

Office of Institutional Integrity | Annual Report 2007

THE IDB GROUP

Leading with Integrity



ABOUT THE INTER-AMERICAN DEVELOPMENT BANK GROUP

The Inter-American Development Bank (IDB), the oldest and largest regional development bank, was established in 1959 to promote economic and social development throughout Latin America and the Caribbean. With novel mandates and tools, the Bank's lending and technical cooperation programs went far beyond the mere financing of economic projects that was customary at the time.

The IDB Group, which today includes the [Inter-American Investment Corporation](#) and the [Multilateral Investment Fund](#), is the main source of multilateral financing for economic, social and institutional development projects as well as trade and regional integration programs in the Latin America and the Caribbean region. Through its loans, grants, guarantees, policy advice and technical assistance, the IDB Group is a key partner with each of its 26 borrowing member countries, promoting sustainable economic growth and poverty reduction.

The Inter-American Investment Corporation (IIC) is a development institution established in 1984 under the auspices of the IDB to promote the economic development of its Latin American and Caribbean member countries through financial support for private enterprise. It particularly targets small and medium-size companies that have difficulty obtaining financing from other sources on reasonable terms.

The Multilateral Investment Fund (MIF) began operating in 1993 to promote broad-based economic growth through private sector development, particularly in microenterprise and small business. A successor MIF (MIFII) was authorized and funded as of March 2007; MIF II's purpose is more specifically focused on economic growth and poverty reduction.

To learn more about the IDB Group, please visit our websites:

www.iadb.org

www.iic.int

www.iadb.org/mif



FROM THE PRESIDENT

With over \$9.6 billion in loan approvals in 2007, the Inter-American Development Bank Group remains the most important source of multilateral finance for the countries of the Americas. Additional financing assistance for development last year included nearly one half billion dollars for small and medium-size business from the Inter-American Investment Corporation and \$135 million for microfinance and small business from the Multilateral Investment Fund. All this adds up to a great deal of financial support for the region—an achievement made possible only with a foundation of integrity.

Last year, the Bank realigned its structure to increase the development effectiveness of this portfolio, giving priority to deepened country focus and sector expertise, with improved risk management and results-based decision-making. This revised organizational model gives renewed emphasis to integrity as a vital success factor in all of our activities—success that begins at home. Towards this end, the entire Bank Group staff completed Ethics training this year; we also strengthened and consolidated our internal *Code of Ethics and Professional Conduct*, filled the position of Ethics Officer and hired an Ombudsperson. In short, integrity is one of the most important principles underlying development effectiveness—we expect every employee to be a leader in this regard.

In everything that the Bank Group does, we remain ever vigilant to prevent fraud and corruption from undermining our goals in economic, social and institutional development. First and foremost, we work closely with our member countries and the private sector to enhance their frameworks for integrity and to avert corruption. And we coordinate efforts with other international financial institutions to leverage results with harmonized approaches to fraud and corruption. The Bank Group does all of this—as I stated earlier this year—because corruption takes opportunities away from the majority, diminishes the competitiveness of our member countries and paralyzes their economic and social development.

Where we do find corruption, we move swiftly to investigate and sanction those responsible. As of 2007, the Bank began publishing the names of individuals and firms responsible for these violations of trust. The message is clear: we will not tolerate those who would take resources from the people who need them most; for those who do, they shall be held accountable, following due process, in a transparent and public fashion.

In 2008, my Office—especially the Office of Institutional Integrity—will continue to make integrity a focal point for the entire Bank Group. To be frank: there is no development without integrity. In this, our mandate is clear.



Luis Alberto Moreno



LIST OF ABBREVIATIONS

AAF	Anti-Corruption Activities Trust Fund
AUG	Office of the Auditor General
COF	Country Office
CSO	Civil Society Organization
DEV/PRM	Development Effectiveness and Strategic Planning Department / Project Procurement Division (Now: VPC/PDP ¹)
EA	Executing Agency
FAO	Food and Agricultural Organization (United Nations)
ICF/ICS	Institutional Capacity of the State Division
IDB	Inter-American Development Bank
IDB Group²	Inter-American Development Bank Group, Multilateral Investment Fund and Inter-American Investment Corporation
IIC	Inter-American Investment Corporation
IFAD	International Fund for Agricultural Development (United Nations)
INT	Integration and Trade Sector
KNL/LNR	Learning Division
LEG	Legal Division
MDB	Multilateral Development Bank
MIF	Multilateral Investment Fund
MOU	Memorandum of Understanding
NGO	Non-governmental organization
OAS	Organization of American States
OCFC	Oversight Committee on Fraud and Corruption
OECD	Organization for Economic Co-operation and Development
OII	Office of Institutional Integrity
OLAF	European Anti-Fraud Office (European Commission)
PACI	Partnering against Corruption Initiative (World Economic Forum)
SCF	Structured and Corporate Financing Department
SME	Small and Medium-Sized Enterprise
TC	Technical Cooperation
UNCAC	United Nations Convention against Corruption
UNODC	United Nations Office on Drugs and Crime
VPC/PDP	Operations Procurement Office
VPF	Vice President for Finance and Administration
VPP	Vice President for Private Sector and Non-Sovereign Guaranteed Operations
WFP	World Food Program (United Nations)

¹ In 2007, the structure of the IDB was realigned—some units were given new titles, others were combined or subsumed into other units.

² The IDB Group is comprised of three institutions each of which addresses elements of private sector development: the Inter-American Development Bank (IDB), the Inter-American Investment Corporation (IIC) and the Multilateral Investment Fund (MIF). The IDB and IIC are public international organizations. The MIF is a trust fund under the administration of the IDB. OII provides services, as described in this Report, to each of these three entities.

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I. INTRODUCTION

The Office of Institutional Integrity (OII) is the IDB Group's primary office for addressing external matters of integrity, fraud and corruption. As a measure of the significance that the IDB Group attaches to integrity, OII reports directly to the President. OII coordinates this work closely with other entities in the Bank Group, particularly the Oversight Committee on Fraud and Corruption (OCFC) and the Sanctions Committee. OII also plays a supportive role in internal ethics and integrity matters and helps member countries develop and refine their own integrity programs.

OII approaches its [mandate](#) based on three "pillars" as defined by [Strengthening a Systemic Framework against Corruption for the Inter-American Development Bank](#), the IDB Group's comprehensive blueprint for addressing corruption. These pillars include staff integrity, support for member governments and the fiduciary obligation to ensure that activities financed by the Bank are free of corruption.

Overall, in 2007, OII made significant progress in streamlining investigative activities, enhancing the department's capacity and building knowledge-based systems to strengthen prevention efforts. OII also broadened its research on past cases, expanded integrity outreach and pursued more complex investigations. Of course, a large part of what OII does is to respond to inquiries regarding possible fraud and corruption. A greater appreciation of this role, both internally and externally, means that OII has been spending more time providing advice on inquiries—a constructive dialogue that builds better awareness. A snapshot of OII's 2007 investigative activities and results is given in [Chapter II: Interpreting our Data](#). Here, there are no significant shifts from prior years with the notable exception of the record number of cases that OII completed in 2007.

A brief overview of the rest of this year's report is given by general focal area and pillar of activity.

PILLAR ONE: SETTING THE STANDARD

In 2007, OII played a key role in a series of watershed efforts that have enhanced transparency, extended outreach and training and helped incorporate integrity more fully throughout the Bank Group's activities. This included completion of Ethics training for the entire Bank Group staff; advisory help on revising and drafting of the Bank's *Code of Ethics and Professional Conduct*; assistance in defining the new roles for the Bank's Ethics Officer and Ombudsperson; and with other matters related to ethics within the Bank Group. [Chapter V: Prevention—The Best Tool for Fighting Corruption](#) discusses these and related activities in detail.

With the arrival of the Ethics Officer and Ombudsperson, OII's role with respect to internal ethics matters will take on a primarily supportive function. It is important to note that OII only investigates internal ethics cases, beyond those dealing with fraud and corruption, when so requested by the Ethics Officer.

PILLAR TWO: SUPPORTING MEMBER COUNTRIES' INTEGRITY EFFORTS

With the realignment of the Bank, primary responsibility for execution of initiatives to aid member countries' own integrity efforts is now with the Institutional Capacity of the

State Division (ICF/ICS). OII will continue to play a significant role in the design of such initiatives. As further described in Chapter V, this work has included development of an innovative anti-corruption trust fund as well as technical cooperations that advance implementation of international conventions against corruption.

PILLAR THREE: COMBATING FRAUD AND CORRUPTION AS A FIDUCIARY RESPONSIBILITY

One of the biggest advances in deterring fraud and corruption is the public posting of the names of individuals and firms that have been sanctioned by the Sanctions Committee. Available on the Bank's website, this additional transparency to the IDB's sanctions outcomes should reinforce the message among all stakeholders that the Bank Group is serious in holding accountable those who misuse the funds provided by the Bank Group or violate its anti-corruption policies.

As in past years, this annual report provides case histories to help readers understand the scope, scale and impact of some of the inquiries that OII is asked to pursue. [Chapter III: Investigative Cases and Outcomes 2007](#) presents this year's sampling of the many types of violations that OII investigated.

Another significant achievement has been the design and development of the Red

Flags Matrix. The Project Procurement Division³ and OII have jointly analyzed some of the most common fraudulent and corrupt practices as identified through OII's investigations. Together, the units are working to develop proactive mechanisms that will flag such practices and allow steps to be taken to prevent them in the earliest stages of the project cycle. The web-based Red Flags Matrix has been designed as a preventive tool and will be applied comprehensively throughout Bank operations and external anti-corruption efforts. More can be read about this new tool in [Chapter V](#).

Other OII efforts within this area of its mandate include assessing IDB Group databases as resources for identifying patterns and trends in violations, beginning with OII's own extensive case portfolio. The results of analyzing over 400 cases have led to a new chapter in the annual report: [Chapter IV: Case Closed: What have we Learned?](#) Finally, OII is rounding out the development of its first full knowledge-based system through additional data mining efforts as described in [Chapter V](#).

BEYOND THE THREE PILLARS

OII activities extend beyond the three pillars to help ensure that the Bank Group maintains its regional and international

leadership in combating corruption and striving for integrity. OII has led joint anti-corruption efforts, worked closely with peer organizations to define common frameworks for anti-corruption activities and has been a principal in international efforts to harmonize definitions and sanctions. [Chapter VI: International Leadership](#) describes these further.

To help readers understand OII's anticipated work for 2008 and beyond, [Chapter VII: The Way Forward](#) gives an overview of the priorities and developments that OII will give focus to in the coming months. An external review of the integrity framework of the Bank Group will receive priority attention when its findings and recommendations are presented to IDB Group leadership. Work will proceed on the use of data to build knowledge-based systems that identify vulnerabilities and promote better risk management. OII will expand integrity outreach to its diverse stakeholders. And the Office will continue in its efforts to shift attention to outright prevention of fraud and corruption whether within the Bank Group or within member countries, while maintaining its leadership role among international financial institutions in joint anti-corruption activities.

³ With the restructuring of the Bank Group, the Project Procurement Division became the Operations Procurement Office in the Office of the Vice Presidency for Countries (VPC/PDP).



II. INTERPRETING OUR DATA

A significant share of OII's efforts and resources is dedicated to pursuing the many inquiries that it receives concerning fraud and corruption. A large portion of these become allegations that are investigated. This chapter gives an overview of case flow from inquiry to outcome, including sanctions. It also provides the cumulative case flow and sanctions outcomes through 2007.

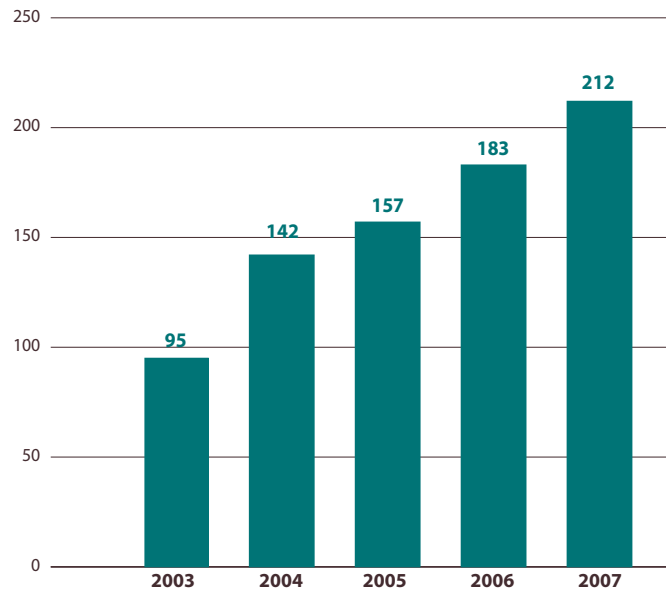
INQUIRIES, CONSULTATIONS AND ALLEGATIONS

In 2007, OII received a total of 212 inquiries. Of these, 136 involved allegations and were categorized as new cases; the remaining 76 were treated as consultations. This represents a 16% increase in inquiries over 2006. The growth in consultations, in particular, reflects a steady expansion in the recognition of OII as a resource for advice related to fraud and corruption as well as broader access to OII through use of the website and e-mail. This is a significant outcome of the recent Ethics training and of OII's ongoing outreach efforts. Inquiries and consultations become a measure of the effectiveness of the messaging concerning the IDB Group's expectations regarding the importance of integrity to the Bank Group's mission and operations. And, with improved understanding of the *Code of Ethics and Professional Conduct*, inquiries that would have come to OII in the past pertaining to the Bank's internal ethics and conduct issues are now appropriately made directly to the Ethics Officer.

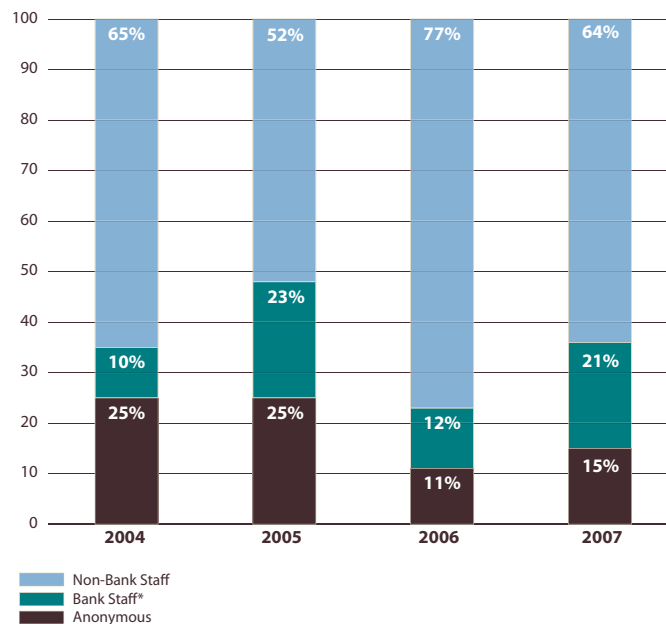
Who made New Allegations

Of the new allegations in 2007, 15% were made anonymously; 64% were made by third parties and the remaining 21% came from Bank Group staff. The substantial percentage of internal sourcing is a very positive indicator of the staff's confidence in the Bank Group's integrity mechanisms. Again, this likely reflects the impacts of the Ethics training and of OII outreach, as well as the Bank Group's new, public disclosure of sanctions.

TOTAL INQUIRIES RECEIVED 2003-2007



SOURCE OF ALLEGATIONS



* Bank staff means both permanent employees and consultants.

Confidentiality of the Investigative Process⁴

The Inter-American Development Bank's provisions to guard confidentiality in investigations include:

- The Bank Group protects the confidentiality of complainants;
- All staff involved in an investigation process are obligated to preserve and protect the confidentiality of the subject, the witnesses, and all other parties concerned;
- Any staff member who compromises the confidentiality of a complainant is subject to disciplinary action;
- The Bank Group accepts anonymous allegations.

Protection for Whistleblowers and Witnesses

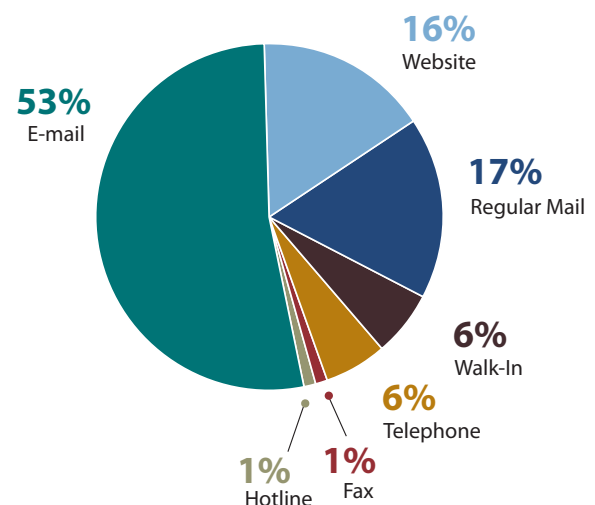
Maintaining the integrity of the Bank's administration and operations, including the Bank Group's systems for administrative investigations and resolution of disputes, requires the active support of all Bank employees.

To ensure that the staff has every confidence that they may come forward without repercussion, the Bank has a Staff Rule entitled *Protection for Whistleblowers and Witnesses* that prohibits reprisal against a staff member for having submitted a complaint or participated in an investigation.

How New Allegations were Submitted

The Bank Group has created multiple ways in which interested parties may make inquiries related to potential issues of fraud and corruption. Inquiries that are classified as allegations are categorized by the way in which they were submitted. Electronic means of making inquiries are by far and away the most common. In 2007, as in previous years, e-mail appears as the most favored method of contacting the Bank Group, accounting for 53% of all allegations. Additionally, there was a three-fold increase in the number of inquiries submitted via the website, both from anonymous and known sources, which may be due to the clarity and convenience added with the 2007 redesign of the site. Most

HOW ALLEGATIONS WERE SUBMITTED



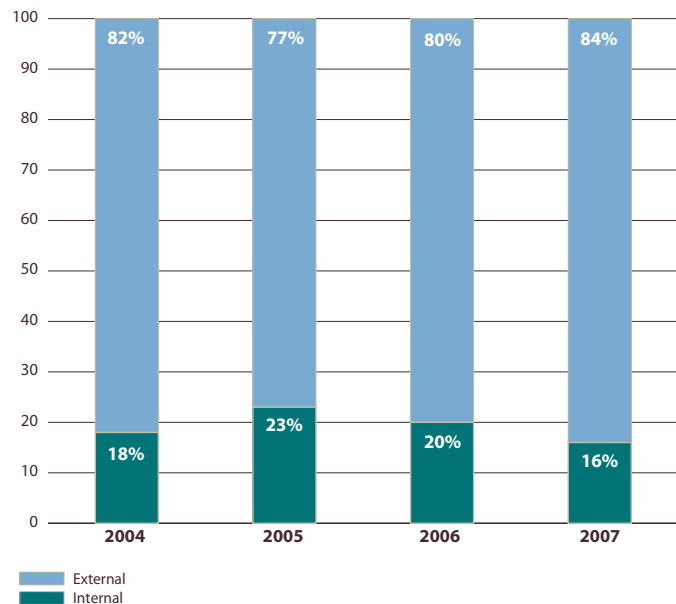
⁴ Confidentiality generally means that the distribution of information shall be limited to those Bank officers who require knowledge of a matter in the performance of their official functions. The sharing of information is subject to the Bank's internal policies and procedures, including the Bank's policies on the disclosure of information. Persons dealing with the Office of Institutional Integrity should be free to ask any questions regarding the treatment of information they may provide.

website inquiries came from non-Bank Group individuals, which could well be a reflection of a growing awareness among third parties regarding IDB Group's anti-corruption efforts.

External versus Internal Allegations

Cases are classified as external when they are related to issues of fraud or corruption but do not involve staff of the Bank Group, and internal if they do involve Bank Group staff, whether for violations of Bank Group policy or in matters of fraud and corruption. In 2007, 84% of the new allegations were external and the rest internal. Again, increased understanding within the Bank of the role of the Ethics Officer in handling internal ethics matters has led to a decline in the number of ethics-related inquiries to OII in 2007.

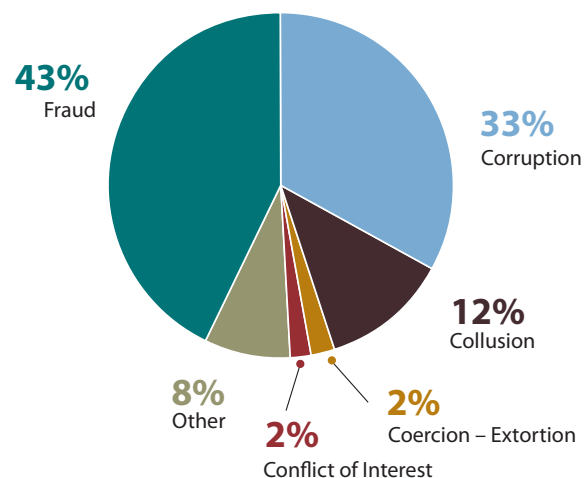
EXTERNAL VERSUS INTERNAL ALLEGATIONS



COMPLETED CASES 2007

OII began 2007 with 123 pending cases and, over the course of the year, opened a total of 136 new cases. At the same time, OII completed 162 investigations—leaving 97 active matters as of December 31, 2007. This represented a significant increase in completed cases over 2006, a testament to a better seasoned staff and more efficient investigatory processes, including enhancements to the electronic case management system launched in 2006, INTIS. Of the cases completed in 2007, 51 were closed at the preliminary (i.e. pre-investigative) stage and 111 were closed following full investigations.

TYPES OF ALLEGATIONS INVESTIGATED (EXTERNAL)*



*This chart shows all outcomes, including cases closed after preliminary consideration

As always, internal and external cases are handled differently. In 2007, prior to realignment of the Bank, internal cases fell under differing jurisdictions of authority. Allegations of fraud and corruption by Bank Group staff still came under the jurisdiction of the Oversight Committee on Fraud and Corruption (OCFC), while all other allegations involving staff were adjudicated by the Ethics or Conduct Review Committees.⁵ A total of 28, or 17 percent, of all the cases that were completed in 2007 were internal. Of these, seven were under the jurisdiction of the OCFC, six of which were investigated. The Ethics Committee adjudicated nineteen cases of which it asked OII to investigate eight. The final two cases fell under the purview of the Conduct Review Committee, both of which OII was asked to investigate

OII has responsibility for all external investigations; as in prior years, the cases that were

completed this year involved a variety of types of prohibited conduct, though fraud and corruption remained the most common.⁶

The initial classification of allegations by OII is based on the information in the allegation. Over the course of the investigation, as more information about the case becomes known, this classification is often modified. For instance, a case that is first submitted as a possible conflict of interest may also be found to involve fraud or collusion as investigators learn more about the details of the case.

CASE RESULTS

Roughly one third of all cases are closed at the preliminary stage; for those that proceed to a full investigation, there are three main outcomes: a case allegation may be substantiated, unsubstantiated or considered as unfounded.

CASE FLOW 2003-2007

	2003	2004	2005	2006	2007
Cases pending from previous year	37	67	117	111	123
New cases	95	142	138	149	136
Total active cases	132	209	255	260	259
Investigations completed	(65)	(92)	(144)	(137)	(162)
Cases pending at year's end	67	117	111	123	97

⁵ Beginning in 2008, all allegations of Bank Group staff misconduct are adjudicated by one committee, the new Committee of Ethics and Professional Conduct.

⁶ For a definition of the various sorts of prohibited conduct that OII investigates, please visit this page of our website: http://www.iadb.org/integrity/project_integrity.cfm?language=EN&parid=3.

Of the 16 internal matters ultimately investigated, allegations were substantiated in eight cases, while five were unsubstantiated and three were unfounded.

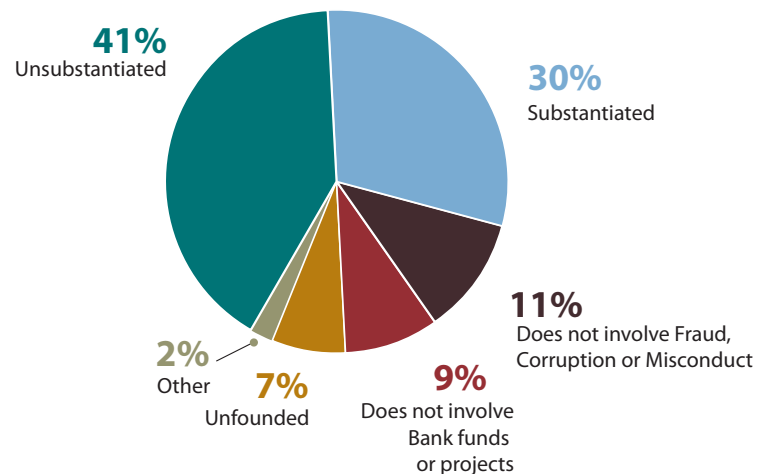
The outcomes for 134 external investigations completed by OII (including cases resolved by preliminary inquiry and those that were fully investigated) are described in the chart to the right, with 30% of the 2007 cases leading to substantiated allegations and findings.

SANCTIONS AND OTHER POST-INVESTIGATIVE ACTIVITIES

Update on Case Histories Reported in the 2006 Annual Report

In the 2006 Annual Report, six of the cases described in [Investigative Cases and Outcomes](#) (Chapter III) were still pending a resolution, two under the jurisdiction of the OCFC and the remaining four under the Sanctions Committee.

OUTCOME OF EXTERNAL INVESTIGATIONS



What Does it Mean if a Case is Unsubstantiated or Unfounded?

At the end of an investigation, OII classifies a case as substantiated, unsubstantiated or unfounded. A case is determined to be:

- *Substantiated* when the evidence sufficiently supports the allegation that a fraudulent or corrupt practice, as defined by the Bank Group, has occurred;
- *Unsubstantiated* when the evidence is insufficient either to confirm or deny the original allegation; and
- *Unfounded* when the allegations are determined to be untrue.

ACTIVE CASES 2007

	INTERNAL	EXTERNAL	TOTAL
Cases pending from previous year	10	113	123
New cases	22	114	136
Total active cases	32	227	259
Investigations completed	(28)	(134)	(162)
Cases pending at year's end	4	93	97

The OCFC has since issued sanctions in one case while the second remains pending. The Sanctions Committee issued sanctions in two cases, including permanently debarring two individuals and one firm and decided not to impose sanctions in the remaining two cases.

As indicated earlier, 2007 was the first year in which individuals and firms sanctioned by the Sanctions Committee are listed publicly on the [IDB's website](#)⁸; the results below will be reflected there.

Sanctions in 2007 Cases

The Sanctions Committee or the OCFC determines the outcome in cases where OII has recommended sanctions. During 2007, these committees imposed OII's recommended sanctions in several cases.⁷ Sanctions ranging from letters of reprimand to permanent debarment were imposed on a total of 28 parties, as summarized in the chart below.

SANCTIONS 2007

TYPE OF SANCTION	LENGTH OF SANCTION	INDIVIDUALS	FIRMS
Letter of Reprimand	1 year	1	1
Debarment	3 years	4	1
	5 years	4	3
	10 years	1	1
	Permanent	10	2
TOTAL		20	8

⁷ This number includes the six cases described in the paragraph above.

⁸ <http://www.iadb.org/integrity/SanctionList.cfm>



III: INVESTIGATIVE CASES AND OUTCOMES 2007

Over the course of 2007, OII had 259 cases at various stages of review. As discussed in the previous chapter, with improvements to investigative processes and more efficient use of an electronic case management system, OII closed a record-breaking 162 cases. Where substantiated, OII has a choice of recommendations including sanctions, in which case the individuals and/or companies implicated receive a Notice of Administrative Action.⁹ Many of the parties described in the cases below received such a Notice.¹⁰

2007 EXTERNAL CASES

84% of all cases investigated in 2007 were external, falling under two different adjudicating bodies of the Bank Group: the OCFC and the Sanctions Committee.¹¹ The wording for some of the outcomes will vary based on the adjudicating committee.

⁹ In 2006, "Notice of Charges" was the term used for the document sent to an individual or a firm, notifying them of the Bank's decision to initiate an administrative process that would determine whether or not its policies had been violated. Towards the end of 2007, the Bank adopted the term "Notice of Administrative Action".

¹⁰ The outcome provided for each case described below reflects the status as of December 31, 2007.

¹¹ The Sanctions Committee has jurisdiction over all cases involving bidders, suppliers, contractors or consultants who are alleged to have engaged in fraud or corruption in connection with a Bank-financed project. The OCFC has jurisdiction over all other cases. Both Committees follow the Sanctions Procedures to adjudicate cases. See Annexes I and II for further overview of the investigations process. For a deeper understanding of the investigative and sanctions processes, please visit [OII's website](http://www.oii.org).

BRIBERY, EMBEZZLEMENT AND EXTORTION

This first set of sample cases highlight ways in which stakeholders are alleged to have embezzled, extorted funds or engaged in bribery.

Case of Bribery includes Payments to Spouse

An Executing Agency (EA) official was accused of soliciting and taking bribes, including payments to his spouse, from a contractor working in a technical cooperation project to improve business performance through information technology. As soon as its senior management learned of the allegation, the EA brought the matter to the attention of both the local authorities and the Bank's Country Office. Local law enforcement authorities were consulted, and after they investigated, OII commenced its own investigation.

The contractor claims that the official threatened the company with actions that would harm the company's reputation and possibly remove the company from the project. OII obtained copies of the checks used to pay the official's wife and identified illegal payments totaling \$11,000 in project contracts valued at nearly \$220,000.

Outcome: Notice of Administrative Action was issued and forwarded to the Sanctions Committee. Because there was no evidence that the payments in question had been extorted, local law enforcement decided not to prosecute. The Executing Agency,

however, asked the involved official to resign as soon as it learned of the payments that he and his spouse had received.

Fish Sales Embezzlement

The General Manager of a technical cooperation to strengthen the fishing industry embezzled money from fish sales made on behalf of local fishermen. Fish buyers were asked to deposit monies owed to the cooperative directly into the Manager's personal bank account.

The program's accountant noticed discrepancies in the buyer's accounts and informed the Country Office. When interviewed, the Manager claimed that funds were owed to him after he had paid bills for the cooperative during a difficult period and that he would pay back any funds taken in excess. OII's investigation revealed that he had been removing funds prior to the cooperative's difficulties. The Manager was dismissed, though he repaid the monies within a few months.

Outcome: The Notice of Administrative Action was drafted and will be forwarded to the respondent to begin the sanctions proceedings.

Extortion and Coercion in Animal Industry

An animal industry association was created for a Bank Group-financed project to develop a related industry cluster in the production, industrialization and commercialization of products from this particular animal.

The Executing Agency, the local breeder association, was also a beneficiary. A complainant alleged that the directors of the EA demanded that coordinators for the new industry association deposit a portion of their salaries into the association's bank account to finance a counterpart fund contribution. (Such counterpart funds are a common project requirement but are to be paid by organizations). Further allegations were made that these EA directors only approved projects related to their individual companies and that they had used Bank-financed project consultants for work in their own companies, had restricted other companies' participation and had abused per-diem funds.

OII's investigation found that the association had received deposits that it could not explain and discovered that the association's counterpart contribution might have been insufficient under the terms of the Bank Group's agreement. However, the investigation did not substantiate fraud or corruption.

Outcome: The matter will be referred to the Country Office and MIF for follow up and consideration of a project audit to determine if the funds were used properly.

Favoring a Friend

A principal technical advisor was hired by an EA for a project to implement transparent procurement processes across numerous government ministries. The advisor was alleged to have received money from one of the contractors on the project and the use of

an apartment—belonging to a principal of the firm—for vacation.

OII's investigation confirmed that the advisor had received \$5,000 from the firm and had used the apartment. These events took place when the contractor was negotiating an extension to the existing multimillion dollar contract; the firm received the extension of six months, which involved payments of more than \$475,000.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

FRAUD

This set of cases involves incidents in which individuals ignore the Bank Group's integrity policies, and misrepresent themselves to gain personal benefit in Bank Group-financed projects.

Fictitious Employees Generate Fraudulent Profits

In a project designed to enhance rural access to markets, stimulate economic growth and production and upgrade living conditions of a rural population, the engineering firm hired as a consultant inflated its costs of services through, among other things, inflating the salaries paid to actual employees and by creating salaries and benefits for fictitious staff.

To begin with, an audit found that the consultant had fewer employees than required for the project, a violation of the contract

commitment. OII also found evidence of diverse forms of fraudulent payments including falsified payment certificates for non-existent employees, inflated payments and benefits for employees who did exist, and unwarranted payments to individuals not associated with the project.

The contract had a value of approximately \$2 million; the full amount of diverted funds may total as much as \$300,000.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

A Contractor Lies to Get “Free” Money

A small project and technical cooperation facility for socially vulnerable groups was approved for \$15 million. The purpose of the facility was to reimburse small projects up to \$500,000 and to finance non-reimbursable technical cooperations for up to the same amount. Small loans up to \$250,000 were also available. One project to encourage local, rural growth and discourage migration to urban environments was financed at nearly \$700,000.

A former contractor to this project claimed to the EA that the Bank Group had awarded him an additional contract to evaluate the project, and demanded advance payment on this “new” contract. Based on this lie, the EA gave him a \$3,000 cash “advance.” Asked to investigate, OII found that the contractor had not only committed this fraud but that he had also failed to provide the full range of training services called for in his original contract.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

Technical Assistance Provider Generates Phony Grants

Providers of technical assistance, in a project to boost the productivity and competitiveness of small and medium-size firms, forged grant applications and falsified both proof-of-training documents and client satisfaction forms to obtain illegitimate payments from the EA. This was done with the knowledge of the project coordinator. Early detection of the scheme prevented payment on the six false grants.

Outcome: The Notice of Administrative Action was drafted and will be forwarded to the Sanctions Committee.

MISREPRESENTATION OF QUALIFICATIONS

Repeated instances of misrepresentation of qualifications highlight the importance of conducting adequate due diligence on bidders and contractors.

Faking a Graduate Degree

A project sought to fill a position to supervise the implementation of a communications strategy for the expansion and improvement of health services in an EA's central office. The Terms of Reference for the job specified certain academic qualifications, with higher points awarded for candidates with both Bachelor's and graduate degrees.

The person selected for the consulting position lied about her undergraduate and graduate degrees and received a contract that was later renewed for nearly three years of work. The consultant was paid \$6,000 a month for this contract. The consultant eventually admitted that she was a bilingual secretary who lacked the academic qualifications stated in her résumé. As a result of this matter, the consultant is no longer working for the project.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

Winning by Deception

The winning bidder for a \$400,000 contract to modernize the Attorney General's data management system falsified information on its bid regarding the qualifications of the consultants that it had employed.

The résumé submitted by the bidder exaggerated the level of experience of its consultants, an action which both qualified the firm for consideration and gave it the winning score. These fraudulent acts were fully substantiated by the investigation.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

Lying about Experience and Resources

An Executing Agency selected a firm to provide pest control services and eliminate the fruit fly in various locales within a province; bidders were to have significant expertise with and knowledge of the complexity of the challenge. The contract total was \$1.5 million.

The winning firm claimed to have specific knowledge in this line of work and presented a list of clients and prior experience.

One of the unsuccessful bidders protested to the Executing Agency, alleging that the winner had lied about its financial statements.

The investigation revealed that the allegations were correct and further found that the inaccurate financial statements had falsely exaggerated the bidder's pest control experience. OII consulted with the EA officials, who acknowledged that they had been aware of the situation from the beginning but justified the decision to select this firm based on the wish to hire a local firm—and as a challenge to the market dominance of the complainant. EA also claimed that the winner had the technical resources to perform the task.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

Providing Forged "Proof" of Efficient Work

A portion of a \$50 million road improvement project was being awarded based on efficiency in prior work, with "time to completion" of work a main criterion. One of the bidders submitted a forged certificate regarding execution time for a prior job, falsely claiming a shorter time frame. The false information raised the bidder's score to the winning position and the contractor was awarded a \$217,000 contract. Had the true time frame been used the contractor would not have qualified for consideration.

The Country Office forwarded information concerning this winning bidder. OII launched an investigation which substantiated the allegation.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

Forged Validation Certificate in Medical Supplies

A Primary Health Care Reform project receives partial funding from the IDB Group to enhance health care services, including constructing new hospitals. To qualify for one project, bidders were asked to submit certificates validating their distribution agreements with medical device suppliers. This bidder submitted a certificate that was inconsistent in appearance with certificates previously provided by the supplier. The US-based, medical device supply company sent a letter to the Health Ministry, protesting that it had not authorized this bidder to distribute its products for this contract; rather it had authorized a competing bidder.

The bidder had once held a certificate from the US company for a prior contract that had been cancelled. OII asked the bidder to supply evidence of its claims that the US company had indeed renewed the relationship and had sent a second certificate. The bidder supplied a series of emails as proof of the renewal and authorization. OII used a computer forensic firm to analyze these emails; examination revealed numerous disparities and evidence of significant manipulation. In sum, the bidder falsified the certificate of authorization as well as the email correspondence offered in proof.

Outcome: The Notice of Administrative Action was drafted and will be forwarded to the Sanctions Committee.

BIDDERS' ATTEMPTS TO MANIPULATE OUTCOMES

The Bank Group is always vigilant in attempting to detect and prevent manipulation of the bidding process. This year, cases revealed attempts to control bid outcomes through cartels, rigged bidding and set prices.

Collusion and Rigged Bidding in Disaster Prevention

In a project to reduce a community's vulnerability to natural disasters, an Executing Agency put forth a bid for services to dredge a river and construct a riverbank. The Bank's Sector Specialist noted that several offers looked nearly identical in terms of presentation, down to the typing errors, and appeared to be coordinated in pricing.

The evidence showed that several bidders agreed to fix a price range for the bid competition and that one of the bidders wrote all of the offers among the parties eventually charged with collusion. The total value of the contract was roughly \$55,000.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

More Collusion and Rigged Bidding in Fruit Seedlings

The Bank's Sector Specialist noted similarities in the presentations and prices of proposals among competing bidders in a series of four bids for the provision of fruit bearing seedlings to rural producers.

OII's investigation found that a group of bidders colluded to set a range of prices and create a cartel to control bid outcomes among and between group members. They rigged a total of nine bids; one bidder created all of the bid proposals for the group and purchased the bid bonds. He also forged three additional offers. The amount of money involved in these contracts was approximately \$230,000.

Outcome: The Notice of Administrative Action was issued and forwarded to the Sanctions Committee.

MANIPULATING BID DOCUMENTS

Among prohibited practices for which the Bank Group is on alert are those in which the bidding processes are manipulated by those in charge of the outcomes.

Internal Fixes: Revising Bid Documents to Favor a Contractor

The EA gave an international organization responsibility for selecting consultants to work on a health sector support project. A bidder complained to the Bank's Country Office that the selection process was not transparent and that he had been given false information regarding its progress.

OII's investigation revealed that the Evaluation Committee, comprised of members from the local offices of the international organization, had significantly altered the academic and professional requirements. This was done both without justification and notice to the participants but also after all the original bids had been received. Though there was insufficient evidence to determine whether or not the revisions had favored the candidate ultimately selected, the changes did result in disqualification of at least one candidate.

Outcome: The matter will be referred to the international organization responsible for the bid process to determine further action.

CONFLICT OF INTEREST

Avoiding conflict of interest seems an obvious principle in any business practice, but for some, the issue must be made more explicit.

Hiding Family Connections and Creating False Qualifications

As in many of OII's investigations, this case revealed more than one violation. In a project to modernize land registration and to promote more efficient land use and planning, an Executing Agency put out a bid for consultants. The investigation showed that the winning consultant had both falsified qualifications and denied any conflict of interest with the Executing Agency.

Falsely representing advanced degrees gave this consultant a higher score than competing consultants, putting her at the top of the selection list. Just as important, she hid the fact that one of her parents was a senior executive in the co-Executing Agency that had responsibility for the final Terms of Reference for the consultant's position.

Outcome: The Notice of Administrative Action was drafted and will be forwarded to the Sanctions Committee.

2007 INTERNAL CASES

For internal cases involving ethics and conduct, the Ethics Officer first reviews the matters and then requests that OII investigate. OII sends its recommendations back to the Ethics Officer for final adjudication. For cases in which a staff member is alleged to be involved in fraud and corruption, OII investigates but sends its recommendations to the OCFC which then makes a determination in the case.¹²

Steering Contracts to Select Bidders

The Bank put forth a bid to outsource certain activities related to the implementation of new technologies to improve management training for public officials.

A complainant working for one of the losing bidders for the contract claimed that a Bank staff member involved in the bidding process asked that consultants from the complainant's firm be released from a "non-compete" restriction, thereby freeing them up to work for the winning bidder. The complainant said that this felt uncomfortable and expressed concern about potential harm to the firm's ongoing relationship with the Bank.

OII found that the evaluation criteria had been altered over the course of the selection process to favor the winner and discovered that, during the execution of the contract, the winning firm did not comply with at least two key conditions of its contract. Further, OII found that this firm was a newly-incorporated entity and that the firm's owner had been, until recently, a Bank consultant. The firm lacked prior experience and had no employees. Bank staff involved in the bid acknowledged that they had been aware of these details, but they chose not to report them to the Project Evaluation Committee.

Outcome: The matter was referred to the Ethics Officer, the Office of the Auditor General and the Project Procurement Division.

¹² In 2008, it is anticipated that jurisdiction to adjudicate staff misconduct involving allegations of fraud or corruption will be transferred from the OCFC to the newly constituted Ethics and Professional Conduct Committee.

Obtaining Personal Loans from a Delinquent Bank Beneficiary

A Sector Specialist had overseen the execution of a Small Project with an NGO that served as the EA. The purpose of the Small Project was to provide credit to micro-producers to strengthen existing business activities and generate new employment. The Country Office received a letter from the NGO requesting that the Bank seize the salary of the Sector Specialist, alerting the Office that something in the relationship between the NGO and the Sector Specialist was improper. The NGO claimed that the Specialist owed money to the organization and it had obtained a judicial order from the local civil court to pursue the claim.

OII found that the NGO had received nearly \$200,000 in loans for the Small Project from the Bank since 2001 but had failed to pay any of its debt. During this period, the Sector Specialist had solicited and received two personal loans from the NGO, totaling \$51,000. The Sector Specialist failed to pay his debts to the NGO, something that he originally denied, but then admitted when confronted with the evidence.

Outcome: The Bank terminated the Sector Specialist's contract.



IV. CASE CLOSED: WHAT HAVE WE LEARNED?

OII has developed an extensive archive of the details and outcomes in over 400 cases that it has investigated since its inception. In 2007, the Office began examining this case collection, using a methodology that analyzes both quantitative and qualitative data.

For each case, every phase in its “life history” was assessed—from the way it came to OII’s attention and the means by which information about allegations was collected and verified to OII’s subsequent findings and recommendations. No matter the outcome, each case is important as a learning tool. Even if the evidence was insufficient to warrant a sanction or when only some of the alleged facts were ultimately proven, the information gathered is often sufficient to identify weaknesses in policies, procedures, project execution or a procurement process.

Over time, it is expected that this analysis will capture patterns and trends on a larger scale and more systematically than through other efforts. These in turn will provide a

strong basis for recommendations regarding improvements to each of the phases of OII’s investigatory work, as well as for broader yet more accurate efforts to identify and mitigate risk. Preliminary findings from this initial review, described below, are categorized as follows:

- Data collection and analysis
- The investigative process
- Classification of investigative findings
- Identification and mitigation of risks

The detailed review of each of these four categories has provided further insight on areas that are critical not only for OII’s performance but for the Bank Group’s development objectives in general. This initiative, combined with efforts to expand data mining and risk detection, will substantially increase OII’s ability to use the results of its work to return value to the Bank Group.

PRELIMINARY FINDINGS AND RECOMMENDATIONS

Data Collection and Analysis

The analysis initially focused on data types and the related scope and scale of information that could be gleaned from OII's activities, as well as on relevant data sets found elsewhere in the Bank Group. This step in the review benefited from a parallel OII effort that is analyzing its capabilities to mine data from elsewhere in the Bank Group. The results of this phase of the review showed that various modifications to processes and tools for data collection and analysis will promote better use of information within the investigative process and for preventive action.

Specific recommendations include efforts to:

- Add additional fields within OII's case database (INTIS) to capture more specific case data;
- Incorporate suggestions and recommendations in each case report prepared by OII; and
- Support the creation of mechanisms that enhance information sharing between and among Bank Group data resources and that build tools to facilitate OII's access to and use of this information.

The Investigative Process

The analysis of the full investigation process has revealed much about its strengths and weakness, generating various recommendations for improvement. At this level, the analysis focused on such aspects as sources of allegations, flow of information, complexity and length of procedures, and type of evidence collected, among others.

A key focus in this analysis was looking at the degree to which allegations are substantiated and the source of such allegations.

Typically, OII substantiates about one third of all of its cases. Analysis shows that the Bank's Country Offices (COFs) are the biggest source of all substantiated cases, accounting for 30%. The Executing Agencies are the next largest source, leading to approximately 18% of the total. Following these, in order of importance, are allegations from contractors and then those from anonymous sources, each contributing slightly less than the Executing Agencies.

When each of the sources is analyzed individually, the case pool shows that approximately half of all allegations from COFs and EAs are substantiated. In contrast, the allegations from the contractors and anonymous sources have a substantiation rate of about 14%. Nevertheless, these two latter sources were shown to be useful resources for other relevant data. For instance, this information allows us to verify whether

certain behaviors or actions—though not specifically prohibited—suggest opportunities for improvement to project management or risk mitigation.

Recommendations to strengthen the investigative process include:

- Increase and broaden OII's outreach at the local level in order to enhance communications with local actors (e.g. oversight agencies, civil society, media and business associations) that may be aware of fraudulent or corrupt practices or have evidence relevant to allegations;
- Reinforce the role of COFs as sources of information and refine their ability to attract legitimate inquiries;
- Build greater awareness with bidders, contractors and others involved in Bank-financed activities to ensure they are fully informed about the Bank's anti-corruption policies and mechanisms for reporting allegations;
- Revise management of information relevant to examination of project execution and performance; and
- Verify that the Bank's documentation and publications accurately and clearly describe the Bank's anti-corruption policies.

Classification of Investigative Findings

Case results were categorized by type of prohibited conduct, revealing that certain classes of allegation are more likely to be substantiated than others. For example, allegations of the use of fraudulent documents are more likely to be substantiated than other types. This is probably because evidence in these cases is generally accessible, objective, easily verified and infrequently disputed.

By comparison, allegations of bid manipulation or misuse of funds are much less likely to be substantiated. As with other similar outcomes, however, the evidence collected can also be of value to strengthen project design, execution and oversight.

Specific recommendations include efforts to:

- Increase investigative capacity to identify patterns and specific indicators of bid manipulation as well as of other prohibited practices that require more sophisticated means of investigation;
- Strengthen analysis and communication of the impacts of substantiated fraud and corruption on project goals and the Bank Group's reputation;
- Use all investigative findings, regardless of case outcome, to identify risks and weaknesses in fiduciary control processes; and

- Implement tools such as the Red Flags Matrix to increase early identification of indicators of fraud or corruption.

Identification and Mitigation of Risk

In the future, the focus of this ongoing comprehensive analysis will be to add value to Bank Group operations by making better use of OII's data to identify risks, trends and other indicators of fraud or corruption and to develop recommendations that will mitigate or even preclude these risks. For example, initial analysis has identified distinct risks relative to specific phases of the procurement process, finding that more allegations arise in the execution phase while fewer allegations relate to the earlier bidding phase.

The review also revealed a pattern of association between certain sectors and specific prohibited practices. For instance, allegations of fraud or corruption in infrastructure projects are more likely to be substantiated than similar allegations in other sectors. In social investment projects, allegations of kickbacks by consultants to project officials are more common than in other types of projects whereas falsified statements of work have occurred with more frequency in water and sanitation projects.

Specific recommendations include efforts to:

- Conduct additional analysis of case results and other data to strengthen the identification of risks, trends and indicators;
- Develop mechanisms to prevent and to mitigate risks of fraud and corruption throughout the project cycle by sector and by type of prohibited conduct; and
- Implement proactive reviews that analyze projects for indicators of fraud and corruption.

LESSONS LEARNED: THE FUTURE

Recognizing the old adage that an ounce of prevention is worth a pound of cure, OII will continue to expand its efforts at transforming the results of its investigations into lessons learned. This analytical exercise, along with the Red Flags Matrix and the Data Mining Project (discussed in the next chapter), will provide a body of knowledge critical to aiding the Bank Group's preventive efforts. Managing this knowledge will become a key priority for OII as a part of its proactive support for Bank Group operations.



V. PREVENTION ~ THE BEST TOOL FOR FIGHTING CORRUPTION

The Bank Group fights corruption at many levels; the most effective strategy over the long-term, of course, is through outright prevention. Towards this end, the Bank Group continues to invest in internal and external prevention measures including outreach and sharing lessons learned. This report is one good example of a mechanism to raise awareness and inform staff as well as those who are involved in Bank Group-funded projects, technical assistance and loans throughout member countries.

2007 INTERNAL PREVENTIVE ACTIVITIES

The Integrity Initiative—Revising Bank Group's Policies and Practices

This initiative, which began in 2006, involves a comprehensive analysis of the Bank Group's primary policies and practices regarding the integrity, ethics and professional conduct of its staff. Implementation of the resulting recommendations is helping the Bank in

its continuing commitment to ensure that its staff acts in accordance with the highest level of integrity and that internal policy and procedures reinforce this objective.

The President convened a special Working Group to initiate the Integrity Review, and to develop and implement recommendations. The Working Group is comprised of the Office of the President, Legal Department (LEG), Human Resources Department (HRD), Learning Division (KNL/LRN), Ethics Officer, Ombudsperson and OII. The Working Group is coordinated by the Vice President for Finance and Administration.

The Integrity Initiative has multiple components for which OII provides ongoing advice, training and outreach support and other assistance. Some of the most important components of this initiative enacted in 2007 are discussed here.

Revisions to the Bank's Code of Ethics and Conduct Policies and Practices

One of the main tasks before the Working Group was the analysis of the existing applicable rules and regulations including the *Code of Ethics* and *Staff Rule 323: "Respect in the Workplace"* and the procedures of the Committees with respective regulatory responsibility: the Ethics and the Conduct Review Committees.

Upon review, the Working Group proposed merging the Code and staff rule into a single new Code and combining the two committees into one that would carry full responsibility for the Code's implementation.

The President approved these recommendations and, in December 2007, the Bank adopted the unified *Code of Ethics and Professional Conduct* and created the Committee of Ethics and Professional Conduct. The Ethics Officer serves as Secretary of the Committee and is directly responsible for consultations and requests for interpretation of the Code, addressing allegations of misconduct and supporting the implementation and enforcement of the Code.

Ethics Training for the Bank Group

In 2007, the Bank Group completed Ethics training for all staff. OII assisted KNL/LRN in conducting the training sessions. As noted in OII's 2006 Annual Report, training began with the President and senior management and

went on to include all staff and consultants at Headquarters and within the Bank's 26 Country Offices. In all, 95% of Bank staff and consultants received training.

KNL/LRN also conducted a "Train the Trainers" exercise for their staff as well as for OII and volunteer staff, the Ethics Officer and members of the Ethics Committee. This group will be responsible for delivering ongoing Ethics training.

OII, KNL/LRN and the Ethics Officer are also creating an e-learning training component—a tool that all staff will be required to utilize periodically to update their knowledge.

Ethics Survey within the Bank Group

To establish a baseline measure of ethics understanding within the Bank Group, the Bank Group teamed with the *Carol and Lawrence Zicklin Center for Business Ethics Research* at the Wharton School of Business to conduct an ethics survey. The survey was developed to explore and assess perceptions of ethics and ethical conduct within the Bank Group. It will also measure staff knowledge of the *Code of Ethics* and the instances and mechanisms by which they can/should seek advice and/or lodge a complaint related to grievances on ethics and conduct matters. The results of the survey will be made available in 2008 and will help management gain a more accurate picture of the ethics working environment and staff perceptions of ethics.

New Ethics Officer for the Bank

In 2007, as part of its commitment to give the appropriate emphasis to ethics as part of daily business, the Bank hired its first Ethics Officer. OII helped write the terms of reference for this position and now works closely with the Ethics Officer in all areas related to integrity for Bank staff. This new addition to IDB is significant, as for the first time, staff have a single source of advice and counsel on ethics matters.

New Financial Disclosure Form for Bank Staff

The Legal Department and OII provided advice to the Ethics Committee and the Ethics Officer on revisions for the new mandatory financial disclosure form and the financial affidavit for staff. With these measures, all staff members—new and existing—are expected to disclose any potential conflicts of interest.

Building Internal Awareness for the Bank Group

All of the above activities work towards a singular goal of making ethics and integrity a cultural norm for the Bank Group. OII will continue to help with internal outreach and awareness building efforts towards this goal. For example, OII holds regular presentations for new hires on the integrity framework of the Bank Group. Additionally, in cooperation

with the Office of External Relations, OII staff will make presentations to Business Seminars organized for firms and individuals doing business with Bank Group-financed activities. These provide a general overview of the anti-corruption policies and regulations of the Bank Group.

Strengthening Integrity in Private Sector Operations

In 2007, the Bank Group implemented the integrity guidelines for private sector operations that had been formally adopted in 2006. These guidelines require that the various units and staff of the Bank Group involved in private sector lending, initiate reviews of proposed as well as existing loans and that they periodically assess loan portfolios for compliance with integrity guidelines. OII was part of the team that developed the guidelines and it will continue to provide: i) advice to project teams as potential integrity or reputation issues arise during the project cycle; ii) advice and recommendations to senior Bank Group management; iii) consultation on database selection, investigation firms and transaction specific terms of reference for analysis by third parties; iv) implementation of related training programs; and v) lead responsibility in cooperation with other multilateral development institutions on integrity matters.

In 2007, OII's help in numerous private sector transactions included clarifying information regarding potential risks, reviewing information related to potential reputational consequences and supplying specialized assistance for more complex integrity issues as they surfaced in proposed transactions. In 2008, OII will add a private sector due diligence specialist to expand its support in this area.

Additionally, OII helped develop the Bank Group's Integrity Due Diligence training for all private sector staff, including a special training session for the President and senior management of the Bank Group.

Data Mining to support Investigative Activities

In coordination with the Information Technology Department, OII conducted a preliminary review of the Bank Group's data systems to determine the ways in which OII could mine this vast wealth of information for proactive identification of fraud and corruption risk. The knowledge base that this will create will improve investigation planning and execution as well as analysis of data sets from investigative outcomes. It will help identify relevant trends of risk and vulnerability within the Bank Group's corporate procurement process and within project procurement and execution. Finally, this knowledge base will augment information derived from lessons learned. As part of this effort, OII is exploring various data mining and analysis tools to assist with ongoing investigations.

Red Flags Matrix

The Operations Procurement Office (VPC/PDP) and OII have jointly analyzed the most common fraudulent and corrupt practices, as identified through OII's investigations, in order to develop a mechanism by which the Bank Group may prevent such practices. In 2007, the two units prepared a report in which they gave significant shape to a new mechanism, entitled the Red Flags Matrix. The Matrix was developed as a practical tool for early detection and prevention of fraudulent and corrupt practices and will provide guidance for staff members supervising project procurement. (See Sample Page of the Matrix.)

The Matrix is a concise checklist derived from several key sources: analysis of OII's case portfolio; the combined knowledge of experts in the procurement sector; and best practices from other international organizations, including the World Bank Group, the Asian Development Bank Group and the United Nations Procurement Office.

When fully implemented, the Red Flags Matrix will be a web-based, interactive tool that will provide users with early indications of risk when reviewing project procurement, allowing them to initiate preventive measures. It will also serve as a data-collection instrument to allow analysis of a wide range of potential indicators of corrupt practices in procurement. The Red Flags Matrix is one component of a more comprehensive strategy to enhance the preventive capacity of the Bank Group and its borrowers during project execution. Other



Inter-American Development Bank

Red Flags Matrix

Based on protests originating with VPC/PDP

Risk Assessment

#	Questions	Answers	Answers	Answers	Answers	Answers	Note
1	Is this activity financed by the Bank Group?	Yes	Yes	Yes	Yes	No	
2	If the facts in the red flag were true, would they constitute a violation of the Bank's prohibition against fraudulent and corrupt practices?	Yes	Yes	No	No	No	See definitions below
3	Are any of the parties included in the sanctions list of the IDB, the IDB or other international organizations or sanctioned by national authorities?	Yes	No	Yes	No	No	
Level of Risk		High	High	Medium	Low	N/A	
Where to submit the concern for Reviewers		OE	OE	OE	PP	N/A	

Fraudulent and Corrupt Practices as defined by the Bank Group

#	Practice	Definition
a)	Corrupt Practice	The offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence improperly the actions of another party.
b)	Fraudulent Practice	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.
c)	Coercive Practice	The 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.
d)	Collusive Practice	An arrangement between two or more parties designed to achieve an improper purpose, including influencing improperly the actions of another party.

Procurement Cycle

A) Preparation Phase

#	Red Flag	What to detect?	Red Flag	Level of Risk	Who Decides?	What to do?	Deviation	
1	Are the TQDs coherent with the outline of the project and/or the document identifying the needs for the Bank-financed project?	Modification of TQDs to inflate the tasks necessary for the execution of the contract and obtain payments for unnecessary work.	Yes	1. N/A	#N/A	#N/A	#N/A	Manipulation: Influence in a devious manner any stage in the Procurement Process.
2	Is the price in one of the bids significantly different than the others?	A bid is exactly 5% lower than the Confidential Estimate when all other bids are 25% over the same Estimate.	No		#N/A	#N/A	#N/A	Breach of Confidentiality: Disclosure of privileged information to third parties in undue circumstances and/or timing.
3	Was the bid advertised for the right period?	Short advertisement or during weekends or holidays only.	No		#N/A	#N/A	#N/A	Manipulation: Influence in a devious manner any stage in the Procurement Process.
4	Was the bid advertised sufficiently?	Bid advertised in the proper media channels, including major circulation newspapers.	No		#N/A	#N/A	#N/A	Manipulation: Influence in a devious manner any stage in the Procurement Process.
5	Was the bid advertised correctly?	Inadequate or incomplete information in the advertisement of the bid.	No		#N/A	#N/A	#N/A	Manipulation: Influence in a devious manner any stage in the Procurement Process.
6	Is the bid request properly structured?	Unclear and ambiguous bidding documents, specifications too narrow or vague, request for too many contracts, unnecessary partnerships, etc.	No		#N/A	#N/A	#N/A	Manipulation: Influence in a devious manner any stage in the Procurement Process.

components will include ongoing training based on the types of risks and findings derived from the Matrix, periodic publications to disseminate information on risks and other related measures. In 2008, the Red Flags Matrix will be piloted in select Country Offices.

2007 EXTERNAL PREVENTIVE ACTIVITIES

Memorandum of Understanding with Organization of American States to Support Implementation of the Inter-American Convention against Corruption

In March 2007, at the Bank Group's Annual Meeting in Guatemala, the IDB and the Organization of American States (OAS) signed a *Memorandum of Understanding* establishing a framework to advance implementation of the *Inter-American Convention against Corruption* and the results of the *Follow-up Mechanism of the Implementation of the Inter-American Convention against Corruption* (MESICIC). MESICIC monitors the degree to which countries have complied with the Convention and issues reports with specific recommendations regarding legal and institutional measures that the country should enact in order to meet the mandate of the Convention.

In the coming years, the Bank Group will help its member countries comply with the various international anti-corruption conventions.¹³ These treaties will also serve as a framework for the Bank Group's dialogue with these countries, to explore and shape their own anti-corruption strategies.

In 2007, the OAS Secretariat and an IDB technical team, representing several divisions of the Bank, met to discuss an action plan for the *Memorandum of Understanding*.

Anti-Corruption Activities Trust Fund

In March 2007, IDB signed an agreement with Norway to establish the first *Anti-corruption Activities Trust Fund* (AAF). The principal objective of the Fund is to strengthen IDB's member countries' tools for access to information as a means to prevent and reduce corruption; the AAF will provide approximately \$4.9 million over a three-year period.

OII worked with the Institutional Capacity of the State Division and the Grants and Co-Financing Management Unit to develop the approach and operational guidelines for the AAF.

To help define the focus of the AAF, OII conducted research on existing initiatives in six Latin American countries that combine

¹³ These conventions are: the *Inter-American Convention against Corruption*, the *United Nations Convention against Corruption* and the *OECD Anti-Bribery Convention on Combating Bribery of Foreign Public Officials in International Business Transactions*.

access to information with anti-corruption measures. Additionally, the AAF technical team organized a two-day workshop to facilitate the exchange of ideas between experts, practitioners, public officials and Bank Group staff. Participants included public officials and NGOs from the countries selected as case studies, IDB Sector Specialists and experts from the Carter Center, World Bank Group, and Norwegian Development Agency.

AAF will seek to finance innovative, replicable initiatives that foster transparency in those sectors that are particularly vulnerable to corruption in Latin America and the Caribbean. Key areas to be targeted include budget and public records management, contracting and procurement procedures, financial institutions, extractive industries, political campaign finance, the judicial system and the health sector.

The fund was launched in December 2007, and began accepting proposals for financing. For additional information regarding eligibility criteria, please consult the Bank's [website](http://condc05.iadb.org/iadbtrustfunds/funds/FundDetails.aspx?FundId=179).¹⁴ IDB's Institutional Capacity of the State Division will manage execution of the fund with advisory support from OII.

Civil Society Partnerships

Support for civil society partnerships to promote transparency and integrity initiatives in the region remains an important ongoing OII activity. OII participated in the Seventh Annual IDB-Civil Society Meeting, joining representatives of 70 NGOs from 23 of the Bank's 26 borrowing member countries in discussions regarding integrity, anti-corruption and fiduciary safeguards.

Also, in 2007, as part of continuing assistance provided to Transparency International (TI) for the prior year's International Anti-corruption Conference, OII—together with two other units of IDB¹⁵—translated, edited and distributed TI's 2006 special report "Corruption in the Health Sector."

Technical Cooperations to Implement International Anti-Corruption Conventions

As in prior years, OII continues to assist Bank operations designed to help member countries implement international anti-corruption conventions and strengthen their own anti-corruption activities. In 2007, OII—in conjunction with Integration and Trade Sector (INT) and ICF/ICS—designed two technical cooperations (TCs) to this end.

¹⁴ <http://condc05.iadb.org/iadbtrustfunds/funds/FundDetails.aspx?FundId=179>

¹⁵ The Integration and Trade Sector and the Office of External Relations.

TC in Support of the Member Countries' Implementation of the United Nations Convention against Corruption¹⁶

This technical cooperation will advance the use of the *United Nations Convention against Corruption* (UNCAC) as an instrument to facilitate investigations and prosecutions by member countries. This includes improving the capacity of prosecutors, investigators and judges to investigate and prosecute corruption cases using international conventions. The TC will be used to expand the Bank's relationship with United Nations Office on Drugs and Crime (UNODC), the entity responsible for the creation and implementation of UNCAC.

The specific objectives of this TC are to:

(i) analyze how current efforts to fulfill the major international conventions against corruption could be streamlined and better coordinated; (ii) identify tools to implement the conventions that can be adapted and replicated, particularly the UNODC toolkit; and (iii) evaluate the ways in which information related to investigations of corruption is shared and identify how to enhance information exchange as part of international cooperation.

TC in Support of Monitoring International Conventions by Civil Society¹⁷

OII and INT worked together in the preparation and approval of a technical cooperation to strengthen the capacity of civil

society organizations (CSOs) to advocate for, and monitor compliance with, international conventions against corruption. The specific objectives of this technical cooperation are to improve: (i) the capacity of CSOs to produce effective reports that meet the follow-up mechanisms provided by international conventions against corruption, particularly the *Inter-American Convention against Corruption*; (ii) the advocacy capacity of CSOs to promote the implementation of policies, regulations and practices consistent with the requirements of international conventions against corruption; and (iii) the ability of CSOs to increase the number of organizations participating in the process of monitoring compliance, producing independent reports and communicating their efforts locally and regionally.

TC activities will produce guidelines for the reporting required under the region's most important international conventions against corruption¹⁸. The operation will also fund activities and tools that help CSOs increase their capacity to advocate for institutional and policy reforms in compliance with the requirements of international conventions against corruption. Finally, the TC will finance activities to help CSOs expand the number of participating organizations in these activities and to integrate their local efforts at a regional level, by exchanging information and best practices of their reporting activities.

¹⁶ This is TC number RGT 1283

¹⁷ This is TC number RGT 1307

¹⁸ See footnote 13.

The Institutional Capacity of the State Division has assumed responsibility for the execution of the operational activities of both of these TCs, while OII remains as an active advisor.

Building Integrity Awareness with Enhanced Communications

OII's annual report remains an important outreach mechanism to the diverse stakeholders in Bank Group projects, loans and TCs. It is distributed widely to Country Offices, Executing Agencies, project coordinators and others involved in day-to-day management of Bank Group-financed activities. This year, OII is adding a related year-end brochure which will be distributed more broadly than the Annual Report. The new publication will include messages tailored to key audiences, such as contractors and bidders, to build broader awareness and will, in particular, reinforce the message of integrity early in a project's life cycle.

The report and lessons learned are also shared during country missions with staff of the Country Offices, EAs and civil society organizations. OII staff makes presentations to various other stakeholders, by request, concerning integrity and anti-corruption efforts.

OII's Website

OII's website was revised and expanded in 2007, making it easier for visitors to access information about fraud and corruption. Interestingly, as mentioned in Chapter II, 16% of all inquiries in 2007 were made via the website— a three-fold increase over the previous year. There is no question that this website plays an important role in informing stakeholders about integrity, fraud and corruption. Annual reports, the names of sanctioned firms and individuals and information about the investigative and sanctions processes are now available on the site. The website will be revised and updated again in 2008.



VI. INTERNATIONAL LEADERSHIP

OII Continued to work with the integrity offices of other leading multilateral development banks (MDBs) to develop harmonization and mutual improvements in integrity and anti-corruption programs. Joint meetings of the MDB integrity offices are held at least semi-annually.

MULTILATERAL DEVELOPMENT BANKS' ANTI-CORRUPTION HARMONIZATION

In 2006, the historic International Financial Institution Anti-Corruption Task Force agreement included provisions for its members to adopt harmonized, common definitions of fraud and corruption. The IDB's Board of Executive Directors adopted these definitions in February 2007.

As a next step, OII is working to ensure that all relevant documents of the Bank include these definitions.

Ongoing, additional work within the MDBs will evaluate and compare anti-corruption provisions in the bidding and procurement

policies of each MDB in an effort to identify other areas where harmonization may be of value. Particular attention is now being given to the exchange of information on debarments, audit clauses and corporate procurement.

UNITED NATIONS OFFICE ON DRUGS AND CRIME

At the request of the Office of the President, OII—together with regional divisions for State and Civil Society¹⁹—organized a technical meeting at the Bank Group with the United Nations Office on Drugs and Crime to identify potential areas of cooperation.

The technical meeting was followed by a seminar organized by what is now the ICF/ICS Division, assisted by OII and other Bank Group units and in coordination with the OAS and UNODC. The focus was the presentation and discussion of the findings of recent research and analysis on crime and violence in Central America.²⁰

¹⁹ The successor to these divisions is the Institutional Capacity of the State Division (ICF/ICS).

²⁰ The publications presented were: "Crime and Development in Central America - Caught in the Crossfire," published by the UNODC and "From the Gang to the Mara - Poverty, Education, Women and Youth Violence," published by the Bank Group and the Universidad Externado of Colombia.

President Moreno also met with the Executive Director of the UNODC, Antonio Maria Costa, to underscore the Bank Group's intent to work closely with the UN to fight crime and corruption. The next step of this effort will be the implementation of the UNCAC technical cooperation, as described above.

UNITED NATIONS CONVENTION AGAINST CORRUPTION

OII represented the Bank Group at the International Cooperation Workshop on Technical Assistance for Implementation of the UNCAC. The meeting identified a number of concrete mechanisms to advance coordination among multilateral and bilateral donors that provide funding for anti-corruption activities worldwide.

WORLD ECONOMIC FORUM'S PARTNERING AGAINST CORRUPTION INITIATIVE

The *Partnering against Corruption Initiative* (PACI) of the World Economic Forum has developed multi-industry principles and practices to promote integrity and prevent corrupt activities within signatory member companies. Spearheaded by a number of large, multinational corporations, the *Initiative* has also developed a self-monitoring mechanism to assure implementation of the Principles.

With assistance from OII, the IDB Group's Inter-American Investment Corporation and PACI signed an MOU and began working together to develop a version of PACI's integrity principles and related toolkit that is specifically tailored to the needs of small and medium-sized enterprises (SMEs) in Latin America.

This effort reflects the Bank Group's leadership and commitment to private sector measures that strengthen internal corporate governance and integrity.

ADDITIONAL INTERNATIONAL COLLABORATIVE ACTIVITIES

Eighth Conference of International Investigators

The Eighth Annual Conference of International Investigators from international organizations was held in June 2007. Topics included the analysis of whistleblower policies, financial disclosure initiatives and other integrity policies; the relationship of investigative offices with legal, procurement and audit departments; and the implementation of lessons learned from investigations.

The Chief of OII, who serves as a member of the Conference Secretariat, chaired the panel discussion on harmonizing and developing investigative standards. The Conference

attendees agreed to consider recommending that the represented institutions adopt the uniform definitions of fraudulent and corrupt practices recently implemented by the multilateral-development banks.

Peer Review and Assistance to Integrity Offices of other International Organizations

Integrity offices of international organizations have increasingly come to rely on one another, as a community, to conduct peer reviews that ensure that best practices are employed. The Chief of OII has participated in two such peer reviews. In 2006, he worked with senior staff of the Office of the UN High Commissioner for Refugees to complete a peer review of the International Fund for Agricultural Development (IFAD). This review resulted in the adoption of several significant improvements in IFAD's investigative mechanisms and structures in 2007.

As 2007 came to a close, the Chief of OII was working with representatives of the European Commission's Anti-Fraud Office, OLAF, on a peer review of the World Food Program's (WFP) Investigation Division. It is anticipated that this peer review will be completed and presented to WFP in early 2008.

Anti-Corruption Coordination

Finally, OII participates in and coordinates various other initiatives:

- OII again represented the Bank Group at the annual meeting of the International Group for Anti-Corruption Coordination.
- OII and the World Bank Group organized a joint training seminar on identification and prevention of collusion in project procurement.
- OII continues to work with the Organization for Economic Co-operation and Development (OECD) and in 2007 helped with the publication of technical materials related to the implementation of the OECD Anti-Bribery Convention in member countries.
- OII also continues to work closely with OLAF, including participating in an anti-corruption training program for Latin American officials.



VII: THE WAY FORWARD

In 2008, OII enters its fifth year of operations. There is much that this office and the Bank Group together have accomplished in OII's first four years, as evidenced by the achievements in both internal and external activities related to integrity and anti-corruption; yet much more can and must be done.

During 2008, a distinguished panel of external experts will deliver their evaluation of the Bank Group's anti-corruption framework. It is anticipated that recommendations for improvement in the IDB Group's anti-corruption activities—including the work of the OII, the OCFC, the sanctions process and enhanced preventive activities—will be included. Examination and implementation of the report's findings and recommendations will be a primary focus in 2008.

REVISING THE THREE PILLARS

OII originally cast its work as belonging to three pillars of support for integrity and anti-corruption. The first, *Setting the Standard*, is one for which it is anticipated that OII will expend fewer resources as the

newly selected Ethics Officer absorbs many of these responsibilities.

OII will recast its primary work within pillars two and three as described below.

PILLAR ONE: SETTING THE STANDARD

The addition of an Ethics Officer and the changes in the ways in which internal ethics issues are addressed should reduce the number of related cases and investigations coming to OII, hence allowing OII to shift investigative resources to more external cases, especially those with broad impact.

OII will continue to assist other units of the Bank Group with responsibility for internal ethics matters, including in the development of training materials and in the review of policies and procedures and other internal outreach and communications. As OII develops its knowledge base of risk and vulnerability issues and trends, it will engage other bank units in areas where steps can be taken to mitigate and prevent such risk.

PILLAR TWO: SUPPORTING MEMBER COUNTRIES' INTEGRITY EFFORTS

In 2008, OII will continue to assist ICF/ICS in the design and implementation of programs and activities that support efforts by member countries to prevent fraud and corruption.

OII will help with:

- Programmatic and lending activities that have anti-corruption and integrity components;
- Design and implementation of TCs targeting anti-corruption activities;
- Anti-corruption initiatives such as the Anti-Corruption Activities Fund;
- Development of the new Action Plan for Anti-Corruption Activities (PAACT);
- Private sector efforts such as PACI; and
- Partnerships in international efforts to increase compliance with international conventions including:
 - The OAS MOU for the *Inter-American Convention Against Corruption*;
 - Technical assistance for UNCAC; and
 - Work with UNODC.

OII will also continue its outreach and communications with member countries concerning integrity development and anti-corruption strategies.

PILLAR THREE: COMBATING FRAUD AND CORRUPTION AS A FIDUCIARY RESPONSIBILITY

OII anticipates that the greatest expansion of its work will be in proactive detection and prevention of corruption risk in Bank Group operations and Bank Group-financed activities. It will also devote more resources to improved communications within the Bank Group, expanded integrity outreach and pursuit of investigative cases with higher impact.

Activities anticipated in 2008 include:

- Greatly expand Knowledge-Based Systems and Management:
 - Pilot and refine the Red Flags Matrix in Country Offices and assist in developing a companion anti-corruption training program for operations staff;
 - Complete the analysis of Bank Group databases to determine the best ways in which to mine information for trends and indicators of corruption risk ; and

- Build a lessons learned knowledge base, derived from analysis of case outcomes, and determine how best to utilize these lessons learned for risk mitigation in Bank Group operations.
- Participate in the IDB's working groups on Bank-wide risk management and fiduciary systems to ensure that risks from fraud and corruption are identified and addressed as the Bank moves forward within its the new matrix-structured environment;
- Develop tools and provide resources to help identify and mitigate corruption risks in project design and evaluation;
- Engage in proactive project portfolio analysis;
- Expand advisory services to operations staff, especially with regard to identification and mitigation of corruption risks early in the project cycle ; and
- Work with all divisions involved in Private Sector Finance (VPP, SCF, IIC and MIF) to review the effectiveness of the *Integrity Due*

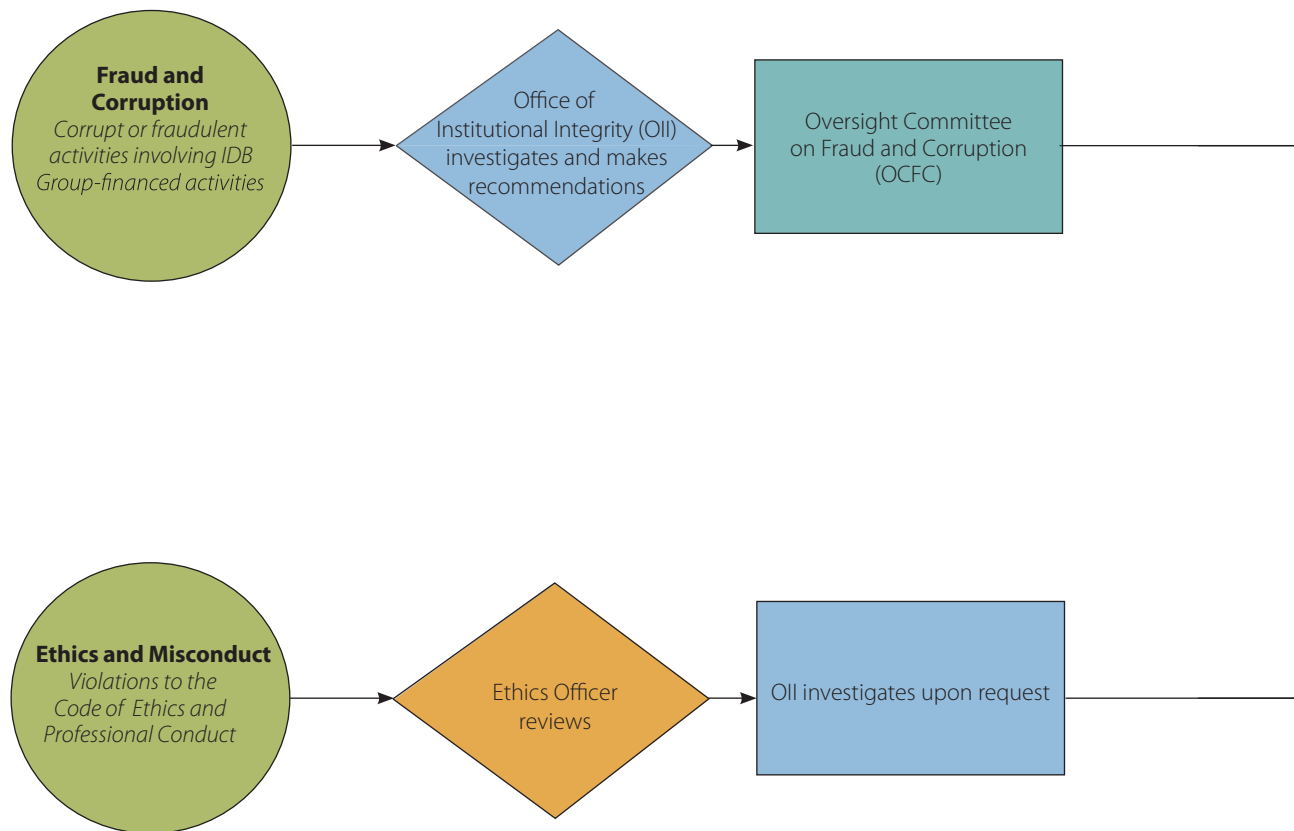
Diligence Framework for the Private Sector as implemented in 2007, and to determine improvements that can be made to ensure integrity in private sector lending activities.

CONCLUDING THOUGHTS

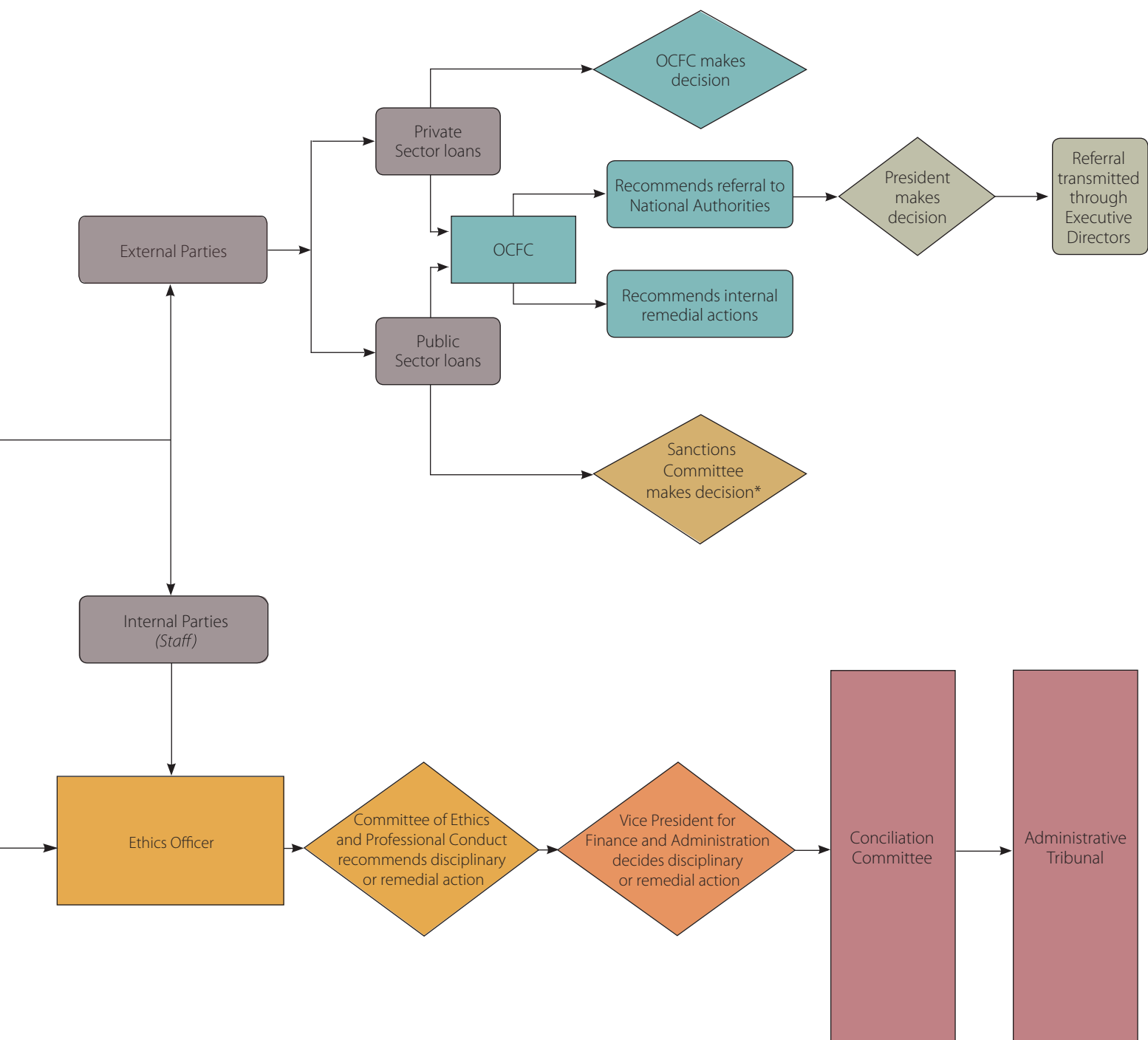
The fight against fraud and corruption and the efforts to maintain integrity as the cultural norm are part of an ongoing journey. As with many objectives, there is no absolute ending point in this journey; rather it is one of constant review and refinement. Advances are made but just as quickly, business models and operations change—creating new opportunity for those who would seek illegal benefit.

Our best outcome is to reinforce integrity as the operating norm and, always, to set the example through IDB Group leadership and actions. Towards this end, OII's specific goal this next year is to deepen our ability to identify new vulnerabilities and close them before they can be exploited.

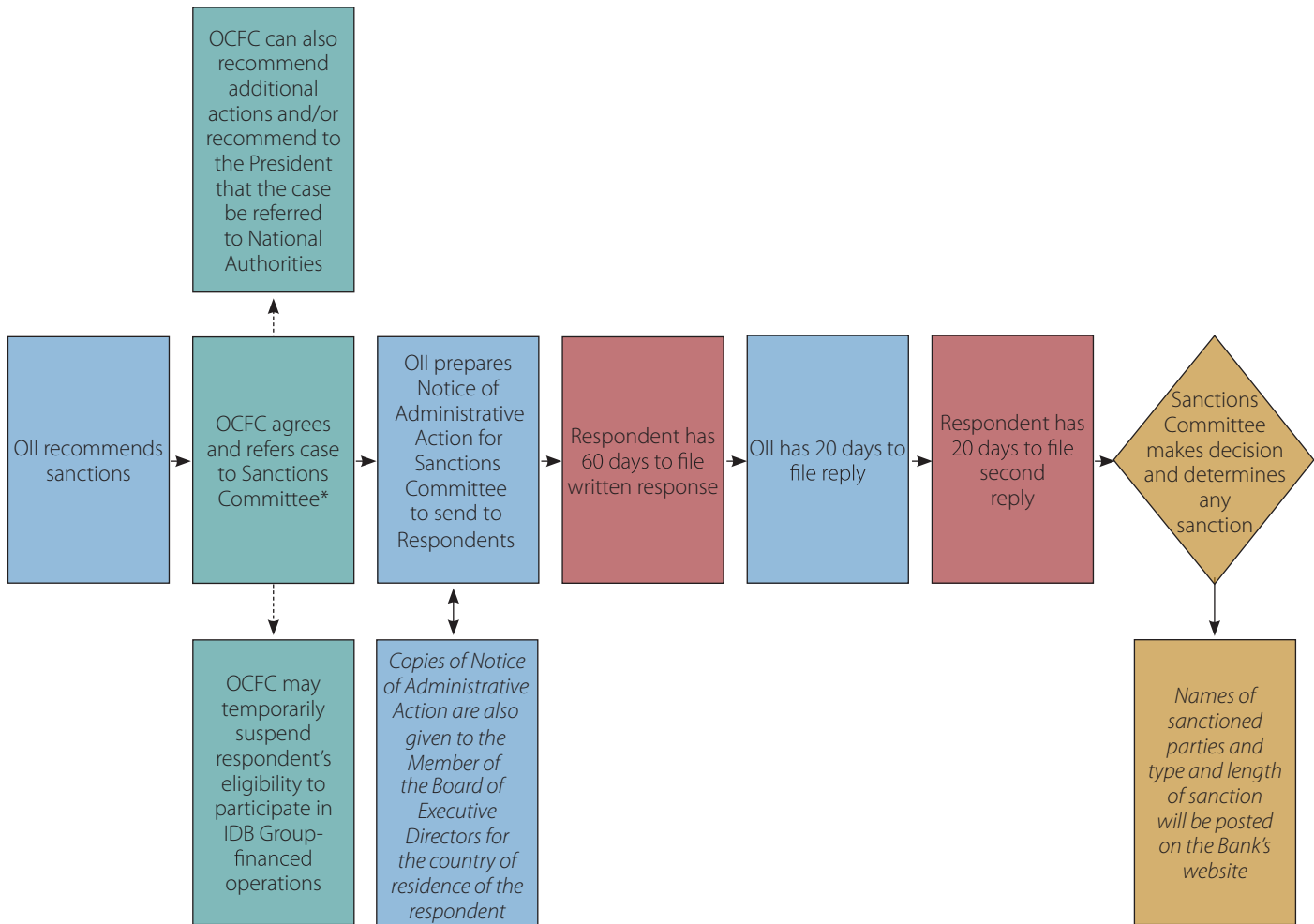
ANNEX I: THE INVESTIGATIONS PROCESS



* See Annex II



ANNEX II: THE SANCTIONS PROCESS



OCFC: Oversight Committee of Fraud and Corruption

OII: Office of Institutional Integrity

Respondent

Sanctions Committee

* Cases involving private sector lending activities or investment by the Multilateral Investment Fund are not referred to the Sanctions Committee; rather, OCFC retains jurisdiction throughout the process

REPORTING A VIOLATION

Allegations of fraud or corruption can be reported confidentially and securely:

e-mail:	ALLEGATIONS@idbfc.org
phone:	See chart below
fax:	1-202-312-4029
regular mail or in person:	Office of Institutional Integrity Inter-American Development Bank 1300 New York Avenue NW, Stop B680 Washington, DC 20577 USA

Mail addressed to OII should be marked “Personal and Confidential.”

Allegations may also be made to the Bank Group President, vice-presidents, managers, senior management of the IIC, MIF, or to the IDB Group Country Office Representative in each of its borrowing member countries, as well as to the Bank representatives in Europe and Asia. Allegations of staff misconduct should be reported to the Ethics Officer.

What Happens Next

After a report is filed, all allegations are reviewed by OII and reported to the Oversight Committee on Fraud and Corruption (OCFC). OII does not reveal the source of the allegation(s) to anyone outside the investigative team.

OII conducts a preliminary review of cases of alleged fraud and corruption before beginning an investigation, asking the following questions:

- Does the allegation concern any activity financed by the Bank Group?
- If the allegation were true, would it constitute a violation of the Bank Group’s prohibition against fraudulent or corrupt practices?
- Does the allegation provide sufficient credible information to warrant an investigation by OII?

If the answer to each of these questions is yes, OII may conduct a full investigation and report its findings to the OCFC for a determination of whether the matter should be referred to the Sanctions Committee and what further action, if any, is warranted.

HOW TO USE THE INTERNATIONAL TOLL FREE HOTLINE

Step 1: Dial the access code provided below for the country you are calling from.

Step 2: You will be asked to dial or provide the number that you would like to call.

Step 3: Dial or provide the number 877-223-4551

COUNTRY	ACCESS CODE	COUNTRY	ACCESS CODE	COUNTRY	ACCESS CODE	COUNTRY	ACCESS CODE
Argentina	0-800-555-4288	Colombia	01-800-911-0010	Haiti	183	Peru	0-800-50-000
Bahamas	1-800-872-2881	Costa Rica	0-800-0-114-114	Honduras	800-0-123	Suriname	156
Barbados	1-800-872-2881	Dominican Rep.	11 22	Jamaica	1-800-872-2881	Trinidad & Tobago	1-800-872-2881
Belize	811	El Salvador	800-1785	Mexico	01-800-288-2872	United States	1-800-225-5288
Bolivia	800-101-110	Ecuador	1-999-119	Nicaragua	1-800-0174	Uruguay	000-410
Brazil	0800-890-0288	Guatemala	99 99-190	Panama	800-0109	Venezuela	0800-2255-288
Chile	800-225-288	Guyana	159	Paraguay	008-11-800		

To view the full list of countries visit our website at: www.iadb.org/oii

**“Corruption paralyzes
the economic and social
development of our
Member Countries.”**

*Luis Alberto Moreno
President, IDB Group*

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