

# OFFICE OF INSTITUTIONAL INTEGRITY

ANNUAL REPORT 2012



Inter-American Development Bank



Inter-American  
Investment Corporation



Multilateral Investment Fund  
Member of the IDB Group

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1300 New York Avenue, N.W.  
Washington, D.C. 20577

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**Cataloging-in-Publication data provided by the  
Inter-American Development Bank  
Felipe Herrera Library**

Office of Institutional Integrity: 2012 annual report.  
p. cm.

1. Office of Institutional Integrity. 2. Transparency in international agencies. I. Inter-American Development Bank. Office of Institutional Integrity.

## INTRODUCTION

Combating fraud and corruption in activities financed by the Inter-American Development Bank (IDB or the Bank) is essential to fulfilling the IDB's fiduciary duty to ensure that its funds are used for their intended purposes. Fraud and corruption undermine the Bank's efforts to contribute to the economic and social development of regional developing member countries. As stated by President Moreno in connection with the events commemorating International Anticorruption Day, "corruption reduces the confidence citizens have in their governments, obstructs efforts to eliminate poverty, and undermines the ability of all citizens in Latin America and the Caribbean to enjoy the benefits of development".

The IDB Group's integrity framework is based on three pillars

- ✓ ensuring that activities financed by the IDB Group are free of fraud and corruption;
- ✓ supporting programs that strengthen good governance, enforce the rule of law, and combat corruption; and
- ✓ promoting the highest levels of integrity in IDB activities.

Responsibility for implementation of the first pillar resides primarily with the Office of Institutional Integrity (OII), the Case Officer (CO), the Sanctions Committee (SNC) and the Anti-Corruption Policy Committee (ACPC). Because the Sanctions System managed by these entities is essentially reactive, OII also seeks proactive, value-added ways to address fraud and corruption through its prevention efforts.

But in a larger sense, ensuring that IDB Group activities are free of fraud and corruption requires the active participation of every person at the Bank, the executing and enforcement agencies in our Borrowing member countries, and the civil society at large. Thus, the results presented in this Annual Report reflect not only the effort of OII and other units of the Sanctions System, but the collective effort of all who have cooperated with OII's mandate, to whom we are grateful. To further the effectiveness of actions taken in support of the integrity framework's first pillar, OII will continue to seek the proactive engagement of partners within and outside the Bank.

### OFFICE OF INSTITUTIONAL INTEGRITY

OII is an independent office of the IDB that reports directly to the President. It also reports on its activities and results to the Audit Committee of the Board of Executive Directors. OII has two primary mandates: investigation and prevention of Prohibited Practices<sup>1</sup> in IDB Group-financed activities. To fulfill these equally important goals, OII's internal structure incorporates an investigative and a preventive team. The first is responsible for investigating allegations and presenting cases before the adjudicative bodies of the Sanctions System. The second is responsible for designing tools and training materials and providing advice to Operational Divisions within the IDB Group to help identify and mitigate integrity and related reputational risks. Both teams conduct training activities for IDB staff and engage in outreach with stakeholders outside the IDB Group.

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<sup>1</sup> Prohibited Practices include fraudulent, corrupt, coercive, collusive and obstructive practices, as defined in the Sanctions Procedures of the IDB.

## HIGHLIGHTS

### INVESTIGATION

- ➔ **Intake.** Reviewed 127 new allegations.
- ➔ **Investigations.** Closed 104 cases, 65 of which had passed the threshold analysis.
- ➔ **Preliminary Notices of Administrative Action.** Submitted to the Case Officer eight Preliminary Notices of Administrative Action against 17 Respondents.
- ➔ **Replies.** Submitted Replies to the SNC for nine cases, involving 17 Respondents.
- ➔ **Cross-Debarments.** Processed 40 Notices of Cross-Debarment received from other International Financial Institutions (IFIs) and issued 55 such notices.

### PREVENTION

- ➔ **Consultations.** Handled 264 consultations.
- ➔ **Training.** Trained SCF and OMJ staff regarding integrity due diligence and use of foreign jurisdictions in non-sovereign guaranteed operations, and designed two online training tools on integrity issues.
- ➔ **Policy Development.** Delivered a draft Partnership Integrity Due Diligence Guideline and Procedures to the Officer of Outreach and Partnerships (ORP).
- ➔ **IRR.** Reviewed the Integrity Risk Review methodology to assess its effectiveness as a risk management tool for the design and implementation of IDB financed Sovereign Guaranteed Operations.
- ➔ **Compliance Screening System.** Sponsored implementation of capital budget project that consists of a system to allow various bank departments to screen names (*e.g.*, recipients of payments, potential counterparties, etc.) against the internal eligibility verification list and external watch lists.

**OUTREACH**

- **International Anticorruption Week.** Organized, in collaboration with several departments, a week-long series of events to commemorate International Anti-corruption Day.
- **IFIs.** Participated in regular meetings with heads of investigation, and, on a day-to-day, basis closely coordinated with the integrity offices at other IFIs.

## INVESTIGATIVE ACTIVITIES

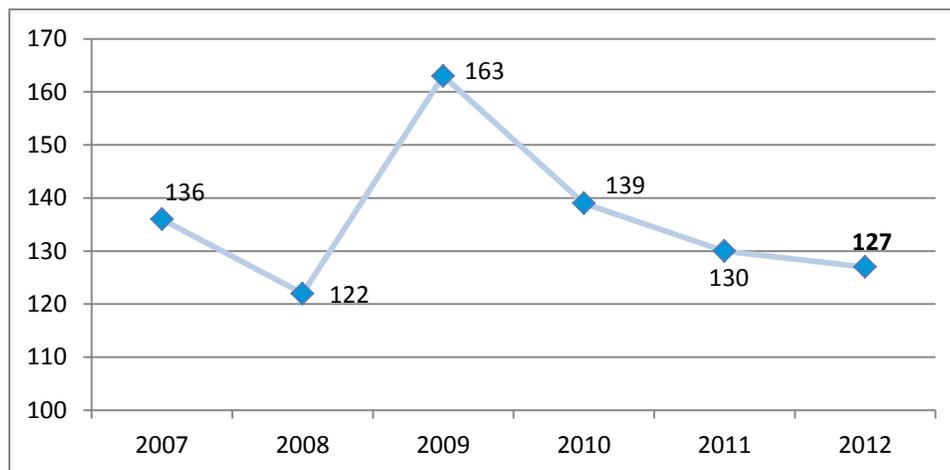
### Caseload

OII started the year with 45 active cases. In the course of 2012, OII opened 127 new cases for a total of 172 active cases. As of December 31, 2012, OII completed 104 cases. The average time of completion for those 104 cases is 129 days.

**Table 1:** CASELOAD SUMMARY, 2007 – DECEMBER 31, 2012

	2007	2008	2009	2010	2011	2012
Pending Investigations (prior year)	123	97	69	80	65	45
New Investigations (Allegations)	136	122	163	139	130	127
Active Investigations	259	219	232	219	195	172
Completed Investigations	162	150	152	154	150	104 <sup>2</sup>
Pending Investigations (period's end)	97	69	80	65	45	68
Post-Investigation Activities (cases)						9

**FIGURE 1:** TOTAL NEW ALLEGATIONS RECEIVED 2007-2012

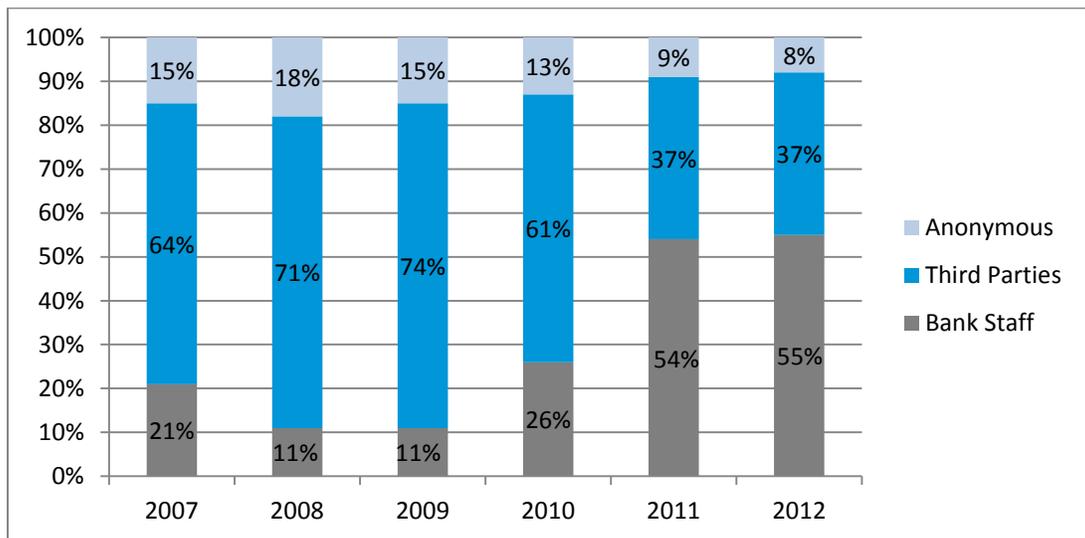


<sup>2</sup> The 6 year average for case completion is 67% and the 2012 was 60%. This minor drop was in part attributed to: (i) fewer cases carried over from previous year; and (ii) several internal vacancies.

## Sources of Allegations and Contact Methods

OII obtains allegations about possible Prohibited Practices mainly from three sources: (i) third parties; (ii) Bank-staff;<sup>3</sup> and (iii) anonymous. Of the cases opened in 2012, 55% of the allegations were received from IDB Group staff, 37% were received from third parties, and 8% were received from anonymous sources. Third party sources include, among others, executing agencies, other public officials, bidders, contractors, consultants, employees of NGOs, and the media.

**FIGURE 2:** SOURCE OF ALLEGATIONS IN PERCENTAGE 2007-2012

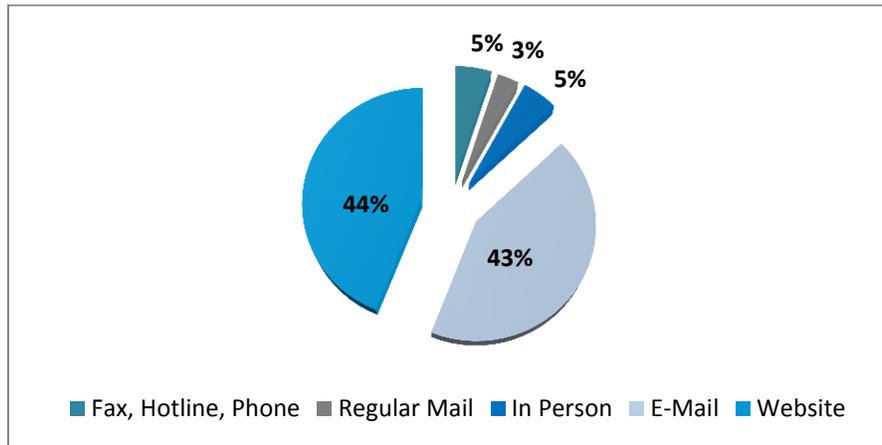


We interpret this increase in the number of allegations received from Bank staff over the last two years as a positive indicator of staff awareness and willingness to collaborate with OII's mandate. However, since that increase has not been accompanied with an increase in the overall number of allegations, it may also indicate that third parties are reporting indirectly, through the Bank Country Offices. This decrease in third party reporting justifies the need to intensify outreach efforts, particularly with supreme national audit institutions and law enforcement agencies.

## Contact Methods

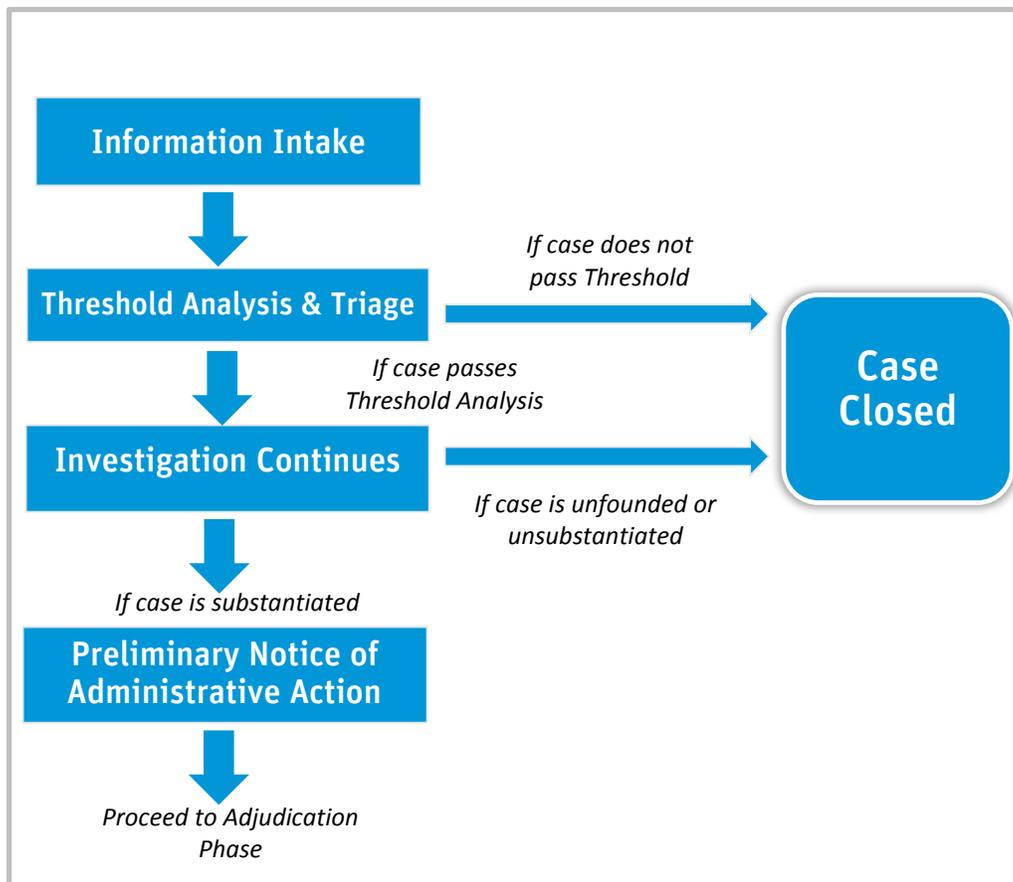
OII offers several methods for submitting inquiries or allegations of Prohibited Practices. These includes e-mail, the website, postal mail, telephone, fax, hotline, and in person. Figure 3 provides a breakdown of the reporting mechanisms that were utilized to submit allegations of Prohibited Practices in 2012, evidencing that the website and email are, as in past years, the principal methods of contact.

<sup>3</sup> This includes information obtained through research conducted by staff of the Office of Institutional Integrity.

**FIGURE 3: HOW ALLEGATIONS WERE SUBMITTED 2012**

### Investigative Process – Anatomy of an Investigation

The diagram below illustrates the different phases of an investigation as well as its possible outcomes.

**DIAGRAM 1: ANATOMY OF AN INVESTIGATION**

## THRESHOLD ANALYSIS

When OII receives an allegation of a possible Prohibited Practice it gathers information to determine if the following criteria are met:

- ✓ The information concerns an activity financed by the IDB Group.
- ✓ The information concerns the IDB Group's Prohibited Practices.<sup>4</sup> (See Box 1)
- ✓ The information is sufficiently credible.

### Box 1

#### The IDB Group's Prohibited Practices

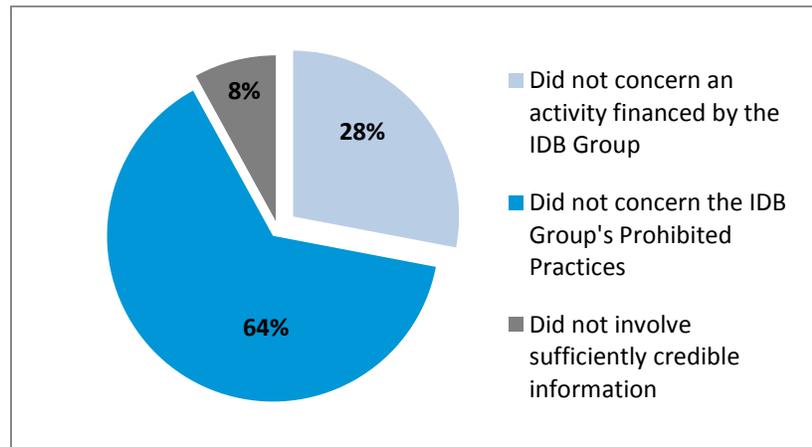
- ✓ A **corrupt practice** is the offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence improperly the actions of another party.
- ✓ A **fraudulent practice** is any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or 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 improperly influence 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.
- ✓ An **obstructive practice** is (a) deliberately destroying, falsifying, altering or concealing evidence material to the investigation or making false statements to investigators in order to materially impede a Bank Group investigation into allegations of a corrupt, fraudulent, coercive or collusive practice; and or threatening, harassing or intimidating any party to prevent it from disclosing its knowledge of matters relevant to the investigation or from pursuing the investigation, or (b) intentionally acting to materially impede the exercise of the Bank Group's contractual rights of audit or access to information.

Of all investigations opened during 2012, 39 (31%) investigations were closed at this initial stage. Of these 25 (64%) did not concern the commission of a Prohibited Practice, 11 (28%) did not concern an activity financed by the IDB Group, and the remaining three (8%) did not involve sufficiently credible information. The average time of completion for those 39 investigations was 57 days.<sup>5</sup>

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<sup>4</sup> Inter-American Development Bank, *Sanctions Procedures of the Inter-American Development Bank*, §2.2 (April 2011).

<sup>5</sup> The initial threshold analysis is generally completed within 72 hours. In certain cases the information provided in the allegation is sufficient to reach a definitive conclusion at this stage. Most cases require that additional information be gathered, before a conclusive answer to the threshold questions can be reached.

**FIGURE 4:** CLOSED CASES AFTER THRESHOLD ANALYSIS 2012

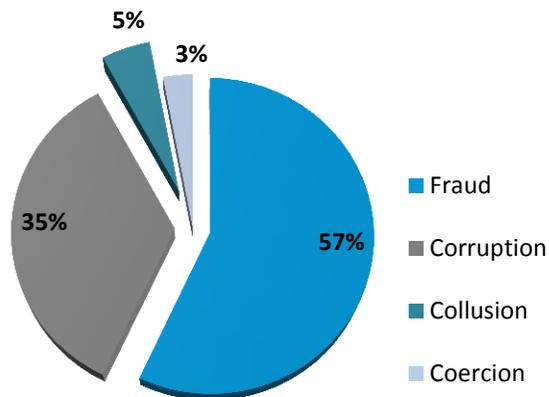
When allegations are not related to IDB Group's Prohibited Practices, but involve IDB Group financed-activities or may otherwise affect the reputation of the Bank, OII liaises with the responsible Bank office to ensure complainants receive appropriate attention.

**TABLE 2:** REFERRALS 2012

REFERRALS OF ALLEGATIONS THAT DID NOT MEET THRESHOLD ANALYSIS	
Ethics Office	12
Legal Department	6
Country Department	1
Country Office	3
Office of the Executive Auditor	2
Office of External Relations	1
International Financial Institutions	3
<b>Total:</b>	<b>28</b>

## INVESTIGATION

After conducting the threshold analysis and based on the information provided in the allegation, OII investigators conduct a fact-finding inquiry to obtain evidence and analyze the established and alleged facts of an investigation. During 2012, this was conducted for 88 new investigations.

**FIGURE 5:** TYPES OF NEW ALLEGATIONS 2012

The distribution of the allegation-types for these 88 new investigations reveals that fraud and corruption are the most common Prohibited Practices investigated, at 57% and 35%, respectively. Collusion accounted for 5% and coercion accounted for 3%. There were no investigations of obstructive practices.

It is important to note that OII bases its initial classification on the information obtained during intake. Over the course of an investigation, as evidence is gathered, additional violations of Prohibited Practices may be uncovered.

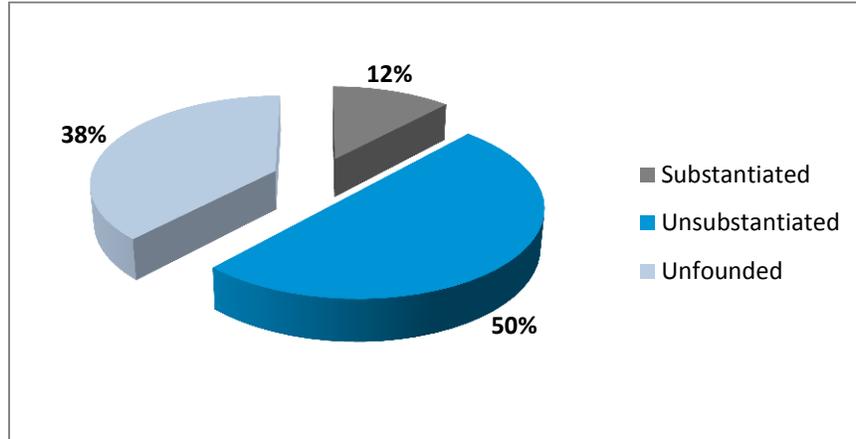
## COMPLETED INVESTIGATIONS AND OUTCOMES

Based on the results of an investigation, if the Chief of OII considers that the evidence supports a finding that the subject of an investigation engaged in a Prohibited Practice, OII submits a Preliminary Notice of Administrative Action (PNAA) to the Case Officer. Conversely, if the Chief of OII determines that the allegation is unsubstantiated or unfounded, OII closes the case.

### Box 2 Case Outcomes

- ✓ A case is **substantiated** when a preponderance of the evidence supports the allegation of a Prohibited Practice. A “preponderance of the evidence” means that it is more likely than not that a Respondent has engaged in a Prohibited Practice.
- ✓ A case is **unsubstantiated** when the evidence is insufficient either to confirm or deny that a Prohibited Practice occurred.
- ✓ A case is **unfounded** when the evidence is sufficient to conclude that a Prohibited Practice did not occur.

During 2012, out of the 172 active investigations, OII completed 65 investigations that had passed the threshold analysis (for a total of 104, when added to the 39 that did not pass the threshold analysis). Of these 65 investigations 12% were substantiated, 50% were unsubstantiated and 38% were unfounded. The average time of completion for the unsubstantiated and unfounded investigations was 162 days, while the average for substantiated investigations was of 238 days.

**FIGURE 6:** INVESTIGATION OUTCOMES IN 2012**TABLE 3:** COMPLETED INVESTIGATIONS AVERAGE TIME

	DAYS
All investigations	129
Did not pass threshold analysis	57
Unfounded and Unsubstantiated (after threshold)	162
Substantiated	238

The substantiated cases resulted in the submission to the Case Officer of eight PNAAs against seven firms and ten individuals. OII concluded that it was more likely than not that these 17 Respondents had engaged in the following types of fraudulent practices:

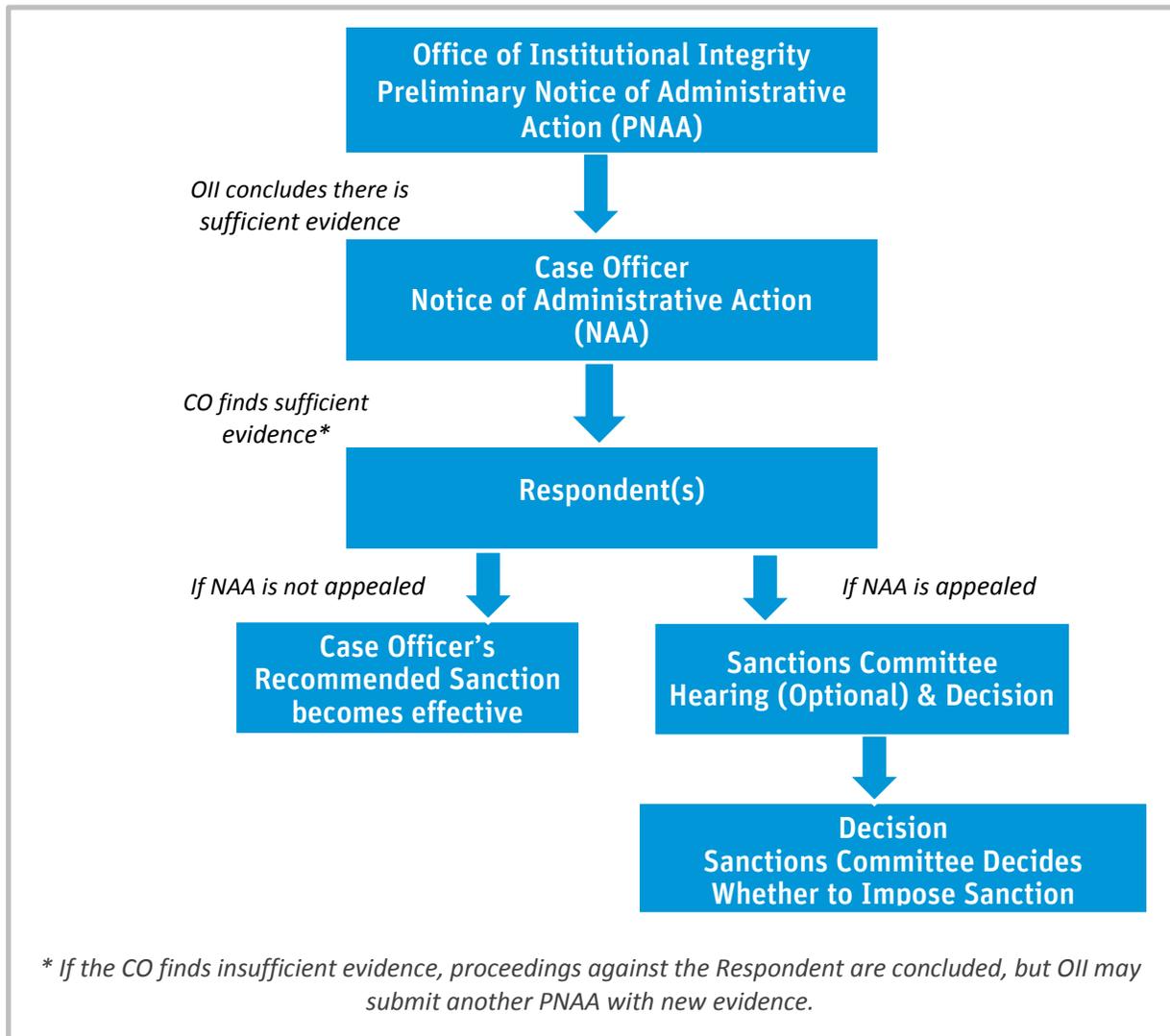
- ✓ Bidders falsified certificates or contracts to demonstrate technical experience required in the bidding documents.
- ✓ Sub-consultant misrepresented qualifications and past experience to meet minimum requirements in the terms of reference.
- ✓ Bidder misrepresented its financial capacity through manipulation of financial statements, the falsification of a certificate of letter of credit and the submission of other bank certificates with incomplete and misleading information.
- ✓ Bidders falsified documentation required in the bidding documents, including certificate of manufacturer of equipment, certificates of good standing issued by tax authorities and certificates that a company was affiliated and in good standing with health insurance provider.

## POST INVESTIGATIVE ACTIVITIES DURING THE ADJUDICATION PHASE

### Sanction Process

The diagram below illustrates the two-tier system of the sanction process:

**DIAGRAM 2:** ANATOMY OF AN INVESTIGATION – ADJUDICATION PHASE



### First-Tier - The Case Officer

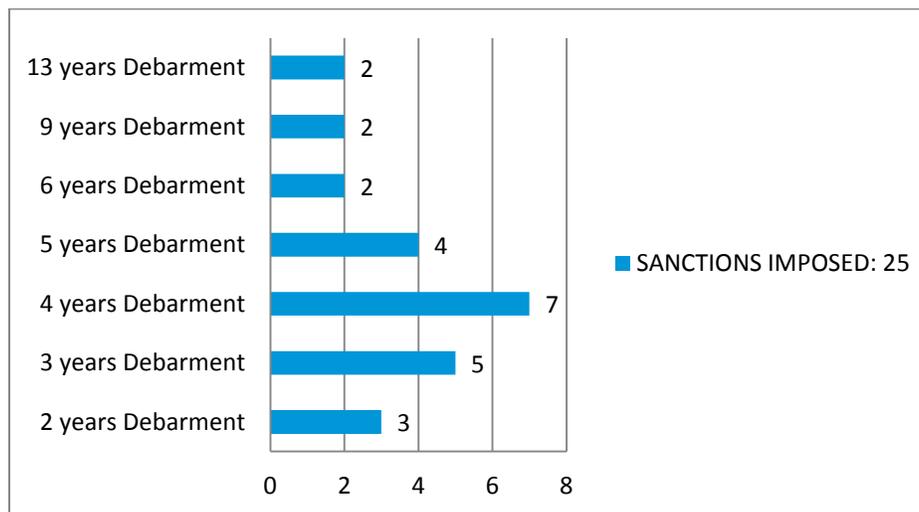
The Case Officer (CO) reviews the PNAAs submitted by OII and may take the following actions for each Respondent:

- ✓ If a preponderance of the evidence supports the finding that the Respondent engaged in a Prohibited Practice, issue a Notice of Administrative Action (NAA).
- ✓ If a preponderance of the evidence does not support the finding that the Respondent engaged in a Prohibited Practice, abstain from issuing a NAA, after consulting with the Chairman of the SNC. The proceedings against the Respondent are concluded, without prejudice
- ✓ If a Respondent has committed a procedural irregularity or an act of wrongdoing other than a Prohibited Practice, refer the matter to other units of the IDB Bank Group.

During 2012, the CO reviewed nine PNNAs (three carried over from 2011 and six out of eight submitted during the period). All resulted in the issuance of NAAs against the involved Respondents. In total, the Case Officer issued 23 NAAs against nine entities and 14 individuals.

Also, the period to appeal the CO's determination elapsed for 42 Respondents. Of these, 25 did not appeal, and the sanction recommended on the basis of OII's investigative activities became effective. 17 Respondents submitted a Response to the NAA, triggering the appeal phase.

**FIGURE 7: SANCTIONS IMPOSED DURING THE FIRST-TIER REVIEW**



## Second-Tier – Sanctions Committee

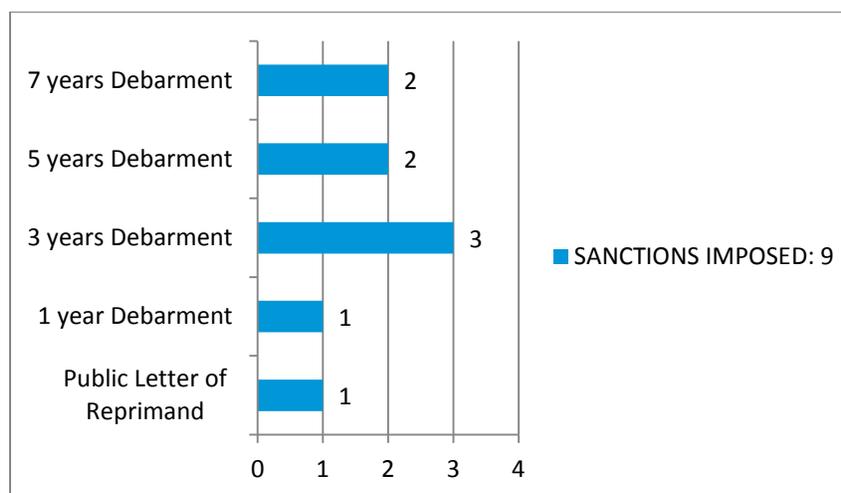
The SNC is the second and final tier of review in the sanctions system. After receiving the Case Officer's NAA, a Respondent may submit a Response to contest the finding of a Prohibited Practice, the level of the Recommended Sanction, or both. In this instance, the SNC is responsible for deciding if the Respondent engaged in a Prohibited Practice. This decision is made after OII and the Respondent are given the opportunity to submit, respectively, a Reply and a Surreply.

During 2012, OII was notified of Responses for nine cases involving 17 Respondents and submitted Replies to contest the arguments of 14 of them.<sup>6</sup> OII submitted three additional Replies to contest the arguments of three Respondents, whose Response had carried over from 2011.<sup>7</sup>

In accordance with the Sanctions Procedures, the SNC has discretion to hold hearings as it deems appropriate. During the first semester of 2012, the SNC afforded two Respondents, in one case, the opportunity of a hearing. These two hearings were the first ever held by the SNC or any of its predecessors. OII presented oral arguments in which it referred to the evidence supporting a finding that the respective Respondents had engaged in a fraudulent practice. The SNC decided the case with the imposition of three sanctions: an issuance of a public reprimand to an entity and the debarment of two individuals.

The SNC decided all cases that had reached maturity. These involved 15 Respondents of whom nine were found to be responsible of Prohibited Practices. The remaining six the SNC did not find sufficient evidence of a Prohibited Practice.

**FIGURE 8: SANCTIONS IMPOSED BY THE SNC DURING THE SECOND-TIER REVIEW**



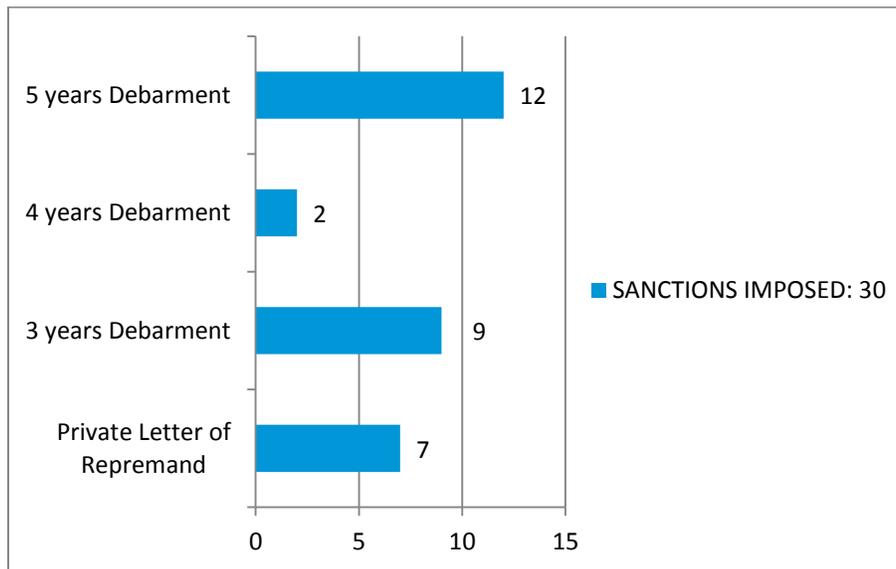
<sup>6</sup> The Reply to the remaining Responses was presented in January, 2013.

<sup>7</sup> In some cases, Respondents opt for presenting their Responses jointly, while in others they present their Responses separately.

### Former Sanctions Committee – Legacy Cases

During 2012, the SNC and the Sanctions Committee, as constituted prior to April 1, 2011, co-existed because 14 cases were pending decision by the latter. In the course of 2012, the former Sanctions Committee decided 11 cases,<sup>8</sup> imposing sanctions in eight of them. The sanctions included private letters of reprimand issued to two entities and five individuals, and the debarment of nine entities and 14 individuals.

**FIGURE 9:** SANCTIONS IMPOSED BY THE FORMER SANCTIONS COMMITTEE



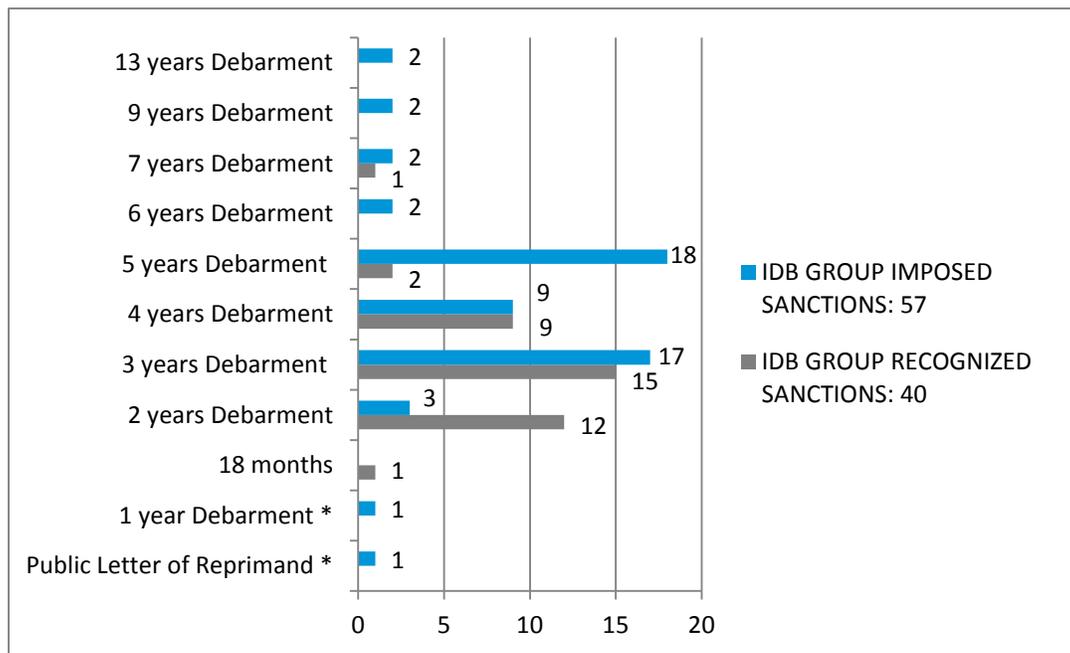
<sup>8</sup> The proceedings in three cases before the Sanctions Committee, as constituted prior to April 1, 2011, have been suspended in accordance with the Sanctions Procedures to pursue discussions for settlement as initiated in the investigative phase.

### Total Sanctions Imposed and Cross-Debarments

In sum, on the basis of OII’s investigative activities and the work of the CO and SNC (including its predecessor), the IDB Group Sanctions System imposed 64 sanctions to 23 entities and 41 individuals during 2012.

Of these, 55 sanctions fulfilled the criteria established in the Agreement for Mutual Enforcement of Debarment Decisions (Cross-Debarment Agreement), and were notified to the participating institutions for which the Cross-Debarment Agreement was in effect<sup>9</sup>. In turn, the IDB Group recognized 40 sanctions (34 entities and six individuals) imposed by other IFIs.

**FIGURE 10:** TOTAL PUBLIC SANCTIONS IMPOSED BY THE IDB GROUP AND RECOGNIZED UNDER CROSS-DEBARMENT AGREEMENT



*\* These two sanctions were public, but did not fulfill one of the requirements for cross-debarment eligibility: a debarment of more than one year.*

<sup>9</sup> The Cross-Debarment Agreement is in effect for all signatory institutions – The African Development Bank Group, the Asian Development Bank, the European Bank for Reconstruction and Development, the European Investment Bank, the IDB Group, and the World Bank Group. The African Development Bank declared its effectiveness in July 11, 2012.

## ILLUSTRATIVE CASES

The complexity and scope of investigations varies from case to case. The following section contains examples of cases for which investigations were completed or sanctions were imposed in 2012.

### DOCUMENT FORGERY HINDERED HOUSING PROJECT

The IDB signed a loan contract with one of its borrowing member countries to finance a program for housing construction and infrastructure improvement. The Executing Agency opened a bidding process to contract a construction company to improve neighborhoods by creating access to potable water.

Corporation A presented, through its legal representative a bid in the above mentioned bidding process. However, the procurement evaluation committee discovered that Corporation A's bid included a forged certificate of good standing with tax authorities, which constituted fraud under the applicable Bank's Policy and the Sanctions Procedures.

After a thorough investigation, OII presented a PNAA to the CO, who determined that it was more likely than not that the Respondents committed fraud, and recommended a sanction.

The Respondents appealed to the SNC. The SNC decided to sanction the Respondents, meeting the threshold for cross-debarment by other IFIs. Although the firm was not awarded the contract, its conduct impacted the credibility of the bidding process and the execution of the program as a result of delays it caused.

### CONTRACTOR ENDANGERED PATIENT HEALTH WITH FRAUD

The IDB signed a loan contract with one of its borrowing member countries to finance a project to strengthen the country's hospital system. The Executing Agency signed a contract with Corporation B for the maintenance of hospital equipment. OII obtained information, published in local newspapers, regarding the poor quality of the maintenance services provided to hospitals.

After an exhaustive investigation, OII found that despite the poor performance or, at times, non-existent performance, the Respondents filed reports with the Executing Agency stating that all services had been provided to the agreed standards.

In consequence, OII presented a PNAA to the CO, who determined that it was more likely than not that the Respondents committed fraud, and recommended a sanction.

The Respondents appealed to the SNC. The SNC imposed a sanction against the Respondents, meeting the threshold for cross-debarment by other IFIs. \

### **FORGED BID SECURITY AND TECHNICAL EXPERIENCE CERTIFICATES**

The Bank signed a loan agreement with one of its borrowing member countries to contribute to a program for water supply and rural sanitation. The Executing Agency opened a bidding process for the construction of aqueducts to serve 15 communities.

As a result of the bidding process, Corporation C was awarded the contract. Later, the Executing Agency discovered that Corporation C through its legal representative included a forged bid security, which constituted the Prohibited Practice of fraud in accordance to the applicable Bank's Policy and the Sanctions Procedures.

OII investigated and uncovered that, in addition to the forged certificates, the Respondents had included in their proposal falsified evidence of their technical experience. OII presented a PNAA to the CO, who determined that it was more likely than not that the Respondents committed fraud, and recommended a sanction.

The CO's determination was not contested and the recommended sanction was imposed, along with cross-debarment by the other IFIs.

### **CONTRACTOR PAID IN FULL WITHOUT DELIVERY AFFECTING PUBLIC HOUSING PROJECT**

The IDB signed a loan contract with one of its borrowing member countries to finance a project for housing construction. The Executing Agency opened a bidding process for the construction of urbanization works. As a result of the bidding process, Corporation D was awarded the contract.

The Executing Agency later discovered that Corporation D had submitted an invoice for execution of works which had in fact not been executed. The invoice was accompanied by a certificate of execution issued by the project supervisor. The submission of these documents knowing that they contained misrepresentations constituted the Prohibited Practice of fraud under the applicable Bank's Policy and the Sanctions Procedures

After completion of the investigation, a PNAA was presented to the CO, who determined that it was more likely than not that the Respondents committed fraud, and recommended a sanctions.

The Respondents did not appeal the CO's determination and the recommended sanctions were imposed along with cross-debarment by the other IFIs.

### **ALLEGED FRAUD RELATED TO PREVIOUS EXPERIENCE**

The IDB financed a project to expand and improve water and sewage systems. During a public bidding, a bidder allegedly submitted false statements as evidence of its prior experience.

Information obtained after an exhaustive investigation by OII led it to conclude that the bidder submitted information it believed to be accurate about its prior experience, though later it became apparent that the information was imprecise. In addition, the bidder submitted information about certain type of prior experience that was, allegedly, misleading since it did not respond to the required criteria.

OII concluded that the type of experience accredited coincided with the type of experience accredited by other bidders. Thus, OII did not find evidence of intent to defraud.

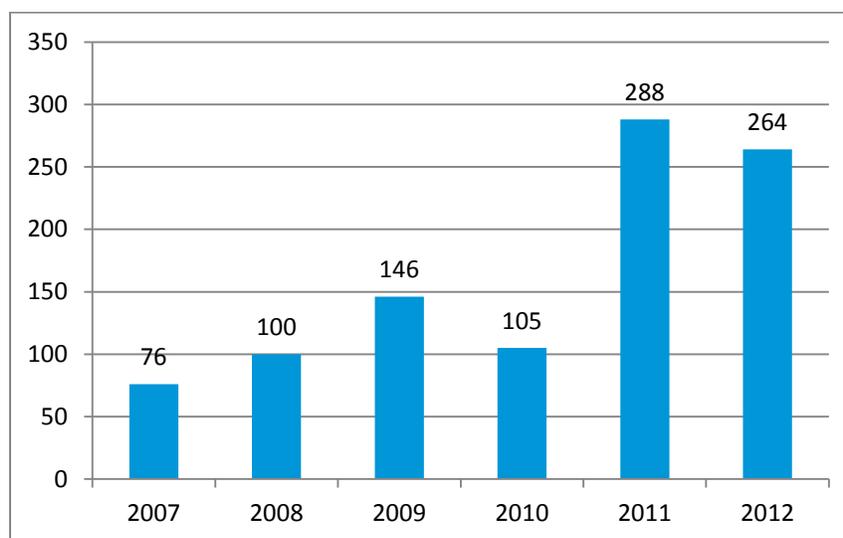
## PREVENTION ACTIVITIES

Through its prevention activities OII seeks to identify and reduce integrity and reputational risks in IDB Group financed activities. Integrity risk is the risk that a Prohibited Practice may occur, while reputational risk is the risk that the reputation to the IDB Group may be harmed in connection with an IDB Group-financed activity.

Much of OII's prevention work is in response to consultations received from Sovereign Guaranteed, Non-Sovereign Guaranteed (NSG), and Corporate Procurement operations. Such consultations relate to a variety of integrity issues, ranging from questions about potential risk indicators in specific projects, to general inquiries regarding compliance with applicable policies, procedures and guidelines.

In 2012, OII handled a total of 264 consultations regarding integrity and reputational risk.

**FIGURE 11:** CONSULTATIONS ON INTEGRITY AND RELATED REPUTATIONAL RISK



### Non Sovereign Guaranteed Operations

OII supports NSG Operations as follows:

- ✓ Advising the NSG Windows regarding integrity due diligence, including
  - Compliance with applicable policies and procedures;
  - Assessment and mitigation of integrity and reputational risks in specific operations;
  - Disclosure of integrity and reputational risks to management and the Board; and

- Participation in the Eligibility and Quality Risk Review meetings for IDB operations.
- ✓ Working with NSG Windows and other internal stakeholders to improve the IDB Group policies and procedures relevant to integrity and reputational risks.
- ✓ Providing training to the staff of NSG Windows on integrity and related issues.
- ✓ Communicating with other IFIs to maintain a harmonized approach and a level playing field for NSG Windows with regard to integrity and reputational risks.
- ✓ Advising NSG Windows in respect to deficiencies presented by certain jurisdictions, in accordance with reports of leading organizations, and the risks such deficiencies may present for projects that involve entities therein.

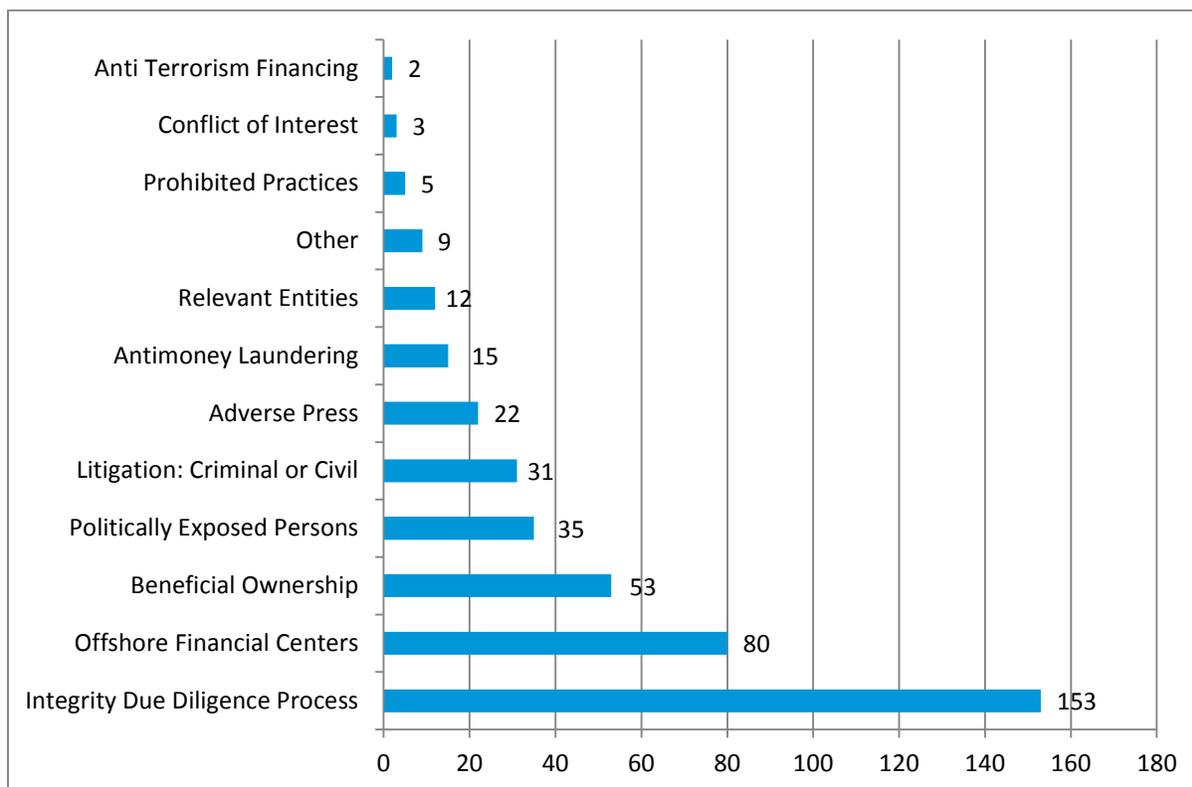
Integrity and related reputational risks in NSG operations are managed primarily through Integrity Due Diligence, which consists of gathering information to identify, assess and mitigate integrity and reputational risks. Integrity Due Diligence is conducted on each NSG operation prior to approval, pursuant to the applicable Bank guidelines (OP-474-1) and related procedures.

OII provides advice to the NSG Windows on all aspects of Integrity Due Diligence, including the disclosure of integrity and related reputational risk to management and the Board. OII also advises NSG Windows regarding compliance with the Non-Sovereign Guaranteed Operations Use of Foreign Entities Guidelines (OP-597-2).

Out of the 264 consultations, 252 were related to NSG Operations. Of these, 152 corresponded to OII's review of project documents to advise teams on the identification, assessment and mitigation of integrity and related reputational risks in the context of Eligibility and Quality Risk Reviews meetings (including for approvals and renewals of operations under the Trade Finance Facilitation Program) of the Structured and Corporate Financing Department (SCF) and Opportunities for the Majority Sector (OMJ). By participating in these meetings, OII has the opportunity to identify and help address potential integrity issues in SCF and OMJ projects prior to approval.

The remaining 100 matters corresponded to advice offered upon consultations received from SCF, OMJ, the Multilateral Investment Fund (MIF) and the Inter-American Investment Corporation (IIC), in respect to specific integrity or reputational issues arising in connection with new operations or operations in their portfolios. These data may be interpreted as a positive trend of early and proactive consideration of integrity and reputational risks in NSG operations.

The issues raised in consultations from NSG Windows are summarized below. Note that many consultations addressed more than one issue.

**TABLE 4: NSG CONSULTATION ISSUES**

On July 13, 2012, OII delivered a technical briefing on Integrity Due Diligence to the Board of Executive Directors. The objective of the technical briefing, which was prepared in coordination with the NSG Windows, was to inform the Board on the scope of Integrity Due Diligence and the responsibilities of the different units involved in conducting it.

During that technical briefing, OII proposed an approach for the mitigation and disclosure of integrity and related reputational risks, which grew out of comments received from Executive Directors. According to this approach, OII will work with Investment Officers to mitigate and disclose integrity and related reputational risks in accordance with the risk presented. The following table summarizes the proposed approach, which has been adopted.

**TABLE 5: APPROACH TO MITIGATION AND DISCLOSURE OF INTEGRITY AND REPUTATIONAL RISKS**

Risk Assessment	Mitigation	Disclosure
Minimal	not recommended	not recommended
Heightened ( <i>i.e., within risk tolerance</i> )	recommended, if possible	recommended
Significant ( <i>i.e., outside of risk tolerance without mitigation</i> )	recommended	recommended, in detail

## EXAMPLES OF ADVICE PROVIDED AND MEASURES UNDERTAKEN

### *Politically Exposed Person*

One IDB Group window consulted OII regarding a potential borrower that had, as a Board Member and significant shareholder, the Minister of Environment for a provincial government. The presence of this politically exposed person (PEP) presented heightened integrity risk, as the borrower would seek approvals from the provincial Ministry for a portion of its business. OII and the team devised mitigation measures that included a representation from the Borrower, a letter from the PEP, and additional due diligence.

### *Criminal Investigation*

OII was consulted when an NSG Window found through integrity due diligence that the CEO and primary shareholder of a potential borrower was under criminal investigation for bribery. OII advised that this presented significant integrity and reputational risk because the company did not disclose this issue when asked, because the criminal investigation involved the CEO, and because the case related to a high-profile corruption scandal. Based on this risk assessment, the Window ultimately decided not to proceed with the operation.

### *Criminal Conviction*

OII also advised that heightened integrity and reputational risk were presented in an operation where a key technology supplier and contractor had pled guilty to criminal bribery in a member country. OII advised that this risk was adequately mitigated, however, because this company – under the supervision of an external monitor approved by the Department of Justice of a member country – had assessed and revised its internal compliance program and invested in a robust implementation program.

### *Politically Exposed Persons*

Two different IDB Group Windows consulted with OII regarding separate projects in a borrowing member country in which persons in upper management of a potential borrower also performed a government role. In each case, OII assessed the degree of risk presented regarding corruption, conflicts of interest and money laundering. Where the government role was participation in an unpaid, short term panel with a defined task, OII considered the risk to be within the Bank's risk tolerance but to merit disclosure. Where the government office was compensated, and the mandate included nonspecific "support" tasks for high government officials, OII considered the risk to be significant, and recommended that the individual give up either the public or the private position.

## TRAINING AND COORDINATION WITH NSG WINDOWS

During the fourth quarter of 2012, OII provided training to investment officers from SCF and OMJ regarding compliance with the Integrity Due Diligence Guidelines (OP-474-1) and the Non-Sovereign Guaranteed Operations Use of Foreign Entities Guidelines (OP-597-2), as well as the substantive issues underlying them.

OII and MIF held coordinating meetings in 2012 to ensure consistent application of the Integrity Due Diligence Model Procedures.

## Sovereign Guaranteed Operations

### INTEGRITY RISK REVIEWS

In 2009, OII introduced the Integrity Risk Review (IRR) as a sector or country-specific risk analysis tool. The IRR consists of an assessment of different sources of information to identify indicators of integrity and reputational risk and provide recommendations on mitigation measures. IRRs were conducted for six countries (Nicaragua, Bolivia, Peru, Paraguay, Uruguay and Argentina) and one sector in the CID region (Infrastructure).

In 2012, OII reviewed the usefulness and effectiveness of the IRR as a risk management tool during the design and implementation of IDB financed Sovereign Guaranteed Operations. OII found that while the process of preparation of the IRRs served as an important tool to raise awareness regarding the Bank's policies, mechanisms and procedures to promote integrity, the conclusions were little known. Moreover, the IRRs did not provide actionable recommendations that Project Teams could refer to when assessing integrity risks at the project level.

Based on the findings of the review, OII reformulated the IRR methodology and prepared a proposal with an enhanced approach for preparation of the IRRs. A presentation of the new approach to the ACPC to define next steps is pending for the beginning of 2013.

Under the enhanced approach IRRs would be transformed into analytical tools that

- ✓ are aligned to Bank's activities in a given country;
- ✓ leverage the information produced by different units of the Bank and external organizations; and
- ✓ are prepared through a flexible, participatory and inclusive approach.

The IRR review also helped OII identify the need to raise awareness of its preventive role and the advice it can provide to manage integrity and reputational risk in sovereign-guaranteed operations.

### AN EXAMPLE OF SUPPORT TO SOVEREIGN GUARANTEED OPERATIONS: PRE-INVESTMENT PROGRAM FOR STRATEGIC TRANSPORTATION PROJECTS, BOLIVIA

The Transport Division invited OII to participate in a workshop it organized for public officials and representatives from the private transport sector in La Paz, Bolivia. The general objective of the workshop was to share with participants knowledge on the crucial elements for the success of strategic transportation projects. OII's participation was intended to increase knowledge about IDB's integrity framework, OII functions and activities, and potential strategies for the identification, assessment and mitigation of integrity and reputational risks.

Going forward, OII will continue to reach out to the Transport Division to remain involved in the implementation of the Pre-investment Program for Strategic Transportation Projects to assist Project Teams with the design of an integrity risk management strategy.

### [RED FLAGS MATRIX](#)

The Red Flags Matrix is an interactive tool developed by OII in collaboration with the Operations Financial Management and Procurement Services Office (FMP). It is based on lessons learned from OII investigations, red flags used in similar tools of peer institutions, and the experience of FMP. The matrix can be used in the context of specific procurements to identify and assess the presence of red flags that could signal an integrity risk (i.e. a risk that a prohibited practice might take place in the procurement). Upon identification of a risk, OII can serve as a resource to help project teams decide on the appropriate measures to mitigate the identified risks.

The Red Flags Matrix is now available for use by Project Teams where the Executing Agency has the procurement plan uploaded in the Procurement Plan Execution System (SEPA, for its Spanish acronym). Throughout the year, OII recommended project teams use the Red Flags Matrix in specific procurement processes that presented indicators of integrity risks. Further OII involvement in the risk assessment of Sovereign Guarantee projects will allow for a more consistent and strategic use of the Red Flags Matrix.

### [Training](#)

OII, together with the Knowledge and Learning Department (KNL), completed two online knowledge tools that were made available to all Bank staff through the INDES platform in March 2012. The first is a training program on Integrity Risks that seeks to (i) present and promote the Bank's policies, guidelines and structures related to integrity, (ii) familiarize the staff with the definitions of Prohibited Practices, and (iii) explain how OII serves as a resource for the IDB Group. The second is a training program on the Red Flags Matrix.

In 2012, OII provided training and presentations on integrity-related issues to staff in the Country Offices of Colombia and Brazil, the latter in conjunction with the Case Officer.

### [Transparency Trust Fund \(TTF\)](#)

Since 2007, OII has participated in the Strategic and Eligibility Committee of the Transparency Trust Fund (known previously as the Technical Review Committee of the Anticorruption Activities Trust Fund). As a member of the Strategic and Eligibility Committee, OII reviewed and made recommendations in connection with the approval of three proposals: (i) Regional: Support for the Operation of the Anticorruption Activities Fund (RG-T2163); (ii) Jamaica: Enhanced information management for more transparent and efficient government audits (JA-T1078); and (iii) Regional: Strengthening the Integrity of

Financial Systems: Improving the Capacity to Prevent Money Laundering and Terrorism Financing (RG-T2224).

### **Compliance Screening System (CSS)**

OII has worked closely with the Information Technology Department in the execution of a capital project to purchase a new compliance system for screening. This will allow various bank entities to integrate screens of names against the internal eligibility verification list and external watch lists. Integrating these screens into IDB Group systems – including payment processing, hiring, corporate procurement and NSG operations – will reduce integrity and reputational risks for the IDB Group, will provide an important control to avoid the use of Bank resources in relation to money laundering and terrorism financing, and will help ensure compliance with IDB Group policies and procedures.

The budget for this capital project was approved for 2012; during the year OII and ITE coordinated with the many internal stakeholders and issued the RFP. Proposals were evaluated and the process is nearing completion. The actual implementation period is estimated to be six months.

### **ORP Partnership Integrity Due Diligence**

OII delivered to the Office of Outreach and Partnerships a draft Partnership Integrity Due Diligence Guideline and Procedures. This effort – the product of a lengthy and close coordination with ORP – will establish a process for identifying, assessing and mitigating integrity and reputational risks that may arise in the context of partnerships. OII also provided an introductory briefing to ORP staff regarding the new Partnership Integrity Due Diligence Guidelines and Procedures.

## OUTREACH ACTIVITIES

A sound strategy requires that borrowers and third parties be aware of the prevailing integrity standards and that they have channels to report allegations and request advice and support to meet these standards. OII's outreach activities during 2012 included:

### Anticorruption Week 2012

As part of the interdepartmental collaborative initiatives OII undertook in 2012, OII worked with the Division of Institutional Capacity of the State, the Department of Research and Chief Economist, the Case Officer, the SNC and the Department of External Relations to organize a series of events to commemorate the 2012 International Anti-Corruption Day.

Anticorruption Week 2012 provided OII with a unique opportunity to forge alliances with an array of stakeholders working on anticorruption issues that will contribute to strengthen current and future initiatives of OII to promote integrity.



The events aimed to strengthen ties with the different participants, including representatives of member countries, leading economist in the area, and the World Bank Regional Advisor for Governance and Anticorruption (Latin-America). It also serve: (i) to present the Bank's efforts to assist countries in the prevention and control of corruption as well as to foster transparency; (ii) to contribute to a better understanding of the red flags that could indicate the presence of collusion in a Bank-financed project and the elements that should be taken into account in subsequent risk mitigation strategies; and (iii) to share knowledge and advance the research agenda on issues such as the measurement of the extent and impact of corruption.

### Collaboration with Other Multilateral Development Banks

OII continued to work closely and collaborate with the heads of integrity offices at other IFIs. OII participated in regular meetings with these entities to discuss best practices and to harmonize its procedures. Outputs of these meetings were the harmonized General Principles and Guidelines for Sanctions and Harmonized Principles for Treatment of Corporate Groups.

In April, 2012, OII participated in the annual Private Sector Integrity Conference hosted by the African Development Bank in Tunisia. The purpose of this conference is to share views and approaches to matters related to integrity due diligence, in order to seek a generally consistent approach among peer institutions. Other participating institutions included the International Finance Corporation, the Asian Development Bank, the Islamic Development

Bank, the European Bank for Reconstruction and Development, European Investment Bank, and the World Bank.

In September 2012, the OII participated in the 13<sup>th</sup> Conference of International Investigators hosted by the European Investment Bank. The Conference was designed to exchange views and information with other multilateral development banks and international organizations. OII co-chaired a panel on prevention that resulted in the creation of a Prevention Community of Practice. This Community of Practice is an online platform tool designed to facilitate knowledge sharing and collaboration between OII and its comparators. The participating institutions are, in addition to the IDB, the Asian Development Bank, the African Development Bank, the European Bank for Reconstruction and Development, European Investment Bank, the Global Fund and the World Bank. The objective of this knowledge sharing is to define a harmonized view on the principles for an effective prevention strategy and design a package of training materials that can be adjusted and used by the participating institutions.

In October, 2012, OII met separately with counterparts from the Caribbean Development Bank, the Islamic Development Bank and the Norwegian Investment Fund to share with them information regarding the IDB's approaches to investigations and prevention activities.

### **Training for Executing Agencies**

In collaboration with the Country Office in Bolivia, OII participated in a one-day training event for a governmental entity responsible for the execution of IDB financed projects. The event focused on early detection of Prohibited Practices with emphasis on how to identify red flags.

## STAFFING AND BUDGET

2012 was a year of internal transformation. To ensure the continued operations of OII, immediately upon the departure of the former Chief by the end of February, the President of the Bank appointed an interim Chief. During 2012, OII reassigned functions among staff to clearly distinguished two teams that collaborate with each other, but that perform separate functions: investigative and preventive. OII intensified recruitment efforts and was successful in hiring investigators and consultants for its investigative team.

At year end, OII was staffed with professionals with experience in investigations, auditing, public policy, law and related fields. This is a diverse team, almost 65% are female (two of which have grade four and above) and it spans nine different nationalities from member countries – representing countries from the Southern Cone, Andean and Central American Regions as well as the United States.

A key priority for 2013 is to bring permanent leadership to OII, through the hiring of a new Chief, and to fill the remaining vacant positions.

**TABLE 5: STAFFING AND BUDGET**

	2008	2009	2010	2011	2012
<b>Budget (\$ in Millions)</b>	2.6	2.7	2.8	3.1	3.0
<b>Approved Headcount</b>	13	13	13	13	13

**TABLE 6: YEAR-END STATUS**

	2011	2012
<b>Headcount</b>	<b>13</b>	<b>13</b>
<b>Bank Staff on Board with OII</b>	10	10*
<b>Complementary Workforce</b>	6	5
<b>Staff seconded to OII</b>	0	1
<b>OII Staff on Special Assignment to other Department</b>	1	1
<b>Vacancies</b>	2	3**

\* Includes Acting Chief

\*\* Includes Chief position

OII is conscious of the need to have more granular information on the costs of its activities to guide its decisions regarding the use of resources and to seek efficiencies. Towards this end, OII redefined the activities used to monitor its indicators under the results based-budgeting framework in order to track time and labor and other expenses at the different phases of the investigation.

## CHALLENGES FOR THE YEAR AHEAD

OII will focus on the challenges outlined below for each of the main areas of activity. As mentioned in the previous section, the most important challenge is to bring permanent leadership to OII, through the hiring of a new Chief, and to fill vacant positions.

### Investigation Challenges

- ✓ Enhance communication and cross-collaboration with Operational Units of the Bank to better understand the potential impact of alleged Prohibited Practices on the IDB Group's operations, and to appropriately channel lessons learned through investigations.
- ✓ Realign internal processes to improve the intake process and prioritization of cases and focus investigator's attention on matters requiring a full investigation. In spite of OII's investigations being reactive, this approach should help in improving quality and quantity of cases.
- ✓ Continue to implement a knowledge program that enriches staff technical competencies to conduct investigations.

### Prevention Challenges

- ✓ Share knowledge that raises awareness of the Bank's mechanisms to address integrity issues in IDB Group financed activities and builds the capacity of IDB Staff to assess and mitigate integrity risks.
- ✓ Develop and strengthen OII tools to support IDB financed Sovereign Guaranteed Operations with the design and implementation of an integrity risk management strategy.
- ✓ Develop value-added products that help IDB Investment Officers reduce the risk of fraud and corruption in NSG Operations.
- ✓ Improve IDB Group systems to better detect integrity and reputational risks.

### Outreach Challenges

- ✓ Leverage on alliances forged in 2012 with internal and external anticorruption stakeholders to improve OII's contribution to the IDB's mission.
- ✓ Share knowledge with executing agencies and other partners in development on how to respond to integrity risks.
- ✓ Liaise and create alliances with superior audit institutions and enforcement agencies to improve capacity to detect and investigate Prohibited Practices.

**HOW TO CONTACT OII**

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**Inter-American Development Bank**

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## GLOSSARY

**Allegation:** information received by the Office of Institutional Integrity in relation to a possible prohibited practice.

**Case:** matter under review of the sanctions system, at the investigation or adjudication stages.

**CID:** Country Department Central America, Mexico, Panama and Dominican Republic.

**CSS:** Compliance Screening System.

**Consultation:** inquiry received by OII pertaining to integrity or related reputational issues.

**FMP:** Operations Financial Management and Procurement Services Office.

**IDD:** Integrity Due Diligence.

**IFI:** International Financial Institutions.

**Investigation:** examination of information related to potential misconduct to determine whether the information evidences a Prohibited Practice.

**Notice of Administrative Action or NAA:** a Notice prepared by the Case Officer including, among others, the recommended sanction and an explanation that the Respondent has an opportunity to trigger the second-tier review by responding to the NAA.

**OMJ:** Opportunities for the Majority Sector.

**ORP:** Office of Outreach and Partnerships.

**Preliminary Notice of Administrative Action or PNNA:** a Preliminary notice prepared by OII that, among others, identifies the Respondent, states the alleged Prohibited Practices, summarizes the facts relevant to the allegation, and attaches all evidence relevant to the case.

**Respondent:** party alleged to have engaged in a Prohibited Practice.

**Response:** written materials submitted by the Respondent presenting arguments and evidence in response to the NAA.

**Reply:** written materials that OII may submit presenting arguments and evidence in reply to the arguments and evidence set forth in the Response.

**SCF:** Structured and Corporate Finance Department.

**SEPA:** Procurement Plans Management System.

**SNC:** Sanctions Committee of the IDB Group.

**Substantiated:** case in respect of which OII concludes that the evidence is sufficient to support a finding that the alleged Prohibited Practice occurred.

**Surreply:** additional written materials that the Respondent may submit presenting arguments and evidence in reply to the arguments and evidence set forth in the Reply.

**Unsubstantiated:** case in respect of which OII concludes that the evidence is insufficient, either, to confirm or deny that the alleged Prohibited Practice occurred.

**Unfounded:** case in respect of which OII concludes that the evidence is sufficient to support a finding that the alleged Prohibited Practice is untrue.