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## International Cooperation to Combat Corruption

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In the summer of 1996, two events signaled a major breakthrough in the development of international instruments against commercial corruption. In May 1996, at a meeting convened by the Organization for Economic Cooperation and Development (OECD), ministers of 26 major industrialized nations agreed that tax deductibility of bribes to foreign public officials should be banned.<sup>1</sup> Ministers also maintained that the bribery of foreign public officials should be criminalized in an effective, coordinated manner. Then in June, the heads of government of the Group of Seven (G-7) strongly backed the OECD statement at their summit in Lyon.

Until recently, European and Asian countries were reluctant to respond to repeated US initiatives against transnational bribery in international forums. For example, when the United States suggested in 1989 that the OECD examine the feasibility of an international agreement on illicit payments in international commercial transactions, the reactions of other OECD members were at best reserved. Some country representatives thought the US proposal invited a replay of the debacle at the United Nations some 15 years earlier. Off the record, other delegates at the United Nations warned there must be a hidden trade agenda behind the

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1. The more diplomatic wording of the communiqué of the OECD Ministerial Council is based on language developed by OECD's Fiscal Affairs Committee that calls on member states to reexamine tax treatment with the intention of denying deductibility.

US move. It was generally maintained that the United States had maneuvered itself into a competitive disadvantage on world markets with the Foreign Corrupt Practices Act (FCPA).

With the help of active, behind-the-scenes lobbying and a shift in the focus of external policy from East-West confrontation to consensus and the globalization of markets, attitudes have changed. OECD member states now generally accept that a worldwide anticorruption policy is in the general interest and that it is necessary for establishing a level playing field for commerce. Correcting market distortions has a new urgency. At the same time, many industrialized countries are uncovering extensive domestic networks of corruption, or even entire corruption cultures, and thus have come to realize that corruption is not restricted to their relations with developing countries.

Since 1994, when the 26 OECD countries initially vowed to take concrete and meaningful steps against bribery of foreign public officials, several other international organizations—including the Council of Europe, the European Union (EU), and the Organization of American States (OAS), as well as large money-lending institutions such as the World Bank—have been reviewing their policies and developing international instruments against corruption. The International Chamber of Commerce (ICC) and other business organizations are also working on guidelines and codes of conduct.

This chapter reviews past and current international initiatives against corruption, lays out the main issues at stake, and outlines how the various organizations' work could be combined in a coherent strategy.

## **The Risks of International Commercial Corruption**

One might ask whether the international community should expend so much effort to control and reduce corruption. It used to be standard for business representatives in industrialized countries to refer to the endemic character of corruption in many developing countries and to claim that it was not up to them to intervene and change local customs. Especially in the 1970s, some economists even argued that corruption was actually helpful to development—"the oil that keeps the engine running smoothly." Another explanation heard frequently in business circles may be more honest: that the strains of globalization and increasing international competition are so considerable that they simply cannot forego bribery as a means of last resort to keep their products in some markets.

But what might be of short-term benefit to the individual business may be quite socially detrimental on a broader scale and over the long term. It is now widely accepted that corrupt practices distort market conditions. Those with access to vital information, connections, the necessary cash, and a certain amount of ruthlessness—not the best contenders—will pre-

vail. These additional resources cannot be treated simply as market factors, as they regularly depend on a whole series of illegal acts: falsified statements, tax evasion, and sometimes fraud may be employed in the creation of “slush funds” that support corruption. Those who fail to take such preparatory measures often turn to suppliers of cheap money, who frequently are members of organized crime entities and are only too happy to filter their criminally obtained funds (e.g., drug money) through companies that generally operate on the licit and visible markets.

The effects on the recipient side, frequently in countries of the South, are no less harmful. As in the North, corruption adversely influences decisions, perhaps leading to the wrong choice among competitors. It may even be the only reason to enter into a contract at all. Rent seeking may be the motive to buy unnecessary or inadequate equipment. There are plenty of examples from past experience in the South in which huge projects that were organized and funded by bilateral or multilateral development agencies generated millions of dollars in bribes to government officials. This often not only resulted in an explosion of foreign debt to be paid off by the next generation under conditions of austerity dictated by the same development agencies but enabled an oligarchy to stay in power for yet another decade. Thus, grand corruption is detrimental not only to the public trust, but also to the functioning of a young democracy (see chapter 2 by Rose-Ackerman and chapter 3 by Johnston for examples of the economic and political consequences of corruption).

Of course, individual businesspersons might accept that corruption generates damaging effects on a macro level, but they would excuse themselves by referring to current practice, to local traditions, and to the difficulty of doing business if they were to abstain from corruption unilaterally. Nor can these individuals be held responsible for the collapse of an entire political system, as has been observed in Italy recently. In other words, there is a free-rider problem that makes an internationally coordinated response essential. In order to achieve this, it is necessary, first, to raise collective awareness and then to enact clear rules. An unambiguous statement, that it is forbidden to bribe a foreign official, would help a great deal. It is furthermore essential to detail possible sanctions and to enforce those rules. Such action, even if taken only by the countries of the North, will have great effects in the South as well, helping to dry up the “supply side” of bribe markets. Ultimately, however, controlling corruption will require both “donor” and “recipient” countries, as well as financial centers, to coordinate this action.

## **A Brief History of Early International Initiatives**

Discussion of policy to combat international corruption has long been treated as taboo. Even codes of ethics of multinational enterprises tried to

avoid use of the term corruption by all sorts of euphemisms. Undoubtedly the United States deserves credit for breaking the ice and introducing the first legislation to combat international corruption. A series of domestic and international corruption scandals in the 1970s led to passage of the US Foreign Corrupt Practices Act (FCPA) in 1977 (see Glynn, Kobrin, and Naím, chapter 1). The rationale and effects of the FCPA are complex. Apart from a moral element, the legislation also has economic and foreign policy implications. But the approach is essentially unilateral; it is intended to protect US interests, and foreign legislation is taken into account only on a secondary level, as a possible excuse.<sup>2</sup>

Early international efforts against corruption began at the United Nations in the mid-1970s. The United States pushed hard in the Economic and Social Council (ECOSOC) for an international agreement on illicit payments.<sup>3</sup> The drafts modeled after the FCPA were, however, caught in the crossfire between North and South, with developing countries maintaining that the concept of “illicit payments” should be understood in a broad sense, including payments also made to the apartheid regime in South Africa. The UN draft also met the stern opposition of other industrialized countries, which argued that it was another US effort to extend a unilateral policy choice extraterritorially. In an atmosphere of mutual distrust, heightened by the still prevailing Cold War, the project had to be abandoned in 1979.

Despite developed-country suspicions regarding US motives, the June 1976 OECD Declaration on International Investment and Multinational Enterprises included language on transnational bribery, but this initiative was never followed up.

Finally, in parallel with the UN initiative, a special commission appointed by the ICC drafted a report on the issue, including “Recommendations to Combat Extortion and Bribery in Business Transactions,” that was released on 29 November 1977. Due to controversy over some of the recommendations, and without the backing of governments, the attempt at self-regulation remained a dead letter until 1996 when a new report was approved.

## **The OECD Initiative, 1989-96**

US officials at the OECD launched a new initiative to combat bribery of foreign officials in commercial transactions in 1989. Finally, in the spring

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2. A 1988 amendment to the FCPA allows firms to invoke as an affirmative defense evidence that a questionable payment is legal under the laws of the country in which it was made.

3. This occurred first in the ECOSOC’s Commission on Transnational Cooperation, later in the Committee on an International Agreement on Illicit Payments.

of 1994, the OECD ministers agreed on a formal recommendation calling on member states to take “effective measures to deter, prevent, and combat the bribery of foreign public officials.” Two years later, OECD ministers approved a second recommendation calling on members to review tax policy and, where permitted, to remove provisions for deducting bribes as a business expense.

It may astonish that it took five years and a considerable amount of pressure to agree on a nonbinding text as general and vaguely worded as the 1994 OECD Recommendation on Corruption in Business Transactions. On the other hand, this is the first international text in which the industrialized nations vowed to take concrete steps against corruption and agreed to follow up by discussing specific measures in greater detail and by mutually evaluating the progress made on a national basis.

The progress made between 1989 and 1994 was vital for the development of international instruments against commercial corruption, not least because it demonstrated that many of the skeptics realized that such an effort was in the genuine interest of their own business communities. The reasons for the change of attitude vary from country to country. Some still-hesitant countries may have felt embarrassed to oppose anti-corruption efforts. Others have realized that common action was not so utopian after all. In a third group of states, the recent flurry of scandals made politicians realize that the general public was fed up with both domestic and international corruption. The issue gained a far more prominent role in public discourse over these five years.

However, only the future will show if the commitments are backed by sufficient conviction to ensure effective implementation. This is where the follow-up procedures contained in the recommendations become important.

The 1994 recommendation, apart from the general commitment to take meaningful steps to combat corruption, listed specific items for domestic or international cooperative action. Thus, the real significance of this text lies in the process it initiated: a follow-up mechanism with regular reviews of the steps taken by member countries to implement their commitments.

## **Implementation Activity**

Since adoption of the 1994 recommendation, several countries have begun revising relevant domestic legislation, especially on tax treatment of bribes and on the criminalization of the bribery of foreign officials. Others have realized that existing legislation already covers the same ground, or much of it, if interpreted accordingly.

Many countries have indicated that ancillary legislation, such as laws

on unfair competition or on conspiracy, could be used to fight the bribery of foreign officials. Britain has notified the OECD that its 1906 legislation clearly covers bribery of foreign officials. The Netherlands and most Nordic states have already drafted legislation on criminalization of bribery of foreign public officials. Japan is considering extending its unfair competition legislation to cover Japanese bribing of foreign officials both abroad and in Japan. In most countries, internal working parties are discussing the issue. In several countries, such as Great Britain, Switzerland, and Norway, tax deductibility of bribes is being banned. Other countries, such as Germany, have taken steps to toughen up national legislation on corruption and might eventually cover the criminalization of international corruption.

Such changes are being recorded as part of the follow-up procedures. At the same time, the OECD has the mandate to conduct in-depth studies on specific items listed in the recommendations. In 1995 and 1996, four studies were launched on the following topics:

- tax deductibility of bribes;
- criminalization of bribery of foreign public officials and of the laundering of the illicit proceeds of corruption;
- adjustment of bookkeeping and auditing rules to prevent corruption;
- establishing a minimal standard on public procurement as well as using access to public contracts as an incitement or sanction.

Each close-up analysis starts with a hearing of experts, followed by a report detailing the problems encountered with existing legislation in various countries and a discussion of options for change. It finishes with a draft recommendation.

The working group has gone into great detail, especially on criminalization. It has so far not attempted to draft a harmonized text for national adoption; it is concerned, rather, with defining a minimal standard for all industrialized countries. Substantial leeway for implementation according to local legal traditions will remain. Still, many questions need to be resolved. For instance, when defining the categories of bribe recipients, the OECD could refer to the “victim” countries’ law or attempt an autonomous definition of public officials. So far, the OECD has concentrated on corruption of public officials, but in view of the privatization of official functions that is occurring around the world, discussion may need to be extended to the corruption of private operators at a later stage. The formerly highly politicized issue of jurisdiction is now being discussed on a more technical level. In particular, some countries restrict application of their laws to crimes committed on their territory—even if the connection to the territory may be slight (such as

a cross-border facsimile transmission). Other subissues at a similar level of detail are under discussion.

The idea is that in May 1997, when the text of the recommendation of 1994 is to be reviewed in the light of recent developments (a procedure agreed upon in the recommendation itself), elements for a substantially tougher recommendation will be readily available. The OECD has not yet decided whether to seek a more binding text on corruption. It may at some point be necessary to define the minimal standard in a convention. A convention has the advantage of precision, but it lacks the flexibility of soft law and is far more time-consuming to enact and to implement. Soft law is especially effective where political will needs to be generated, as long as it follows strict monitoring procedures.

An example of the effectiveness of this process is the Financial Action Task Force on Money Laundering. This group developed ideas for controlling money laundering in just half a year and achieved implementation over five years in all the major financial centers without drafting a formal treaty. The process started with the 1988 Vienna Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances. This text, however, covered only a small part of the money laundering problem. The detailed proposals for preventing money laundering were developed in the task force.

Implementation of the task force's recommendations on money laundering was supported by regional initiatives such as the Council of Europe's Convention 141 on Laundering, Search, Seizure, and Confiscation of the Proceeds of Crime, achieved in 1990. That same year, the European Union also approved a directive creating binding standards to discipline activities that facilitate money laundering.<sup>4</sup> The OAS's Inter-American Drug Abuse Control Commission (CICAD from the Spanish) in 1992 and the United Nations in 1995 also released model texts for the prevention of money laundering.

However, the actual motor driving implementation of the task force's 1990 recommendation on money laundering has been a tough, worldwide (but still voluntary) mutual evaluation scheme. Under this mechanism, members monitor not only changes in legislation but also current practices of each member country. OECD procedures also allow for such evaluations. The way forward on the issue of corruption does not have to replicate the task force process for combatting money laundering, but it certainly will be inspired by the experience.

The 1994 OECD recommendation on corruption contains another dynamic element that allows the organization to broaden the scope of

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4. Convention 141 ensures mutual legal assistance in confiscation cases, even where national legal concepts diverge. The EU directive transposes the regulatory recommendations of the Financial Action Task Force—for monitoring the “know your customer” policy and awareness standards—into binding law for member states. The program has since been implemented by most EU members.

international cooperation on this issue. It asks the secretariat of the OECD to consult with international organizations and international financial institutions on a joint approach. It furthermore asks the secretariat to include nonmember states in the process. This clause is especially relevant to those doing business with, or in competition with, economies in transition, especially in Southeast Asia. As a first step, the OECD hosted a worldwide symposium in March 1995. In addition, the Council of Europe, the European Union, the OAS, and the World Bank regularly attend meetings of the OECD Task Force on Bribery as observers. Mexico, Hungary, and the Czech Republic have joined the OECD, and Korea's accession was approved in late 1996. Argentina is also interested in assisting the group. The issue of further broadening participation will be taken up below in the discussion of development of a worldwide strategy.

### **The 1996 OECD Council Recommendation on Tax Deductibility**

In 1995 and 1996 a working group of the Fiscal Affairs Committee of the OECD examined the issue of tax deductibility of bribes to foreign public officials, one of the items raised in the 1994 recommendation. After some tough negotiation, the committee suggested that the council adopt a separate recommendation calling on member states to reexamine tax treatment with the intention of denying deductibility. The recommendation was approved by the OECD Council at its meeting in April 1996 and by the ministers in May. Even if the text sounds weak, it is the first straightforward international instrument—adopted by member states—asking for a ban on tax deductibility of bribes.

At the May 1996 meeting, the ministerial council also considered the issue of criminalization of transnational bribery, as well as the laundering of such funds. The working party on bribery has been invited to present detailed suggestions both in substance and on the choice of the right instrument (recommendation or convention) at the next ministerial meeting in 1997.

These two issues are of considerable symbolic significance to a worldwide approach to corruption. Their adoption would signal an important breakthrough. That will depend, however, on the willingness of members to take the domestic actions required to implement their commitments. Close monitoring will be necessary, especially since some countries needed much convincing to subscribe to the final document.

### **Other International Initiatives against Corruption**

As described by Glynn, Kobrin, and Naím in chapter 1, anticorruption initiatives appear to be cropping up all over the globe. I will describe some of these initiatives below, focusing on the international financial

institutions (IFIs), regional organizations, and nongovernmental organizations.

## **International Financial Institutions**

Multilateral development agencies, especially the World Bank, have long been acquainted with the risk of corrupt schemes undercutting their aims. The traditional approach on a project level has been to insist on open, competitive bidding. This has been only a partial success, however, since many ways exist to evade the controls (Moody-Stuart 1994). The World Bank and International Monetary Fund have also tried more general approaches, especially making loans conditional on structural reforms with the goal of reducing corruption. With its recent emphasis on the importance of “good governance” in development, the World Bank often requires a wide range of public-sector reform activities to increase transparency, accountability, and participation in lending countries.

As some critics point out, however, the effects of many structural reform programs have been ambiguous regarding corruption. Often the required reforms have resulted in the reduction of public servants’ wages, actually pushing them into illicit means of meeting their costs of living. Bank and Fund conditionality also usually requires some degree of austerity, which is felt heavily by the population, but without always securing strict enough controls on the use of the loans. Under such conditions, corruption may undermine public support for structural reforms.

One barrier to greater IFI activism against corruption is the understanding some lending institutions have of their political neutrality. Recently, however, attitudes have begun to change, and there is currently an active discussion in the World Bank taking place on how best to prevent corruption in projects it funds. The recently revised World Bank Guidelines on Procurement reserve to the World Bank the right to declare a procurement null and void where a contract was awarded on the basis of corrupt practices (appendix 4, Guidance to Bidders, paragraph 3). The role of the World Bank in the prevention of corruption is absolutely vital. Current and expanded efforts will be a necessary counterpart to action by industrialized countries.

## **Regional Initiatives**

Regional international organizations in Europe and the Western Hemisphere also are tackling the issue of corruption.

Following a request by the meeting of European Ministers of Justice in Malta in 1994, the Council of Europe is examining the drafting of an international convention on corruption aimed at creation of binding laws. The approach is very broad, with a definition of public and

private corruption that addresses both national and international corruption. It is of special significance that this effort includes countries in Eastern Europe. The Council of Europe also has the right to invite other participants. So far, the United States, Canada, and Japan have been participating in the meetings. The secretariat has prepared two draft conventions: one conceived as a framework convention containing the general principles and another more specifically concentrating on aspects of criminal law. The group is currently working on the drafts. Further working parties of the Council of Europe have been discussing administrative and private law sanctions.

Separately, in December 1995, the European Union finalized a protocol to the Convention on the Protection of the European Communities Financial Interests that commits member countries to criminalize the corruption of European officials and of officials of the other member states. This initiative is restricted to the context of "community fraud." The approach is binding but limited *inter partes* to members. A more general convention on internal EU corruption was initiated by Italy during its presidency of the European Union in the spring of 1996.

At the regional level, the OAS has made a most impressive attempt to harmonize rules against corruption. The Inter-American Convention against Corruption was adopted at an OAS conference on 29 March 1996 in Caracas. In contrast to an earlier draft, it goes beyond a mere multilateral treaty on extradition and mutual legal assistance. It calls on member states to criminalize both national corruption and transnational bribery and makes both extraditable offenses, subject to each member's constitutional and other fundamental legal principles.

## **Nongovernmental Organizations**

Several NGOs have also been intensifying their work on international corruption. The International Chamber of Commerce (ICC) recently reviewed its 1977 guidelines, and in March 1996 the executive board approved a revised and updated set of recommendations (see Heimann, chapter 8, for a description of the new ICC recommendations). While reminding international organizations and governments of their role, it recommends specific rules of conduct for enterprises, toughening up the language of the 1977 report. The rules are meant to be adopted in company codes, applicable also to subsidiaries. Special attention is given to handling agents to prevent them from corrupting foreign government officials.

The Interparliamentary Union at its conference in Bucharest on 13 October 1995 adopted a resolution for controlling corruption and calling for international cooperation in this field. Among other points, it recommends criminalizing the bribery of a foreign official as well as cooperation in preventing the laundering of illicit corruption proceeds.

Transparency International, the specialized NGO concentrating on the prevention of corruption, has been rather active in its brief existence. It has founded chapters all over the world, organized conferences, edited a comprehensive source book on corruption, and, above all, has developed a *renomé* as a reliable partner: it fulfills an essential liaison role between international organizations, governments, and the business communities. One of its most original ideas is the creation of “islands of integrity,” in which all participants in an area or a specific market or even a large project (officials and privates) are invited to formally declare that they will not engage in corrupt practices.

## Future Developments

Of course, the essential question is whether all these initiatives and activities fit together and how best to pursue a coherent strategy to reduce international corruption in a business context worldwide in the near future.

Starting from the perspective of the businessperson, I am convinced that we have to take the anxieties of the business communities seriously, especially the problem that huge public procurement contracts may be lost due to corrupt payments. To submit individual competitors to a prohibition of corruption under current circumstances means to inflict a trade disadvantage on them. Therefore, the expansion of actions against corruption has to bind all major competitors simultaneously. Orchestrating such coordinated action is what international organizations can offer in this field. I would, however, like to advocate a flexible approach—one might call it the principle of “joining the club.” It involves three stages:

- securing the political determination;
- broadening the geographic scope;
- integrating the business community.

## Securing the Political Will

It may seem inadequate to concentrate on the corruptors of foreign public officials, predominantly to be found in multinational companies based in the North. Such an approach is for the time being favored by the OECD, since that reflects both its membership and its mandate. I would not maintain that corresponding action is not necessary on the recipient side, both in the North and the South. However, an approach focusing on the supply side of corruption seems more feasible in the short run, given the relatively smaller number of actors.

Political resolve to combat international bribery in business transactions is growing. The G-7 leaders' declaration in June 1996 to support OECD efforts is a breakthrough in efforts to establish coordinated standards—at least in industrialized states. The commitment of formerly reluctant states such as France, Germany, and Japan has been essential. But a consensus on exactly what to do and how to implement it still needs to be achieved. Here, the work done in a regional context—through the OAS, the European Union, and the Council of Europe—will be very valuable because this work has generated first solutions to some difficult technical problems. Furthermore, the acceptance of multilateral measures to prevent international corruption will grow when there are regional concepts in place. There is still a certain risk in delay: some states insist on the drafting of a treaty, especially on criminalization. If the forum chosen is too regional (for example, the European Union), it will not reach the decisive markets (i.e., Southeast Asia). If, on the other hand, the forum is too wide, a replay of the UN debacle of 1979 must be anticipated. The main political challenge of the near future will be to keep up the momentum and still do some very concrete and relevant work.

It may be added at this point that backsliding into unilateralism would be detrimental to the results already achieved. It is a matter of honor for some self-respecting nations to join the efforts on their own terms. They also join because they are convinced that concerted action is preferable to blackmail. Too much pressure from one country or a group of countries could derail collective efforts.

As for the OECD, the organization's role will be to build political will and apply indirect pressure through peer review and follow-up procedures. The next step will be creation of a concrete, formal recommendation against which members, observers, and potentially other countries may be evaluated.

## **Broadening the Geographic Scope**

Again, simultaneous efforts should be made both on the donor and recipient sides of the bribe transaction. There is no longer a clear-cut distinction between North and South, since corruption seems to be universal. Still, there are marked differences between forms of bribery limited to a specific industry (for instance, the construction industry in a Western European country) and an endemic corruption culture that affects all aspects of public life.

Even if it makes sense to coordinate actions of development and lending agencies, regional organizations such as the OAS, and economic organizations such as the OECD and WTO, there is an argument for keeping efforts by the countries of the North relatively independent of wider circles until the concepts are firmly accepted. To establish links between

the OECD and WTO makes sense. As a first step, the United States suggested including commercial corruption on the agenda of the first WTO ministerial in Singapore in December 1996.

Of course, timing is key. On the subject of money laundering, the Financial Action Task Force maintained that a standard could be submitted to a much larger circle for new discussion as soon as it had been accepted by the smaller group. But the standards on corruption stand a much greater chance of being accepted by the large countries of the South if the North demonstrates its own commitment and readiness to take responsibility, part of which is the resolve to implement its own standards. This step has yet to be taken.

## **Integrating the Business Communities**

I regard it as fundamental to include the business communities when developing a broad concept for combatting international corruption. It is a common experience in talks with responsible businesspeople to find that they strongly favor stiff sanctions against corrupt practices, provided they are applied universally, effectively, and in a coordinated way. Concepts should not be developed without consultation and without the support of the private sector. In this spirit, the OECD held a joint meeting with representatives of business organizations and of active businesspeople in its member states in the fall of 1996.

The recent ICC recommendations also clearly signal the corporate interest in cooperating with international organizations and governments. The elementary contribution by the business communities and each individual company is not only the development of company codes but of the actual compliance programs for day-to-day work.

## **Final Remarks**

This paper has placed a special emphasis on the rationale for maintaining or creating a level playing field for commerce. It has furthermore concentrated on initiatives suggested for and by industrialized countries. This is certainly only a partial perspective. The approach has been chosen predominantly for strategic reasons. With the cooperation of industrialized countries as well as the business communities, an internationally coordinated approach could be feasible in the near future.

## **References**

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