Multilateral Development Banks’ integrity management systems

Query

What is considered best practice when it comes to the content and scope of the efforts against corruption in multilateral development banks? Are there any studies on anti-corruption in the multilateral development banks, and specifically in the African Development Bank?

Purpose

To learn about best practices in regards to anti-corruption policies, guidelines and organisational structure in multilateral development banks.

Content

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Caveat

Although the anti-corruption efforts of multilateral development banks (MDBs) also include support provided to the anti-corruption initiatives of partner countries, this answer focuses exclusively on how, at the organisational level, MDBs deal with fraud and corruption in their own projects and operations.

Summary

Although there are very few studies specifically focusing on corruption risks in multilateral development banks, there is a broad consensus - confirmed by anecdotal evidence from the MDBs special investigative bodies’ annual reports - that corruption affects MDBs financed projects in all sectors. Corruption covers a wide range of behaviours that are of fraudulent, coercive or collusive nature, primarily occurring in the vulnerable areas of contracting and procurements.

Multilateral development banks have started addressing these issues in the last ten years by developing “zero tolerance” anti-corruption policies, reviewing internal procedures, setting up fraud and corruption investigative bodies, and supporting partner countries’ anti-corruption initiatives. In line with other MDBs’ initiatives, the African Development Bank (AFDB)’s efforts have focussed on strengthening its anti-corruption framework along four major dimensions, namely prevention, detection, investigation and sanctions.

MDBs – including the AFDB - have also made significant progress in recent years in harmonising their anti-corruption policies to promote a consistent approach to governance and corruption. These
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coordination efforts have culminated in April 2010 in the agreement between a number of MDBs to cross debar firms and individuals that have engaged in corruption in MDB financed projects.

1 Evidence of corruption in Multilateral Development Banks (MDBs) activities

Aid is at great risk to be affected by corruption when it flows to countries with weak governance systems, poorly functioning state institutions or low absorption capacity. It has been also been suggested that certain donor practices and patterns of incentives can further increase corruption risks, including disbursement pressure, lax control and follow up and donors’ need for success stories (Fritz, V. and Kolstad, I. 2008). Case studies of countries such as Mozambique (Hanlon J. 2004) and Uganda (Tangri, R. and Mwenda, A.M. 2006) also suggest that by continuing to support corrupt governments, donors can contribute to sustain local patronage, rent seeking and corruption patterns.

There is growing awareness of these concerns among donors – including MDBs – who have started addressing these issues in recent years by developing anti-corruption strategies (Weth, F. 2010), reviewing internal procedures, setting up fraud and corruption investigative bodies, and supporting partner countries’ anti-corruption initiatives.

Yet, although corruption in aid has become an important area of research for organisations such as the U4, there are very few studies specifically focusing on corruption risks in MDBs’ activities. According to the World Bank’s own account, there is a deeper understanding of the nature of corruption risks in Bank-financed projects, yet knowledge on the frequency, scope and depth of these risks remains limited (World Bank 2007).

In spite of this relative lack of information on the extent of the problem, there is abundant anecdotal evidence that corruption is prevalent in MDBs’ supported projects. Big scandals periodically hit the headlines such as the World Bank financed Lesotho Highlands Water Project. The chief executive of the Lesotho Highlands Development Agency was found guilty of accepting bribes from multinational companies to secure tenders (Transparency International 2008). Other cases confirm that MDBs’ projects are highly vulnerable to corruption risks such as the corruption riddled Chad-Cameroun pipeline project (Bretton Woods Project 2004) or more recently, a corruption scheme involving a Russian subsidiary of Siemens in the Moscow Urban Transport Project (World Bank 2010).

The MDBs’ special investigative bodies’ annual reports are a precious source of information on corruption patterns in MDBs’ projects, as they reveal specific corruption risk areas in MDB-financed activities.

The World Bank

In the financial year 2010, the World Bank’s Integrity Vice Presidency (INT) received close to 450 complaints relating to more than 300 Bank supported projects in 91 countries (World Bank 2010). The complexity of the cases varied from one-time fraud cases to multi-jurisdictional matters involving local and joint venture companies. Close to half of the allegations received were related to bid manipulations and collusion (46%), followed by practices such as forgery (31%), corruption (21%), procurement irregularities and kickbacks.

During the reporting period, INT closed 117 investigations, debarred 45 entities – including multinationals, individuals and NGOs - , and referred 32 investigative findings to government and national anti-corruption agencies. While these figures demonstrate a growing concern to effectively address and sanction corruption, the Bank recognises that these statistics may only represent the tip of the iceberg and that INT may not have the resources and capacity to effectively deal with a problem of such scale, as reflected in the 2006 annual integrity report: “the allegations INT receives are only a subset of the entire universe of corrupt activities” and “INT has a finite ability to actively investigate all the allegations it receives” (World Bank 2007).

The Asia Development Bank (ADB)

Similarly, the ADB’s Office of Anti-corruption and Integrity (OAI) reports a number of fraud and corruption allegations that have been investigated in 2009. During the reporting period, the OAI received close to 200 complaints of fraudulent and corrupt practices relating to ADB-financed activities and alleged misconduct by ADB staff members. Fraud and corruption collectively represented the vast majority (77%) of all investigations opened, while collusion was the second major area of concern, representing 12% of OAI investigation work. Other cases included matters such as conflicts of
interest, staff misconduct, or allegations of coercion. The 32 fraud cases opened in 2009 comprised misrepresentations, submitting false claims for compensation or reimbursement, and submitting false documents. As in previous years, most of these allegations were related to bidding, tendering, and procurement for projects (OAI 2009).

The African Development Bank (AFDB)

Statistics from the AFDB’s 2007-2008 Integrity and Anti-corruption Report also describes the nature of fraud and corruption allegations that have been reported and investigated by the Integrity and Anti-corruption Division (IACD) - the Bank’s investigative body. During the reporting period, the IACD received 389 allegations of fraud and corruption, out of which 58 were considered relevant complaints. 25 cases were considered substantive and of sufficient priority to warrant at least preliminary investigations. Based on the investigative findings, the Bank’s management took action in 11 cases, resulting in disciplinary actions of dismissal for 12 Bank staff.

Cases involved practices such as soliciting illicit payments to expedite disbursements in a Bank funded project, fraudulent education benefits claims by Bank staff, soliciting kickbacks from a bank supplier in an internal procurement process, abusive use of Bank property, etc. Staff members reporting a suspicion of fraud and corruption in a Bank-financed project complained of having experienced retaliation after blowing the whistle (AFDB 2009).

The European Investment Bank

In the European Union, a recent report by Counter Balance, a group of non-governmental NGOs, describes how the European Investment Bank’s use of intermediated loans and private equity funds may facilitate corruption and tax evasion. The report claims that a large proportion of EU aid for Africa from the Bank may have been handed over without sufficient public scrutiny to banks and private equity funds that then funnel the money into tax havens. The report presents a number of cases where the EIB’s due diligence and project partner selection have allegedly been compromised, including €4m in private equity investment destined for Angola that may have gone to a company based in Delaware but registered in Luxembourg, considered by many to be a tax haven. (Counter Balance 2010).

These various reports highlight the scope and nature of the corruption challenges faced by MDBs activities. More research would be needed to systematically identify specific risks associated with MDBs’ activities and operations. Yet, generally speaking, there are striking similarities across donors in terms of how corruption is taking place in many different sectors and contexts (Kramer, M. 2007). Fraud and corruption often occur during the planning and design phases of development projects, when many of the funding commitments are made. It also primarily takes place in the vulnerable areas of contracting and procurement. They typically include bribes, kickbacks, front companies, bid rigging and fraud by contractors and consultants such as overbilling, delivering sub-standard goods or failing to meet contract specifications.

2 The integrity management systems of MDBs

Faced with such challenges, MDBs led by the World Bank have, in the last decade, invested considerable resources in improving internal controls and establishing appropriate integrity management systems to prevent and combat corruption in their projects and activities. Efforts have mainly focussed on strengthening the basic elements of any comprehensive anti-corruption framework, namely prevention, detection, investigation and sanctions.

Prevention

Prevention of corruption implies that explicit anti-corruption policies, guidelines and internal integrity management systems are in place at the organisation level, backed by credible leadership and adequate resources that demonstrate the institution’s firm political will and institutional commitment to effectively address corruption issues.

“Zero tolerance” policies towards corruption

Internally, most multilateral agencies have put in place comprehensive anti-corruption policies and guidelines that promote a zero tolerance approach to corruption. For example, similarly to the World Bank, the ADB has committed to a ‘zero tolerance’ policy on fraud, corruption and misconduct in its lending operations and requires that all ADB staff and parties carrying out activities financed by ADB to adhere to the highest financial and ethical standards. As part of this obligation, managers and staff are required to address
corruption issues openly, comprehensively and rigorously throughout the entire range of ADB operations and at all stages of the programme cycle. (Herz, S. 2004). Similarly, the AFDB has adopted a zero tolerance policy against fraud, corruption and misconduct.

While such “zero tolerance” approach is essential for shaping institutional attitudes towards corruption, the implementation of such policies faces major resources and capacity challenges, making it very difficult to effectively operationalise them in practice. Some analysts recommend applying a cost-benefit analysis to anti-corruption policies to prioritise interventions and promote a rational use of scarce resources (Elliott, K.A. 2004), an approach that can be counter-productive when taken too far towards tolerating a certain degree of corruption that will eventually jeopardise the overall credibility of the MDBs’ stance against corruption.

Anti-corruption policies also need to provide a clear definition of sanctionable practices to promote a common understanding of the practices covered by donors’ anti-corruption strategies both internally and externally among the various stakeholders and development partners. In 2006, for example, leaders of seven multilateral organisations including the AFDB agreed on a standardised definition of corrupt and fraudulent practices they all adhere to (International Financial Institutions Anti-Corruption Task Force 2006):

- A corrupt practice is the offering, giving, receiving, or soliciting, directly or indirectly, of anything of value to influence improperly the actions of another party.
- A fraudulent practice is any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a party to obtain a financial or other benefit or to avoid an obligation.
- A coercive practice is impairing or harming, or threatening to impair or harm, directly or indirectly, any party or the property of the party to influence improperly the actions of a party.
- A collusive practice is an arrangement between two or more parties designed to achieve an improper purpose, including influencing improperly the actions of another party.

Corruption risk assessments at country, sector and project level

An emerging good practice to prevent corruption in MDBs’ activities involves systematically integrating anti-corruption approaches into the early stage of project design.

The ADB, for example, requests all projects to include an explicit assessment of how the project may be affected by corruption - including a complete financial accountability and procurement assessment -, provide a careful evaluation of the capacity of the various development partners to manage corruption risks and explicitly outline how to address these risks, including an action plan for high risk projects. These provisions are meant to ensure that during the preparation and appraisal phase of the project cycle special attention is given to design interventions in ways that limits corruption and promotes transparency and accountability. At the implementation stage, project documentation, reports, and assessments and evaluations should also explicitly and systematically address and monitor corruption-related factors.

Similarly, in its Governance and Anti-Corruption (GAC) strategy implementation plan, the World Bank recommends assessing corruption risks by conducting a systematic analysis of GAC issues in the design and implementation of Country Assistance Strategies (CAS), as well as in sector work, sector programmes and projects. This involves looking at country or sector environments, as well as the nature of project activities to identify specific areas of vulnerabilities. A detailed anti-corruption action plan including necessary risk mitigation measures can be developed for projects or programmes that are exposed to very high risks of corruption. In addition, regular risk reviews of project and lending portfolio can be conducted to identify the projects exposed to the highest risks that need to receive enhanced managerial oversight. As part of these efforts, in 2010 INT’s preventive services unit conducted a review of integrity risks in two vulnerable sectors: the road sector and community-development projects. Anti-corruption teams can also be established at country level to oversee project design in risky settings, including governance advisors, operation managers, key sector coordinators and fiduciary staff (World Bank 2007).

At sector level, the AFDB also recommends mitigating risks by assessing corruption risk and designing corresponding mitigating measures (sector governance
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Operational guidelines supporting increased transparency, participation, disclosure and oversight

In addition, MDBs staff is also guided by a set of guidelines and policies that have been reviewed in recent years to reflect good practice in areas such as disclosure policies, public financial management monitoring and controls, procurement policies, etc.

The World Bank’s GAC strategy for example insists on the importance of disclosure, participation and oversight, including third-party monitoring to prevent corruption. This includes strengthening supervision and oversight mechanisms, ensuring timely disclosure of project information and giving voice to beneficiaries using tools such as beneficiary surveys and citizen score cards.

In the sensitive area of procurement, most MDBs have also reviewed their policies in recent years, requiring competitive bidding and increased transparency for most projects, as well as strengthening anti-corruption provisions in all procurement processes. Within the broader framework of the aid effectiveness agenda, efforts have been undertaken in terms of institutional harmonisation of policies, procedures and documents for MDB/IFI-financed procurement which are now considered as being “substantially harmonised”. MDBs efforts are also increasingly converging in the area of electronic government and procurements (AfDB, ADB, EBRD, IDB, World Bank 2005).

The AFDB in particular revised its rules for the procurement of goods and services and rules and procedures for the recruitment of consultants in a way that have made them consistent with the policy documents being used by the other Multilateral Development Banks, as a step towards greater harmonisation between the MDBs. Reviews are also underway to the Bank’s Staff Rules.

The AFDB, along with six other multilateral organisations, has also agreed to integrity due diligence principles in its private sector lending and investment decisions, including adequate “know-your-customer” procedures and close scrutiny of politically exposed persons or parties investigated or convicted for serious crime or act of financial misconduct, etc (IFI Anti-Corruption Task Force 2006).

Promoting ethical standards

An important way to prevent corruption is to promote a culture of integrity and high ethical standards at all levels of the organisation. To achieve this goal, the MDBs’ commitment against corruption needs to be communicated both internally and to external partners through codes of conduct, ethical trainings, awareness raising activities, etc.

In the financial year 2010 for example, the World Bank’s INT trained 1200 professionals inside and outside the institution on prevention and integrity risk mitigation measures. INT’s Preventive Services Unit also collaborated with other Banks units to develop new training and advisory tools, including a handbook on fraud and corruption and a red flags manual (World Bank 2010).

The AFDB has also engaged in promoting ethical standards through different initiatives targeting both its staff and external partners. All Banks anti-corruption rules and policies are made public on the website, including the Whistleblower Policy and the investigative process. The Bank also developed a Code of Conduct for staff members and a separate Code of Conduct for Executive Directors to promote high ethical standards among its staff. The code covers misconducts such as conflicts of interest, abuse of authority, gifts and hospitality, post-bank employment, etc. In terms of awareness raising activities, the Bank provides training for Bank staff and partners through the preventive activities of the IACD, covering the Bank’s rules regarding ethics, procurement integrity, and avenues for registering complaints about corruption, fraud and misconduct.

Detection

Most MDBs have established a complaint mechanism supported by whistleblowing protection provisions to encourage people involved with Bank supported projects to report suspicions of corruption and wrongdoing.

Typically, any person who has knowledge of alleged corruption involving activities supported by MDBs is entitled to report that information per mail or through secured hotlines. The main receiving points for complaints are usually the Banks’ respective
investigative bodies. In addition, the World Bank has set up an independent, third party hotline that forwards allegations to INT. Complaints can usually be filed anonymously. For example, the AFDB accepts any complaint irrespective of their source, including complaints from anonymous or confidential sources. Complaints can be made through established Hotlines and other avenues, which operate 24 hours a day, seven days a week.

In addition to setting up a complaint mechanism, the World Bank has launched A “Voluntary Disclosure Program” (VDP) in 2006 with the view to facilitating the detection of corruption and increasing risks of detection for firms engaging in fraud and corruption (World Bank 2006).

The VDP allows entities – whether firms, NGOs or individuals - which have engaged in past fraud and corruption to avoid administrative sanctions if they disclose all prior wrongdoing and satisfy a number of terms and conditions, including a commitment to renounce bribery and to implement a robust and monitored compliance program. In exchange for full cooperation, VDP participants avoid public debarment for disclosed past misconduct, and benefit from the Bank’s assurances of confidentiality. The AFDB also encourages firms or individuals involved in Bank projects to volunteer information on corrupt practices they may have been involved in, in exchange of leniency in the application of sanctions against the firm or individual making the disclosure.

One of the biggest obstacles that prevent staff or project partners to report corruption is the fear of reprisals. All MDBs have whistleblowing provisions in place to protect whistleblowers against retaliation. The AFDB’s Whistleblowing and Complaints Handling Policy, for example, provides full protection for Bank personnel against retaliation. Similarly, the IADB has a staff rule that prohibits reprisal against a staff member for having submitted a complaint or participated in an investigation. This practice will be expanded shortly to include third parties as well. The Bank may also notify the national authorities when it receives allegations of reprisal by or against third parties, involving IDB Group financed activities.

Investigations

All MDBs have established an investigative body in charge of uncovering fraud and corrupt practices in projects and investigating allegations of possible staff misconduct. The World Bank has been one of the first MDBs to pioneer this approach with the creation of INT in 2001. Other similar initiatives include institutions such as the European Bank for Reconstruction and Development (EBRD)’s Chief Compliance Officer, the IADB’s Office of Institutional Integrity or the ADB’s Integrity Division under the Office of the Auditor General.

Created relatively recently (in 2005) under the Bank’s Auditor General Office, the AFDB’s Integrity and Anti-Corruption Division (IACD) became operational in 2006 and conducted its first investigations in 2007. It is mandated to investigate allegations of fraud and corruption and staff misconduct, assist member countries to detect and deter fraud and corruption in Bank’s activities and raise awareness on corruption and anti-corruption among staff. It is still relatively early to assess the impact and effectiveness of the IACD. From the Bank’s own account, a key challenge at this stage is the anticipated caseload volume, complexity and the length of time needed to complete investigations, as drawing on the experience of other MDBs with establishing similar investigative units, the IACD expects a major increase in complaints in coming years (AFDB 2009).

One of the major challenges faced by MDBs’ investigative units is one of resources and capacity. In the past four years, the ADB has doubled its integrity staff to address these issues. In addition, the World Bank and the ADB track allegations and investigations with sophisticated computer programs (Freshfields Bruckhaus Deringer US LLP 2010).

In terms of investigative process, most MDBs – including the AFDB - have adopted common principles and guidelines for investigations that are outlined in the IFI Anti-Corruption Task Force’s uniform framework for preventing and combating corruption (IFI Anti-corruption Task Force 2006). These guidelines are based on the principle that all investigations must be thorough, professional and respectful of the parties involved.

As part of these principles, confidentiality is an important dimension to ensure the integrity of the investigative process. Confidentiality usually refers to the principle of limiting the distribution of information to officers who require knowledge of a matter in the performance of their official functions. While the sharing of information is subject to each Bank’s internal disclosure policies and procedures, specific safeguards
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can be established to ensure the confidentiality of the investigative process. The IADB for example specifies that safeguards for confidentiality in investigations include: 1) the protection of the confidentiality of complainants; 2) an obligation for all staff involved in an investigative process to preserve and protect the confidentiality of the subject, the witnesses, and all other parties concerned; 3) disciplinary action for any staff member who compromises the confidentiality of a complainant and; 4) the acceptance of anonymous allegations.

Sanctions

Sanctions by MDBs typically include reprimands, conditions imposed on future contracting or debarment which consists of declaring a company or an individual ineligible to participate in future bank supported activities, either for a period of time of permanently. In December 2010 for example, The World Bank barred a US company for 12 years, alleging fraud and corruption in development projects for engaging in fraudulent practices in bank financed projects implemented in DRC, Tanzania, Ukraine, Ethiopia, Gambia and Liberia (Agence France Presse 2010).

In addition, MDBs such as the AFDB or the World Bank can refer the case to the appropriate authorities of the member country’s government for a determination of whether a criminal investigation is appropriate.

Involvement of MDBs’ staff in irregularities can lead to disciplinary actions including the termination of their contract and legal actions.

Some MDBs such as the World Bank and the IADB publicly names companies and individuals found to have been engaged in corrupt practices in their projects as a deterrent. The IADB proactively disseminates the List of Sanctioned Firms and Individuals through personalised notifications of updates, and an e-alert created for those wishing to receive automatic e-mail notifications of each update (http://www.iadb.org/ealerts).

Cooperation among MDBs on anti-corruption issues

There is a growing awareness that coordination among multilateral development banks (MDBs) and other international financial institutions is crucial. In its absence, partner countries may be tempted to turn to donors that are less stringent on anticorruption issues. MDBs have made significant progress in this area in recent years and strived to harmonise their anti-corruption policies and frameworks to promote a consistent approach to governance and corruption.

The International Financial Institutions Anti-Corruption Task Force

In February 2006, the leaders of the AFDB, ADB, EBRD, European Investment Bank Group, International Monetary Fund, IADB and the World Bank agreed to establish a Joint International Financial Institutions (IFI) Anti-Corruption Task Force (ACTF) to work towards a consistent and harmonised approach to combat corruption in member institutions’ activities.

In September 2006, the ACTF adopted a Uniform Framework for Preventing and Combating Fraud and Corruption, which committed the banks to developing a harmonised approach towards integrity. As part of this effort, the framework includes the above mentioned common definition of fraudulent and corrupt practices, as well as principles and guidelines for investigations. In addition, it emphasises the importance of exchange of information in connection with ongoing investigations among member institutions to promote a common approach to anti-corruption, while respecting confidentiality provisions established to protect whistleblowers.

Another important area of coordination is the mutual recognition of enforcement actions. The Task force calls member institutions to explore how enforcement actions taken by one institution can be supported by the others and recommends that each member institution requires all bidders, sponsors, firms and individual participating in activities financed by an institution to disclose any sanction imposed by another institution.

Cross debarment of firms and individuals involved in wrongdoing

A major breakthrough in this regard has been the recent agreement by a number of MDBs on multiple debarments of firms and individuals involved in fraud and corruption. In April 2010, the ADB, the AFDB, the EBRD, the IADB and the World Bank signed an agreement to cross debar firms and individuals that have engaged in wrongdoing in MDB financed projects. Under the new agreement, entities debarred by one MDB for more than one year may be sanctioned for the
same misconduct by other participating development banks. Criteria for cross debarment include: 1) debarment has to be public; 2) it has to exceed one year; 3) it should be based on independent findings; and 4) sanctionable practice should have been committed within the previous 10 years. This collaborative process aims at increasing the cost of corruption in development projects by preventing a company found to be using corrupt means by one development bank from obtaining contracts from another bank. The AFDB is still currently in the process of operationalising cross debarment (IACC 2010).

Impact of such measures and recommendations

In spite of the considerable efforts that MDBs undertook on the anti-corruption front during the last decade, the actual implementation of a “zero tolerance” corruption policy, as well as the ability of their newly established integrity management system to effectively address corruption have been questioned by several reports and evaluations.

A 2004 evaluation report of ADB’s efforts to limit the incidence and impact of corruption in its lending operations shows, for example, that the ADB almost never complies with the requirements of its anti-corruption policy to explicitly address corruption issues in its operations (Herz, S. 2004). Corruption risks assessments and action plans have only been partially implemented, and staff does not systematically link project design to reducing opportunities for corruption. The report concludes that the ADB’s current incentive system does not encourage staff to invest time, resources and efforts into the implementation of anti-corruption policies. The review further highlights a lack of guidance, training, capacity and in-house expertise to implement these policies. The report also mentions the strong pressure on staff to finance new projects rather than to ensure that current ones are successful as an important factor to the ADB’s disappointing record in complying with the requirements of its policy.

Although the World Bank has been an important driver of MDBs’ anti-corruption efforts, alarming findings from an internal evaluation report from the Bank’s Independent Evaluation Group made public in 2009 also suggest that the institution has still failed to adequately address fraud and corruption risks in its activities (Alexander, N., Edwards, B., and Rich B. 2010).

The evaluation found that internal controls were so weak as to constitute a “material weakness”, resulting in high risks of Bank resources being stolen through bribery, collusion, over-pricing and under-delivery. Furthermore, the evaluation found that there was a lack of timely follow up on audit, investigation and evaluation findings. A contributing factor could be that the Bank’s incentive system does not sufficiently link rewards to ethical behaviours and project performance. The evaluation pointed to inconsistent ethical signals given by senior management, contributing to create a perverse internal culture where staff fears reprisals for reporting infringement. The report further outlined twenty two “significant deficiencies” in compliance, with a number of operational policies not directly linked to any key controls or business processes. In particular, the evaluation identifies non-compliance with appraisal and supervision policies as particularly problematic. The report concludes that a reliable, independent enforcement of the Bank’s anti-corruption guidelines and regulations is needed as well as a mandate to work with law enforcement officials in borrowing counties to prosecute corrupt officials and end impunity, all important lessons also for other MDBs.

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