has been, and will continue to be, a strong proponent of the independence of the Internal Functions. The Bank's President now expresses support for independence of the evaluation function, and we anticipate the Board will approve a change in 2005. We, and other members of the Audit Committee, do not believe that management's initial proposals for guaranteeing the independence of the evaluation function are sufficient, and we will be working to improve the final product. We will continue to push this year, in the Audit Committee, for complete independence for the evaluation function and for further independence of the other Internal Functions.

Of course, having good policies and procedures in place is only the first step in a comprehensive corporate governance and anticorruption program. Coordination of the Internal Functions and making use of their individual activities are important. For example, the Internal Auditor reported to the Audit Committee that an examination of compliance by bankers with the Bank's integrity check requirements found failures to comply fully. That has led to a number of improvements which the United States has promoted and supported. These include development by the CCO of an integrity training program which is required for all directors, officers, and employees of the EBRD. I participated in the pilot program and in the final program as well. To date, virtually all employees, directors, and management have completed the "Integrity Matters" training course, which is mandatory for all new employees.

Code of Conduct

In my September 20, 2004, letter to you, I wrote that I, and my fellow Audit Committee members, believed that the EBRD's existing Code of Conduct was outdated and that we would work for adoption of a new, revised version. The Board is in the

process of considering a new Code of Conduct to replace the existing Code, which was adopted in 1991 and which has not been formally amended since. We anticipate adoption of a new Code of Conduct in 2005.

THE EBRD'S COMPLIANCE FUNCTION

The EBRD's Office of the Chief Compliance Officer ("OCCO") is charged with promoting good governance and ensuring that the highest standards of integrity are applied to all activities of the Bank in accordance with international best practice. It deals with conflicts of interest, corruption, confidentiality, and money laundering.

The EBRD did not have a compliance officer before 2000, and since then the Bank has had three CCOs and an Acting CCO. In June 2004, the Bank hired its third CCO after an extensive search lasting more than a year from the time the prior incumbent gave notice of his intention to leave the EBRD. Notwithstanding the Bank's initial record, there are grounds for optimism that the new CCO will build on the record of accomplishment of the predecessor Acting CCO and will establish an efficient and well run compliance function which is part of the EBRD's everyday operations. She has extensive experience in creating a compliance function at the OECD where she was head of the Anti-corruption Division and led the drafting and implementation of a mechanism to monitor an international treaty on corruption. She brings a long record of experience with the Financial Action Task Force, or FATF, and with anticorruption NGOs.

Since her arrival, the CCO has been engaged in bringing on board staff with which to meet the considerable demands on the Office in making the compliance function a part of the everyday work of the EBRD. The OCCO is now responsible not only for handling all matters related to fraud and corruption, but also for the functioning of the Bank's Independence Recourse Mechanism which enables individuals outside the Bank to submit complaints concerning individual projects. In assessing a complaint, the CCO can recommend a compliance review (i.e., has EBRD complied with certain policies) or a problem-solving initiative, or both or neither. Since it was launched in mid-2004, there has been only one complaint submitted, and the CCO determined that it was not covered by the IRM procedures.

At the moment, the CCO reviews some, but not all, projects presented to the Board. This review includes checking the integrity of the beneficial owners, promoting more transparent ownership structures, and reviewing corporate governance standards and practices. We have been promoting further CCO participation in the project approval process to address any integrity concerns with the persons or entities involved in projects. At a recent Board meeting, the President supported increased involvement by the CCO in the project preparation process. This will require additional resources, and there is general support within the Audit Committee—the terms of reference of which require it to review the adequacy of resources for the Internal Functions—for greater involvement and for providing the necessary additional resources to the CCO. Our Office will continue to push for that involvement in every project that is submitted to the Board for its consideration and will support providing the additional resources necessary for that complete involvement to be effective. The Bank's President has committed to us that he will make the necessary resources available to the CCO, and this commitment was reiterated by the management before the full Board when it considered the 2005 budget. The Audit Committee will receive a status report from the CCO in May and will review the adequacy of OCCO's resources.

Given our concern that each proposed project should have undergone a thorough integrity review prior to its submission to the Board and our belief in the importance of accountability, we developed an integrity certification and worked successfully with other shareholder offices to require the inclusion of the certification in all project documents. It says: "all actions required by applicable EBRD procedures relevant to the prevention of money laundering, terrorist financing, and other integrity issues have been taken with respect to the project, and the project files contain the integrity checklists and other required documentation which have been properly and accurately completed to proceed with the project." The CCO has determined that intentionally misleading the Board constitutes misconduct, and a false certification certainly should have consequences for those responsible.

We have urged the Bank management to compile and publish an annual anticorruption report and have provided them with copies of the reports of the Asian Development Bank and the World Bank. We have requested that statistical summaries and case studies of fraud and corruption cases pursued by the Bank's investigations unit be part of any such report. EBRD Management has approved in principle the production and publication of an anticorruption report, and the CCO is currently putting together an internal working group which will meet to consider the

report's scope and format. The first EBRD anticorruption report is now scheduled to be published in late fall. Our goal in 2005 is to have clear and comprehensive reporting of the Bank's anticorruption efforts which is easily available to the public.

More broadly, we do not believe that the EBRD's public disclosure practices meet the test of best practices for MDBs. We voted against the Public Information Policy in 2003 for that reason and we continue to press for more information to be made public on a timely basis. For example, we consistently argue that the Country Strategy Development process would be enhanced by making drafts available for public comment and that summaries of minutes of Board meetings should be made public as well. (U.S. votes on projects are made available on the U.S. Treasury Web site.) Our support for enhanced public disclosure is not shared by all directors, and we will likely not be able to effect material improvements until 2006 when the next scheduled review will take place.

In sum, while important work remains, the requirement for inclusion of the integrity certification, directors' support for the new CCO and discussion of integrity matters in Board and Audit Committee meetings evidence an increased Board interest in integrity issues.

ALLEGATIONS OF FRAUD AND CORRUPTION WHISTLEBLOWER PROTECTIONS

The EBRD maintains a telephone hotline for reporting of allegations of fraud, corruption, or other misconduct in Bank activities or projects. An independent contractor operates the hotline. Access to the hotline is toll free, and use is confidential. All matters reported to the hotline are referred to OCCO for followup and investigation. The EBRD's Web site sets out detailed information about the hotline and compliance issues at the Bank, including the access codes for toll-free reporting on a country-by-country basis. Collect calls can be made from most of the EBRD's countries of operations. The EBRD keeps statistical records of the use of the hotline. The contractor provides monthly reports on the use of the hotline. The EBRD's Compliance In-Box, which can be accessed through the EBRD's Web site, appears to be the preferred method of making fraud and corruption allegations. In 2004, there were no reports of corruption or misconduct to the hotline; however, the In-Box receives about one complaint per month relating to internal staff misconduct or to procurement.

The EBRD has a whistleblower protection mechanism, which is based upon three separate, but inter-related, procedures. EBRD employees have a duty to report suspected misconduct to the CCO, and it is the CCO's responsibility to assess if such allegations warrant further investigation. If an investigation into an allegation is warranted, the CCO commences a fact-finding inquiry and upon its conclusion, makes a recommendation to the Vice President for Human Resources as to whether a formal accusation of misconduct should be raised. While EBRD makes every effort to protect the identity of a whistleblower, it does not guarantee anonymity because disclosure may, in some cases, be required in order to proceed with an investigation. Whistleblowers are protected against retaliation and the CCO will respond to any employee who acts to retaliate against a whistleblower, which has not been needed so far. In addition, a whistleblower can pursue an independent course of action via the EBRD's Administrative Tribunal.

The Board recently met with the CCO to discuss the Bank's whistleblower protections. The CCO stated that EBRD has in place a viable whistleblowing protection mechanism. Nevertheless, the CCO has made recommendations for improvements. The CCO has recommended that EBRD should be more proactive in making employees aware of their reporting duties and protections. EBRD has posted a whistleblower statement with questions and answers on the Intranet with links to the three relevant procedures and on the Internet. The CCO's view, which we support, is that the whistleblower mechanism is evolutionary and should be kept under review to ensure it meets best practice. In the next few months, the Bank will also review the procedures that form the whistleblower mechanism. At that time we will consider areas for improvement.

ANTIMONEY LAUNDERING AND ANTITERRORIST FINANCING EFFORTS

The EBRD applies measures for combating terrorist financing in both its public and private sector operations. These measures are based on detailed due diligence procedures and internal training programs. In addition, the EBRD promotes more effective antimoney laundering and antiterrorist finance practices with both the banks and national authorities in the Bank's countries of operation.

The EBRD has "know your customer" procedures, and the responsibility for their implementation falls on the Operation Team for each of the Bank's investment projects. Operation Teams must perform extensive due diligence on the integrity of

all prospective clients. Integrity checks undertaken before committing any funds include verification that no client, or prospective client, is on the United Nations Security Council lists of entities and individuals suspected of supporting terrorist activities. The use of the Office of Foreign Assets Control (OFAC) list is a required part of the due diligence process, and the CCO has worked with EBRD's Banking and Risk Management division to revise the current procedures in order to ensure that several important lists, including OFAC's and those of other U.S. Government agencies, are included as part of the due diligence process.

Because operations with financial institutions pose additional risk, the Bank requires additional due diligence before proceeding with a financial institutions project. Procedures for financial institutions include an Anti-Money Laundering Red Flag Checklist to assist the Bank's team to properly assess the client's antimoney laundering policies and procedures, including counterterrorist financing activities. Key requirements, such as know your customer, staff training, reporting suspicious transactions, recordkeeping, and the role of the antimoney laundering compliance officer, should be in place and properly implemented by the prospective client before any disbursement. The nature of the specific requirements for a given client is tailored to reflect the perceived risks. Some requirements (e.g., training for all staff members) could be fully achieved at a later stage of project implementation, such as during the disbursement phase, if that would not materially affect the soundness of the client's overall antimoney laundering framework.

Moreover, to address the specific risks emerging in the Bank's financial institutions portfolio of operations, the Bank's standard loan agreement includes an affirmative covenant committing the borrower to institute measures to prevent money laundering/terrorist financing when using EBRD funds. After the borrower signs this certification potential money laundering/financing terrorism risks are assessed by the EBRD at each periodic project review. The Bank typically conducts project reviews at least semiannually and does so more frequently if a project is on the EBRD's watch list.

Where there remain unanswered questions after completion of the EBRD's standard due diligence procedures, the Bank has four investigative firms on retainer under a framework agreement to conduct additional investigations. The decision to use an outside firm can be initiated by the Credit/Transaction Risk Unit in the Risk Management Vice Presidency, the OCCO, or the Banking Department, which can use their services not only for AML/ATF purposes, but whenever there are integrity or reputational risk concerns. In 2004, the Bank commissioned 67 investigations. In exceptional circumstances where an investigative firm, which is not a party to the framework agreement, has special expertise or knowledge, the Bank can retain the services of that firm.

The EBRD provides antimoney laundering/counterterrorist financing (AML/ATF) training for staff as well as for the banks with which it does business and governmental authorities. In the past, the Bank's Risk Management section regularly organized AML/ATF seminars for staff and conducted three seminars in 2004. Responsibility for this education effort now lies with the CCO, and during 2005, participation in a new AML/ATF training course will be compulsory for all the staff members involved in the development of projects.

The EBRD seeks to improve AML/ATF procedures in its countries of operation through engagement with banks and the national authorities. The EBRD has two primary objectives. First, the EBRD wants the authorities to impose realistic obligations on banks instead of extensive reporting requirements with no followup of the suspicious transactions reported. Second, it wants bank managements to commit their organizations to actively pursue AML/ATF measures rather than passively comply with government regulations.

In late 2003, the EBRD organized three pilot seminars in Kazakhstan, Macedonia, and Bosnia-Herzegovina to promote better understanding of sound AML and ATF procedures. These seminars indicated that training is needed to nurture an almost nonexistent communication channel between banks and AML/ATF authorities and to provide them with the benefit of lessons learned from Western banks and financial intelligence units.

Following the pilot seminars, the EBRD has designed, with EU and Swiss Government support and financing, a €1 million training initiative to raise awareness of the importance of a proper AML/ATF legal framework at the political level and to help banks to design, review, and improve their policies. The training, involving experts from large Western banks known for their proactive work on AML/ATF, will take place in the region to ensure that the people responsible for AML policies in the banks can attend. The CCO expects to roll out seminars by July 2005 and will focus on the poorer countries of operation, where practices are least developed. Attendance at the seminars will not be confined to EBRD clients.

ADOPTION OF A COSO SYSTEM OF INTERNAL CONTROLS

Beginning in 2003, we urged the Bank to adopt a COSO system [1] of internal controls over its financial reporting. In May of last year, management agreed to do so and committed that the internal controls would be in effect for the preparation and publication of the Bank's financial statements for 2004. At the May 2004 annual meeting, Deputy Secretary Bodman acknowledged management's commitment and said:

> . . . we are pleased that the Bank has committed to establish a strong framework of internal controls and assessment procedures for the 2004 financial statements and beyond. This commitment will serve as a powerful example to other international financial institutions.

Bank management delivered on its commitment. It identified and tested 847 financial controls. This process, in which both the Bank's internal and external auditors were involved, required many hours of staff and management time, and the EBRD incurred substantial costs.

The EBRD completed successfully the testing of its financial controls, and its 2004 financial statements, which have been approved by the Board, contain a Management statement signed by the President and the Vice President, Finance, and audited by the Bank's external auditors, PricewaterhouseCoopers, confirming that the Bank maintained effective internal controls over its financial reporting as contained in the Annual Financial Report for 2004. This is the first time the Bank has included such a statement in its Financial Report, and the EBRD is one of the first organizations to do so outside the United States where this assertion is mandatory for listed companies.

As part of the COSO project, the Bank also completed an operational risk self-assessment exercise and established a framework for continued development of an operational risk identification, measurement, mitigation, and management capacity. Management, which expresses a low tolerance for operational risk, refined key risk indicators and identified 239 controls for dealing with operational risk. These controls address a variety of risks, including reputational risk. The Bank is in the process of hiring an operational risk manager. Starting this year, Management will provide the Board with quarterly reports on the Bank's exposure to credit, market, and operational risk.

Management has expressed confidence that the COSO system of internal controls is a sustainable part of the culture of the EBRD. It believes that the certification process relating to financial controls is now entrenched, and the operational risk management process is well underway. To maintain intra-Bank co-ordination and facilitation and to ensure maintenance of focus and continuity, management has established a COSO and Operational Risk Management Unit. This unit reports to the Vice President, Finance, with respect to internal financial controls certification and to the Vice President, Risk Management, with respect to the operational risk management process. On a day-to-day basis, the unit will work with the Controller and the Director of Risk Management. Moreover, the Certification of Internal Financial Controls Steering Committee, which was formed to oversee the process of adopting and implementing the new controls system, will continue its function and meet several times a year to provide supervision over the certification process, while the Operational Risk Management Group will continue its role of providing supervision over the operational risk management process.

PROCUREMENT

The EBRD's public sector operations frequently involve procurement of goods, civil works, and services by governmental entities. In 2004, the EBRD's public sector borrowers signed 157 procurement contracts with an aggregate contract value of €681 million. EBRD financing of these contracts was €559 million. The number of contracts signed by borrowers and the aggregate volume represented declines of 13.3 percent and 22.5 percent respectively from 2003. In 2004, 77.7 percent of all contracts and 96.6 percent of total contract value was procured by open tendering.

The foregoing figures do not include contracts for consultancy services. The Bank's Consultancy Services Unit ("CSU") administers. the majority of these contracts. The Office of the General Counsel, the Turn Around Management Group, and the Nuclear Safety Department all have the authority to retain consultants directly. The total value of the 1,620 consultancy contracts issued by the EBRD in 2004 was

[1] COSO (Committee of Sponsoring Organizations of the Treadway Commission) is a voluntary private sector organization dedicated to improving the quality of financial reporting through business ethics, effective internal controls, and corporate governance.

€118.76 million. This represented an 8.25-percent increase in value and 1.0 percent increase in number over 2003. CSU issued 730 contracts with an aggregate value of €65.91 million, and 78.04 percent of these contracts in terms of the value were awarded following competitive selection procedures.

In connection with the adoption of the COSO system of internal controls, the CSU reviewed its controls and procedures with the Bank's external consultants and the in-house team. CSU's controls and processes were considered to be appropriate and the audit trail relating to its compliance functions sufficient to demonstrate the proper application of the necessary processes and approvals.

The EBRD, with the assistance of an outside consultant, has developed a course for new staff that provides them with training in the basic principles of public sector procurement. The course was finalized in 2004, and one seminar was held. Additional courses will be held in 2005 for all professionals who have been working at the EBRD for at least 6 months.

During 2004, the EBRD retained the services of an independent procurement consultant to review three completed projects to assess whether the procurement, contracting, and implementation processes, which had been followed, were consistent with the corresponding loan agreements and whether the principles of economy and efficiency, transparency, and accountability as stated in the Bank's Procurement Policies and Rules ("PP&R") were satisfied. The report has been delivered, and the EBRD is assessing which recommendations for followup action can be implemented this year.

The EBRD's Procurement and Technical Support Unit is charged with reviewing all proposed contracts above specified levels as an integrity check before the EBRD's Banking Department registers its "no objection" to a proposed contract. Last year, 38 percent of the contracts subject to the selective review process were sent back for completion, clarification, or improvement before a "no objection" could be provided. This represents a reduction from the percentage sent back in 2003, which was 45 percent.

The EBRD addresses the problem of potential fraud and corruption in these procurements by following the procedures set out in its PP&R. The EBRD has established its Procurement and Contracting Committee ("PCC") to review all allegations of fraud and/or corruption in the context of the procurement process or when the Bank receives procurement-related complaints. If the PCC concludes that the allegations are substantiated, it refers the case, together with its recommendation, for appropriate measures (e.g., barring firms or individuals from future participation in the procurement for EBRD-financed contracts). With respect to firms or individuals, the EBRD will reject a proposal for an award to such firm or individual and will declare him or it ineligible, either indefinitely or for a stated period of time, to be awarded a Bank-financed project. In the event that a representative of a client or a beneficiary of the Bank's financing has engaged in fraud or corruption, the Bank will cancel the portion of the Bank's financing allocated to the contract in question.

The Bank does not limit its actions to its own funded projects, but has the ability to "cross bar" where a client has been found, by a judicial process in an EBRD country of operation or other official enquiry, to have engaged in corrupt or fraudulent practices. This would include enquiries conducted by another MDB. EBRD policy would require the names of firms or individuals that are debarred to be published on the Bank's Web site. To date the World Bank is the only other IFI that requires that names of sanctioned firms and individuals be made public. The EBRD receives, on a strictly confidential basis, the ADB list of debarred firms. The EBRD examines both the World Bank and ADB lists to determine whether any firms or individuals to which the Bank is considering providing financing, or that it may be transacting business, with are on the lists.

There were 16 procurement complaints concerning EBRD financed or administered contracts in 2004 as compared with 24 in 2003 and 14 in 2002. The Bank did not uphold any of the complaints in 2004, but did so for three complaints in 2003 and two in 2002. Three of last year's complaints came through the EBRD's Compliance In-Box and alleged fraud and corruption. The OCCO referred them to the PCC, but no evidence substantiating the allegations was found. The CSU received one procurement complaint in 2004, and after review by the PCC, the complaint was not upheld.

We understand that all allegations of corruption and fraud have been investigated according to the Bank's procedures, but these investigations have not resulted in debarment of any firm or individual or the cancellation of financing in recent years.

We recently questioned why the EBRD has never debarred a firm or individual when the World Bank, the Asian Development Bank, and the African Development Bank have. In response to the foregoing question, Bank staff outlined plans for 2005 to strengthen oversight of public procurement, including a greater emphasis on up-

front work to improve fiduciary compliance and increased due diligence and monitoring during contract implementation. Bank management is sensitive to the fact that there have been no substantiated cases of procurement-related fraud or corruption in EBRD-financed public procurements in recent years. This sensitivity follows naturally from the EBRD's awareness, that many of its projects are implemented in a high-risk environment for fraud and corruption.

In March 2005, EBRD took additional steps to strengthen oversight of public procurement. The PCC's membership was expanded to include the CCO and the Head of COSO and Operational Risk, and the chair of the PCC will be the Deputy General Counsel to reduce any perception of potential conflict of interest. In addition, the PCC's terms of reference were amended to transfer the responsibility for investigating allegations concerning fraud and corruption to the CCO from the Director, Procurement and Purchasing Department. The process of independent procurement reviews will be expanded in 2005. Because the EBRD recognizes that ensuring a fair and transparent procurement award process is insufficient to prevent corruption that can occur in the implementation phase, it will engage in more proactive monitoring with early identification of possible implementation red flags.

The EBRD expresses confidence that its ex-ante approval process at various stages of the tendering process is conducive to a fair and transparent contract award process. Furthermore, tenderers can and do avail themselves of the Bank's complaint procedure as stipulated in its PP&R. Third parties can use the hotline or Compliance In-Box to flag possible problematic cases. There have been relatively few allegations that have been brought to the attention of the EBRD.

Standard Contractual Provisions

The Bank imposes a number of financial covenants on its borrowers. For example, banks to which the EBRD makes loans must comply with an affirmative covenant to "institute and maintain internal procedures satisfactory to the Bank for the purpose of preventing the Borrower from becoming an instrument for money laundering, terrorism financing, fraud or other corrupt or illegal purposes." Similarly, nonbank borrowers must represent and warrant that they are "in compliance with all applicable laws concerning money laundering" and that neither they nor any of their officers, directors or authorized employees, agents or representatives has (i) paid, promised to pay or offered to pay, or authorized the payment of, any commission, bribe, payoff, or kickback related to the project that violates any applicable law or entered into any agreement pursuant to which any such commission, bribe, payoff, or kickback may, or will, at any time be paid; or (ii) offered or given any thing of value to influence the action of a public official, or threatened injury to person, property, or reputation, in connection with the project in order to obtain or retain business or other improper advantage in the conduct of business. At each loan drawdown or interest rate rollover period, each borrower must report that it continues to be in compliance with its covenants.

As a matter of routine, borrowers must maintain procedures, records, and accounts adequate to reflect, in accordance with internationally accepted accounting standards consistently applied, the operations, resources, and expenditures relating to EBRD-financed projects. In addition, private sector borrowers must have audited financial statements prepared in accordance with internationally accepted auditing principles and standards. Typically, the Bank requires borrowers to authorize their auditors to communicate directly with the EBRD at any time concerning their account and operations.

The Bank's Operations Administration Unit, which is a part of the EBRD's Finance Vice Presidency, monitors compliance with material loan conditions including covenants. Failure to comply can lead to acceleration of the loan. Bank management confirmed to the Board that failure to comply with the Bank's anticorruption covenants is a material breach which will be enforced as vigorously as the breach of a financial covenant. Urged strongly by the United States, the Audit Committee has been increasingly interested in the process of assessing the systems in place for ensuring compliance with these legal covenants. As a result, the EBRD now must inform the Board of the issuance of any waivers of material conditions. The Audit Committee has directed the Project Evaluation Department to report on the use of waivers, and this report is due to be delivered in 2005.

CONCLUSION

Since my arrival in 2002, the U.S. Director's Office has made improvements in EBRD governance and anticorruption measures a priority. Last year saw progress, and there is a foundation for further progress this year. We intend to push for greater independence of the Internal Functions, increased resources to enable them to take on more responsibility, and a continued focus at all levels on integrity issues.

Mr. Chairman, as noted earlier in my testimony, our goal is, and has been, for the EBRD to have a corporate culture and environment that features enhanced corporate governance, internal controls, and compliance and that promotes good governance in its countries of operations. My Office is committed to continuing our efforts to that end.

The CHAIRMAN. Well, thank you very much, Mr. Sullivan, for your testimony.

I'd like to ask you, Ambassador Speltz, to give a mental image of what your headquarters looks like. It is located in Manila, in the Philippines. Is it a separate building, and how many persons are employed in the whole operation? In other words, how large of a situation, physically, is this?

Mr. SPELTZ. Thank you, Mr. Chairman, and as you and I have talked in the past, I certainly do welcome you to come visit us sometime, out there in Manila, if you're in Asia.

First of all, I'd like to state why the Asian Development Bank is in Manila; a lot of people ask that. In 1967, when the Bank was set up under the period of time under President Lyndon Johnson and the United Nations. Many of us, who are in this room, remember that the Philippines was the center of economic growth in Asia after Japan. Hong Kong was a British colony; China was closed; Vietnam was a war; Singapore was just starting; Korea was just beginning. Two other countries applied—one was Iran—for headquarters, we won't go into that, and Japan. So, the selection of Manila took place.

I'd like to also state that the reason it's still there today, people say "Why is that Bank still in Manila?" Yes, the Bank could be moved, but in fact, I think there's a reality check, you know, the Asian Development Bank, as all these banks, with your support, are really valuable institutions, if they're doing their job right, if they're helping to eliminate poverty and build sustainable growth. And nowadays, very sadly, the ADB is right smack in the middle of one of the poorest cities in the poorest countries in the area. So, when I'm in my Office, I look out the window, Jay Branegan has seen it, you look out the window, and there's a lot of poverty outside the window.

The building itself on any particular day, an average of maybe 4,000 people a day go in and out. We're certainly not as big as the World Bank, but it's a pretty good size, and that includes staff, professional staffing, I believe, of over 800, and the local staff and many consultants, but on an average, about 4,000 a day move in and out.

We are in two tied-together buildings, similar in fashion, I think if you could, to the World Bank, on a smaller scale, with the IMF across the street. We have offices, regional representation offices around the Asian area, so that is the physical structure of it. The Board members are housed all upstairs on one floor, which I think they do in all of these multilateral development banks. I'm not sure whether that's to keep us out of the main fire, or whatever, but anyways, we're all up there together. I think an interesting aspect of that, Mr. Chairman, is that we all have the same offices, same furniture, same everything, which is pretty good, because it keeps us on an equal basis when we're trying to work with our fellow countries, which is so important in coalition building.

The CHAIRMAN. How many countries are there on this floor?

Mr. SPELTZ. Today—I'm always trying to keep track—there are 63 country members, and of the 63 there are 12 Board members. And of the 12 Board members, only China, the United States, and Japan represent only our constituents. So, the remaining nine Board members have the responsibility—some on a fixed basis, and some on a rotation basis, of representing the other 59 or 60 countries. The Asian Development Bank, in many regards, is a misnomer, because it really covers everything—as you know—from the Pacific all the way through to Afghanistan, and my overlap with Mark with the EBRD and Khazistan, and then the nonregional members, which are all of the European countries and Canada, and other areas of that nature.

The CHAIRMAN. Right. Thank you very much for that important history, as well as the physical description. Those who are working with us in this hearing may have that same impression that I do, vividly, from what you have mentioned.

Let me just say that last year the committee was informed that development projects in the Philippines supported by the Asian Development Bank had a low success rate. When asked about that report, Mr. Roberto Tan, Assistant Secretary of Finance, responded, "The low performance can be attributed to a number of implementation problems, including poor contract award performance, cost overruns, and delayed provision of counterpart funds." The logical question I have for you, Ambassador Speltz is, What is your assessment of the low success rates of ADB development projects in the Philippines?

Mr. SPELTZ. Well, it appears that your staff and I have also been reading the newspapers last night; I saw the Manila Times late last night. The Philippines is a very difficult situation. Without getting into all of the details of it here, because it's a political matter of some sensitivity, when I first came in to the Philippines I believe it was close to $2 billion in undisbursed loans, of which the Philippines was paying a small fee for these undisbursed loans. I wanted to know why. What was happening? And we took it upon ourselves in our office to begin to activate that question of why? What's going wrong? And over the next year, including very much the involvement of the President of the Philippines, Gloria Arroyo, we began delving into this and found out that, for a variety of reasons, including lack of disbursal of third-party funds by the Philippine Government, sometimes concerns about potential free flow of the appropriate funds, whether or not there was potential corruption or not, concerns that that might happen, but essentially that many things were not in place. And, we advised, up to the President, that they take a look at canceling some of these loans, taking them off the books, some of them were 10 years old, and rebuilding them, restructuring them. And to the credit of the Bank, the Bank worked very carefully with the administration of the Philippines, and cancelled, I believe, almost a billion dollars in loans. And then have been re-structuring.

I noticed in yesterday's paper, Manila Times, last night's paper, that a comment had come out about this. But in that same article, it was not criticizing the ADB, it did state that it was working with the ADB and trying to restructure these loans. It really, much of this, Mr. Chairman, honestly is in the hands of the Philippine Gov-

ernment. The Philippine Government must take certain steps in order to help us help them.

The CHAIRMAN. Give me some indication. Procedurally you say $2 billion of loans were in the hands of the Philippine Government. The Board of Directors of ADB, at some point in history, loaned the Philippine Government the $2 billion? Or, what was the nature of the transaction? How did the $2 billion come into play?

Mr. SPELTZ. No, first of all, let me make it clear, Mr. Chairman, the Philippines don't have $2 billion in their bank account, ADB had the $2 billion in the bank account. ADB does not disburse funds if they feel there is a program that is not going to go ahead on the structure that we've set up, so the cash is in our bank. Number two, with regard to the $2 billion, that was made up of many different loans. And almost every one of them was project loans. It was cleaning up Pasak River, it was cleaning up environmental issues, it was working on airports in Mindanao, and some of those areas, especially in Mindanao, due to the terrorist activities down there, the Bank and the Philippines could not go forward with because of danger. So, I would say, and I can come back to you on this, but clearly, much more than 80 percent of that was specific project loans which we just did not disburse.

The CHAIRMAN. So some governmental units are in the Philippines. You have mentioned, say, Mindanao. The Bank initially then, put—at least a hold—on those funds in your vault. They remain there, but the idea was that although you had committed to move forward, you haven't disbursed the funds, apparently because, essentially whoever was wanting to do this decided they couldn't do it right now. Administration was just inadequate. I'm just trying to probe all of these projects. Who mentioned them? And why did the Bank say, "That's a good idea, we ought to go ahead with it"?

Mr. SPELTZ. Your questions are excellent, sir. When I got into the Bank, of course, my whole education started. One of the things, of course, that I discovered is that there were many difficulties of reform which we felt were needed, and we pushed forward on it. And I'm pleased today that many other constituents in other countries are working with us on reform.

But I was also pleased to see that there was actually a great number of hard-working, good people in that Bank who were, in their own way, working on trying to protect the Bank, to protect the moneys going out, and I was thunderstruck at the amount of money that had been committed in loans, but not disbursed. And I started diving into this; why? Why was this money not disbursed? And the overriding reason was that those countries had not met the regulations of the Bank—before I got in—the regulations of the Bank in meeting the qualifications which were necessary to proceed with the implementation of the loans, or we stopped. In certain cases, we began a project, and we stopped. I thought that was bad news that the money hadn't been disbursed, but I thought it was good news that the checks and balances were in place to stop the money going out.

Then I wanted to take it to the next step—don't ignore it, start working on it—to try to figure out how to either cancel those loans, or reactivate them and get them out to the people.

The CHAIRMAN. And as you just mentioned in that second examination, you've cancelled about half of the money, $1 billion of the $2 billion or so, so that those loans are not out there. And so in play are something less than a billion dollars, apparently, at this point. Is that right?

Mr. SPELTZ. It went actually down, I believe, to less than a half of a billion.

The CHAIRMAN. Half a billion.

Mr. SPELTZ. And if I recall, and perhaps your staff can help here, too, if I recall the statements in this morning, late last night's Manila Times, a representative from the Philippine Government acknowledged the fact that they were restructuring these loans, so that is what's going on.

The CHAIRMAN. Good. I appreciate those responses, although Manila is far away from Washington. Today you are here and others are there. I would just observe that papers in other countries, such as The Manila Times, have been interested in our hearings, interested in your responses and your appearance before this committee. I am grateful that is so, because this has brought a sensitivity in the international community on these problems that may be helpful to an administrator such as yourself.

Mr. SPELTZ. Mr. Chairman, if I may, just in closing on this, if you'll permit it. I think it's important also, as the Senate Foreign Relations, that the President of the Philippines, I've met with her on many occasions, and she personally has taken this into her own area of concern. She particularly is interested in education, in the education problems, and the water problems, and the environmental problems in her nation, and she was also very concerned and upset when she found out some of the bureaucratic holes that were not permitting this money to get to her people. And she's been working very well, not with me, but with the staff at the Bank, to work on this.

The CHAIRMAN. I appreciate that. Let me just say, anecdotally that 20 years ago, 1985, in this committee, we were hearing testimony from the then much younger Rich Armitage and Paul Wolfowitz, with regards to the Philippines. Their testimony was riveting. The committee was besieged with dilemmas about the governance of the country. Without belaboring the history, the fact is that the deliberations of our committee, in part, led to an appearance on national television of President Marcos calling for a snap election on an American Sunday news program, and calling for the world to witness that he did have authority and that he would be elected. And from that, a number of things followed. I especially appreciate your management of the situation, and your working with President Arroyo.

Mr. SPELTZ. Two other comments, with your permission. First of all, I don't think President Arroyo would really appreciate me very much if she called for a snap election tomorrow, and number two, I do want to stress very much that Ambassador Richard Downey, the United States Ambassador to the Philippines is, number one, a very close personal friend of mine, but he and his staff have also worked with us intimately with these problems with the Government of the Philippines, and I very much appreciate that support by him and the State Department.

The CHAIRMAN. Well, I'm pleased to learn of that relationship. I am not surprised. I commend that support of the Philippines and that close relationship. At the end of the day, we're hopeful—and that was the purpose of the question originally—to inquire if there will be constructive loans and a higher success rate, and if there would be movement by the government, as well as the rigor that you have imposed with the banking regulations.

Let me ask one more question dealing with the metrics of the situation. Since the regional development banks, particularly the Asian Development Bank, began implementing anticorruption practices, has there been a reduction in corrupt activities? Is there any way to measure declines or increases in corruption? This is pertaining to the whole portfolio, all of the countries, and a very general assessment, but I just want to get some idea as to how things are proceeding, or how you're able to measure how they're proceeding.

Mr. SPELTZ. I assume you're asking me, sir?

The CHAIRMAN. Yes.

Mr. SPELTZ. That's hard to measure, and I'd like to answer this in parts. I really believe in my heart that the efforts that your committee and also many Members of Congress, the Hill, the Senate, on both sides, have taken in meeting with me, and the Asian Development Bank, with my colleague Mark, with Bob Holland, World Bank, his predecessor and so on, I think sends a very strong message to those who might consider being involved in what we clearly call corruption, that they don't necessarily call corruption in their own minds. It gives them pause to consider that those days have changed. That's, I think, very, very important. I think the trends of the banks in general, and I won't speak for Mark's bank here, but I feel it's the same way on anticorruption is good, what is needed now is more restraints, more measures to carry forward on that, and specifically, I had a couple of things I had that I wanted to bring up to that.

It's impossible to measure the amount of corruption that's been out there in the past. I've seen testimony by Mr. Rich and others, who, I think, are well meaning, in some cases, I believe out of date. But, the fact is, there is, has been, corruption in the past, but I want to take the positive side of it. One of the things that we're dealing with, one of the problems we're dealing with, is that many of the countries that we work with, in the Asian Development Bank, do not have control systems in place for combating corruption, because it's not that important to them. And if you don't have a control system in place, then it becomes under the decision of an individual as to what that individual is going to do. What ADB is trying to do, and I applaud them, they are really working at this very, very difficult problem, is to work on the education, from my opinion, grassroots up. Not the top down, grassroots up. The education of the negative effects of corruption, and the fact that those very people who need it most are the ones that aren't getting the money. They are the ones that are getting hurt the worst. And so, we're working with them on educating them, we're working through technical assistance programs, we're working with government officials, and yes, many of these governments are trying to work with us in setting up these control systems. Checks and bal-

ances on corruption, and we're trying to show them how to implement them.

And then, most importantly, they know that we don't disburse the funds, a very good point that you brought up, sir, that if we are not satisfied at the Bank that things are not in place, we simply don't disburse the funds. So, I would say that, at this time, without knowing anything about the amounts of money or anything else, the trend has changed, there is very significant action being taken place, and I think the efforts are generally there, by many countries to try to clear this up.

The CHAIRMAN. I appreciate that testimony, and I appreciate the questions and possible answers about specifics year by year. The trend, I think, has clearly changed, and it's in part because of officers like yourself who have made that change. I would say, without being hypercritical of anyone, as we began these hearings, that there was a certain amount of skepticism as to why we were even involved at all in these issues. Essentially, it was a challenge of authority, or the fact that we had some oversight capacity. It was just that members don't get into this type of thing, and banks take care of the situations. In part, for a moment or two, we even had with our own Treasury Department, a feeling that, after all, they simply don't offer testimony to committees like this, and that they have their own procedures. Now, in fairness, they have changed, and they're constructive, and they have been helpful. That has been true of the World Bank, and that's been true of others that may have had some skepticism at the outside, because they understand—perhaps informed by another investigation that our committee commenced, being the very, very tragic Oil-for-Food Program, at the United Nations—that the whole credibility of institutions, and the officers, may come into question when something is escaping oversight of anyone.

And, so I would simply say that we want to have strength in the banks. We want to have confidence in the American people, before we offer the reauthorization legislation. We want to make sure to them that we can try to say that some due diligence has been exercised on our part, as well as on yours, and to give you an opportunity to testify to that effect.

Mr. SPELTZ. Thank you.

The CHAIRMAN. Let me ask you, Mr. Sullivan, as a general question, do the regional development banks adequately share information among themselves, and with the World Bank, about firms and individuals that have been sanctioned for corrupt violations? In other words, are there lists of firms or individuals that are made public at the regional development banks as they are at the World Bank?

Mr. SULLIVAN. My understanding is that there are other lists to which the EBRD has access, the Asian Development Banks, the others I do not believe are public. We do look at those lists, and I would like to say, generally on the matter of procurement, that's been a subject of Audit Committee interest in recent weeks; we had a meeting on the 21st of March, we will have another. What is clear to me is that there is an increased effort to deal with procurement issues, which your question addresses apart, the amount of effort that has been put into pre-award examination of those who

are bidding, and the amount of effort that will be devoted to post-war implementation, which will be substantially increased.

I think that you will see, because of institutional changes, the involvement of the Chief Compliance Officer in these two areas that I've talked about, that we will have much better results, and of course, we do take cognizance of the lists of others, but to my knowledge, I think it's only the World Bank that publishes one. If we were to have someone disbarred, that would now be published on our Web site. That's a new policy, but it is in place.

The CHAIRMAN. Well, I raise the question for obvious commonsense reasons. If there are experiences out there in the field with any of the regional development banks, as factors are uncovered, it would certainly be essential information. I think that the other banks would be so informed, and I appreciate the whole governance question who does what and what's the responsibility for this? At the same time, I raise the question simply because you have some responsibility, as do Mr. Speltz and others, to make certain that this information is available, so that mistakes are not made inadvertently. And that's why I'm curious about the proper spread of information in a timely way.

Mr. SULLIVAN. I completely agree with your observation. They ought to be sharing information. I believe they do share information, whether or not it can be improved, I'm not certain. I do know that our Chief Compliance Officer and the new people who are in charge of procurement at the Bank are very cognizant of the importance of going ahead and making sure that people do not take advantage of these systems for the reasons that Paul has mentioned in terms of the efficiency of the money provided.

We do have a very active program of supporting open, public, tenders using standard documentation. I believe last year over 96 percent of all procurements by the EBRD were subject to open public procurement, and, of course, using the standard documentation.

The CHAIRMAN. At least on your own, you're making this open. You could also, I suppose, share your observations with the other banks.

Mr. SULLIVAN. I believe they do.

The CHAIRMAN. Mr. Speltz.

Mr. SPELTZ. Mark and I work as a team together. I was asking permission to help him out here, just on the ADB side of this, because you are talking about all the banks, again, you're bringing up a very good point, and somewhat of a sensitive one from a legal point of view. The World Bank does publish its, we call, "black list" and many of the banks make a policy of, I believe it's all, of exchanging, at least on a need-to-know basis, all the lists of both consultants, individuals, and corporations that they are debarring, or blacklisting for a period of time, including the ADB. We have over 230 companies, as of yesterday, that have been debarred, or blacklisted for potential corruption or illegal activities, or just that we don't want to do business with them on the basis of the way they operate. That list we share with the EBRD, we share that list with the World Bank, with the African Bank, and the IEDB.

There is, however, a point that's been brought up by your staff that is of a deep concern to them, and I share that concern, that is, that within the ADB we do not publish that list, and that is

something that we are working on, that we do believe that that list should be published. But there are legal problems within the Philippines, with regard to the publishing of these companies names, due to very interesting laws there. With regard to the activities of the Bank, though, every debarred company is submitted to all the other banks, and very interestingly, effective November last year, when we receive a list of debarred companies or other companies that have been debarred from the World Bank or from EBRD, or others, we look right into—our Audit Committee looks into it—and if they believe there's justification for also debarring, they simply just don't do business with them any more, and they notify them.

And one other very interesting thing to keep these folks on their toes—if a company is debarred at the ADB, and reapproaches through another channel and tries to bid, the Bank further debars them for a longer period of time.

The CHAIRMAN. Well, that's very important information. I would just observe that clearly you have to follow legal counsel carefully with regard to the laws of the Philippines or others. On the other hand, this issue is serious, not just for the banks, but in terms of our overall public diplomacy in this country. I would say that if this is an issue with the Philippine Government, again this is something that probably needs to be discussed by our Ambassador, or Mr. Zoellick, our Under Secretary, or Secretary Rice. I'm simply raising the fact that we, as a country, are determined to make certain that anticorruption procedures are literally pervasive, that there is publication, and that there is follow-through in the Philippines as well as anyplace else. And that the ramifications of lack of cooperation here could be very substantial.

The failure to do this is ultimately going to lead to an undermining of these programs, with our body politic, that is, with the American people, quite apart from what is occurring out in banks. The American people have not been that well informed about what's occurring out there. Now, they're getting better informed all the time. I don't want it to come as a terrible shock. I would like it to come through thoughtful meetings like this one, in which professionals discuss what the facts are, what you are doing about it. There's a strong record of recognition, an action that makes a difference, because one can say, this is the way the world works. But what we're trying to say in these hearings, and what you're saying as administrators of these banks, is that the world has got to work—at least if money is going to be distributed, taxpayer money from our country and from others—in a way that stops corruption of the efforts, and does not put extra burdens upon the poor people of those countries that are the victims of this type of thing. This is preaching to the choir. You have to face this out in the field every day. But this reinforces that, and that is to say, I hope that you might raise these questions in the proper departments, such as the State Department, the Treasury Department. And if you do, more power to you. I just mention to you that I may raise them, too. This is—as a part of American diplomacy—something that you, Secretary Rice, or Under Secretary Zoellick need to be cognizant of, because this is important in our national image and effort.

Well, let me just ask one more question. Let me just observe, Ambassador Sullivan, that it's our observation that there are still

limited whistleblower protections at EBRD. There is not very much protection for staff testimony and independent recourse mechanism proceedings to resolve complaints by third parties at the EBRD at the behest of the G–8.

Describe what is being done to strengthen the whistleblower procedures at the EBRD, and how this general criticism has been met.

Mr. SULLIVAN. Thank you, Mr. Chairman.

We have expressed reservations about the current whistleblower protection scheme at the EBRD. We've raised it in the policy committees and in the Audit Committee, we will, we've talked to the Chief Compliance Officer about it. I think that the whistleblower scheme was hard to follow for people, is now in the process of being consolidated, made more readily accessible to people. There are questions and answers now on the Web site, notwithstanding what has been done to date, it has been agreed that there's more that needs to be done. There is concern about not only the protection of whistleblowers generally, but on the question of anonymity. The counsel to the EBRD advises that in certain circumstances, because the European Union Human Rights Convention requires people to be able to confront their accusers, that there may be times, as a consequence of an investigation, when that anonymity cannot be protected. This came up in the Audit Committee twice. The Board's belief is that we do need to protect whistleblowers. One member of the Board was actually formerly a whistleblower, and understands this all very well. I do not believe this process is at an end. I do believe that we, as an office, the U.S. Office at the Bank, will continue to pursue it until we get it right. But your concern is not misplaced. On the other hand others share your concern, including the Board of the EBRD, and certainly my Office and obviously I, personally, want to make sure that it's done correctly. I do think that having the new Chief Compliance Officer on Board who comes to the EBRD from the OECD where she built up a very strong compliance function, is a very positive development for working through the successful resolution of these issues.

As to the IRM, we have at the EBRD, very little experience with it. As you know, the United States raised some questions, and had reservations about it at the time of its adoption. I regard that, too, as a work in progress. We'll have to see how it works. There is a report due out later this year on how it's done in the first full year of its implementation by the EBRD.

The CHAIRMAN. Well, thank you very much. I appreciate your own personal conviction with regard to this, and the steps that you are taking, and likewise the compliance procedures that you've instituted and that you're supervising. This is an important step forward, and we appreciate your being here personally to give that testimony.

I thank both of you for your testimony, your original statements as well as the summaries, and the forthcoming responses to our questions. Obviously, this is of great interest to our committee and our staff. They have appreciated your hospitality as they have visited with you, and we are hopeful those visits will continue. We're grateful to you for encouraging that.

Mr. SULLIVAN. Well, thank you Mr. Chairman. We, too, appreciate the opportunity to be here, the opportunity to work with your

staff, and as you and I have discussed, we were looking forward to the visit of your staff to the EBRD and I'm delighted to learn that that visit has been postponed, but not cancelled, and we will look forward to working with you and the committee.

I do believe that it's important, for what we're all trying to accomplish that the countries with which we deal understand that the United States speaks with one voice on anticorruption efforts, and it's very helpful to us to be here today to talk with you. Thank you, sir.

The CHAIRMAN. Yes, sir; Mr. Speltz.

Mr. SPELTZ. Thank you very much, Mr. Chairman.

I think you know from both your staff and yourself, personally, the passion I have with regard to what you're trying to do here. I would like to respectfully request one thing for you to consider as you go forward.

You mentioned at the beginning of this, you're looking at putting in new legislation. I think on behalf of all of us who are Executive Directors at the Bank, that we hope that you work very, very closely with the U.S. Treasury Department with regard to those, and what aspects of new legislation would help us, and what might potentially hinder us.

We have a situation which you know very well, sir, in dealing with foreign relations, of the sensitivity of dealing with so many other countries that don't necessarily always share our opinion, and do not necessarily like it if they think that we're putting something down their throat. I think all of us have built very good consensus and relationships with our fellow Board members, and as you look at whatever you're going to do, I would only personally request that you work closely with our Treasury people in sorting out which ones you agree, and Treasury agrees, and we agree will help us, and which ones could be misinterpreted, where Board members could sit there and say, "Don't call Speltz, or Sullivan into this meeting because we have a document from their Congress that clearly says they're not open to discussion, they've mandated it." I hope you'll understand that.

The CHAIRMAN. I do, and I think that's good counsel. Staff has been advised to do just as you've suggested. But at the same time, Senators likewise should take that counsel very seriously, and we will.

Well, I thank you both, and we will now call upon our second panel of the morning.

The CHAIRMAN. The Chair welcomes Mr. Hemantha Withanage, and Mr. Tom Devine. I would ask that you testify in the order that you have been introduced. We are appreciative that you came. I know both of you have had an opportunity to hear the testimony of the first panel. You have already prepared statements, and they will be made part of the record in full. If you would summarize or proceed in any way you wish, I would appreciate that, and then we'll have questions.

Mr. Withanage.

STATEMENT OF HEMANTHA WITHANAGE, CONVENOR, SRI LANKAN WORKING GROUP ON TRADE AND INTERNATIONAL FINANCIAL INSTITUTIONS AND EXECUTIVE DIRECTOR, CENTER FOR ENVIRONMENTAL JUSTICE, COLOMBO, SRI LANKA

Mr. WITHANAGE. The Chairman, thank you very much for the opportunity to testify this morning. I am the President in the Sri Lankan Working Group of Trade and International Financial Institutions, and the Center for Environmental Justice which is based in Sri Lanka.

It's important to note that organizations who focus on environment and social welfare are also focused on the promotion of environmentally sustainable lending policies in the international financial institutions, and on corruption.

My close monitoring on certain Asian Development Bank projects in Sri Lanka shows that rather than alleviating poverty, they have often created poverty and corruption. I will give you just one example. Southern Transport Development Project involves the construction of 428 km long expressway. The road crosses through many wetlands, villages, home gardens, and more than 5,000 households in all categories will be affected.

About 40 percent of the final roadway is not covered by the Environmental Impact Assessment. People wanted the Asian Development Bank and the Road Development Authority to follow the proper Environmental Impact Assessment process to save their sustainable home gardens and respect of their lifestyles. They approached all the legal and administrative forums, including the Supreme Court of Sri Lanka, and the inspection mechanism of the Asian Development Bank, to receive justice. The matter is now with the United Nations Human Rights Commission, too. The project involves a different type of corruption, other than the type of corruption that was mentioned before this committee by Mr. Bruce Rich on the 28th of September, 2004. Certain people are provided unprecedented compensation to convince others, but others are not paid the same.

Three settlement officers asked for bribes to approve better compensation packages. Those who disagree and who do not pay, they were given rocky lands. Government officers were told that if they complete the land acquisition early, they will be paid an incentive. Certain politicians, and some political supporters also ask for bribes from the construction company.

After Mr. Rich testified, the contrary presentation of the Asian Development Bank explained why Kumagai Gumi, the construction company, was included, and he stated that it's a slight relaxation. But I wonder, why slight relaxation, only for this particular company, and why they did not include some others, too.

There are many bad stories. People who are still fighting for their rights were told that 25 percent of their compensation will be deducted if they do not leave the land early, and in one case, police arrested one woman from a village in the southern area, and beat her. She was the single parent of her young child.

In certain plots, one portion was valued for $600, but when they valued the other portions, it gave less amounts. So this particular case, he was given a rocky land, he was not able to buy better land for the compensation he received, and the land next to his land was

owned by another female schoolteacher, and her land was treated as a low-lying land, and paid only $70 per perch, which is one of the local units for the land measurement.

And I have a picture in this newspaper, appeared in the front page of the newspaper which shows that one woman lived, until the photo appeared in the newspaper, in this kind of small hut, and this has been submitted for the record.

When people complained to the Asian Development Bank Anticorruption Unit, they wrote back and said, "We received allegations, and we did not find any evidence, and we are closing the case. When people wrote back and asked for a copy of the report, anticorruption specialists wrote back and asked, "Would you please provide us more evidence." I don't understand why those high-level officers lie to the lay people.

Since I don't have enough time, I will not go into the corruption issues related to other projects which are explained in my statement, Mr. Chairman.

Finally, I want to touch tsunami, which devastated lives of many coastal communities. It is not my intention to explain the damage which you all have seen in the media. I thank all of the people and governments who performed their duty to support affected people and countries at this unfortunate moment. Sri Lanka also received a large amount of funds, this is not only donations, but a major portion of them are loans. Having bad experience of bad fund management and corruption, I believe, receive enough large amounts of funds, easily lead to corruption and mismanagement. We should have better monitoring on the ground. Asian Development Bank is talking about the monitoring and better coordination, but unfortunately the ground situation is not very good. No monitoring and better compensation among the agencies.

Just one example, fisherman in Batticaloa, which is a city in the east coast, received boats and fishing nets more than palatable for the lagoon and for the fishery resources. Some aid agencies think it will devastate the fishing resources soon if they put all the boats and nets to the waters. We believe that tsunami-affected people should have the right to participate in the decisionmaking, which is not the case on the ground.

When I complained about the corruption related to the Bank projects, one senior staff member told me, "They are not corruptions," but they call them as commissions. But I believe this was public funds from your government, and we people in borrowing countries pay them back, therefore, nobody can make commissions. It's the general notion in Sri Lanka that Asian Development Bank money involves with corruption one way or other. I have explained in my statement how large amounts of money goes for the other purposes which have no direct benefits to the people.

Mr. Chairman, to conclude, as a person who represents this hearing from the receiving end of the fund, I believe that the Asian Development Bank's development effectiveness is highly eroded due to many types of corruption and fund mismanagement. They misuse the Bank's immunity to the legal system to escape from any allegations. It is apparent that because the Asian Development Bank is not fully committed to accountability or transparency, it, in effect, enables and encourages corruption, which in turn delivers

unsustainable projects. Therefore, it would be irresponsible to authorize hundreds of millions of dollars for this institution without a clear idea how they combat corruption. In my testimony, I have made a series of recommendations, I hope it will help you to reconsider the involvement of the Asian Development Bank in our countries and combat corruption.

With your permission, I want to propose some other recommendations. One would be having a better policy, and policy implementation is very important in this regard. Stopping the loan disbursement if there is a reasonable corruption allegation, is very important, and educating people on how corruption policy works is also very important. And also, I believe consider the corruption track record of agencies in project design is also very important. And also make a corruption risk checklist to understand possible events and activities which are vulnerable to corruption of the particular type of project at the design stage, and continuous monitoring is also important. And also, I believe, sending independent ADB missions from anticorruption divisions to the site during the implementation, and consulting the public, also very important. Thank you very much for this opportunity.

[The prepared statement and photo submitted by Mr. Withanage follow:]

PREPARED STATEMENT OF HEMANTHA WITHANAGE, CONVENOR, SRI LANKAN WORKING GROUP ON TRADE AND INTERNATIONAL FINANCIAL INSTITUTIONS, AND EXECUTIVE DIRECTOR, CENTRE FOR ENVIRONMENTAL JUSTICE, COLOMBO, SRI LANKA

1. INTRODUCTION

Mr. Chairman, Senators of the committee, thank you very much for the opportunity to testify this morning at the hearing on "Combating Multilateral Development Bank Corruption: African, Asian and European Regional Development Banks." The chairman and the committee are to be commended for organizing these hearings, which address one of the most critical but hidden threats to the proper use of Bank funds that hinders sustainable development.

As of December 31, 2004, the ADB had approved US$3.476 billion in loans to Sri Lanka for some 128 projects and programs. However the development effectiveness of many of these loans and their role in poverty reduction is highly questionable, even according to the ADB's own statistics.

A presentation made by Mr. Bruce Murray of the Asian Development Bank (ADB) Operations Evaluation Department (OED) to the NGO FORUM on the ADB on March 31, 2005, showed that over half of completed ADB projects (59 percent) were rated highly successful (HS), generally successful (GS), or successful (S). Thirty-one percent of completed ADB projects were rated partly successful and 9 percent were rated unsuccessful by this internal evaluations unit. For Sri Lanka, OED had evaluated 36 projects and 47 percent were considered HS/GS/S, 45 percent were rated partly successful, and 8 percent unsuccessful. In this context, the performance of projects in Sri Lanka ranks third from the bottom of ADB borrowers, with only Papua New Guinea and Bangladesh generating lower ratings. The rating of Partly Successful seems to be generous for many projects, considering that it was given to projects, such as Lunugamwehera, which are actually dismal failures and creators of poverty on-the-ground. If we take the ADB's self-evaluation at face value, more than half of Sri Lanka's ADB debt accumulated over three and a half decades is from projects the ADB itself considers to be less than successful.

The World Bank Poverty Reduction Strategy Paper (PRSP) presented to the Sri Lankan Development Forum in June 2002 says that poverty in Sri Lanka had not decreased over the last 10 years, and continues to be around 40 percent of the population. It is admitted that the actual figure for poverty in Sri Lanka would be higher if the conflict areas were taken into consideration.[1] In fact, the poverty level used

[1] "Poverty in South Asia 2003, Civil Society Perspectives," SAAPE, October 2003, Katmandu, p. 185.

in Sri Lanka of Rs 1500/month (equivalent to US$15/month) is much lower than the internationally recognized poverty level of US$1/day/person.

Neither GDP growth nor its distributive effects have been sufficient to bring about a marked reduction in the poverty level in Sri Lanka. In other words, the benefits of economic growth have not automatically trickled down to the poor and the economic strategy adopted in Sri Lanka has not succeeded.[2] The PRSP acknowledges this in relation to the decade of 1990s. But this failure was even more apparent in the previous one and a half decades.[3]

Mr. Chairman, Senators of the committee, Sri Lanka has been a client of the Asian Development Bank since 1968. ADB is involved in project financing as well as in macroeconomic policy development. Poverty alleviation has been a major focus of ADB-financed projects since the new mandate of the ADB was established. However, it is very clear that the ADB and the Sri Lankan Government have failed to realize their mission to reduce poverty and increase growth.

Contrary to the ADB's mandate, certain ADB-funded projects and macroeconomic policy changes have actually created poverty. In the next few pages of my testimony, I will discuss a number of projects that are controversial due to the destruction of people's sustainable livelihoods and the related failures of the ADB and local implementing agencies to control corruption.

2. ASIAN ENVIRONMENTAL ORGANIZATIONS THAT MONITOR THE ADB

The Sri Lankan Working Group on Trade and IFIs (International Financial Institutions) is a network of civil society organizations that monitors the impacts of projects and policies of the IFIs on local communities, their livelihood, natural environment and resources. Its secretariat is located at the Centre for Environmental Justice in Colombo, which is a local environmental organization, working toward good governance and environmental justice.

The Sri Lankan Working Group of Trade and IFIs is an evolution of the Sri Lankan Working Group on ADB, which was established in 1998. There are 15 member groups who are concerned about ADB's involvement in development projects and in promoting macroeconomic policy changes. Recently we assisted people affected by the Southern Transport Development Project (STDP), a major road project funded by the ADB, to bring their inspection claim to the ADB's Special Project Facilitator and Compliance Review Panel. We have also helped people to develop their complaints to the ADB regarding the loss of their rights to water due to water transfers under the ADB-financed Water Supply and Sanitation projects through the Water Supply and Drainage Board. Our network member, Green Movement of Sri Lanka, helped affected communities from the Kirindi Oya Irrigation and Settlement Project (1986), the Upper Watershed Management Project (2002), and the Protected Area Management and Wildlife Conservation Project (1999)[4] to raise their concerns with the ADB and local implementation agencies.

I was the elected International Convener for the NGO FORUM on the ADB for the period of 2001–2003. Recently I accepted the Executive Director position of the NGO FORUM on the ADB (Forum) and will take up my new position in May 2005. The NGO Forum on the ADB is a network of more than 300 civil society organizations based in ADB borrowing countries and donor countries that monitor the projects, programs, and policies of the ADB. Its Secretariat is based in Manila, Philippines, and it is governed by an international committee comprising members from both borrowing and donor countries.

The Forum was established in 1989 by Philippine NGOs and NGOs from the United States. Since then it has lobbied the ADB to develop necessary safeguard policies and address the failures of its projects and programs to provide benefits to the local communities. The Forum has been involved in the campaign for accountability at the ADB, which resulted in the establishment of the first Inspection Mechanism in 1995 and the new Accountability Mechanism in 2004. The Forum has also been involved in campaigns around gender, environment, involuntary resettlement, indigenous people, and disclosure at the ADB, many of which have led to the adoption and/or strengthening of ADB policies. Forum activities also involve assisting local communities to bring their concerns to the ADB.

Mr. Chairman, Senators, it is important to know that these organizations, who are primarily focused on the environment and social welfare, and are focused on promoting environmentally sustainable lending policies in the international financial institutions, are also concerned about corruption. They are very concerned about

[2] Sri Lankan Development Forum 2002.
[3] "Poverty in South Asia 2003, Civil Society Perspectives," SAAPE , October 2003, Katmandu.
[4] This project is jointly funded by the ADB and the World Bank.

the negative impacts on the social, environmental, and economic sectors coming from projects with ADB involvement They are also concerned that although ADB is a development bank with anticorruption, social, and environmental responsibilities, its staff and management often seem to have relatively little concern for these issues.

3. ADB: SUSTAINABLE DEVELOPMENT OR POVERTY CREATION

As stated by Mr. Bruce Rich in his testimony on September 28, 2004, at the hearing before this committee

> . . . the "culture of loan approval" and "pressure to lend," which has been documented in the World Bank and other MDBs for more than a decade, has often also contributed to failures in the implementation of policies designed to mitigate adverse environmental and social impacts of MDB lending.

Close monitoring of some recent ADB projects, such as the Thailand Samut Prakan Wastewater Management Project, Melamachi Water Project in Nepal, and the Chashma Right Bank Irrigation Project in Pakistan, shows that the ADB's stated mission is in trouble.

My close monitoring of certain projects in Sri Lanka, namely the Kirindi Oya Irrigation and Settlement Project (1977), Sri Lanka Southern Transport Development Project (1999 to date), Upper Watershed Management Project (2000 to 2006), and Protected Area Management and Wildlife Conservation Projects (1998 to date) shows that rather than alleviating poverty, ADB projects have too often created poverty for local communities and fostered corruption.

Mr. Chairman, Senators of the committee, I would like to address a few Sri Lankan case studies to illustrate this point.

4. CASE I

ADB's Poverty Creation at Lunugamwehera in the Southern Dry Zone (1977) (Kirindi Oya Irrigation and Resettlement Project)

Kirindi Oya is a river that flows to the ocean in the southern province of Sri Lanka. The Kirindi Oya Irrigation and Settlement Project (KOISP) was started in 1977 with US$60 million in loans from the Asian Development Bank. The project involved the construction of a large earthfill dam and irrigation canals in the dry zone of Sri Lanka. Nearly 5,000 families were settled in the area as part of the project.

Water distribution in Kirindi Oya began in 1986, but there was not adequate water for rice paddy cultivation. Many settlers were given land before irrigation water was provided and then had to be "sustained by food assistance under the World Food Program for longer than anticipated."[5] The river was dammed in the wrong place and more people were resettled in order to satisfy needs of the politicians. Both the Irrigation Department and the ADB failed to design the project to cater to the river flow. In most years, not a single plot is cultivated in the new development area. According to the ADB's OED report, "Destruction of livestock land, shrimp lagoons, and wildlife habitats adversely affected the livelihoods of some groups in the project area and led to increased conflicts between settlers and herdsman."[6]

Mr. Kumarasinghe, Secretary to the Federation of the Integrated Farmers Organisation-Kirindi Oya, said

> We were given only one hope that we will be provided with water for both "Yala" and "Maha" seasons. But today it has become only a dream. Farmers have been indebted day by day and it has developed to an extent that some farmers commit suicide.

According to the ADB's evaluation report, the Kirindi Oya project was considered to be politically expedient as the Sri Lankan Government sought to address civil unrest in the impoverished area and promote "more balanced development." This same political imperative meant that less expensive project alternatives were not adequately considered.[7] Social tensions and inequality increased in the area because of

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[5] ADB, Operation Evaluation Office. "Project Performance Audit report on the Kirindi Oya Irrigation and Settlement Project in Sri Lanka." December 2000, quoted in "Asian Development Bank: In Its Own Words," Fried, Lawrence, Gregory, 2002.

[6] Ibid.

[7] Ibid.

the project, and "many settlers brought in from outside the project area appear to have obtained their allotment by political influences."[8]

Kirindi Oya had time overruns of more than 100 percent and, despite its high cost, was not "relevant" to the development needs of the local population.

> The expenditure of close to $100 million to benefit a relatively small number of settlers can be considered of limited relevance in the context of overall development needs and poverty alleviation in the southern dry zone."[9]

The Green Movement of Sri Lanka and Oxfam Community Aid Abroad produced the report "Too Little Too Late" in 2001, which addressed the grave problems in the Kirindi Oya project. This report and a letter from the Federation were presented to ADB President Chino during the ADB Annual General Meeting in 2001. Although a response to the letter was received from ADB, there were no steps taken to correct the problems.

Although the Federation had hopes that the ADB will provide a new water source, assistance did not materialize. Mr. Jayaweera says

> Newly settled families have now doubled. Since the population in the project is increasing they have no income for living. There is no education for the children. Although ADB is responsible for this poverty creation we have no access to the ADB.

Furthermore, our information revealed that land allocation in the Kirindi Oya project was full of corruption. According to villagers, both politicians in the area and the government officers were involved in requiring bribes from the people who were not their political supporters in exchange for their land allocation. This is one reason more lands were cleared and developed than could be irrigated by the reservoir. Although we presented documents and evidence to prove the allegations of corruption in a letter from villagers to the ADB President in 2001, ADB failed to address these issues. They responded to the people's letter and sent a consultancy firm to the project area, but there were no changes on the ground.

While the destruction caused by the Kirindi Oya project, which was funded more than 25 years ago, still needs to be corrected, ADB continues to provide funds for new projects. The Southern Transport Development Project is a recent example of violations of social, environmental, and human rights and inadequate controls to guard against corruption.

5. CASE II

ADB's Accountability Experiment through the Southern Transport Development Project (STDP) 1999

The Southern Transport Development Project (STDP) is one of the most controversial projects of recent times. But it is a dream for some politicians. The project has been characterized by mismanagement, corruption, social unrest, delay, disregard of social and environmental concerns, and in some cases, police abuse and threats. Sri Lankan Government bureaucrats as well as the lending institutions (both ADB and the Japan Bank for International Cooperation [JBIC] in this case) and consultants are responsible for these injustices.

STDP involves the construction of an Expressway connecting Matara (a southern city) and the outskirts of Colombo by a 128 km road. The road crosses through 4 river basins and over 100 small and large wetlands and paddy fields. It also passes through many villages, home gardens, and demolishes over 1,300 houses. In total, 8,745 land lots are planned to be crossed by the Expressway. In 2002, estimates showed that 5,683 households of all categories will be affected. Resettlement cost for STDP would be US$29.75 million.[10] The total project cost is 33 billion rupees or approximately US$230 million. The local implementing agency is the Road Development Authority (RDA), which comes under the Ministry of Transport and Highways.

ADB's Environmental Policy requires the consideration of environmental problems since this is an environmental Category A or high-risk project with significant impacts. The Environmental Impact Assessment (EIA) was done for a 3–4 kilometer-wide corridor, with detailed studies for a corridor of 200 meters for housing, but as it turned out, it did not address the actual impacts of parts of the road trace that was subsequently chosen. In fact, as described in more detail below, about 40 percent of the entire final trace of the road financed by the ADB was not covered by

[8] Ibid.
[9] Ibid.
[10] Resettlement Implementation Plan, October 2002.

the EIA. As a result, numerous groups of people and households have had their livelihoods and quality of life affected without adequate compensation. The EIA was subject to heavy criticism, as it had not properly addressed these environmental and social impacts.

The project is guided by the Sri Lankan National Environmental Policy and the Resettlement Policy as well as the ADB safeguard policies such as Involuntary Resettlement, Environment, Information Disclosure and the Inspection Policy. However, these policies are being breached and the project has serious social, environmental, and legal issues.

Since 2001, people have been exploring legal redress through the local judiciary. They went to the Local Human Rights Commission, Appeals Court, and to the Supreme Court. Although the Supreme Court decided that human rights have been violated in the STDP project, it did not make any changes in the project's design, or influence the attitude of the ADB and the RDA.

Construction in the ADB-financed area started in 2003. Many people were displaced. Numerous social and environmental issues were created.

The committee has heard testimony of Mr. Bruce Rich last September 28, 2004, on the allegations of corruption in this project concerning the bidding process and contract award, which I will give an update on. But the corruption and irregularities in management in this ADB project permeate down to the level of the poor and displaced, which I will first describe in the following section.

5.1 Forms of corruption at the local, implementation level

Many people, who have received compensation for their land which was taken for the project, are not happy. But the Land Acquisition & Resettlement Committee (LARC) for the project provided unprecedented compensation for a few individuals. This is one type of local corruption and abuse of power that happens under the STDP. Many people thought that they would get the same compensation. But they never did. Initially people were paid the market price. But now they are given only the very low government value plus 25 percent.

The affected people do not have access to the Resettlement Implementation Plan. Displaced people have never seen a copy of the plan. RDA does not give a copy. Those who have been displaced people have moved out without proper guidance or knowledge of their entitlements. They were told to leave before receiving compensation. Many people were intimidated into removing their roofs, they were told they would get no compensation if they did not do so immediately. Often they got only Rs 50,000 (US$500) as a rent allowance and nothing more. Their neighbors do not even know where they live now.

According to the villagers, Divisional Secretaries (government officials below the provincial level) were told by the RDA that they will be given Rs 250,000 (US$2,500) for early clearance of the trace. Divisional Secretaries instructed Grama Niladhari (Village Officers) and certain villagers who were provided better resettlement packages to demonstrate to the ADB officials that there were many satisfied people. This is the second type of local corruption.

RDA resettlement officers ask for bribes from the affected people to approve better compensation packages. This includes better land for the new house. Those who disagree are given rocky lands. This is the third type of local corruption.

People living in Gelanigama, which is a village located close to Kalutara, say

> . . . we went to all the authorities including the Inspection Panel of the ADB, but with no success. We were threatened with arrest by the Parliamentary Member of the area, if we do not allow the road to be constructed.

They said surveyors came to their village with police officers from five police stations. They cry for justice.

Affected people in Akmeemana say that road trace was changed to protect land owned by a rich businessman. They said

> . . . our politician took bribes to protect those lands and change the trace. We now have no faith in them.

They went to all available judicial mechanisms in Sri Lanka. They also wrote to the Inspection Panel of the ADB with no success. The first Inspection request in 2001 was denied by the ADB, which misconstrued facts and pretended that the affected people were all within a 3 km corridor. This was proved false at that time, but it was only in 2004 that the ADB admitted this.

The surveying of the road was accompanied by police abuse and threats in some areas. The surveyors came with police. Gelanigama people say they came to their

village and threatened that they would arrest them. Police arrested one woman from Akmeemana and detained her. She was the single parent of a young child.

There are many unresolved issues. The design process is full of intimidation, bribery and corruption, betrayals and displacements.

5.2 Corrupt contract award—can ADB wash its hands?

The consultants involved in the design are Wilbur Smith Associates in association with Resource Development Consultants (WSA & RDC). The EIA report was done by the consultants of the University of Moratuwa. The EIA process is full of errors. About 48 kilometers (40 percent) in both JBIC and ADB sections in the Final Trace are not covered by the EIA. The design was changed to a new trace by the RDA without authority and without any studies or a new EIA. The Supreme Court ruled that the process of approval had not been followed.

The construction contract for the Southern 62 km has been awarded to Kumagai Gumi, a Japanese construction company.

As stated by Bruce Rich in his testimony on September 28, 2004

> Allegations regarding contracting irregularities emerged in Sri Lankan newspapers in 2001 and 2002, which were confirmed by a parliamentary Committee on Public Enterprises. In the bidding process for the project, 29 companies applied, and three met the prequalification bidding procedures, based on a number of considerations, including the financial condition of the prospective contractors. A Japanese company, Kumagai Gumi, did not meet the prequalification criteria,[11] and in fact had a negative financial worth. Kumagai hired an agent, Access International, to help win the contract. As is typical with this sort of arrangement, Access would win a hefty fee if it paved the way, as it were, for a successful contract award for its client. Sri Lankan newspapers reported that Access had influential political connections, including in the Prime Minister's Office.[12] Access is alleged to have bribed the RDA project official, for example by installing a new diesel generator in his home, giving him the use of a new SUV, and promising financial rewards if Kumagai won the contract.[13] This use of agents as motors of corruption to win contracts in some respects recalls the case of the Lesotho Highlands Project, discussed in the committee's July 21, 2004, hearing.
>
> After the prequalification process was complete, the ADB reportedly sent a letter to the Sri Lankan Treasury requesting that Kumagai Gumi nevertheless be considered as a bidder on the project. Three companies, including Kumagai, participated in the final bidding; only Kumagai was allowed to submit a second alternative bid. Kumagai knowing the lowest bid of the other two companies, was naturally able to submit another, lower bid, and win the contract. All of this is recounted in two Sri Lankan newspaper articles, which I have submitted for the record. In the aftermath, the bidder that would have under normal procedures won the contract, protested, repeating the same allegations, and threatened to bring legal action.
>
> The Sri Lankan parliamentary Committee on Public Enterprises (COPE) conducted an investigation, and concluded that both national government procurement guidelines and those of the ADB had been violated.[14] The Attorney General of Sri Lanka, when asked how Kumagai could have won the contract in violation of national and ADB tender guidelines, reportedly stated: "Kumagai Gumi had been accommodated purely on a suggestion by the ADB on February 13, 2001, particularly since it is an ADB funded project and the guide on prequalifications specifically provides [in such cases] for ADB approval."[15]
>
> When the ADB Anti-Corruption Unit undertook its first mission to perform spot procurement audits in a borrowing country last year, it went to Sri Lanka, but did not look at the Southern Transport Development

[11] To prequalify, companies had to score 60 points in an evaluation framework assessing their financial stability, technical capacity, etc. The prequalifying companies had scores of 95, 79 and 75. Kumagi's score was 54.

[12] Frederica Jansz, "COPE Shoots Down Southern Highway," Sunday Leader (Sri Lanka), October 27, 2002; Frederica Jansz, "Of Highways and Backroom Access," Sunday Leader (Sri Lanka), November 1, 2001.

[13] Ibid.

[14] Ibid.

[15] Ibid.

> Project.[16] According to ADB staff, they do not wish to pursue anticorruption claims against a project where an Inspection Panel claim may be underway or pending. This is truly a perverse and counterproductive approach, since not only does the Inspection Panel not appear to investigate corruption, it is likely that projects with Inspection Panel claims underway may be precisely the ones where corruption abuses may be better documented.
>
> Meanwhile, the STDP project proceeds and Kumagai remains the contractor. Neither ADB management nor the ADB Board appear to be interested in investigating the extremely serious procurement irregularities and cost overruns in this case.

Responding to this claim, which also appeared in the Sri Lankan newspaper, the Daily Mirror, on October 2, 2004, Mr. Alessandro Pio, Country Director of the ADB resident mission in Sri Lanka states that

> During the hearing, allegations were made about the Southern Transport Development Project in Sri Lanka, which were not new. In fact, ADB had addressed many of the issues relating to the project, in your own publication in May 2002.
>
> On the prequalification process highlighted in your article, the objective was to ensure that sufficient and appropriately experienced and resourced companies were eligible to tender for the ADB-funded project, thereby achieving a cost and quality effective outcome.
>
> Three companies were originally prequalified and another—the fourth company referred to in your article—met the basic financial, experience, and resource requirements but fell slightly short of a passing mark when these criteria were combined.
>
> Since the objective of the process was to maximize competition, and because the deficiency was of a technical nature only, the company was permitted to participate in the tender process. It is important to note that the company became eligible simply to tender for the work, in competition with the originally prequalified companies. There was no question of the company being awarded the contract as a consequence of the prequalification process.[17]

Although this response rejects the allegations, it proves that ADB has interfered with the bidding process which means the process is not transparent. According to Alessandro Pio, this was a "slight relaxation."[18]

A subsequent article appeared in the Sri Lankan newspaper, the Sunday Leader, on October 10, 2004, reiterating the ADB's involvement and stating that

> . . . after the prequalification process was complete the ADB reportedly sent a letter to the Treasury requesting that Kumagai Gumi nevertheless be considered as a bidder on the project. The Attorney General of Sri Lanka, when asked how Kumagi could have won the contract in violation of national and ADB tender guidelines, reportedly stated: "Kumagi Gumi had been accommodated purely on a suggestion by the ADB on February 13, 2001, particularly since it is an ADB funded project and the guide on prequalifications specifically provides [in such cases] for ADB approval."[19]

This article also states that

> Secretary to then Prime Minister Ranil Wickramasinghe, Bradman Weerakoon articulated similar sentiments stating Kumagai was awarded the contact after the ADB intervened to ensure the project went to the Japanese firm.[20]

Responding to Mr. Pio's article, Sarath Athukorala and Heather Mundy of the Joint Organization of the Affected Communities on Colombo-Matara Highway state that

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[16] The Anti-Corruption Unit examined another project, and no corruption. It found weak financial controls which could have been exploited for corruption if corruption were present in the project.

[17] Alessandro Pio, Country Director, ADB Resident Mission, "ADB Clarifies Inaccuracies on Corrupt Project in Lanka," Daily Mirror, October 6, 2004.

[18] "ADB Chief Refutes Charges," The Sunday Leader, October 10, 2004.

[19] Federica Jansz, "Southern Highway—The Access to Corruption," The Sunday Leader, October 10, 2004.

[20] Ibid.

> Mr. Pio says "There has been a general misunderstanding that the project cost increased from 11–12 billion rupees to 27 billion rupees, because of the alignment changes. However this is actually a misleading comparison between the cost of the ADB financed section and the total project cost, which includes the section financed by the JBIC."
>
> This is totally untrue. Mr. Alessandro Pio is either unaware of what he is commenting on or he is deliberately misleading the people of Sri Lanka. The major documents of the project include the cost for the entire road in the range Rs 11–15 billion, not as Mr. Pio indicated for only a section of it.[21]

The response of the affected people also addresses Mr. Pio's explanation with regard to the prequalification. Affected people state that

> With regard to the points allocated at prequalification, there has been more than enough publicity of the computations, all recognize that the disqualification was not of a technical nature. Kumagai Gumi, has financial problems, its Bank had to write off an enormous amount of debt in 1997 and again in 2000. More recently its executives have also allegedly been involved in bribery, illegal political donations, and money laundering. See Mainichi Newspaper about Imajo in Japan in 2002, and again in 2003 and Papua New Guinea Post Courier about 1995 to 2000. So much for Mr. Pio's "deficiency of a technical nature."

The ADB's main explanation for its pressing for the involvement of Kumagai Gumi despite the company's failure to prequalify is not convincing: "The objective was to ensure that sufficient and appropriately experienced and resourced companies were eligible to tender for the ADB-funded project, thereby achieving a cost and quality effective outcome." If this were the case, why did the ADB intervene, not to increase the number of prequalifiers, but to urge that one specific company, and one company only, be included, one indeed that had failed the prequalification tender because of its risky financial condition? And after this same company was finally chosen, the project's cost has increased by over 100 percent.

The ADB's anticorruption unit (the Integrity Division), in response to the submission from affected communities regarding these corruption allegations in the STDP, simply replied, "We have conducted an investigation on the concerns that were raised. We did not find evidence of fraud or corruption, as defined by ADB, or that ADB's funds were misused. Thus, we are closing the case." When the affected communities requested more information on the investigation, they were told that no report was produced. The ADB's Integrity Specialist then asked that the communities provide evidence of "who received the payment, how much was paid, when the payment was made, how the payment was made, which contract were you referring to, any corroborating evidence to indicate the allegation, any information that you may have that would help us to determine if further investigation is warranted, etc."[22]

The ADB cannot wash their hands of the corruption either because of the involvement of its own staff and due to the failure of its own policy implementation. Since this project is a joint-funded project of the ADB and the JBIC, the selection of a Japanese construction contractor could have been a prerequisite or a factor leading to undue influence and pressures to choose a Japanese company.

We have seen similar pressure from the Japanese Government during the selection of the construction company for the Upper Kotmale Hydro Power project, which is a very controversial project funded by JBIC. This project will have negative impacts on six beautiful waterfalls located in the hill country of Sri Lanka.

5.3 STDP destroys environment and sustainable livelihoods, too

The STDP Expressway crosses four major rivers in the southwestern-southern part of Sri Lanka, viz KaIu Ganga, Bentara Ganga, Gin Ganga, and Polwatta Ganga.[23] The Expressway traverses through 60 percent high ground and 40 percent wetlands. Due to its undulating nature and for easy filling material, the road will be constructed by cut and fill. This will create some major environmental problems.

It has many negative social and environmental impacts as it crosses through many rural villages where people still have sustainable livelihoods. Villagers say

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[21] Sarath Athukorala, Heather Mundy, "ADB—The Truth Behind the Highway," Daily Mirror, October 18, 2004.

[22] E-mail from ADB Integrity Specialist to Joint Organisation of the Affected Communities on Colombo Matara Highway, March 2005.

[23] These four rivers create severe flooding in the southwest monsoon annually.

> We don't need many inputs from the cities. The villages are surrounded by paddy fields owned by us, which gives rice in two seasons. Jak, bread fruit, green vegetables come from our home gardens. We have plenty of water and fertile lands. Our cattle are grazing in the nearby field. The temple is in the vicinity. Our relatives are living around us. What else do we want? Who wants to leave such a heaven? This is a sustainable life.

When the road is constructed it will destroy this natural environment. The agriculture will be destroyed. The paddy field will be filled with soil. Stagnant water will destroy the remaining fields. No more good soil or lands for agriculture will be available. There will be no more home gardens or lands for grazing. Flooding will increase. Wetlands will be destroyed.

The compensation is not sufficient to complete the replacement houses they have started constructing. They were not given enough compensation to maintain, let alone improve, their living standards as the project promised. No one has been given the market value of their land or assets.

Rice is the staple food of the Sri Lankans, but it seems all major and minor development projects destroy paddy fields day by day. Agriculture is the main economic activity of the affected people and the affected area of STDP. Paddy is one of the main crops. However, 299.9 hectares of paddy lands will be acquired for this project. This is about 31.53 percent of the total land acquisition for the STDP. While these plots are directly affected, hundreds of acres of other paddy lands will be destroyed due to soil erosion, water clogging, etc. No paddy lands will be developed under this project. Therefore those farmers will lose their employment.

It was estimated that 265 people would lose employment in paddy sector for the combined road trace which the ADB loan was originally granted for. The area this road trace would cross had large tracts of abandoned paddy fields. For the combined trace, the total annual estimated economic loss in terms of paddy cultivation is Rs 5,990,484. For large parts of the current trace, which traverses through villages and cultivated paddy lands, there are no studies to estimate the total value of lost paddy lands. Isn't this a destruction of sustainable livelihood?

Yes, the road will give access to major cities. It may increase industrial development, too. There will be benefits to the general public. It will give more jobs to some people who now depend on agriculture. But this all could be achieved at much less cost and without needlessly impoverishing hundreds of households, if corruption and mismanagement did not permeate this ADB project.

Although those who are engaged in agriculture will be temporary laborers for the road construction when their fields are destroyed, what will happen to them afterward? The temple and the school will be separated from the people by an Expressway. Relations will be separated. Community will be dispersed. There will be no village anymore. Sustainable livelihood will be destroyed.

5.4 ADB's accountability mechanism failed

In 2002, four cases concerning the project were filed in the Sri Lanka Court of Appeal. The Court appointed a Judicial Committee of Retired Supreme Court Judges to investigate the position. Their Report stated "the alterations are of a significant nature and should be approved afresh."

Instead of ordering an EIA and Social Impact Assessment (SIA), the ADB did just the opposite. It declared the loan effective on a Resettlement Implementation Plan which said there were only 31 objectors when there were actually 51 petitioners still in the Court of Appeal. At the same time, the ADB acknowledged receiving over 150 letters objecting to the unstudied change of road trace.

Nevertheless they pressurized the Sri Lankan Government to sign the contract with Kumagai 2 months later, 5 months prior to the verdict in the Court of Appeal. These very signatories to the letters continue to protest, causing delay to the project which is costing the Sri Lankan Government.

In 2004, 2 years after the contract had been awarded to their favoured contractor, Kumagai, and work had progressed, affected people approached the ADB's new accountability or inspection mechanism through its ADB's Special Projects Facilitator (SPF) process and Compliance Review Panel (CRP). The Special Projects Facilitator has recently been added to the ADB accountability mechanism as an initial step to promote consultation or mediation between the affected people, the government implementing agency, and the ADB's operations department. The Compliance Review Panel investigates the affected people's claims of ADB policy violations that have caused them harm.

Belatedly, the ADB SPF admitted that the 3 km argument which was used by the ADB to deny the first inspection request in 2002 was not valid. The SPF acknowledged that indeed neither an EIA or an SIA exist for the final road trace.

However, subsequent delays by ADB in carrying out its own accountability process had the effect of buying time for the contractor and RDA to advance their activities to a point of no return. The SFP's investigation of the complaint was delayed from the required 49 days to over 100 days. The pretext was to allow the report of a committee appointed by the Prime Minister and an ADB Safeguards Review Report to be published. Neither of these reasons are in line with the ADB's own Accountability Mechanism Procedures. The complainants have not been allowed access to either of these reports to date.

In December 2004, the SPF appointed an international mediator who spent half a day with the complainants. Without further discussion, he and the SPF suddenly closed the mediation process in January 2005, claiming that he could not reach consensus on the dispute that had been going on for over 3 years. The refusal of the implementing agency (RDA), with the backing of ADB, to study their road trace changes was allowed to block the facilitation.

Whilst the CRP is still investigating ADB policy violations, the SPF decided to close the mediation or consultation process.

The ADB thought fit to hasten the signing of a contract with Kumagai when it was patently obvious that strong protests would continue, as, in fact, they are. The ADB continued to ignore the protests of the people from 2001 onward, and made every effort to hasten the commencement of the project which violated its environmental, social, and economic policies. During this entire period, the project was under a growing cloud of corruption and bidding irregularities widely publicized in all of Sri Lanka.

One can define corruption in various ways. In the view of many Sri Lankan civil society groups, there is institutional corruption when ADB management uses—or rather misuses—ADB accountability processes like the Inspection Panel, the SPF and CRP, and the Safeguards Review Report to allow loans which violate ADB policies and covenants to continue. This may be because money is changing hands or because, as Mr. Rich has pointed out, the ethic at ADB is loan disbursement, not development effectiveness.

The ADB is the largest multilateral lender to Asia; there is a real threat of some Asian countries becoming another economic burden like Africa if institutions like ADB are not forced to become more transparent and accountable and made to remember that they are not responsible and accountable only to themselves.

As ADB is increasingly using cofinancing in projects, it is even more important that they work strictly within policies and guidelines, since the ADB through cofinancing leverages multiples of its own financial contribution often based on confidence in the integrity of its procedures and financial management.

5.5 What is questionable?

Corruption is manifest throughout the Southern Transport Development Project (STDP). It is not limited to the transactions described in the testimony to the Senate Foreign Relations Committee by Mr. Bruce Rich on September 28, 2004. It is underpinning and contaminating the whole project.

Why is it that the Implementing Agency—RDA—has worked so hard to avoid any sort of study of the changes to the road trace they have made? Why have they sought to proceed with a plan that harms more than double the families that were on the recommended trace for the Expressway? Why has the cost more than doubled? Why did they choose some of the most difficult places for construction to build the Expressway?

Why is it that the ADB has sought to block any investigation? Why is it happy to ignore breaches of Loan Covenants? Why is ADB happy to ignore the many breaches of its Safeguard Policies?

We think the most plausible answer can be found in the gains to individuals throughout the process. For ADB personnel, possibly it is to keep their record clean and increase their portfolio, though one of the individuals involved did so much to substantially alter the project from its original concept that one cannot help but question whether there was not some personal gain somewhere.

Corruption does not mean that only money is passed from hand to hand, it means ignoring major safeguard policies that are designed to protect local communities. It also means a lack of transparency and accountability. It means using Accountability Mechanisms that are supposed to solve problems to buy time so that projects with gross irregularities proceed past the point of no return and foreclose the benefit of correction.

6. CASE III

Upper Watershed Management Project: Another Example for Corruption and Irregularities

Upper watersheds for the main rivers in Sri Lanka (Kalu ganga, Uma-oya, and Kirindi-oya) are badly affected by soil erosion that has taken place due to the cash-crop plantations started in the British period, subsequent population growth and land use for new agricultural development. As there are many adverse changes in the waterways and the surroundings in the area at present, the ADB with the assistance of the Government of Sri Lanka has inaugurated a project under the Ministry of Forestry and Environment to conserve the upper watersheds of above-mentioned rivers.

The ADB-funded Upper Watershed Management Project of Ministry of Forestry and Natural Resources has an estimated total cost of US$23.7 million, which consists of 70 percent from the ADB, 25 percent from the Government of Sri Lanka and 5 percent from the beneficiaries. The project started on May 5, 1998 and was to be completed by December 31, 2004.

The investigation done by the Green Movement of Sri Lanka, a local environmental organization, shows that the project has many irregularities, including slow project performance, the absence of a consultative process for affected people, failure to implement the participatory fire prevention plan developed by the Provincial Secretariat, failure to integrate the involvement of the village-level government officers (Grama Sewakas) and village-level officers of the government poverty alleviation program (Samudri), field and provincial officers, in the Project even after their request, failure to take action on the reported irregularities that have taken place in the replanting process by officers. There are a number of financial irregularities relating to purchases of the rubberized coir pots, plant material, etc., that is necessary for the project.[24]

The Project failed to address soil conservation measures. The project failed to reach some important areas but carried out work in areas that are not that important. Some of the findings and observations on financial management and policies in the project are also cause for concern. All the above-mentioned activities of the Upper Watershed Management Project have led to financial and administrative irregularities. The Project money was used for printing religious books for certain politicians in the area, and constructing roads across the forests to satisfy local politicians. The Project had deviated from its original basic concept and objectives. The rest of the Project staff made a complaint to the authorities about the irregularities, but no action was taken.[25]

The money loaned from the ADB is being utilized haphazardly in an irresponsible way under this Project. The Project Management has grossly violated the institutional fundamentals and ethics of the ADB. The citizens of this country are paying this loan and will be paying in the future, too.

The Green Movement of Sri Lanka requested the ADB to evaluate the present situation by an independent body, and to take appropriate action to control these financial misappropriations under the Project before it is too late. The report prepared by the Green Movement was sent to the ADB Resident Mission, Government agencies, and the relevant Minister. This was also raised with the ADB mission who visited to study the performance of the project in late 2004. According to the Green Movement no action to date has been taken to solve the problems.

7. LACK OF ACCOUNTABILITY AND CORRUPTION

The above three cases show that ADB-financed projects are facing serious accountability problems. The projects can go wrong in (a) design stage, (b) contracting stage, and (c) implementation stage. The problems in the Kirindi Oya Project and STDP are at the design, contracting, and implementation stages. The problems in the Upper Watershed Management Project is at the implementation stage.

Although the ADB has a number of safeguard and accountability policies, it exercises inadequate scrutiny over the implementing agencies for its loans in Developing Member Countries (DMCs). While some irregularities may be unavoidable, the problems in the bidding processes have, in some cases, been caused by the ADB itself, such as in the STDP project detailed above.

According to Mr. Jak Jabes, the Director of ADB's Governance and Regional Cooperation Division, corruption in Asia can cost up to one-sixth of a country's GDP. He also states that governments pay between 20 percent and 100 percent more for

[24] Forest in Trouble, Green Movement of Sri Lanka, 2003.
[25] Ibid.

goods and services due to corrupt procurement practices.[26] The ADB is aware of the corruption in its borrowing members.

The above three cases show that the corruption in ADB-financed projects is on several levels. At the first level, government officers involved at the local implementation level may ask for bribes in exchange for compensation for villagers' lands or assets which are taken for the project. The second level involves the local politicians and their supporters who ask for bribes to allow for construction or project implementation. They also ask for subcontracts and jobs for their supporters. This includes misuse of project assets. The third level of corruption is related to big companies, which can involve high-level Government Officers, Project Designers, and possibly ADB officials.

For example, hiring of Government Officers for ADB projects and paying them multiples of their normal salary is a practice which encourages corruption. Furthermore, employing foreign experts and paying them salaries more than 50 times the amount paid to the equally qualified and experienced local employees is also a practice that encourages irregularities and corruption in ADB projects.

Mr. R. Dissanayake of Kotte, Sri Lanka stated

> I was appalled to read in the newspapers recently that an enormous amount of money is to be spent on a water resources management project with a loan obtained from the ADB. A breakdown of the Rs 1400 million project budget indicates that Rs 62 million is to be spent for import of vehicles, Rs 182 million for purchase of equipment, Rs 248 million for employing foreign specialists, and Rs 492 million for training. I venture to predict that this project will also end up with very limited benefits to the people of this country but will bestow ample benefits to the lender, the politicians and state official's associated with the project.[27]

It is the general perception among the public in Sri Lanka that ADB-funded projects are often involved with some kind of corruption. There is a wide belief that these projects somehow give fewer benefits to the people while significant amount of funds seep to corrupted officials and politicians. There is also a popular perception that senior government officers design projects to earn very high income before they retire.

There has been, for example, serious fights between officers for the project manager post for the ADB Upper Watershed Management Project and the Protected Area Management and Wildlife Conservation Project. The result is the implementing agencies divide and one group does not allow other groups to implement the project.

Mr. Chairman, Senators of the committee, the ADB is not accountable to the people in the borrowing countries or in the donor countries. They are only dealing with the governments. ADB is also immune to any legal action. ADB management and the staff take this as a freedom to design and fmance projects that may destroy local communities, their livelihood, environment, and natural resources. ADB's lending target (culture of loan approval) approach and the internal evaluation of performance based on how much money has been released through the ADB is a killing approach.

This is one reason for the staff to approve destructive projects that destroy the sustainable livelihoods of local communities. But also many ADB staff strongly believe that they will not be punished for any of their wrong actions. The only penalty is that they will be transferred to another division. I strongly believe that this approach should be changed.

The people forcibly resettled under Lunugamwehera are still suffering after more than 25 years for the wrongs done by the ADB, local staff, and politicians. In the STDP, resettled people are suffering because of the wrong actions of ADB and the Sri Lankan RDA. Those who complain or seek justice through local courts and the Inspection Mechanism of the Asian Development Bank are threatened with reduction of compensation or delay of compensation. The case of the Upper Watershed Management Project shows that the country suffers from the many irregularities of the project managers and the ADB staff. We strongly believe that this culture of the Bank and the attitude of its implementation partners need to change very quickly. The above case studies show that the Bank often exercises no control or monitoring over the local implementation agency after the loan agreement is signed.

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[26] Daily Mirror, May 25, 2000.

[27] R. Dissanayke, Kotte, Foreign funded project rackets, Opinion page, The Island, January 30, 2003.

If loan covenants are violated, the ADB has to stop disbursements. The STDP case shows that RDA continues to violate loan covenants but no action has been taken by the ADB.

I strongly believe any measure to address the institutional problems relating to corruption at the ADB would also improve overall project quality with respect to environmental and social impacts as well as enhance overall economic performance.

8. TSUNAMI RECONSTRUCTION

Mr. Chairman, Senators of the committee, I would also like to address one more issue at this hearing. It is none other than the tsunami which affected several Indian Ocean nations including Sri Lanka.

8.1 Consequences of the tsunami

In Sri Lanka, the tsunami killed approximately 30,740 people; 3,858 people are still missing. About 15,683 are injured; 833,780 people belonging to 178,886 families have been displaced. According to UNICEF, about 30 percent or 12,000 of the dead and missing people are children. More than 800 children in Sri Lanka are left with no mother or father. About 88,022 houses have been completely destroyed and 25,737 have been half destroyed; 200 schools have been seriously damaged.

Several beach hotels, houses, and other commercial buildings vanished. Vehicles with passengers were also washed out to sea. The railway line and roads were also damaged. A train with eight coaches was totally destroyed, adding 1,800 lives to the death toll; 65 percent of the fishing fleet has been destroyed. Ten out of twelve fishery harbors located in these areas have been destroyed. Sea waves destroyed a 200-meter to 5 km wide zone. In places such as Mulativue Sea, waves went more than 5 km inland. It has destroyed the biodiversity in the area. The Coast Conservation Department states that more than 600 million Rupees (US$6 million) damage has been done to the coastal revetments which were constructed using boulders to block the waves.

The natural environment was also destroyed by the tsunami. Environmental experts are now studying the affected coasts in tsunami-hit countries to assess the damage caused to the environment. The scale of the tsunami's environmental damage is readily apparent, as the coastline has changed almost beyond recognition.

The damage to the marine environment is equally devastating. The debris that flowed into the sea from the land smashed coral reefs. Some initial research shows that 50 percent of the coral has been damaged due to the harbor waves and debris. The natural environment of many marine organisms changed in a just a few hours. Toxic materials including PCBs would have entered the sea at many points, further affecting marine life. The amount of silt, sand, and organic matter mixed with the water will also smother them. On land, wells and freshwater streams have been contaminated with seawater, posing more problems.

According to the Central Bank of Sri Lanka, the total loss for the country is about 150 billion Rupees (US$1.5 billion). This does not include the human losses and the environmental damage. According to the Central Bank, Sri Lanka needs 550 billion Rupees (US$5.5 billion) for reconstruction of the infrastructure damaged by the tsunami.

There are many reasons for the high level of damage. These include a lack of awareness and information, the high population density in the coastal zone which is about 4.88 million people within only 4 percent of the land area, as well as a disrespect for the law such as the Coast Conservation Act No. 57 of 1981, as amended, No. 64 of 1988, a lack of a relevant authority and expertise, and destruction of natural barriers such as coastal sand dunes, mangroves, green belts, etc.

Sri Lanka is now aiming for a shoreline conservation zone of 100 meters in all areas and 200 meters in the Eastern province. But this needs proper and equal examination under the law. A proper environmental restoration plan is an urgent exercise. The Sri Larikan Government needs support for an accelerated environmental restoration plan. Civil society awareness and participation must be brought into this restoration. Civil society organizations, especially environmental organizations, can play a major role in this exercise.

8.2 Scale of proposed donor support and need for greatly improved monitoring and coordination of use of funds

After a Needs Assessment, the ADB, JBIC, and the World Bank announced that Sri Lanka needs US$1.5 billion for Tsunami Recovery and Reconstruction.[28] The Donor Needs Assessment further states

[28] Joint Press Release ADB, JBIC, World Bank, February 2, 2005.

> . . . the assessment, prepared in close cooperation with the Government of Sri Lanka, sets out clear guiding principles for the reconstruction strategy, with an important emphasis on the inclusion of affected communities in the planning and process of rebuilding. It estimates the overall damage to Sri Lanka at US$1 billion with a large proportion of losses concentrated in housing, tourism, fisheries and transportation. Total losses are estimated to equal 4.4 percent of GDP with about US$500 million in external financing required in the short term for 2005.

Alessandro Pio, Country Director of the ADB, said

> The human impact has been even more staggering than the damage to infrastructure. In some coastal communities, entire families, livelihoods, and social networks have simply disappeared. Reconstruction efforts must be very sensitive to this human dimension, and do everything possible to help restore communities, mitigate the psychological, emotional and economic loss and restore hope, while working to rebuild shelter and physical infrastructure.

The Donor report stressed the need for strong monitoring, transparency, and accountability to ensure that the millions of dollars of external assistance reach their intended sources and are utilized efficiently. Also, the monitoring of the sustainability of the reconstruction work and plans is very important. Civil society movements have to monitor this. Otherwise transparency, participation, and accountability will be neglected when the country receives foreign aid.

The three Donor Country Directors emphasized that nothing is more demoralizing for the people in need, and for those trying to help them, than to hear that funds are being siphoned off or wasted. It was, therefore, imperative that all key stakeholders in this—the government, the International Community, Civil Society, and the Liberation Front for Tamil Elam (LTTE)—agree upon a transparent monitoring and accounting system for all the resources that will be deployed in the reconstruction effort.

The Needs Assessment identified the guiding principles for the recovery and reconstruction strategy as:

- The allocation of resources, both domestic and international, should be strictly guided by the identified needs and local priorities, without discrimination on the basis of political, religious, ethnic, or gender considerations;
- Reconstruction activities are carried out by the appropriate level of government, with an emphasis on decentralization where feasible;
- Communities are empowered to make their own decisions during recovery;
- Communication and transparency are present in decisionmaking and implementation;
- Reconstruction avoids rebuilding existing vulnerability to natural hazards; and
- A coordinated approach is used to prevent duplication in activities.
- To translate the principles into reality, the assessment team recommended a vigorous process of public consultation, a communications program, and development of district-based reconstruction plans for the affected areas.[29]

However these principles are too often not being carried out on the ground. The biggest challenge is better coordination among the relief agencies. In certain areas, the number of boats donated by the agencies is a few times higher than the actual number required. This is the situation with fishing nets as well. Many fisherman and experts think that the fish will soon be depleted if all the boats engage in fishing. This is only one example.

The construction of housing is the biggest challenge. With the 100 m no-construction zone, a severe land problem was created. Due to the unavailability of lands, the housing development designs have been delayed and still most of the people who live in relief camps have no hope that they will be given a house in the near future.

Although the ADB, the World Bank, and JBIC state the importance of empowering communities to make their own decisions during recovery, as well as the importance of communication and transparency in decisionmaking and implementation, this is not a reality on the ground. People are not aware of the plans of the government.

The slow reconstruction process leads to uncertainties about their future among affected people.

Mr. Haruhiko Kuroda, ADB President said

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[29] "Sri Lanka 2005 Post-Tsunami Recovery Program: Preliminary Damage and Needs Assessment," Asian Development Bank, World Bank, JBIC, January 2005.

> Given the scale of the recovery, even with our best efforts at coordination, the potential for gaps, overlaps and duplications is significant We need to develop tools that can assist us in identifying gaps, and avoiding duplications.
>
> It is largely for this purpose that a draft tracking mechanism has been developed for your consideration at today's meeting. Adoption of the tracking mechanism will allow us to coordinate, monitor and manage the overall rebuilding effort. But it is so meaningful, it must be "owned" by the countries involved.[30]

It is too early to understand whether the ADB's monitoring tool is effective. But we don't see either coordination or monitoring on the ground.

The large amount of funds that will be quickly disbursed by the ADB and World Bank for tsunami relief also underscores the need for immediate reforms of performance incentives for ADB and World Bank staff, and greatly improved anticorruption measures at the Banks.

9. CONCLUSION

In the final analysis, it is apparent that because the ADB is not fully committed to accountability or transparency, it in effect enables and encourages corruption, which in turn delivers unsustainable projects. It is our experience in Sri Lanka that the ADB is not concerned whether its safeguard policies are complied with, nor is it even interested whether its loan covenants are met.

Whilst it is not possible for me to show that ADB personnel are corrupt in receiving money or benefits personally, what is clear is that the corruption in our country and of the overseas contractors is in practice assisted and empowered by the ADB's practices and lack of priority in addressing this issue. The ADB currently has only very weak tools or mechanisms to control this corruption.

Our experience in the STDP case is that the ADB Accountability Mechanism consultation phase listens only to the Government and the Executing Agency and does not try to stop the breaches of safeguard policies or corruption.

Mr. Chairman, Senators of the committee on behalf of the 19 million citizens of the teardrop in the Indian Ocean which is Sri Lanka whose lives are affected by such careless lenders, we appeal to you to use your hold over the purse strings of ADB to pressurize them to care about development and respect the sustainable livelihoods, to care about the affected people, to stop the ADB feeding corruption.

As Mr. Bruce Rich of Environmental Defense stated before this committee last September 28, we also believe the record of the ADB in addressing corruption is so poor that it would be irresponsible to authorize hundreds of millions of dollars for this institution without a clearer idea as to the steps ADB is taking to implement reforms that will effectively address corruption.

In this regard I would like to make the following recommendations.

- The ADB should strongly implement its Anti-Corruption Operational Procedures to explicitly assess corruption risk in its country strategy programs, project appraisal, and project performance evaluation reports.
- The ADB should improve transparency and information disclosure. We are very unhappy about the present draft version of the ADB's Public Communication Policy which says ADB also understands that full disclosure of information is not always possible for legal and practical reasons. It also says that ADB must safeguard the privacy of its staff and protect confidential business information of private projects sponsors and clients.
- The ADB should halt loan disbursements when government borrowers are not addressing corruption.
- There should be a mechanism to control borrowing government implementing agencies when they violate the ADB's safeguard policies.
- The ADB should get serious about enforcing its loan covenants.
- We also ask for a proper investigation on the corruption charges in the STDP and the Upper Watershed Management Project.
- Finally, we ask ADB involvement in finally correcting the problems to help the affected people in the Kirindi Oya Irrigation and Settlement Project.

Thank you very much for this opportunity.

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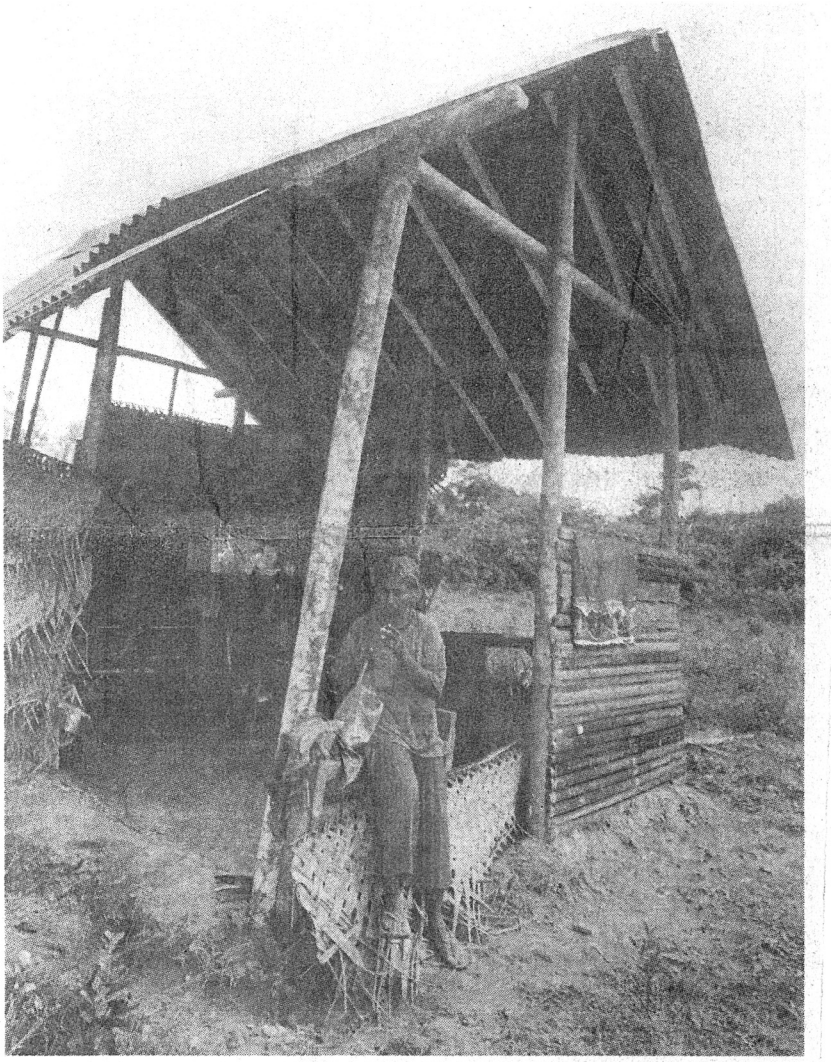
[30] Harmonization and partnerships for Effective Recovery ADB Press Release, March 18, 2005.

FROM THE SUNDAY LEADER, SRI LANKA, OCTOBER 24, 2004



A WOMAN relocated to make way for the southern highway sits outside a partly built house, unable to complete it due to the poor compensation paid by the government. The Southern Transport Development project is already marred with charges of corruption

The CHAIRMAN. Thank you very much for that testimony. I would simply observe, as you've pointed out, that you have submitted for the record an extensive statement with a number of case histories, at least from your observation, that certainly beg investigation, as well as the conclusions that you have reached. We'll raise some more of that during our question period, but I'd like to call now on

Mr. Devine for his testimony before we get into questioning both of the witnesses.

STATEMENT OF TOM DEVINE, LEGAL DIRECTOR, GOVERNMENT ACCOUNTABILITY PROJECT, WASHINGTON, DC

Mr. DEVINE. Thank you, Mr. Chairman. Thank you for this invitation, and also thank you for this forum. It just doesn't get any more responsible than this committee's preparation.

The CHAIRMAN. Thank you.

Mr. DEVINE. Whistleblowing is the human foundation of transparency reforms against corruption, and other betrayals of MDB institutional issues. What we can contribute comes from 27 years of experience in this field. In particular, last summer the Ford Foundation sponsored an in-depth research assessment of the whistleblower policies at multilateral development banks. We published the first four assessments of Changing the Culture of Secrecy, coauthored by our first International Director, John Fitzgerald, to assess those institutions. We held off from the African Development Bank, because they said release of the whistleblowing policy was imminent there, so we thought we'd give them a chance. That's what they said this year also, some time after we sought to finalize an assessment included as an attachment to my testimony.

The bottom line was that we could not responsibly recommend the policies of any institution as safe channels to make the difference. That's very unfortunate, because it deprives whistleblowers of the opportunity to work within the system if they don't want to be silent observers. That just can't be healthy for the checks and balances of these institutions. Since then we've heard from numerous whistleblowers responding to our report, and the actual practices are far worse than the paper policies.

The policies and practices of these banks must reflect the values of transparency and the respect for human rights that they expect for the rest of the world. As the first witness pointed out, there are severe consequences. I can second his experiences from a One World Trust Conference last fall, where there was dramatic visual evidence of how corruption in the Asian Development Bank turned irrigation projects into basically a desert, in the area they were supposed to be benefiting.

Communities that are supposed to benefit from venture capitalism see their water supplies poisoned when the funds are diverted to large corporations that are constructing gold mines. There are very serious grounds, in terms of the human consequences, as well as the fiscal.

There are also real grounds for hope. We have not seen grounds for optimism, but we're excited that there are grounds for hope. The dynamic at every institution, except the Inter-American Development Bank has shifted from stagnant to dynamic in terms of their environment, their rhetoric.

For example, at a One World Trust Conference last fall, the EBRD's Deputy Compliance Chief teamed up with us at GAP to recommend consensus principles for reform. But so far there has been no action. And in response to this morning's testimony we could say that one thing they could do right away is give witness protection rights to people who testify at their Institutional Review

Mechanism. That would be a good sign of good faith. And with respect to their concerns about the European Union, they're not insurmountable. The EU has their own whistleblower protection system, and those could be coordinated.

In particular, there's a potential for great spillover effect from a project at the World Bank, which has commissioned highly respected professor Robert Vaughn of American University Law School to prepare a report recommending an overhaul of its whistleblower policies. We're hoping this can be a precedent for the regional banks as well. And we feel that this committee's oversight vigilance will make a major difference, whether Professor Vaughn's work is a foundation for whistleblower reforms with widespread application, or becomes another example of objective professional expertise that gathers dust.

Quite clearly, the magic formula for results will be persistence, persistence, persistence. This is the time to intensify our efforts, because we're seeing some cracks in the wall. It is particularly true for the Treasury Department, which is responsible to monitor implementation of the McConnell-Leahy amendments to last year's appropriations law. They have to issue progress reports on whether the banks were implementing whistleblower rights, external audits, publication of loan agreements and other reforms for transparency. Last September's report was little more than a rubber stamp of the status quo. The March report was a far more serious effort. Treasury started to use its assignment as a bully pulpit to press the banks. That's very encouraging, but they need to go farther.

For example, at two banks without whistleblower policies they credited reforms that seem to be getting stale because they haven't been implemented. They failed to disclose or assess the empirical track records of any MDB policies, and they didn't offer specific recommendations.

We have four areas of specific recommendations in our testimony. I'm glad to discuss them in response to any questions. But we do want to commend you for your work. Yesterday, Secretary Snow testified that the United States can give increased funding to these banks because of institutional commitments to reform. Our experience indicates that in terms of empirical results, those assertions are largely a bluff. Stepped up vigilance will make the difference between bridging the gap from rhetoric to reality.

[The prepared statement of Mr. Devine follows:]

PREPARED STATEMENT OF THOMAS DEVINE, GOVERNMENT ACCOUNTABILITY PROJECTWASHINGTON, DC

Mr. Chairman, thank you for this invitation to speak before the committee. My name is Tom Devine and I am the legal director of the Government Accountability Project (GAP). I commend Chairman Lugar and the other members of the committee for your serious commitment to congressional oversight of the multilateral development banks (MDBs). It just does not get any more responsible or thorough than this committee staff's broad-based, indepth research as a foundation for reform.

Whistleblowing is the human foundation for transparency reforms against corruption or other betrayals of the MDB's institutional missions. What we can contribute comes from our own oversight of whistleblower policies at the regional development banks and the World Bank. Our credentials to assess whistleblower policies are grounded in some 27 years of experience. GAP is a nonprofit, public interest organization dedicated to helping whistleblowers exercise free-speech rights to challenge abuses of power that betray the public trust. Our mission is to advance governmental and corporate accountability by promoting whistleblower rights, inves-

tigating their claims, litigating their cases, sharing our expertise through publications, and developing legislative and regulatory reforms. We have led the campaigns to enact, or defend, virtually all national whistleblower laws in the United States. On the international front, GAP works with national governmental bodies. With colleagues from American University Law School we coauthored a model whistleblower law approved by the Organization of American States (OAS). Although as GAP's legal director I am presenting this testimony, it is a composite work product from our international team that also includes its leader, director Melanie Beth Oliviero, and coordinator Sophia Sahaf.

Citizens in countries around the world aspire to the same freedom of expression and the right to know information that will protect them from unsafe and wasteful practices by government and private companies, as do the American people. The multilateral development banks are critical agents for other governments to meet these rights of their citizens. We wholeheartedly support these organizations' development missions but are acutely aware they are under threat from corruption, waste, and abuse of power. We also remain mindful that the United States has contributed billions of taxpayer dollars as donations and in the form of private investor funds to these institutions. We have a right to know if our money is being used to advance the welfare of poor people worldwide in a responsible, accountable manner. This committee's pioneering oversight work has demonstrated that conclusion would be a fantasy.

We also know, because GAP has been investigating policies and practices of the African Development Bank, the Asian Development Bank, the European Bank for Reconstruction and Development, the Inter-American Development Bank, and the World Bank regarding whistleblower protection. In 2003 the Ford Foundation sponsored our indepth research to assess the procedures on which MDB whistleblower policies are based. Last summer we released the first four volumes for "Challenging the Culture of Secrecy," our assessments of those institutions. We held off on the African Development Bank, because their leaders said a whistleblower policy was in the final stages of preparation. That is what they told the Treasury Department this year. So far, nothing has happened. As a result, we are finalizing a report on the current reality faced by African Development Bank whistleblowers. Unless there is dramatic improvement soon, a summary of our anticipated findings is enclosed as exhibit 1.

The results of our audit of paper procedures were summarized in written testimony last July 26. It is enclosed as exhibit 2. The bottom line was that we could not responsibly recommend the policies at any institution as safe channels to make a difference, instead of bypassing the institutions with leaks. Since then we have learned from over two dozen whistleblowers, that as practiced, actual practices are far worse than paper policies. Their anticorruption claims are more rhetorical than real. While there is no doubt that some light has been shone on corrupt practices, the banks are too eager to direct that light on client countries.

It is imperative that the policies and practices of the banks themselves reflect the values of transparency and respect for human rights that they expect by the rest of the world. That is because these practices can have life and death consequences. For example, at a One World Trust conference last fall on organizational accountability, we saw dramatic visual evidence how corruption in Asian Development Bank irrigation projects functionally have turned the area they are supposed to benefit into a desert. Whistleblowers have told us how pipeline projects are severely undermining the lives of beneficiaries supposedly helped by increased energy access. Communities supposed to benefit from venture capitalism see their water supply poisoned, when the funds are diverted to large corporations that spend it on gold mines.

GROUNDS FOR HOPE

We have not yet seen grounds for optimism, but we are excited that there are grounds for hope. Particularly with respect to whistleblower rights, the dynamic at every institution, except the Inter-American Development Bank, has shifted from stagnant to dynamic. At the One World Trust conference last fall, the new leader for EBRD whistleblower investigations teamed with GAP to recommend consensus principles for whistleblower reforms. But so far there has been no action at that Bank, which still does not have a specific policy. It is not credible for the Bank to continue asserting that protection can be inferred from composite procedures.

In particular, the World Bank has commissioned highly respected Professor Robert Vaughn of American University Law School, a coauthor of the OAS Model Law, to prepare a report recommending an overhaul of its whistleblower policy. Unfortunately, the Bank so far has declined to release his work, creating the procedural

equivalent of another oxymoron—secret transparency reforms. This committee's oversight vigilance will make a major difference whether Professor Vaughn's work is the foundation for whistleblower reforms that could be applicable to all MDB's, or becomes another example of objective professional expertise gathering dust.

The magic formula for results will be persistence, persistence, persistence. We have come this far largely due to this committee's steadily increasing vigilance. Now is the time for all of us to intensify our efforts.

That is particularly the case for the U.S. Treasury Department, responsible to monitor implementation of the "McConnell-Leahy" amendment to last year's appropriations law. That provision requires the United States to use its voice and vote to implement transparency reforms by this coming June 1, including whistleblower policies consistent with U.S. and international norms. The law required Treasury to issue September 1 and March 1 progress reports to Congress. Last September's Treasury report was little more than a rubber stamp of the status quo that could have been written by the Banks, and actually may have been to some degree. The March report was a far more serious effort, and Treasury used its assignment as a bully pulpit to press the banks. However, at two banks without whistleblower policies, the AfDB and EBRD, Treasury credited promised reforms that have been pending long enough to become stale, failed to disclose or assess empirical track records, or offer specific recommendations. There is a long way to go before Treasury's optimism is grounded in reality. GAP's comments on the September and March Treasury reports are enclosed as exhibits 3 and 4.

RECOMMENDATIONS

Last summer we made a series of reform recommendations, which below have been further refined and expanded from the lessons whistleblowers have taught us since.

- Create a baseline for protected speech based on dissent against misconduct that threatens the institutional mission, rather than institutional self-interest.
- Protect direct disclosures to external authorities such as the U.S. Congress, Treasury Inspector General or other law enforcement agencies when necessary to avoid a significant threat to public health and safety, damage to the bank's mission or criminal violations of national or international law.
- Protect participation in the citizen complaint mechanisms for addressing harm caused by MDB-financed activities. Safeguards could be included to prevent public release of proprietary information.
- Provide a flow of information from secure hotlines to each Bank's Boards of Directors.
- Break through the conflict of interest in internal appeals adjudications. This can be accomplished by offering alleged reprisal victims the opportunity to seek justice through third-party, independent, binding arbitration by a decision-maker selected through mutual consent.
- Institutionalize the legal burdens of proof from the U.S. Whistleblower Protection Act to judge whether a whistleblower's rights have been violated, as the World Bank does for reprisal investigations.
- Provide prevailing whistleblowers full make-whole relief from confirmed retaliation, including provision of attorney fees and the right to reinstatement as necessary to maintain national residency rights.
- Establish independent autonomy and performance standards consistent with the U.S. Inspector General Act of 1978 for bank investigative agencies, to eliminate the conflicts-of-interest that too often have turned those offices into legalized retaliation units instead of credible institutional checks and balances for accountability.

The conceptual basis for these recommendations is summarized below:

1. Align all personnel, lending, and project policies—staff rules, environmental and social safeguards, policy review strategy papers (PRSPs), country assessment strategies (CAS), and the like—with pre-existing universal standards embodied in U.S. and international law, starting with whistleblower protection.

U.S. constitutional and statutory law, and international human rights norms all confer fundamental rights to freedom of expression, the right to receive and impart information and the right to due process before a fair and impartial tribunal. Within the United States, the Sarbanes-Oxley standards for whistleblowers at public corporations now set the international pace for whistleblower rights. Within the last few years the United Nations, Organization of American States (OAS), and Council of Europe all have reinforced a mandate for whistleblower protection through their anticorruption treaties. The OAS has approved a detailed model law that is a composite of international and U.S. norms.

There also is a long-established body of universal standards enshrined in enforceable international instruments such as the International Labor Standards of the International Labor Organization (ILO), and the protocols and conventions that enable enforcement of the Universal Declaration of Human Rights.

Witnesses to misconduct and abuse at the Banks live in fear of coming forward. Our evidence demonstrates that their fears are well founded. The Banks routinely victimize the messenger rather than hold accountable those who defraud donor countries and recipient countries alike. For any MDB to be accountable it must provide safe channels for reporting corruption, fraud, and harassment.

When senior staff such as public health specialist, Dr. Sunil Chacko, challenged MIGA (the Multilateral Investment Guarantee Agency) policies that result in dislocation of communities, and environmental degradation that undermine sustainable economic development, he found himself harassed. His duties were diminished and then his job terminated. Despite winning an appeal that validated his contention of reprisal and the written assurances of World Bank President James D. Wolfensohn that he would be reinstated, Dr. Chacko has never been offered a contract.

2. Adopt and enforce modern rules of procedures for the systems of justice and conflict resolution within the MDBs. The various appeals and tribunal mechanisms can only ensure due process if they are free from conflicts of interest, if all parties have access to legal representation (not just the Bank) and genuine relief, and if resolution includes recourse to third party alternative dispute resolution.

All of the Banks' appeals processes and administrative tribunals are tainted by conflicts of interest that render them no better than suspect grievance procedures. Quite simply, they lack independence. At most, the systems are thinly camouflaged procedures where a reprisal victim can ask an institutional bully to change its mind. They could do that without a whistleblower policy. In the EBRD, for example, the Bank president has discretionary authority to terminate employees. Since it is the Bank's president who also selects the Tribunal president, this "justice" mechanism is fatally flawed. In the case of the AfDB, the Appeals Committee makeup has seven members chosen by the president, including the Chair and Alternate Chair, versus five members chosen by the Staff Council.

Further, the adjudicators in these justice mechanisms are not professionally equipped, and recordkeeping is inconsistent. Often there are no transcripts of proceedings. Even worse, in other instances transcripts and hearings are secret. Secret trials and justice are oxymorons. Petitioners have no rights to face their accusers and are generally not entitled to bring a lawyer with them to their hearings. Nor do rules permit the recovery of legal fees when the findings uphold their cases.

Persons seeking to challenge retaliation for reporting wrongdoing endure further abuse and institutionalized defamation for exercising their rights. For example, Dr. Yang-Ro Yoon, a senior World Bank economist, reported a 40-percent overrun ($15 million) in a 1996 loan for schools in that nation. In return for her service to the Bank's mission in reporting misappropriation of project funds, she has been harassed, humiliated, had her duties diminished, her office "downsized," been terminated, and when she finally won reinstatement, it was to a lesser assignment.

Dr. Yoon's attempts to resist this reprisal have led her through a 3-year nightmare of the Bank's conflict resolution system. Despite "winning" her case, she lost salary, benefits, and adjustments, such as not factoring in inflation, She has been compensated for only one-third of her legal costs, burdening her with $30,000 in personal expenses and placed in a position beneath her capabilities and credentials. She has been exiled from her former work and her expertise, to new duties irrelevant to her background. When she filed new appeals to enforce her initial ruling, the same Administrative Tribunal turned on her with decisions published on the Bank's Web site that most graciously could be called judicial defamation. She has been warned that it is misconduct for her to continue seeking enforcement of her paper victory.

In order for the MDBs to provide the right to a fair hearing, new procedures must be adopted that provide equal access to legal representation, witnesses, and documentation. There must be independence for decisionmakers, at least from the supervisory chain of command and more preferably from the institution, which can be accomplished through independent, mutual strike arbitration. Adjudicators must be selected in a fair and objective manner. Genuine "make whole" relief in the form of compensation for lost income, benefits, and reimbursement of legal fees is required.

3. Extend requirements for independent external auditing of managerial and financial controls, and the range of appropriate authorities to which staff may report wrongdoing.

All the MDBs operate within a closed loop of responsibility. Staff are not permitted to report corruption directly to Board members. Management can and has misrepresented information to Boards. In cases we have investigated this amounts to hundreds of millions of dollars. Only external oversight can assure accountability. External audits of both managerial and financial controls, such as are currently contained in the Sarbanes-Oxley legislation in the United States for all publicly held companies, should be applied to the MDBs.

Similarly, the Banks' current policies deny free-speech rights to whistleblowers by limiting disclosures through prior restraint. Although whistleblower protection is supposed to further freedom of speech, the Bank policies could not be more Orwellian. Every Bank whistleblower policy is an Official Secrets Act, gagging employees from disclosing anything outside institutional walls that could undermine the interest of the relevant Bank, regardless of the impact relevant misconduct could have for the Bank's mission. All the regional MDBs ban external whistleblowing, even to national and international law enforcement agencies, Ministries of Finance and legislative bodies, including the U.S. Congress. Their own inspection panels for redress by aggrieved "beneficiaries" of Bank loans are treated as external bodies. Amazingly, employees are vulnerable to discipline for testifying at a relevant Bank inspection panel with the same evidence that would be officially protected when disclosed to a supervisor or in-house investigator. In recent years we have seen enough scandal resulting in massive waste and betrayal of the pubic trust to recognize that external oversight is a fundamental prerequisite for accountability.

4. Create truly independent investigative units with modern legal burdens of proof.

The existing investigative units to which allegations of corruption are referred—such as the Inter-American Development Bank's Office of Institutional Integrity (OII) are handicapped at best, and at worst, abused as tools of reprisal. It is not surprising that they do not have a significant track record of accomplishments from working with whistleblowers. We have seen evidence of investigations being instigated against whistleblowers in retaliation for their disclosures to these bodies. We have even seen investigations initiated as a tool for mass intimidation of whole office staffs. Requiring these units to report to external oversight bodies could significantly improve legitimacy. This would be consistent with the model of departmental inspectors general in the United States. One option would be for them to report directly to Bank Boards of Directors. The committee's own series of oversight hearings on the MDBs and the recently launched JEC study of MDB accountability are testament to the need for this systemic reform.

Beyond independence of these investigative units, there also is a demonstrable need for standard, modern investigative procedures to ensure fair, impartial, and replicable treatment of all credible allegations. Employees working with these units, voluntarily or involuntarily, have no rights against investigators who turn on them, which is frequently the case from our review. Hotline procedures and standards vary drastically. Confidentiality procedures are inconsistent.

CONCLUSION

Yesterday Treasury Secretary Snow testified that the United States can justify increased MDB funding based on their institutional commitments to reform. Our experience indicates that in terms of empirical results, these assertions are largely a bluff. Whistleblower policies are in a time of transition, but so far those commitments largely have been a bluff with little positive impact. This committee's stepped-up vigilance will be extremely significant in bridging the gap between the rhetoric and reality of accountability through transparency reforms like whistleblower protection.

The CHAIRMAN. Thank you very much, Mr. Devine.

Let me begin, Mr. Withanage, by just observing that on page three of your written testimony, you mentioned that Asian Development Bank, ADB, had approved over $3.4 billion in loans for 128 projects and programs over the years, and you charged that many of these loans and their role in poverty reduction are highly questionable. In fact, you offer illustrations in which the results led to negative setbacks, quite apart from progress in Sri Lanka.

If we take ADB's staff evaluation at face value, more than half of Sri Lanka's ADB debt now, accumulated over three and a half decades, is from projects the ADB itself considers "less than suc-

cessful." This makes the point that I was trying to make in my opening statement, that the consequences, sometimes, for developing nations, of maladministration of these loans is not only disappointment that things did not occur for the benefit of people, but worse still, that debt ensures for the people—in this case, quite a bit of debt in Sri Lanka, left over from unsuccessful efforts. And therefore, when we're talking about history—and that's important in reviewing why what we're doing now is urgent—we must seek ways to reverse that history.

The question still will remain, how strenuous are those efforts? How comprehensive? As we just heard from Mr. Devine, not all the returns are in even from the African Development Bank, as to what they're going to do, quite apart from evaluating how well it is going. That's somewhat discouraging, at least if you were an African country and potential recipient of one of those loans, and particularly if you were a rather powerless, defenseless citizen of one of those situations, depending upon the integrity of those in power—not only in the government—but also those dispensing funds who have some authority. They have revenues that can make a difference in this.

Both of you have stressed transparency, and the ability for the people in the country, and for the world, and for everybody else who may be interested, such as the U.S. Treasury, our State Department, and so forth, to peer in and see what is going on. At the same time, there are different cultures, different traditions and so forth. We understand from previous hearings, as well as this one, that people in the opposition would say, in quotes, "this is not the way the world works, this is the American view, and who are you, as Americans, to assert that there ought to be this degree of openness?" The world press, as well as the local press, have the opportunity to raise questions on the scene. I wonder, where are there enough study commissions out there in the world to take a look at all of these projects, to come up with some evaluation that might make some difference for us as we have some chance to look at all of this today? You, sir, have looked at some projects in detail. Will you take this opportunity to describe in more detail some of what you found, and why this is important, and what the bank that was involved in making the loans might have done differently, so that the results would have been more constructive?

Mr. WITHANAGE. Thank you, Mr. Chairman.

I think one of the big problems is people who are living on the grounds; they are not part of any decisionmaking with regard to the projects. In most of the cases, people know best, not the consultants and not the government officers who come from other places, they don't have any idea about the local situations. Now one of the examples which I explain in this one, which happened in 1977 which is a dam project, a construction of a dam, across one of the big rivers, and all the local scientists and the local people, they said, "Okay, if you construct this dam in a—it's a short dam, but it's a small reservoir—it will be more sustainable." But because of the political reasons, the Asian Development Bank and the local agencies, which is the irrigation department, they constructed the bigger dam, and they cleared more lands and brought so many people. So, if they heard the people and the local scientists, they would

not have had this kind of end results. So, this is one of the major problems.

The CHAIRMAN. Why did the dam construction result in difficulty? Could you make a case that it would help more people if you build a larger dam?

Mr. WITHANAGE. The issue is there is not enough water for a larger reservoir.

The CHAIRMAN. I see.

Mr. WITHANAGE. So, the river, it should be dependent on the river attachment, if the attachment is not adequate enough, then having the big reservoir is just a waste of funding, and also they cleared a lot of lands to allow more people to come to this site, and that also devastates the whole habitats.

The CHAIRMAN. So there's less water, there are more people, and there is a misalignment between the amount of water and the size of the dam. Your testimony, therefore, is that if you had been having local town meetings or some sort of hearings on the site and so forth, and people had indicated what the situation was, the decision might have been better than back at headquarters with whoever was planning this project.

Mr. WITHANAGE. I think the biggest problem here is now there's no adequate water and the people are suffering there, and the Asian Development Bank has a right to do something to correct this problem. So, this is my message, bringing this case to this forum.

The CHAIRMAN. So, you're saying now, in addition to the fact that after the ADB evaluates the thing and says, "Well, this is partially successful, or unsuccessful," what have you, still this is 1977 you're talking about, that's now 28 years ago. There ought to be some mechanism for correction of these errors, as opposed to simply chalking them up and indicating, "Sorry it all turned out badly for these thousands of people."

Mr. WITHANAGE. Yes, Mr. Chairman, because we are still paying this money back to the Asian Development Bank, so still we have a right to ask for them to correct this project, because the people in the field, they don't have water, and for the last several years, they didn't cultivate a single acre of paddy in that area, and people are suffering and because of the Asian Development Bank should spend their money and they have the funds to correct this problem, and give a better life for these people.

The CHAIRMAN. Now, this occurred in Sri Lanka, is that correct? This dam that you're discussing? This project occurred in the country of Sri Lanka?

Mr. WITHANAGE. Yes.

The CHAIRMAN. You know, sometimes, let's take a case in the United States. If such a thing occurred here, and there were material losses for lots of people, my quess is that a class action suit of some sort might have occurred. Specific farmers or landowners who were dispossessed and so forth might have filed lawsuits. What happens in Sri Lanka? Is there any recourse to people who believe that they have been either dispossessed, or badly damaged, or continue to be damaged? How does the legal system work at that point?

Mr. WITHANAGE. With regard to this project, there was no lawsuit, but Southern Transport Development Corridor, which I explained earlier, it's a case that went to the Appeal Courts, it's a case that went to the Supreme Court also, and the Supreme Court decided human rights have been violated, but it did not change the rule. So, the people are still fighting to change the rule, because the Supreme Court decision did not change the whole trade, so certain—in several other issues, there is a lot of public interest litigation in Sri Lanka with regard to mining cases—but in this particular case there was no such a case. But, it's happening, in Sri Lanka, that's one of the best case holders came because of the public interest litigation.

The CHAIRMAN. That was 1977. This is now. What is your observation currently about the ADB as it takes a look at civil society efforts to bring about better results, as well as to combat corruption? In other words, did you note improvement? Is there, out there in the field, a sense that times are changing?

Mr. WITHANAGE. In my opinion, in 1977 there was no policy for the Bank.

The CHAIRMAN. No.

Mr. WITHANAGE. Now, since 1995, Asian Development Bank has a lot of policy safeguards, policies accountability mechanism and access to information, various policies. But the two cases I want to state in this statement, because that's the same situation after having so much of policies within the Bank. We have the public affected people, so they have gone to the ADB asking justice from the inspection mechanism, and they wrote several letters with regard to the safeguard policies, but the Bank's response is the same, that they don't find any evidence. In one other case, with regard to the corruption, people got the same response after sending all of this information, they say they haven't got enough evidence, and at first they reacted, and later they say, "Send us more evidence." So, why are we having all of these policies, if they are not implementing at the ground? So, this is the question today that we have.

The CHAIRMAN. I thank you for that response. We've been joined by the distinguished Senator from Florida, Senator Martinez, who is the chairman of our African Subcommittee. Senator, I'd like to give you the opportunity to make a comment or raise questions of our witnesses.

Senator MARTINEZ. Thank you, Mr. Chairman. I really would just want to, first of all, say thank you to you for holding this important hearing, I think that some of the things that have been going on in this exchange—in a very different way—but I think in also a very common way, remind me of some of the work I did at HUD, and how difficult it was, and as you know, as a former mayor, we share that in common, how difficult it is to be in a department of government whose purpose it is to encourage and promote better housing for America, and then see that some of those very-needed funds are diverted for purposes that are not appropriate, and so fighting that very thing here in our country with domestic funds through well-intended entities that are formed for that very purpose. I always felt that it was really not taking from government, but it was really taking from a family that might be wanting to improve their housing, or a single mom with a couple of young chil-

dren who's trying to give them a nice, stable place in which to live. And so, in a way I also feel the frustration and the sense of loss when projects like you've been discussing occur in the international arena, well-intended funds that, and in this instance, not only—as you so well pointed out—that are not only diverted from the purpose to which they were intended, but that now create a tremendous burden on the country with debt. And so, I think this is a very important topic and a very important hearing, and I want to commend the witnesses for being here.

And I very much would like for the record to reflect, unfortunately because of another hearing, I missed the testimony of Director Sullivan who is a dear and wonderful friend, and a great public servant, and I know he, I saw him outside as we were coming in, and I'm very sorry I missed his testimony, but I know he's doing a great job of serving our country in an interesting place, and doing a great job with the European Bank of Reconstruction and Development.

So, Mr. Chairman, I just simply want to thank you for holding the hearing, and wanted to come by to, at least, glean a little bit of the import of this moment, and encourage those that are working in this international institution to continue to do the good work not only of the financial transactions that provide wherewithal for international development, but also to be vigilant about the appropriate usage of funds, the appropriate usage of projects, and as we see, so much need around the world. It is unfathomable that some of the misuses of the money would only add to the misery that we often, too often see, for lack of development. So, thank you, Mr. Chairman.

The CHAIRMAN. I thank the Senator, and particularly given your long experience in government and the responsibilities you have mentioned, as a Cabinet member and as a mayor, you have seen at the local level, as well as the macroeconomic level, the effects of what we're talking about today. I appreciate your endorsement of our efforts.

I'd like to ask you, Mr. Devine, you come as Legal Director of the Government Accountability Project, and you have been studying these situations in that role as well as during the totality of your career. What advice can you give to the U.S. Treasury or to the Congress, to us, in these areas of fraud and corruption related to development banks? You have made some recommendations in your testimony, but amplify these a bit more, in your own words. As a veteran of the trail of auditing these responsible officials, what do you think should be the priorities if you were in our situation?

Mr. DEVINE. Thank you, Mr. Chairman. I think with respect to Congress, one of the first things I could suggest is to do a lot more of what you're doing with my colleague this morning, making a record of the human consequences from the corruption. Groups like ours go to international conferences with NGOs and we hear the victims talking to each other, and it's very powerful testimony. It needs to be funneled into the oversight and legislative permanent record as a foundation for reform. Even if it's just written statements that are collected.

The second is following through with the temporary legislative mandate last year from the McConnell-Leahy amendments, and that's why our group is so appreciative and so available to help with your legislative initiative.

The third is to try and restore GAO's mandate for oversight within the institutions. They've been getting the whistleblower treatment since their hard-hitting reports at the end of the 1990s.

The CHAIRMAN. What do you mean by that? What sort of resistance is GAO getting?

Mr. DEVINE. Well, we've been understanding from talking with them that there are severe obstacles, procedural obstacles to releasing information to them.

The CHAIRMAN. From the banks?

Mr. DEVINE. From the banks. Yes, sir. The GAO contributions have been very thorough, sound, good faith, they might as well be working with your staff, the work that they do, and they deserve to be re-enfranchised, in our opinion.

The CHAIRMAN. What grounds do the banks have for resisting GAO? What are the arguments that lead to this resistance?

Mr. DEVINE. My understanding is that it's, we'd need to go into more specifics, but it's a clearance process that was established after the 1999 audit that GAO made of the World Bank. This has been spreading to some of the other institutions, and the clearance process has functionally resulted in their denial of timely information necessary to keep doing follow up, to find out what progress has been made since their earlier hard-hitting audits.

As far as the Department of Treasury, the first thing we think that they need to do is set some standards for these institutions, tell them what's expected. That was referred to briefly in my testimony. They're supposed to be making specific recommendations, and they skip that step in the McConnell-Leahy amendments. To illustrate, we had a very inspiring meeting with the Assistant Secretary of the Treasury, where he was calling for the NGOs to rally behind U.S.-led reform efforts and help get grassroots support. But then when we contacted his office to find out what reform efforts we should be recruiting people to rally behind, we couldn't get our phone call returned. They need to set down some standards that they're pressing for.

A second thing would be to unleash their Office of Inspector General. They have a "hands-off" policy there. But these are U.S. taxpayer funds which are at risk, it should be part of their work. That's an example of what we think the Treasury could do.

Another way they could do this is by calling the rhetorical bluffs at the bank. For example, if the IG can't go in and gather information then demand that the banks provide proof of results behind their rhetoric. It seems like too many things are just taken at face value. If there's a good meeting, the problem gets credit for being solved. And we need proof. I think for all of us, there's a few steps that could really help. And the first is to pin down the track records of these institutions in terms of actions, not just program descriptions. What we're learning is, despite all of the reports and procedures, nobody's been helped by the whistleblower systems, or almost no one has been helped, or no one in this millennium. That's really the point of all of this.

A second would be to support the pioneering work of Professor Vaughn at American University Law School. This has the potential to be a beachhead for transparency reform.

The CHAIRMAN. What is he doing?

Mr. DEVINE. He was commissioned by the World Bank to recommend an overhaul of their whistleblower system, and what we've learned over and over is that they're setting the pace for the regional development banks. And Professor Vaughn was a coauthor of the model whistleblower law to implement the OAS Inter-American Convention against Corruption, and he's state of the art in terms of academic expertise for standards.

I think another thing that we might consider doing, all of us, is encouraging Mr. Wolfowitz, the new World Bank leader, to adopt whistleblower rights as a flagship issue there in the hope that that can be contagious at the regional institutions.

The CHAIRMAN. Well, that's an excellent suggestion. Mr. Wolfowitz is starting out in that new responsibility and has had a very strong organizational track record. And in fairness, Mr. Wolfensohn, whom he is replacing, and with whom I visited personally, and has offered assurances and some evidence, just as you're suggesting, of additional steps that the World Bank has been taking, and the seriousness that they have with this. So there seems to be some momentum there. I add just to offer an encouraging word in light of otherwise rather dispiriting evidence elsewhere.

But, it's a new phase. Let me just be very candid. Most of the international development banks are not used to questions such as the ones that we're raising today, certainly not in public forums. There is almost a feeling of temerity, with people raising these questions. After all, there's a big world out there and it's all very interesting for parochial people to be raising these questions esoterically, but I think bit by bit people understand the point that I'm making without being repetitious, and that is that there are American taxpayer funds involved in these banks. Revenues don't just simply come out of the blue, and there's going to be responsibility for those funds, whether the banks like it or not.

So, as a result, as I suggested to the first panel, if our American officers of these banks are running into some resistance from others, whoever they may be, our Secretary of State needs to know that, our Under Secretary needs to know that, maybe I and members of this committee need to know that, because there will be consequences from that. And I think, without being tedious, that needs to be understood. What you are saying today is a serious matter.

Now, the fact that they have not been explored very extensively in a public forum for a while is too bad, but nevertheless, they are being explored here, now. This is the fourth hearing we've had in a series in which, it seems to me, things are beginning to happen. I cited a few in my opening statement. Other countries are taking more seriously their role as legislators, because they have funds, too, they have taxpayers, and they have press and open democracies. You wonder who is blowing the whistle, who has accountability for all of this?

Now, finally, at the end of the day, there can be honest differences on projects. That is why I get back to more scholarly re-

search, as you were pointing out, Mr. Withanage. Out in Sri Lanka, you have 128 projects. Some studies have been made. You've made some yourself. You have made some assertions about whether they work, whether they don't. In fairness, the Asian Development Bank made evaluations. They can be questioned as to whether they were too sanguine about what they saw. You allege that in some cases we were really not very successful at all. There was a failure in costs, including debt for Sri Lanka, but at the same time, there have been some efforts. This will be something that our committee will want to explore even more. What kind of scholarly effort is there with these large sums of money involved? Just for Sri Lanka alone, $3.4 billion is a lot of money. And the ramifications for that country have been substantial, for better or for ill. But this is just one part of a very large number of countries and people that are involved here. This is the reason I ask you the question, Mr. Devine, because your group has attempted to get into this.

Now, what kind of funding or support do you have? Who is behind you? Why would they be interested in all of these issues?

Mr. DEVINE. I think the only funding we've had so far, and I might be wrong on this, is from the Ford Foundation.

The CHAIRMAN. The Ford Foundation hasn't been a grantee to you.

Mr. DEVINE. Yes, sir; they've made a commitment to this issue as one of their cornerstones for their civil society initiatives. I just second so much the statement that you made about the taxpayer funds. Our usual work is trying to have taxpayer accountability. And one of the things that got us into this was that Treasury, for so long, had been giving a free lunch to the banks and they were using that funding to buy junk food that might as well have been contaminated with *E coli* and *Salmonella.* It was putting good money after bad, and we can say that this is a time when, maybe, the stagnation is ending.

Just from personal experience, about a year ago our group went to the EBRD to follow through on our research and they told us that they only talk to governments, and we weren't, so goodbye and nice of you to drop in. Last fall, the EBRD's new Deputy Compliance Chief teamed up for a consensus whistleblower principles. We feel that now is the time to really step up our efforts, because they're starting to get results.

The CHAIRMAN. Well, this is good news, and we are grateful for your recognition and that the Ford Foundation grants and perhaps other foundations in our society outside of government will be seized with this issue, too. It is a humanitarian issue of great proportion, as you gentlemen are illustrating today. Because debt occurs for countries, and we're concerned about that, sometimes, when we're seized with the problem we forgive debts, wholesale, debts that were created in the same process. Ultimately our committee is enthusiastic about international relationships. We are proponents of that, advocates of that situation. Some Americans have less enthusiasm for that. Our country goes through periods of protectionism and isolationism, and I don't stress those sad times, but we've been through some of that, and frequently there's attention as to what we should be concerned about.

We're, prospectively, trying to raise in this committee, the courage, the will, maybe the wherewithal, for people to do better who want to do better in our international banks. Those include very fine American administrators who were confirmed by this committee, and by this Senate as a whole, and have responsibility, frequently, for these situations. So, this is a long editorial, but it is to reinforce some of the efforts that you are making, and a recognition of the time and effort you have given to preparing your testimony.

Now, it's an encouragement to do more. So, before we have any more hearings, and in the interim period, as you might accumulate additional information, and you might have studies that would be relevant and helpful for the committee and the American people, please be forthcoming. Because that, I think, will help the people who are out there in the world to understand that these banks are attempting to help, and that a large majority of all the civil servants of all the countries involved are attempting to help, but they may need our help in order for this transparency, these checks and balances, this thoughtfulness to occur.

Let me ask the two of you if you have any final comments before we conclude the hearing.

Mr. WITHANAGE. Thank you very much. It's the public funds going from these funds to do something, do development in my country, or any other third world country, it's the name of the Asian Development Bank, which means the development. Why the money from the public funds goes in the name of the development in my country to destroy the existing resources, to destroy the sustainable life of the people. So, this is the question we had when we were starting all our advocacies with the international financial institutions. That is why we got together, and that is why we are raising these questions, together with the donor agencies, the private foundations in the United States and other countries, and with the Civil Society Organization in these countries to bring this voice to the relevant agencies, the decisionmakers of the international financial institutions. So, this is the very basic issue, and the people living out there in the villages, in the communities served, they are suffering day by day because of various ill-effects of the nonproperly planned, nonproperly designed projects.

Although we have these various new policies, safeguard policies, that doesn't affect, or that doesn't give any support or protection to the people living there. So, this is, we are expecting something from this particular committee that if you are able to change the views of these visions, and the implementation procedures of these international financial institutions, we hope, at least, that will give some more benefits to the people. So this is what we are asking, and the corruption should be totally, really removed from all of these efforts, so the corruption has various different level which is from the local agencies up to the big companies, and the big, maybe the international financial institutions, although I cannot pinpoint these other particular people, but this is there, and we need to somehow remove all of these corruption issues, which hinders the real development in our countries.

Thank you very much for giving this opportunity.

The CHAIRMAN. I appreciate that. Mr. Devine, do you have a final thought?

Mr. DEVINE. Yes, Mr. Chairman, I have two. One is the cornerstone for legitimacy of the whistleblower policy at any of these banks, and that is to end the underlying premise of all of them currently, which is, they're serving as official secret sects. In reality the policies all are institutionalized gag orders that theoretically protect free speech within institutional walls, but make that a firing offense if employees commit the truth outside of the banks. For example, if a bank employee who is protected for making a disclosure internally, bears witness with the same evidence before this committee or before the inspection panels that are responsible to redress citizen grievances, that would be a firing offense. There is a very significant precedent that the United Nations just adopted with the active participation of this committee. That's the first time in my experience there's been a breakthrough on public free speech rights, and we hope that beachhead can be expanded.

My second comment is to say, thank you for your leadership. Without it, we'd all be on the road to nowhere, and you can count on us to do our share on the follow through.

The CHAIRMAN. Well, thank you very much for your testimony, both the written statements and your forthcoming responses. We are grateful to you. My invitation to give us some more is ongoing. We thank you and the organizations that support you. Having said that, the hearing is adjourned.

[Whereupon, at 11:32 a.m., the hearing was adjourned.]

ADDITIONAL STATEMENTS AND OTHER MATERIAL SUBMITTED FOR THE RECORD

PREPARED STATEMENT BY AMBASSADOR CYNTHIA S. PERRY, U.S. EXECUTIVE DIRECTOR TO THE AFRICAN DEVELOPMENT BANK

Mr. Chairman, Ranking Member Biden, members of the Foreign Relations Committee, thank you for inviting me to discuss the efforts of the African Development Bank Group (the Bank) to combat corruption.

Let me at the outset emphasize that corruption on the African Continent remains a major impediment to economic growth and poverty reduction. Far-reaching changes are required to reduce it dramatically. As the premier development institution in Africa, the Bank is at the center of our efforts to combat corruption and improve aid effectiveness in African countries.

The United States has advocated and pressed strongly for greater transparency and improved governance at all levels of the Bank's operations and management, and we will continue to do so. While the Bank has made significant progress in terms of institutional accountability, transparency, and operational controls, further efforts are needed. I would like to focus my statement, today, on the Bank's efforts to combat corruption and strengthen governance in three related areas: At the institutional level, the project level, and the country level.

The Bank's anticorruption efforts aim to reduce the risk of corruption in its operations and increase the amount and quality of assistance to its regional member countries in support of good governance. The Bank is also actively promoting good governance through a number of partnerships with regional and international organizations, which I will highlight for you.

INSTITUTIONAL EFFORTS

At the institutional level, the Bank has made good progress toward mainstreaming anticorruption efforts into its functions as a development finance institution. The Bank's Policy on Good Governance, approved in 1999, emphasizes combating corruption as one of the pillars of the Bank's mandate to promote good governance in member countries. The Bank's Strategic Plan for 2003–2007 also un-

derscores the linkages between good governance, including combating corruption, and the Bank's poverty reduction mandate. To strengthen these linkages, the Bank has put in place effective internal controls and procedures intended to deter, detect, and punish corrupt practices.

The most important institutional reform that the Bank is currently undertaking is to establish a Anti-Corruption and Fraud Division alongside the existing Internal Audit Division, both of which will report to a new Office of the Auditor General. The Anti-Corruption and Fraud Division will be the focal point for investigating allegations of fraud and corruption with respect to the Bank's operations and staff. A high-level Oversight Committee on Corruption and Fraud will provide oversight on policy compliance. The proposal to establish the new institutional structures is working its way through the Board's audit committee, and we are hopeful that the Board will approve it shortly after the Annual Meetings in May. My office is focusing on this initiative as its current number one priority.

Once it is established, the Anti-Corruption and Fraud Investigative Division will also manage the implementation of a formal whistleblower protection program designed to protect the identity of those disclosing information or reporting allegations concerning fraud or corruption.

In the past year, the Bank has developed a Code of Conduct for Bank staff, Guidelines for Preventing and Combating Corruption and an Information Disclosure Policy, all designed to increase transparency, enhance the professionalism of Bank staff, and standardize the Bank's interactions with its clients.

- The Code of Conduct for staff is a statement of basic ethical principles to guide Bank staff in the fulfillment of their duties. Failure to abide by the Code of Conduct results in sanctions, as specified in the Bank Staff Rules. As with any large organization, not all staff abide by the rules and laws. In recent years, the Bank has disciplined, and in some instances terminated the services of staff after determining their involvement in corrupt or unethical practices related to Bank operations.
- At the insistence of the United States, we are in the process of reviewing the Financial Disclosure policies of the Bank for its staff and management so that we can improve information collection and dissemination in order to avoid any conflicts of interest with Bank operations. Currently, all staff are required to submit a disclosure to Bank management and update it annually.
- Building on the Bank's good governance policy, the Guidelines for Preventing and Combating Corruption outline where and how corruption and fraud may occur in the Bank's operations, modalities for its prevention, and procedures for Bank staff to follow in responding to incidents of corruption and fraud in Bank operations. One of the key features of the Guidelines is the Bank's zero tolerance position with regard to fraud and corruption. In line with the Code of Conduct for staff, the zero tolerance position means that staff proven to have engaged in corrupt or fraudulent practice will be disciplined in accordance with Bank Staff Rules.
- With regard to transparency, the Board of Directors, with our strong support, approved a new Information Disclosure Policy last year, which will significantly enhance the transparency of the Bank's operations by making a wide range of Bank documents publicly available. As the U.S. Executive Director, I have been the strongest advocate in the Board for greater transparency, and will continue to lead this effort in order to achieve the goals specified in section 581 of Division D of the FY 2004 Consolidated Appropriations Act.
- At our urging, the Bank maintains strict recruitment procedures and is strengthening its capacity to combat corruption and promote good governance through staff training programs. In addition, the Bank continues to take steps to build its institutional capacity.
- In the area of recruitment, the Bank's procedures explicitly forbid nepotism or favoritism on the basis of nationality or group identification. Staff members who fail to comply with these rules are subject to reprimand, dismissal, or legal sanction.
- Internal staff training has been organized to promote the Bank's good governance policy and to familiarize operations staff with new diagnostic assessments such as the Country Governance Profile and new instruments such as Policy-Based Loans for Governance. Enforcement of the Bank's zero tolerance position will require strengthening the Bank staff's capacity to deter, investigate, and penalize corrupt activities. The Bank intends to increase the number of staff experts assigned to anticorruption activities, and enhance the technical skills of Bank staff through specialized training in areas such as forensic auditing, detection of money laundering, and financial investigation techniques. For example, in 2004 the U.S. Treasury Office of Technical Assistance conducted a train-

ing seminar for Bank staff on antimoney laundering and intends to continue its cooperation with the Bank in this field. Last year the Bank also conducted a very well attended two-day training workshop for Bank staff on the implementation of Country Governance Profiles and Policy-based Loans for Governance. In the Board of Directors and in dialog with Bank management, I will continue to stress the need for strengthening the capacity of staff working on governance and anticorruption activities in the Bank.

PROJECT-LEVEL EFFORTS

The Bank has instituted a range of controls to help mitigate the risk of corruption in its projects. These controls include auditing, supervision, the use of special accounts for higher risk lending, due diligence on private sector borrowers and cofinancers, and strict procurement procedures. The Bank requires annual audits of its projects and enforces contractual audit provisions in its loan and grant agreements. Through active participation in the discussions of the Bank's Audit and Finance Committee, my office reviews internal audit reports of Bank projects.

The Bank's Internal Audit Department safeguards the Bank's assets by certifying compliance with its policies and ensuring that auditing standards are met. A critical function of the Internal Audit Department is to assess the strength of internal controls and institutional arrangements in regional member countries and to assist national audit institutions with outsourcing audit functions until adequate national audit capacity can be developed. The Bank's Operations and Internal Audit departments evaluate the quality of independent audits of Bank projects, and implement the Bank's audit policy, which may include suspension of disbursements to some projects. Two projects (in Mali and Kenya) were investigated for fraud and corruption in 2004 and one (in Mozambique) is currently being investigated for fraud and corruption. Last year, the Bank terminated its involvement in four projects because of concerns about corruption. So far this year, the Bank has canceled one project due to similar concerns. Preliminary assessments have revealed some improvements in the submission of annual audit reports of Bank-funded projects, but the Bank needs to remain vigilant in its oversight to ensure project audit reports are completed consistently across projects in a timely manner.

Supervision missions focus on good financial management of projects as a way to eliminate opportunities for corruption. When compliance with financial management standards is lacking, the Bank proposes corrective measures and may impose sanctions. The Bank's ability to conduct supervision missions was significantly impaired by the temporary relocation of the Bank's operations to Tunis in 2003. The Bank is now fully operational at the temporary relocation site, and more frequent supervision missions have resumed. This year, in response to efforts by my office to implement the provision of section 581 of Division D of the FY 2004 Consolidated Appropriations Act pertaining to internal controls, the Operations Evaluation Department of the Bank will undertake an independent evaluation of the Bank's supervision and monitoring systems.

The Bank's procurement regulations were last modified in January 2000, to be more explicit in their treatment of fraud and corruption. As a result, the Bank will now cancel at least part, if not all, of a loan or grant for a project if the procurement process for the project was tainted by acts of fraud or corruption. Firms proven to engage in corrupt or fraudulent practices can be declared ineligible from participating in future Bank-funded activities indefinitely or for a period determined by the Bank. Over the past few years, about 30 tenders have been cancelled—4 last year alone and 1 so far this year. The Bank maintains a list of sanctioned or debarred firms and the United States believes it should publish this list. The Bank also shares information on sanctioned firms regularly with other MDBs through a network of senior officials responsible for procurement and anticorruption. The Bank is currently revising its procurement policies to bring them into line with the MDB harmonization agenda. The revised policies should be presented to the Board of Directors by the end of the year.

The Bank's Procurement Review Committee of senior managers and operations directors appointed by the President receives and investigates complaints from bidders who are not satisfied that their bid was handled in accordance with established Bank procurement rules. The committee is an independent body whose decisions, which can include cancellation of a procurement process, are final and binding.

To help improve corporate governance, particularly in private sector projects, the Bank has prepared a Corporate Governance Strategy, which will be discussed by the Board in the coming months. The Bank conducts due diligence assessments on potential borrowers to ensure full compliance with corporate governance principles for Bank-supported projects. The Bank also provides direct assistance to private sector

investors to endorse and implement corporate governance principles as a precondition for Bank financing.

Within the overall framework of promoting good governance, the Board of Directors has approved the establishment of an Inspection Function, a combined compliance and problem-solving mechanism. Prior to its approval, the proposal was posted on the Bank's Web site for several months to invite comments from interested stakeholders. Recruitment for the Director of the Compliance Review and Mediation Unit is underway, and the Bank expects the mechanism will become fully operational by the end of the year. My Office has been at the forefront of the effort to establish this inspection mechanism at the AfDB, which will reinforce the Bank's accountability for the impact of its project operations.

COUNTRY-LEVEL EFFORTS

The Bank provides financial and technical assistance to regional member countries in their fight against corruption. Requests for assistance are determined on a case-by-case basis and subject to a clear and credible demonstration of commitment to principles of good governance and combating corruption.

Since 2001, the Bank has approved more than $1.5 billion in loans and grants for governance-related activities in over 35 regional member countries. Following the successful completion of the Tenth Replenishment of the African Development Fund (ADF), the concessional window of the Bank Group, in December 2004, we expect this trend to continue.

Good governance is a key factor in determining country allocations of ADF resources during a given replenishment cycle. The Country Performance and Institutional Assessment (CPIA) is based on formulas that place nearly 60 percent effective weight upon the quality of governance in ADF-eligible countries. With the prospect of greater allocation of concessional resources, countries are encouraged and rewarded for making progress toward good governance.

Policy-based loans for governance (PBLGs) are an instrument that the Bank will use to support institutional reforms to consolidate macroeconomic stability and a favorable environment for sustained growth in its regional member countries. PBLGs will be used to support governance-related reforms in areas such as judicial and legal frameworks, trade policy, public finance, fiscal and monetary policy, public sector management, financial sector policy, and competition policy. The United States provided substantial input into the PBLG Guidelines, approved in 2004, to ensure that this instrument would be used only in appropriate policy environments. Since the approval of the guidelines by the Board, two PBLGs, for Malawi and Tanzania, have been approved. My Office will continue to monitor the Bank's use of this instrument very closely.

The Bank collaborates closely with the World Bank in conducting various diagnostic assessments of public financial management systems and recommends actions for implementation. To date, this collaboration has produced 12 Country Financial Accountability Assessments (CFAAs), in Burkina Faso, Chad, Gambia, Malawi, Mali, Madagascar, Mauritania, Senegal, Tanzania, Uganda, Togo, and Zanzibar. Since 2002, the Bank has also collaborated with the World Bank to carry out six Country Procurement Assessment Reviews (CPARs), in Benin, Senegal, Côte d'Ivoire, Angola, Togo, and Guinea. It is my hope that these collaborations will continue and strengthen in the years to come so that the two institutions can leverage off of each other's comparative advantages.

The Bank also conducts Financial Management Reviews of its projects. The Financial Management Review is an AfDB innovation designed to improve the financial management and audit functions of specific projects. The Bank has successfully carried out Financial Management Reviews in five countries (Cameroon, Madagascar, Malawi, Uganda, and Zambia), covering four key sectors (agriculture, transport, public utilities, and the social sector).

Another important and innovative diagnostic tool, employed by the Bank since 2002, is the Country Governance Profile. Country Governance Profiles are used to identify key governance issues in regional member countries, including corruption, and to develop a common understanding of the strengths and weaknesses of country governance arrangements. These profiles allow the Bank to better assess risks to Bank funds and to help countries develop governance reform and capacity building programs. The Country Governance Profile is the key instrument for mainstreaming governance priorities into Bank operations. The new cycle of Country Strategy Papers for 2005–2007 will address governance issues based on the governance profiles. To date 14 Country Governance Profiles have been completed (in Nigeria, Ghana, Mauritania, Malawi, Zambia, Chad, Cameroon, Benin, Kenya, Tanzania, Burkina-

Faso, Swaziland, Senegal, and Gabon), and an additional 5 Country Governance Profiles are scheduled for completion in 2005.

Institutional capacity in regional member countries is critical for effectively combating corruption and complying with the anticorruption safeguards in loan agreements with the Bank. For countries ranked low in the CPIA governance factors and where the risk for corruption is deemed high, the Bank will undertake more rigorous assessments through Country Governance Profiles, CFAAs, and CPARs, and propose corrective measures. Government officials from regional member countries will benefit from selective and specialized governance- and corruption-related training organized through the Joint Africa Institute, housed at the AfDB, in partnership with the World Bank and International Monetary Fund. Such training will be country specific and based on areas of weakness identified through assessments.

PARTNERSHIPS

The AfDB is actively engaged in partnerships with a number of institutions, to combat corruption on the continent. The Bank is an active member of the MDB Working Groups on Financial Management, Procurement, and Environment. The Bank is also collaborating on good governance promotion activities with the Economic Commission for Africa, and has conducted a series of workshops on developing national strategies and action plans for combating corruption in collaboration with Transparency International (TI), the World Bank Institute, and the Global Coalition for Africa. In 2005 the Bank hosted delegations from two specialized agencies mandated to combat corruption: The United Nations Office on Drug Control (UNODC)—the arm of the United Nations responsible for fighting corruption, and TI. The purpose of these visits was to explore possible modalities for cooperation with the Bank on combating corruption at the country level. Through ongoing discussions with such institutions, the Bank will endeavor to develop joint strategies and programs to complement its anticorruption efforts.

The Bank was the lead institution involved in developing the standards and benchmarks for banking, financial regulations, and corporate governance for the New Partnership for Africa's Development (NEPAD) initiative. It is providing technical assistance to the African Peer Review Mechanism (PRM) component of the NEPAD and will also participate in the first PRM scheduled for Ghana this year. The AfDB was also a key partner of the African Union in finalizing the Africa Convention on Combating Corruption. More specifically, Bank sector experts are participating in the peer review exercise in the areas of economic and political governance, banking regulations and standards, and corporate governance.

Responding to the call to tighten antimoney laundering controls after September 11, 2001, the Bank is actively supporting existing institutions such as the Financial Action Task Force (FATF), African regional FATF-style bodies, and specialized subregional antimoney laundering taskforces. The Bank cross references its development partners with the United Nations list of entities designated as terrorist organizations, and we are working with Bank management to use Treasury's Office of Foreign Assets Control (OFAC) list so that no Bank funds are abused by terrorists or money launderers. There has been, and will continue to be, very close cooperation between the Bank and the U.S. Treasury on finding solutions to end financial abuse. In addition, an internal Bank working group is exploring how the Bank can work with member countries to develop appropriate legal and regulatory systems and regimes to address the problem of financial abuse.

The Bank's participation as an observer in FATF meetings has allowed it to get acquainted with FATF rules, and to present updates on the Bank's efforts on a number of issues concerning financial controls in Africa. The Bank is also working with a number of African financial sector regulatory boards to inform its AML/CTF strategy, now under preparation. The Bank has secured financing from France to fund the development of this strategy on AML/CTF, which will include Guidelines and a Plan of Action and is expected to be completed this year. The Bank is also working to build a network with regulators, experts, bilateral partners, and IMF and World Bank specialists to strengthen its institutional capacity in the AML/CTF field.

CONCLUSION

Despite these significant and ongoing efforts to combat corruption and improve governance at the institutional, project, and country levels, the African Development Bank itself recognizes that additional efforts are required, particularly with regard to implementation and enforcement of existing policies and procedures, and strengthening the Bank's internal capacity to fight corruption. As the Bank works to build and strengthen the appropriate skills mix to carry out its good governance

promotion initiatives, I will continue to press the Bank to review periodically its organizational arrangements, procedures, and policies to ensure an appropriate enabling environment and strategy for combating corruption.

The Office of the U.S. Executive Director will continue to challenge and support the Bank to further strengthen its anticorruption efforts, enhance the transparency of its operations, and realize its objective of becoming the lead institution on good governance in Africa.

Thank you.

PREPARED STATEMENT OF ELDER AKIE HART, THE NATIONAL PRESIDENT OF THE MANGROVE FOREST CONSERVATION SOCIETY OF NIGERIA

The highly respected and distinguished chairman, Senate Foreign Relations Committee of the United States of America, other distinguished Senators, and NGO Committees of the United States, here present.

We, the Civil Society Community of Nigeria (CSCN) hereby commend the United States Senate for its active oversight role of multilateral development Bank in the collective mission of fighting poverty and to improve the living conditions of the developing countries.

The issue of "Combating Multi-Lateral Development Bank Corruption," in Africa, Asia, and European Regional Development Bank, today is another milestone of the democratic dividends of America to the developing world.

The African Development Bank is one of the sponsors of the 4th and 5th train of the NLNG (Nigeria Liquefied Natural Gas) project called NLNG PLUS, and this project as well as previously related trains 1, 2, and 3 have impacted negatively on the physical and human environment, development, and progress of Bonny Island, Rumuji, Soku, Ogba, Ayambo, Oguede, Peterside, Iwoma, Kalaibiama, etc.

It is an accepted practice for operating companies to set aside 2.5 percent to 3 percent of their total project costs for community development but in the case of Bonny, the whole companies budget, NLNG and others is not up to 1 percent and this has led to several reactions that has resulted to the death of those Bonny people, protesting for their rights.

The last communal uprising led to the intervention of Rivers State and Federal Government, to bring about peace in the areas. It is imperative to the State that before a project like NLNG is to be executed, the Environmental Impact Assessment (EIA) must be conducted to evaluate the effect of the project on the environment, but in this regard, nothing was done, which is a negation of the rule.

The Mangrove Forest Conservation Society of Nigeria (MFCSN) protested loudly, and a haphazard attempt was done. As at today, what NLNG/AFDB have is a conditional permit, with a list of several conditions that must be met before their conditional approval will be confirmed and certificate issued. AFDB was contacted earlier enough by MFCSN on 31/10/02 and 14/11/03 respectively to carry out the standards/compliance to National and International Environmental Conditions: In their response, we observed that there was no transparency. This is because a genuine public hearing ought to have been done in Bonny Island—host community of NLNG or any of the project communities. We feel the host communities are the "proximate sufferers" and cannot afford N50,000 to N100,000 to go to Abuja for such public hearing. This means that the few members of the host communities who went to Abuja were handpicked, friends/stooges of NLNG, the common people were not there and not even informed, too.

It is also worthy of note that NLNG/AFDB, acknowledged the fact that the project did not meet the due diligence standard of AFDB/World Bank, as their consultant of that of NCM—report bank said so in their report. Surprisingly, AFDB granted the loan without addressing the issues raised which we believe was not ordinary in view of the millions of dollars paid to consultants/company officials by TSKJ—the consortium handling the project.

Today, Bonny, Rumuji, Soku, etc., bear the scars of the AFDB corrupt influence of unfulfilled promises. It is also painful to state here that Bonny community was not the only community that lost lives to such wicked marginalization and repeated brutality, oppression, and suppression of the people by the police, sent by Government on the request of NLNG.

Bin Tolo in Malaysia cannot be compared to Ilioma in Bonny where NLNG has altered its geographical location with AFDB funding, to the extent that access to the community is difficult due to pipe lines crisscrossing and pipe laying havocs.

The impacts of NLNG/AFDB's funded activities in Bonny

1. Destruction of forestry;

2. Housing crisis due to unplanned population explosion;
3. Reduction of fisheries on the sea;
4. Deterioration of road due to heavy-duty vehicles and unanticipated increased usage;
5. Educational pressure, in terms of more students for schools and no new schools, no teachers, as the few prefer the casual work at the sites;
6. Increased traffic accident/crime;
7. Inflation and loss of income;
8. Overstretching of public utilities like water, electricity;
9. Transportation hardship—more people using fewer roads.

AFDB in other parts of Nigeria

From the interactions of the NGOs/CBOs movement, we discovered that AFDB-funded projects are full of deceit and corruption, such as the Bonny project, the Edo state water project, etc., funded by AFDB to the tune of $300 million led to the importation of rusty and obsolete pipes now lying waste with no water. While Edo/Delta States are now saddled with the deduction of several millions as interest payments, not even the principal. This has led to deepening poverty, money that could have been used for other developmental projects, is now used to pay fake debts and Edo cannot even pay salaries of its workforce due to these dubious debts.

Edo/Delta State landed in this trouble because AFDB did not follow its internal control in granting such loans. Its officials were corrupted to look the other way and the Vice President of AFDB confirmed that they (AFDB) did not do what it is supposed to do which has confirmed that the process was irregular.

African issue

On further investigation, we discovered that the same corrupt influences occurred in AFDB-funded projects in Lesotho and Uganda which means that urgent and radical solution is needed, if AFDB activities must impact positively on the people and we see U.S.A.

Commendation/recommendation

1. We commend the U.S.A. Senate for its interest in the true development of Africa through its support to AFDB and its further interest to see that intended goals are met.
2. We appreciate the Anti-Corruption Crusade of His Excellency, the President of the Federal Republic of Nigeria, Chief Olusegun Obasanjo. He needs international support in his antibribery crusade. His Excellency is tackling both the giver and receiver at the domestic level. We, therefore, suggest that the international community should be ready to tackle the Multi-National Companies like Halliburton that involved in NLNG/AFDB bribe/stealing of radio-active materials in Nigeria that led to its ban and it did the same in Iraq, too. The question is that what is the position of the American Congress to curb this menace, especially as this is an American Company. The Secretary of U.S.A. blew the lid off the bribe.
3. Transparency International should also beam its categorization of not only corrupt countries but also the countries of origin of bribe paying Multi-National companies, so that we would know their corruption index, too.
4. It is very important for American Government to play more roles in AFDB's activity. It should go beyond broad policymaking to active participation as one of its financiers as the social and economic impacts of its operations are impoverishing the people, leads to human rights abuses and giving loans not used for productive activities.

Summary

AFDB activities have impacted negatively on Africans, instead of the positive and purposeful ways it was designed, because of its involvement in corruption.

Therefore, current strategies to curb this ugly trend are welcomed. It should be strengthened and new policies made to eliminate it with U.S.A. playing more active role that is beyond policymaking.

The U.S.A. should also investigate and solve the issue of bribe—giving in the form of P.R. or Lobby by Western Multi-National Companies.

MINUTES OF THE 659TH SESSION OF THE SENATE OF THE ITALIAN REPUBLIC, XIV LEGISLATURE, SEPTEMBER 28, 2004

I hope the Assembly will understand and appreciate this commitment, approve it and sustain it with actions suitable to guide it and promote it.

PRESIDENT. I postpone continuation of the debate on the above-mentioned Bill to another session.

Continuation of the debate on the following Bill: (2667) Italy's financial contribution to replenish the resources of international funds

PRESIDENT. The item on the agenda is the continuation of the debate on Bill No. 2667.

I remind everyone that the general debate on the topic began in the September 23 morning session.

Senator Martone is scheduled to speak. During his remarks he will also address agenda item G1.

Senator Martone has the floor.

MARTONE (Green Federation/The Union). Mr. President, honorable colleagues, Mr. Under Secretary, the acronyms that fill the Bill being debated distract us from some of the great challenges that the international community has been facing for decades: from the fight against poverty to a sustainable development, from the reduction of the foreign debt to the fight against hunger and underdevelopment in Africa.

The GEF [Global Environmental Facility], an organization established before the 1992 Rio de Janeiro Conference by the UNEP, the UNDP, and the World Bank for the purpose of protecting the world's public resources (water, biological diversity, climate, the ozone layer), is a case in point. Its efforts, however, are often jeopardized and counteracted by destructive development projects financed both by public funds and private banks, including the World Bank. Another case in point is the Trust Fund to support the HIPC initiative, whose launch was unduly delayed, and which is struggling to effectively attack the foreign debt problem of the developing countries, cornered as it is between the lack of political will on the part of the creditor governments, and access criteria that are based primarily on macroeconomic concerns rather than on those that promote human development.

In these remarks, however, I want to focus on the IDA (International Development Association), an agency of the World Bank Group that is dedicated primarily to lending to developing countries—to the poorest countries among them.

The most recent negotiations for the thirteenth IDA replenishment, which ended in 2002 and which is under discussion today, centered around several crucial issues, the most important of which referred to the percentage of IDA funds to be used as donations and the percentage to be used as repayable loans, albeit at zero percent interest.

The issue at hand, ultimately, is whether we should increase the yearly percentage of donations, which is now 34 percent of IDA's annual budget, to 50 percent or more. While such an increase would undoubtedly entail, on the one hand, a lowering of the debt owed by the impoverished countries over the long term, it would, on the other hand, gradually deprive the World Bank of financial revenue resulting from repayment of the loans.

This American strategy (the United States is a leading supporter of this shift from loans to donations) is being met with opposition, now as in the past, by the European countries because it masks a desire to see the IDA's budget gradually shrivel up, whereupon the aid from the World Bank would be progressively and easily replaced by bilateral aid that would be more open to political control and influence. Such a change would in effect bypass the governments. It would constitute, by and large, a privileged source of financing for the leading private United States charity organizations that are often willing partners in the U.S. Government's foreign policy, and, as such, apply selection criteria driven exclusively by political and strategic convenience.

The "grants versus loans" issue is also being debated at the non-governmental level. In fact, many observers believe that the gradual replacement of loans with donations would make the IDA simply another agency in competition with the UNDP, a United Nations specialized agency that already distributes donations, in effect making the latter superfluous.

Hence there is a contradiction in mandates, in the roles assigned to the World Bank on the one hand, and to some specialized United Nations agencies on the other. This contradiction is currently jeopardizing many of the United Nations efforts to fight poverty and to promote sustainable development.

The 2002 Monterrey Conference on "Financing for Development" tried to address this contradiction. One of its recommendations was to strengthen the role of the ECOSOC (United Nations Economic and Social Council). However, the Conference took no position on what we see as the fundamental factor (especially today, with respect to the possibility of reforming the United Nations), i.e., the proposal, put for-

ward by many parties, of creating an Economic and Social Security Council to address and resolve the root causes of these contradictions.

Other issues surrounding the IDA are also under discussion. One concerns specifically the basic philosophy and the intervention criteria that underlie aid for development and international cooperation. Among these issues, I would like to recall the discussion being held within the IDA about the role of the private sector and the possible use of these public funds (which are earmarked to fight poverty), to expand the private sector's direct foreign investments or to expand privatization programs that in fact would entail, among other implications, the introduction of fees for the use of basic social services.

The effectiveness of the private sector is one of several crucial issues being discussed in the debate over strategies to fight poverty. However, this discussion is based on purely ideological assumptions that we believe could subvert the very meaning of international cooperation, for example, through the introduction of user fees.

We believe that an approach that seeks to attach a monetary value to the fundamental rights of citizens, such as the right of access to welfare, to basic services such as health and education—which, quite to the contrary, should be removed from the marketplace and guaranteed public access—is unacceptable.

The second crucial issue in the fight against poverty, and therefore also in the context of IDA discussions, relates to the principle of aid selectivity. This concept has been defined by World Bank economists. According to this definition, the Bank's meager resources should increasingly be given more and more to "best performer" countries, i.e., to those governments that decide to open up their economy, removing barriers to private foreign capital and making the free market and privatization cornerstones of their development strategies.

We believe that this possibility constitutes a serious attack on the sovereign rights of governments, on the very principle of economic sovereignty of each nation, which is enshrined in the United Nations Charter. Aid selectivity is one of the most devious tools for creating a global market and for imposing in an unchecked, undemocratic way, the Washington Consensus.

However, today's debate also allows us the opportunity of discussing more contingent issues.

In the next few days—tomorrow or the day after—the World Bank and the International Monetary Fund will hold their annual meetings in Washington. Our government is under pressure to pass the finance bill and go to Washington with our house in order.

I wish to remind my esteemed colleagues that this financing also is extremely late with respect to the original schedule. In any case, the fundamental issues that will be debated at the sixtieth annual meeting of the World Bank and the International Monetary Fund revolve, first of all, around the need to inject innovative and radical ideas into possible solutions for the foreign debt problem of developing countries.

Two important proposals are being put forward on this issue. The U.S. Government wants to write off 100 percent of the multilateral debts held by the World Bank and the International Monetary Fund. The British Government also has a similar proposal for next year's G–8 Summit.

Apart from the two above proposals, we believe that there is still an urgent need to craft truly participatory processes, whereby the debtor governments may participate in the same degree as the creditor governments, and thus moving beyond the confines of exclusive bodies, such as the London and Paris Clubs. We also envision the participation of the civil society groups and communities that suffer the most from the burden of foreign debt, through the use of international arbitration rules. Governments and community action groups around the world—and even the United Nations—have already put forward such ideas with regard to Argentina.

On this issue, we believe that the last G–8 Summit meeting held in Sea Island offered some encouragement, since it voted to continue support of the HIPC initiative (criticized by many observers as being "too little, too late") extending it for two additional years. However, it did not review the access guidelines, hence preserving an exclusively economist-oriented approach instead, of a development-oriented approach. It also failed to recognize that in its eight years of existence, the HIPC has yielded only partial results, having cancelled only one third of the foreign debt of the poorest countries—countries that today still groan under an overall debt of US$90 billion.

This is the fundamental contradiction: the G–8 countries did not hesitate to discuss the need to completely cancel Iraq's debt, using the foreign debt issue simply as another tool of foreign policy, in a purely discretionary and opportunistic manner.

Even James Wolfensohn, the President of the World Bank, in a recent interview with the Financial Times, denounced this inconsistency: more and more funds are

being set aside for war and weapons, and the attention that the international community concentrates on the fight against terrorism detracts from the priority of fighting poverty, of reaching sustainable development and of writing off the debt.

I would like to remind you that according to the most recent UNDP report on human development, the amount of money that the countries of the Southern Hemisphere send to our cash registers in the form of debt repayment, lack of market access, and so on continues to be enormous: a total of about US$200 billion.

Contrast this to the fact that (as reported by Wolfensohn in the Financial Times interview), the world spends US$900 billion on weapons every year, a figure that is 20 times the total amount of public funds distributed for development purposes world-wide. This inconsistency is proof that not even the international community was able to profit from the peace dividend that many of us hoped would be generated from nuclear disarmament and the end of the rivalry between the Eastern and Western blocs.

In addition to these commitments that were not followed through, there are other issues that we believe our government should support, with greater effort, issues that worry not only us, the community action groups and NGO's of Italy and the rich countries, but also, and especially, the civil society organizations that are active in the developing countries.

Important, worthy initiatives supported even by the World Bank such as the Commission on Large Dams [sic] or the extractive industries review have fallen on deaf ears. The moratorium on the construction of large dams, the principle of prior informed consent, the principle of compensation to the local communities for the damage sustained as a result of destructive projects, the moratorium and support of the extractive industry (which could also help in starting to reduce the dependence of our development models on oil by promoting renewable, small-scale energy sources and the principle of sovereignty with respect to energy), have thus far come to naught. As a matter of fact, the commitments of the World Bank are in contradiction with its own recommendations.

For the above reasons, we believe that the Italian Government should have a more decisive voice on the World Bank Board, to ensure that these recommendations and requests are finally accepted and implemented, since they result from a process of bilateral cooperation that has involved governments, international financial institutions and civil societies working together to formulate suggestions.

Finally, I would like to add that the World Bank Group has a leadership role in strengthening approaches and methods with regard to development aid. Accordingly, the correct application of internal safeguard standards in the assessment of social and environmental impact, public consultation, participation, access to information, and third-party objective evaluation of its projects and plans constitute some of the best guarantees for an independent check on the work performed by these entities and on the use of the public funds that Italy gives to them (in the case of IDA, every three years).

Notwithstanding the above, and notwithstanding the encouraging position that President Wolfensohn took early in his term in office, we continue to watch the World Bank and its management as they endeavor to weaken and loosen the abovementioned safeguard measures, by granting to the governments of the countries that receive the loans, greater discretionary power in defining the social and environmental standards by which they must abide.

In our opinion, this could cause further serious damage to the quality and effectiveness of the actions of the World Bank and the use of public funds. Damage would also be inflicted on the functionality and mandate of independent evaluation mechanisms, which Italy supports as well, such as the Inspection Panel.

The effects of this change in direction—which is being discussed right now by the International Finance Corporation (the World Bank agency in charge of the private sector, among other duties), could be very serious indeed. On this matter, I would like to mention my personal experience. A few months ago I attended the Americas Social Forum in Quito, Ecuador. On that occasion, a sort of "people's court" on the World Bank and on food sovereignty was set up, with the participation of campesino leaders, union leaders and activists from Latin America who work in the area of food sovereignty, the right to water and the right to food.

According to the above testimonies and in keeping with factual evidence, in Latin America the World Bank has a policy of supporting the expansion of intensive, single-crop farming and of GMOs (genetically modified organisms) as well as the privatization of water. This is an encroachment upon a country's sovereignty in terms of food supply; it also creates a condition whereby our countries and the aid agencies begin to build a real ecological and social debt toward the indebted countries (who in this case become creditors).

Last but not least, I want to call your attention to the investigation that is being conducted by the United States Senate Committee on Foreign Relations about reports of corrupt practices with respect to World Bank development projects, some of which, such as the Yacyretá Hydroelectric Project (between Argentina and Paraguay) and the Lesotho Highlands Water Project (in Lesotho) are also using Italian companies and Italian public funds through bilateral cooperation and export credit mechanisms (SACE—Society for Alternative Culture and Education, an NGO).

To give you an idea of the magnitude of the problem, I wish to remind you that detailed, independent and reliable analyses that are included in internal World Bank documents, show that in the case of Indonesia, at least US$8 billion of World Bank funds were allegedly lost due to the corruption of those governments and even of World Bank officials.

In addition, according to a report by Richard Lugar, Chairman of the U.S. Senate Committee on Foreign Relations and a Republican (therefore someone who undoubtedly does not have great support for the views of my political group, but whose own views must be mentioned, in deference to fair political reporting), since 1946, because of corruption, at least US$130 billion in World Bank funds were diverted from their institutional targets.

We believe that this sort of situation can cause great harm to the very institutional mandate of the World Bank, its credibility, and its effectiveness, further increasing the foreign debt of the developing countries.

Therefore, it is imperative that the Italian Government commit itself to support reform initiatives to make these institutions more accountable for their activities and to tackle the main cause of corruption, strengthening the oversight and transparency mechanisms in contract-awarding procedures and public access to information, and proposing, among other solutions, the creation of an independent oversight body to serve as watchdog and prevent the embezzlement of funds earmarked to fight poverty.

Given the above considerations, it is compellingly clear that the Parliaments themselves must exercise more control. We are sorry to see that this room is almost empty precisely when we are discussing vast amounts, such as the €500 million or more that will be earmarked for this institution, which, as I have tried to explain, is often all too happy to act in ways that contradict its very reason for being, outside of any parliamentary oversight.

We therefore believe it is important that we continue to insist, in all venues, that these entities become more transparent. The agenda item and the amendment that I submitted with some of my colleagues address this issue, and I trust that the government and the sponsor will accept them.

In an old confidential World Bank document that was leaked and created a lot of scandal (starting with the fact that it was leaked), some evaluators of the World Bank's activities stated that institutional loss of memory goes hand in hand with institutional optimism.

What they meant was that the World Bank is often all too willing to forget the damage it inflicts, while continuing to offer an optimistic view of its work. As far as institutional policy is concerned, the World Bank tries to give more importance to the amount of funds it disburses rather than the quality of the disbursements, since it is incapable of learning from its past mistakes, mistakes that are highlighted in its own original documents.

I believe that this Parliament, together with the civil society and community action groups, can and must treat this lack of memory not with a homeopathic cure, but with a radical treatment, by better monitoring the political orientation of the World Bank's activities, thus contributing, albeit modestly, to a renewed focus on politics and democracy rather than on market and laissez-faire imperatives.

We are convinced that an ideology centered on neo-liberalism and the Washington Consensus has already shown so many limitations and incompatibilities. So much so, in fact, that our first imperative is now to rethink, immediately and radically, the very reason for being of institutions such as the World Bank and the International Monetary Fund—institutions that have continued to champion a laissez-faire ideology and have relentlessly carried that ideology out.

PRESIDENT. The general debate is ended. The sponsor has the floor.

CASTAGNETTI, acting sponsor. Mr. President, I waive my right to speak.

PRESIDENT. The government representative has the floor.

MAGRI, State Under Secretary for Economy and Finance. Mr. President, as mentioned, Bill No. 2667 authorizes Italy's participation in replenishing the resources of several International Funds such as IDA–XIII; the Special Fund of the Caribbean Development Bank–V; GEF–III; the African Development Fund–IX; IFAD–VI and the replenishment of the HIPC Trust Fund. The Italian Government took on these commitments in 2001–2002.

The Senate Bill No. 2667 was duly approved by the Foreign Relations Committee on March 3rd, and was also approved by the Budget Committee.

It is important that Parliament approve this bill before the end of the year in order not to lose the corresponding financial allocation for the 2004–2006 three-year period. Failure to approve this bill would also have a heavy negative impact upon Italy's image in the context of international financial relations on public aid to development, since it would postpone indefinitely the payments that our country owes, thus increasing the already long delay that has accumulated up to now.

Unfortunately, we agree with Senator Martone that these all-important measures are not receiving the attention they deserve.

To give you an example, I briefly recall that the International Development Association, part of the World Bank Group, is the leading source of financing for the 79 poorest countries of the world, those countries whose per capita income, in the year 2000, was at or below US$885.

The Special Fund of the Caribbean Development Bank is the fund-disbursing arm of the Bank—Italy has been a member since 1988. Said agency grants low-interest loans to countries in the Caribbean area. It is financed with contributions from its member countries and its leading goal is to reduce poverty and increase social development.

The Global Environment Facility is a multilateral fund managed by the World Bank and composed of 173 member countries, to which 32 donor countries contribute financially. Its projects, approved by a specially appointed Committee, are carried out by three implementing agencies, i.e., the World Bank, UNDP and UNEP.

With respect to replenishing the financial resources of the African Development Fund, I recall that this Fund is the loan-disbursing arm of the African Development Bank. Through low-interest loans it finances projects and plans in the poorest countries that would otherwise be ineligible to receive bank loans.

At present 38 countries, mostly from Sub-Saharan Africa, have access to the funds of this agency. This area is definitely among the poorest in the world, hence the African Development Fund represents one of the most important resources for these countries.

The IFAD, the International Fund for Agricultural Development, is especially dear to us. With its headquarters in Rome, it was established in 1978 as the thirteenth specialized United Nations agency, the result of a decision taken at the 1974 World Food Conference.

The IFAD's main goal is to supply direct funds and mobilize additional resources for programs promoting the economic development of the poorest populations in rural areas, mainly by improving the productivity of agricultural projects.

Most of IFAD's resources are made available to low-income countries in the form of loans on highly facilitated terms, such as a 40-year period for repayment of the principal with a 10-year, no-interest grace period (but with a yearly service fee of 0.75 percent). Any State that is a member of the United Nations or a U.N. specialized agency may participate to the Fund.

The Fund has designed and carried out several different environmental, socio-economic and cultural projects, financing more than 600 projects and programs in 114 countries. It has also funded donations for technical research and assistance amounting to about US$420 million.

For each dollar invested on behalf of the poorest among the rural populations, IFAD has mobilized US$2.9 from the donor countries, for a total of about US$22 billion. Therefore, considering the scarcity of available resources, resource mobilization has always been one of the leading roles of this entity.

Finally, there is the replenishment of the HIPC (Heavily Indebted Poor Countries) Trust Fund. The HIPC initiative was launched in the fall of 1996 by the World Bank and the International Monetary Fund, at the urging of the G–7 countries. Its goal is to promote the cancellation of the debt of the poorest countries that have the largest debts (mostly Sub-Saharan African countries).

In fact, a large debt is one of the major reasons that stymies the economic development of these countries. Most of the people who subsist on less than one dollar a day live in the 40 poorest, most heavily indebted countries.

In view of the above reasons, Mr. President, I request that this Bill be approved quickly. The Bill's humanitarian inspiration and, above all, our government's fulfillment of the obligations it has committed itself to, merit the most serious attention.

I acknowledge the care and attention that Senator's Martone has given to working and cooperating with us in the Committee to finalize this Bill, whose approval is imperative.

PRESIDENT. I adjourn the debate on this Bill to a future session.

ANNOUNCEMENT ABOUT INTERPELLATIONS AND INTERROGATIONS

PRESIDENT. This is a notice that this Office has received one interpellation and several interrogations; they are published in Attachment B to the Minutes of today's session.

I remind you that the Senate will reconvene in a public session today at 4:30 p.m. with the same agenda, as amended.

The session is closed. (11:39 a.m.)

ATTACHMENT A

BILL

Italy's financial contribution to replenish the resources of international funds (2667)

ITEM ON THE AGENDA

G1

MARTONE, BRUNALE, SALVI, Paolo BRUTTI, MARINO, FLAMMIA, DI SIENA, PAGLIARULO, BEDIN, DE ZULUETA, RIPAMONTI, FALOMI, DE PETRIS, CORTIANA, DONATI, PETERLINI, LONGHI, ZANCAN, TURRONI, MANZIONE, ACCIARINI, MALABARBA, BOCO, GIARETTA, Franco DANIELI.

The Senate:

Whereas Bill No. 2667 on "Italy's financial contribution to replenish the resources of international funds" includes Italy's contribution to the thirteenth replenishment of capital of the International Development Fund (IDA–13), a World Bank agency dedicated to granting loans to the poorest countries for the purpose of fighting poverty;

Taking into account the investigation currently under way in the United States Senate on cases of corruption involving the alleged participation of World Bank officials in infrastructure projects, some of which, such as the Yacyretá Hydroelectric Project (Argentina-Paraguay) and the Lesotho Highlands Water Project (Lesotho) also involved Italy's contribution, by way of SACE bilateral cooperation and export credits;

Recalling that according to detailed analyses that are part of several internal World Bank documents, at least in the case of Indonesia, at least US$8 billion in World Bank funds were allegedly lost due to corruption, and that according to a report by Senator Richard Lugar, Chairman of the U.S. Senate Committee on Foreign Relations, at least US$130 billion in World Bank funds have been diverted from their institutional goals as a result of corruption, starting in 1946;

Underscoring that corruption can cause great harm to the institutional mandate of the above-mentioned institution, and to its credibility and effectiveness, thereby increasing the foreign debt burden of the countries receiving aid, and jeopardizing efforts in the fight against poverty;

Considering that the World Bank Group plays an active leadership role in strengthening approaches and methods with regard to promoting development, and that the correct application of internal safeguard policies for the assessment of social and environmental impact, consultation, and evaluation of projects and programs are the best guarantees for an independent, democratic control of said institutions and for the highest degree of effectiveness in the work they carry out;

Recognizing the steps forward that the World Bank has taken in this respect, for example, by setting up independent appeal and verification mechanisms, such as the Inspection Panel;

Acknowledging however, the World Bank's intention to revise these safeguard mechanisms to made them more flexible, thereby assigning greater discretionality to the governments of the loan-recipient countries in defining social and environmental standards, with serious prejudice to the quality and effectiveness of the World Bank's intervention and the use of public funds, such as those that Italy is earmarking for the replenishment of the IDA,

Commits the government:

(a) To support initiatives to reform the activities of the World Bank, with a view to remedying the main causes of corruption and to strengthening transparency and oversight mechanisms for contract bidding and awarding, as well as public access to information;

(b) To propose the establishment of an independent oversight body to watch over and prevent the embezzlement of funds earmarked to fight poverty;

(c) To support the strengthening of independent evaluation and review structures, such as the Inspection Panel, and to ensure a greater commitment on the part of

World Bank personnel to following and carrying out existing policies, instead of proposing a greater degree of discretionality;

(d) To report to Parliament about these initiatives, and about the position that the Executive Director for Italy at the World Bank has expressed on these matters.

LETTER TO THE COLOMBO DAILY MIRROR, JANUARY 30, 2003

FOREIGN FUNDED PROJECT RACKETS

I was appalled to read in the newspapers recently that an enormous amount of money is to be spent on a water resources management project with a loan obtained from the Asian Development Bank. A breakdown of the Rs. 1400 million project budget indicates that Rs. 62 million is to be spent for import of vehicles, Rs. 182 million for purchase of equipment, Rs. 248 million for employing foreign specialists and Rs. 492 million for training.

I venture to predict that this project will also end up with very limited benefits to the people of this country but will bestow ample benefits to the lender, the politicians and state officials associated with the project just like the fifteen or more similar projects related to water that were completed during the last two decades with loans from the World Bank and the Asian Development Bank.

From what I have seen and continue to hear I can predict how a good portion of these loan funds will be used. As far as vehicles are concerned, a few luxury jeeps each costing over 30,000 U.S. dollars will be imported by the project in addition to a large number of utility vehicles. The Minister, Deputy Ministers and high ranking officers will requisition the luxury vehicles for their use if they are even a little superior to what they are using at present, and some of the less expensive vehicles will be allocated to their Coordinating Secretaries while the rest will be distributed among the officers working in the project.

It will be a very common practice for even second level and third level officers working in the project to travel daily from their homes in these vehicles as far as from Nittambuwa to Colombo and from Kurunegala to Anuradhapura in flagrant violation of government regulations.

Spending Rs. 246 million on foreign specialists will be an unpardonable waste of public funds, especially in a field such as water resources management when there is an abundance of local talent. The engineering faculties of the Sri Lankan universities have produced thousands of very competent engineers, many of whom have obtained MScs and PhDs from reputed universities and are presently employed in the Irrigation Department, Water Resources Board, Mahaweli Authority, the universities and other local institutions.

There is little justification for employing foreign engineers and paying them salaries more than fifty times the amounts paid to the equally qualified and experienced local engineers.

Much of the 492-rupee-million budgeted for training will be wasted. The Minister and Deputy Minister, Secretary of the Ministry, Head of the Department, officers of the Treasury and even few of the Coordinating Secretaries of politicians will undertake study tours in developed countries.

An ongoing water related project in the state sector can be cited as an example of such waste. The Minister, Deputy Ministers, Secretary of the Ministry, Director General and Directors were among those who visited the Tennesse Valley Authority in the U.S., numerous Australian water resource institutions and attended international seminars on river basin management in U.S.A. and Europe utilizing project funds.

Of the above who undertook foreign travel utilizing loan funds, the Minister and Deputy Ministers do not hold office any more, the Secretary was transferred to the Ministry of Health, the Director General moved to the Ministry of Highways and the Director of Technical Services who went to Europe and several other countries attending seminars is positioned in the Ministry of Defence.

What then was the gain to the country from these foreign tours?

The tragedy of our country is that hardly any one is bothered about such waste.

Has the Department of External Resources ever gone back to an institution which has completed a project, thoroughly evaluated it and ascertained whether project objectives have been met and monies spent frugally and justifiably?

If not, what action has been taken against those responsible for inefficiency and waste? The lukewarm attitude to project supervision by the Department of External Resources is well known and clearly shown by the lackadaisical attitude of their staff at quarterly monitoring meetings of projects. They hardly utter a word, eat the cadju nuts, drink the tea, collect the honorarium and depart in peace.

The public should be made aware of the craft and the techniques adopted by the lenders. They plan their activities with meticulous care and thoroughness seven or eight years in advance. One strategy they adopt is to identify a small short term project that has great potential for expansion and lending, and to offer a grant of about half a million dollars for its implementation. The government gleefully accepts this and the lenders quickly set up the project, get a foothold, establish themselves and take the opportunity to prepare a project expansion proposal for a tidy sum of 20 to 30 million dollars, but this time as a loan. The locals readily agree to this too. This is how projects flourish in this country and how the public debt keeps on increasing.

In my view, most of the World Bank and Asian Development Bank projects are big rackets with the beneficiaries being the lenders, politicians and corrupt state officials. Somebody has to take a quick and hard look at these projects funded by loans and the manner in which the funds are used.

How long is the country going to allow the importation and use of luxury jeeps, or costly junkets overseas by politicians and bureaucrats using taxpayers' money?

These are the parasites of the country sucking the blood of our people with impunity. I suppose it is only the Prime Minister who can stop this utter waste of public funds and more importantly, arrest the spread of this corrupt culture. May the Prime Minister pay attention to this matter.

R. DISSANAYAKE,
Kotte.

LETTER TO THE COLOMBO DAILY MIRROR, OCTOBER 6, 2004

ADB CLARIFIES INACCURACIES ON CORRUPT PROJECT IN LANKA

We refer to the recent article entitled "U.S. Senate Highlights Corrupt Projects in Sri Lanka," published on October 2, 2004. We have always regarded the Daily Mirror to be a well-researched and respected publication. In this case, however, the article contained a number of inaccuracies which we wish to clarify.

First, the statements attributed to U.S. Senator Richard G. Lugar, Chairman to the Senate Foreign Relations Committee appear to be those of Bruce Rich, Senior Attorney with the NGO Environmental Defence who testified before the committee. As you know, the Senate Foreign Relations Committee is looking into combating corruption in the multilateral banks and has been holding a series of meetings of which the Asian Development Bank, African Development Bank and European Bank for Reconstruction and Development were the focus of last week.

During the hearing, allegations were made about the Southern Transport Development Project (STDP) in Sri Lanka, which were not new. In fact, ADB had addressed many of the issues relating to the project, in your own publication in May 2002.

On the pre-qualification process highlighted in your article, the objective was to ensure that sufficient and appropriately experienced and resourced companies were eligible to tender for the ADB-funded project, thereby achieving a cost and quality effective outcome.

Three companies were originally pre-qualified, and another—the fourth company referred to in your article—met the basic financial, experience, and resource requirements but fell slightly short of a passing mark when these criteria were combined.

Since the objective of the process was to maximize competition, and because the deficiency was of a technical nature only, the company was permitted to participate in the tender process. It is important to note that the company became eligible simply to tender for the work, in competition with the originally pre-qualified companies. There was no question of the company being awarded the contract as a consequence of this pre-qualification process.

The article also claims that the road is being realigned and that this realignment will result in an almost 100% increase in cost. This is not correct. The project will experience some cost overruns as a consequence of design and other issues but these are not a consequence of the change of alignment. There has been a general misunderstanding that the project cost increased from 11–12 billion rupees to 27 billion rupees because of the alignment changes. However, this is actually a misleading comparison between the cost of the ADB-financed section and the total project cost, which includes the section financed by the Japan Bank for International Cooperation.

Finally, the article states that the company that was awarded the contract was able to submit a second bid, once the bid prices of the other companies were known.

This is also not correct. Perhaps the misunderstanding has arisen because the bidding documents permitted all bidders to submit alternative technical and financial offers reflecting different design options.

Only one company, the one eventually awarded the contract, did so but this alternative bid was submitted concurrently with all other bids, prior to the date fixed for bid opening, not afterwards. This was completely in accordance with the bidding documents and procedures agreed to by the Government and ADB.

Regardless of all the above considerations, given the interest this issue has generated, ADB will review this process to ensure that it meets the highest standards of transparency and accountability.

The claim that ADB does not seriously address the issue of corruption in its projects is without foundation and misleading. Indeed, ADB has had an anti-corruption policy since 1998.

In conclusion, we are concerned that such serious errors of fact are being reported as accepted truth. We hope that our clarification reassures you and your readers that the article to which we have responded contains factually incorrect information or is based on a misunderstanding of the process that led to the selection of the contractor.

ALESSANDRO PIO,
Country Director, ADB Sri Lanka,
Resident Mission.

LETTER TO THE COLOMBO DAILY MIRROR, OCTOBER 18, 2004

ADB—THE TRUTH BEHIND THE HIGHWAY

In the Daily Mirror of October 6, titled "ADB Clarifies Inaccuracies on Corrupt Project in Lanka." Mr. Alessandro Pio, Country Director, ADB, made statements which were not true. All the citizens of Sri Lanka are clients of the Asian Development Bank and need to be informed of the truth.

To quote the ADB's own words indeed there are many "inaccuracies", but they are in their letter, not in the Daily Mirror article. We highlight below the most blatant of the inaccuracies in their letter.

Mr. Pio says, "There has been a general misunderstanding that the project cost increased from 11–12 billion rupees to 27 billion rupees, because of the alignment changes. However this is actually a misleading comparison between the cost of the ADB financed section and the total project cost, which includes the section financed by the Japan Bank for International Cooperation."

This is totally untrue. Mr. Alessandro Pio is either unaware of what he is commenting on or he is deliberately misleading the people of Sri Lanka. The major documents of the project include the cost for the entire road in the range Rs. 11–15 billion not as Mr. Pio indicates for only a section of it.

The following are extracted from project documents of the Government's and those of ADB. The documents show costs as follows:

- The Environmental Impact Assessment for this project done in 1999 shows the cost as Rs. 12.8 billion for the Combined Trace and Rs. 13.3 billion for the Original Trace. (Combined Trace Rs. 12,765.476 million, Original Trace Rs. 13,285.316 million.)
- The Feasibility Study done by WSA Engineering for the Government and paid for by ADB gives costs for the whole length from Kottawa to Matara as between Rs. 9.3 billion and Rs. 15.2 billon depending on whether the Expressway will be 2 or 4 lanes and on the junction type. (Section 3.3 Table ES1 Financial Construction Costs.)
- Asian Development Bank Report and Recommendation of the President (RRP). This is the document on which Board of the ADB grants its loan. The report covers the whole Expressway including the JBIC section and shows the cost of construction as Rs. 12.1 billion. (Economic Internal Rate of Return Construction cost—Total of costs to be incurred Rs. 12,123 million.)

With regard to the points allocated at pre-qualification, there has been more than enough publicity of the computations, all recognise that the disqualification was not of a technical nature. Kumagai Gumi, has financial problems, its Bank had to write off an enormous amount of debt in 1997 and again in 2000. More recently its executives have also allegedly been involved in bribery, illegal political donations and money laundering. See Mainichi Newspaper about Imajo in Japan in 2002, and again in 2003 and Papua New Guinea Post Courier about 1995 to 2000. So much for Mr. Pio's "Deficiency of a technical nature."

Let us now address the issue of alignment changes. Three cases went to the Supreme Court, where the petitioners from the Bandaragama and Akmeemana areas specifically complained about alignment changes which did not comply with the laws of Sri Lanka. The Supreme Court agreed with them, saying that ". . . the deviations proposed by the RDA were alterations requiring CEA approval after compliance with the prescribed procedures and the principles of natural justice . . ." This confirms that the traces described in the EIA were changed and these changes required approval in line with the National Environmental Act.

ADB insisted that an EIA be done as part of their loan requirements. The traces studied by the EIA were as mentioned above quoting table 9.1. The costs were 12.7 billion for the Recommended trace, they are now 27 Bn. Mr. Pio's figure. (Ministry figure at a meeting with the Prime Minister and Affected People 29 Bn.)

If the increase from Rs. 12.7 Bn. to Rs. 27.0 or 29.0 was not due to trace changes which have been proved to exist, where did the money go? If Mr. Pio knows the answer he owes the public a duty to share his information with us.

We strongly advise those who have access to the Internet to read the full text of the U.S. Senate testimony by Mr. Bruce Rich. It draws many parallels with another ADB project in Thailand where the project cost overrun was huge, the location was altered the public were protesting and ADB turned a blind eye to the corruption, disbursing the loan regardless. Eventually the ADB Inspection forced by the affected people with great difficulty said they were not at fault, and carried on. Hon. Mr. Takshin came to power, investigated the corruption and stopped the project. Court cases are proceeding against the Contractor and Government Officials. JBIC who also ignored the peoples voice and let the project carry on, asked for its money back and is probably laughing all the way back to their Vaults!

These episodes show the ADB as irresponsible lenders and more dangerously, are not truthful in their statements.

SARATH ATHUKORALE and HEATHER MUNDY,
Joint Organization of the Affected Communities on Colombo/Matara Highway.

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