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## Odious Debt or Odious Payments - Using Anti-Corruption Measures to Prevent Odious Debt

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# **Odious Debt or Odious Payments? Using Anti-corruption Measures to Prevent Odious Debt**

*Anita Ramasastry<sup>†</sup>*

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### **I. Introduction**

What do the British Prime Minister Tony Blair, rock star Bono, South African President Thabo Mbeki, and Liberian President Ellen Sirleaf Johnson all have in common? All of them recently sat down for a chat at the World Economic Forum in Davos. The topic was debt relief in Africa and the problem of odious debt.<sup>1</sup> The so-called odious debt doctrine focuses on the

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<sup>1</sup> William L. Watts, *Bono Returns to Keep Focus on Africa*, MARKETWATCH, Jan. 26, 2007, <http://www.marketwatch.com> (search for "Bono Returns to Keep Focus on Africa," click on "Davos Notebook: Bono returns to keep focus on Africa" hyperlink).

DAVOS, Switzerland (MarketWatch)—Few celebrities were invited to Davos for this year's annual gathering of the World Economic Forum, but rock star Bono, a regular fixture of the gathering for the world's corporate and political elites, returned to a warm welcome Friday, sitting down with Bill Gates, Tony Blair, Liberian President Ellen Sirleaf Johnson and South African President Thebo Mbeki to spotlight Africa's woes.

Bono said corruption is a top impediment to the continent's progress, but charged that the way industrialized countries treat Africa is also a problem.

Liberia, for instance, still struggles with "odious debt" left over from dictatorial regimes, he said.

forgiveness or cancellation of sovereign debt once it has been created.<sup>1</sup> This type of analysis centers primarily on the role of the borrower and whether or not the terms or conditions of lending were "odious" in nature. Scholars and policymakers who have grappled with the issue of odious debt have focused on when successor regimes may have a reason for nonpayment of loans, or for debt cancellation.<sup>2</sup>

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In an iconic moment for the annual retreat, Bono in 2005 joined with Gates, former President Bill Clinton, Blair and Mbeki to call for a concerted effort to end poverty in Africa.

*Id.*

<sup>1</sup> PATRICIA ADAMS, *ODIOUS DEBTS: LOOSE LENDING, CORRUPTION AND THE THIRD WORLD'S ENVIRONMENTAL LEGACY* (1991) (quoting ALEXANDER SACK, *LES EFFETS DES TRANSFORMATIONS DES ÉTATS SUR LEURS DETTES PUBLIQUES ET AUTRES OBLIGATIONS FINANCIÈRES* [THE EFFECTS OF STATE TRANSFORMATIONS ON THEIR PUBLIC DEBTS AND OTHER FINANCIAL OBLIGATIONS] (1927); ALEXANDER SACK, *LA SUCCESSION AUX DETTES PUBLIQUES D'ÉTAT* [THE SUCCESSION OF THE PUBLIC DEBTS OF THE STATE] (1929)), available at <http://www.odiousdebts.org/odiousdebts/index.cfm?DSP=subcontent&AreaID=3>; see also Ashaq Kalfan, *Odious Debt: Definition, Application and Context*, EURODAD Annual Conference (2006), available at <http://www.odiousdebts.org/odiousdebts/publications/ODashfaqEURODAD.pdf>.

If a despotic power incurs a debt not for the needs or in the interest of the State, but to strengthen its despotic regime, to repress the population that fights against it, etc., this debt is odious for the population of all the State.

This debt is not an obligation for the nation; it is a regime's debt, a personal debt of the power that has incurred it, consequently it falls with the fall of this power.

The reason these "odious" debts cannot be considered to encumber the territory of the State, is that such debts do not fulfill one of the conditions that determine the legality of the debts of the State, that is: the debts of the State must be incurred and the funds from it employed for the needs and in the interests of the State.

"Odious" debts, incurred and used for ends which, to the knowledge of the creditors, are contrary to the interests of the nation, do not compromise the latter—in the case that the nation succeeds in getting rid of the government which incurs them—except to the extent that real advantages were obtained from these debts. The creditors have committed a hostile act with regard to the people; they can't therefore expect that a nation freed from a despotic power assume the "odious" debts, which are personal debts of that power.

ADAMS, Chapter 17, available at, <http://www.probeinternational.org/probeint/OdiousDebts/OdiousDebts/index.html>.

<sup>2</sup> See, e.g., Seema Jayachandran & Michael Kremer, *Odious Debt*, 96 AM. ECON. REV. 82 (2006); see also Patrick Bolton & David Skeel, *Odious Debts or Odious Regimes?*, 70 LAW & CONTEMP. PROBS. 1, 9 (forthcoming 2007) (advocating UN Security Council as intergovernmental entity that would declare regimes odious); Lee C.

Rather than focusing on debt in isolation, it may be useful to view odious debt as one category of problematic payments made to a state—payments corrupt political leaders use for illicit personal enrichment or to engage in repressive behavior. Funds from loans as well as revenues can be diverted from state treasuries into the personal bank accounts of corrupt leaders.<sup>3</sup> Loans and revenues can also be used to fund systematic oppression of individuals or minority groups.<sup>4</sup> Odious debt is but one category of odious payments generally. This paper uses the term “odious payments” to refer to payments made to a sovereign that are misappropriated by corrupt political leaders or that allow them to perpetuate violence against their populations. The funds that are used by the corrupt leaders are not available to successor governments that need funds to repay sovereign debt and to feed their citizens.

Putting an end to borrowing or lending is not the best solution to the problem of odious debt. A better solution would be to create mechanisms that allow for an accounting of funds disbursed to odious regimes and to require that odious regimes keep the funds within their respective countries. To the extent that a leader knows that sovereign loans or royalty payments are being disclosed, and that he cannot have access to Swiss or Cypriot

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Buchheit, G. Mitu Gulati, & Robert B. Thompson, *The Dilemma of Odious Debts*, 56 DUKE L.J. (forthcoming 2007) available at [http://eprints.law.duke.edu/archive/00001567/01/Dilemma\\_of\\_Odious\\_Debts\\_9-20-06.pdf](http://eprints.law.duke.edu/archive/00001567/01/Dilemma_of_Odious_Debts_9-20-06.pdf).

<sup>3</sup> *Time For Transparency, Coming Clean on Oil, Mining and Gas Revenues*, GLOBAL WITNESS (2004), [http://www.justiceinitiative.org/db/resource2?res\\_id=102698](http://www.justiceinitiative.org/db/resource2?res_id=102698) (“Across the globe, revenues from oil, gas and mining that should be funding sustainable economic development have been misappropriated and mismanaged. This Global Witness report considers five major examples of this problem: Kazakhstan, Congo Brazzaville, Equatorial Guinea and Nauru.”); David C. Gray, *Devilry, Complicity, and Greed: Transitional Justice and Odious Debt*, 70 LAW & CONTEMP. PROBS. (forthcoming 2007) abstract available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=957811](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=957811) (“[t]raditional odious debt doctrine therefore fails to capture many of the evils of abusive regimes and the variety of financial burdens left for their successors”).

<sup>4</sup> See HUMAN RIGHTS WATCH, SOME TRANSPARENCY, NO ACCOUNTABILITY: THE USE OF OIL REVENUE IN ANGOLA AND ITS IMPACT ON HUMAN RIGHTS 57-76, Jan. 13, 2004, available at <http://hrw.org/reports/2004/angola0104/angola0104.pdf>; Jill Shinkleman, *Managing Natural Resource Wealth*, U.S. INST. OF PEACE, (Aug. 2006); CORENE CROSSIN & JESSIE BANFIELD, CONFLICT AND PROJECT FINANCE: EXPLORING OPTIONS FOR BETTER MANAGEMENT OF CONFLICT RISK 7 (2006), [http://conflictsensitivity.org/files/publib/Conflict\\_Project\\_Finance.pdf](http://conflictsensitivity.org/files/publib/Conflict_Project_Finance.pdf).

banks, he may be less likely to plunder.

Why might these solutions be preferable to invoking a doctrine of odious debt? First, as some commentators have noted, all funds are fungible.<sup>5</sup> To the extent that a particular loan is not granted, a despot may take funds from another source to line his pockets or fill his private bank accounts. Second, the issue of which regimes are “odious” requires one to make a foray into the realm of political decision-making.<sup>6</sup> It may be difficult and unrealistic to find any particular intergovernmental body that can or will declare regimes “odious.”

This article focuses on ways to stem the tide of odious payments and to stop such payments, when made, from moving offshore into foreign bank accounts. To the extent that such payments leave a country, fewer funds are available to repay sovereign debts in the event of a regime change, or to feed and shelter the population.<sup>7</sup> This article focuses on emerging anti-corruption mechanisms as a means of dealing with odious payments and odious debt. It also focuses on the role of financial institutions (banks) as gatekeepers. Part I of this article focuses on the way in which banks are involved in odious payments: lending or extending credit, advising corrupt regimes, and helping hide the assets of political elites. Part II examines the use of a “publish what you lend” framework to provide for transparency in sovereign lending. Part III focuses on the use of anti-corruption measures to deal with capital flight. The use of procedures, such as heightened scrutiny for politically exposed persons, may be an important step in stopping capital flight when odious debt payments are being concealed by financial institutions. Also, the criminalization of illicit enrichment or inexplicable wealth may prove a valuable tool for prosecuting corrupt leaders.<sup>8</sup>

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<sup>5</sup> Bolton & Skeel, *supra* note 2, at 2.

<sup>6</sup> *Id.* at 11-12, 21; Jayachandran & Kremer, *supra* note 3, at 91-92.

<sup>7</sup> In sub-Saharan Africa, some empirical evidence shows that external borrowing may have fueled capital flight from the 1970s through the 1990s. See James K. Boyce & Leonce Ndikumana, *Africa's Debt: Who Owes Whom?* 2-7 (Univ. of Mass. at Amherst, Political Econ. Research Inst. Working Paper Series No. 48, 2002), available at [http://www.peri.umass.edu/fileadmin/pdf/working\\_papers/working\\_papers\\_1-50/WP48.pdf](http://www.peri.umass.edu/fileadmin/pdf/working_papers/working_papers_1-50/WP48.pdf).

<sup>8</sup> WORLD BANK, ANTI-CORRUPTION TOOLKIT 6, 214-19 (2001), <http://www.worldbank.org/publicsector/legal/aclawissues.pdf>.

## II. Bank Involvement in Odious Payments: Lending and Concealing

There are several ways, including financial advising, lending, and capital flight, in which banks provide financial services to sovereigns that may promote violence or corruption.

One method of promoting violence or corruption can occur when banks serve as financial advisors to a sovereign that is engaged in human rights violations.<sup>9</sup> For example, in 1997 a banker for Jardine Fleming was fired for providing financial advisory services to the Papua New Guinea government.<sup>10</sup> The government reportedly requested financial advice about how to finance mercenaries employed in an effort to contain a popular uprising against the Bougainville copper mine, operated by Rio Tinto, an Australian mining company.<sup>11</sup>

Banks may also be involved with sovereign lending activities that lead to the disbursement of odious payments.<sup>12</sup> Such lending can occur in many forms. Financiers may provide loans to sovereign governments that engage in human rights abuses or other forms of systematic repression.<sup>13</sup> In this regard, many commentators have pointed to commercial loans made to the apartheid government in South Africa.<sup>14</sup> Many European and North American banks were active in apartheid South Africa, such as the United Kingdom-based Barclays which reportedly made

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<sup>9</sup> JESSICA BANFIELD & CORENE CROSSIN, CONFLICT SENSITIVE PROJECT FINANCE: BETTER LENDING PRACTICE IN CONFLICT-PRONE STATES 17 (2006), available at <http://www.international-alert.org/publications/271.php>, (follow link to "Download Pdf Version") (citing J. Ridding, *HK Banker Fired Over Mercenaries: Jardine Fleming Acts on PNG*, FIN. TIMES, May 15, 1997).

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*; Jayachandran & Kremer, *supra* note 3, at 83; Charles Peter Abrahams, The Doctrine of 'Odious Debts': Does International Law Provide a Remedy to Instances Where Debts Are Contracted for Purposes of Committing Recognized International Wrongful Acts? A Contemporary Case of the Apartheid Debts 82 (Aug. 2000) (unpublished LLM Thesis, University Leiden), <http://www.odiousdebts.org/odiousdebts/publications/ApartheidDebtThesis.pdf> (Abrahams is the attorney for Jubilee South Africa as well as for plaintiffs in the apartheid litigation ongoing in the U.S. Court of Appeals for the Second Circuit).

USD \$725.4 million in loans to the apartheid regime.<sup>15</sup> Sovereign bond offerings may also be used by repressive governments to raise capital.<sup>16</sup> Commercial banks, for example, may provide trade finance that enables governments to import weapons and other equipment to be used in warfare.<sup>17</sup> Banks and other financial institutions may also support the manufacture of war-related items.<sup>18</sup> According to the non-governmental organization International Alert, "AXA, Dexia, Fortis, ING[,] and KBC have been linked to the financing of cluster bombs, landmines, nuclear weapons[,] and depleted uranium weapons."<sup>19</sup> Export credit agencies may also provide financing to support problematic infrastructure projects in corrupt states as well as the support of arms sales.<sup>20</sup>

In some countries—including Liberia and Angola—conflict commodities such as timber, cobalt, diamonds, gold, and oil generate "hard currency" that repressive regimes use to fund civil war or violent conflict.<sup>21</sup> The connection between international financial markets and conflict commodities has been well established, and in some cases the conflict commodities themselves are used for loan repayment.<sup>22</sup> During the Sierra Leone civil war, conflict diamonds were sold by the government and rebel groups to finance a bloody conflict.<sup>23</sup> International

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<sup>15</sup> BANFIELD & CROSSIN, *supra* note 9, at 17.

<sup>16</sup> *Id.* ("Morgan Stanley led a sovereign bond offering by the government [Republic of Guatemala] in November 2001. Citigroup served as the bookrunner for Guatemala's USD 330 million 30-year sovereign bond issue in 2004.").

<sup>17</sup> *Id.*

<sup>18</sup> *See id.*

<sup>19</sup> *Id.*

<sup>20</sup> *See id.*; ECA Watch: International NGO Campaign on Export Credit Agencies, Problems by Issues—Arms Trade, <http://www.eca-watch.org/problems/arms/index.html> (last visited Mar. 19, 2007).

<sup>21</sup> BANFIELD & CROSSIN, *supra* note 9, at 18.

<sup>22</sup> *Id.* "For instance, ING, UBS and HSBC have all extended loans or revolving cash facilities to the Angolan government that were repaid in crude oil cargoes, rather than cash." *Id.*; see GLOBAL WITNESS, A CRUDE AWAKENING: THE ROLE OF THE OIL AND BANKING INDUSTRIES IN ANGOLA'S CIVIL WAR AND THE PLUNDER OF STATE ASSETS 15-17 (1999), available at <http://www.globalpolicy.org/security/sanction/angola/1999/cru de.pdf>.

<sup>23</sup> *See* BANFIELD & CROSSIN, *supra* note 9, at 18.

human rights nongovernmental organizations have identified several banks, including ING Bank, ABN Amro Bank, and specialty diamond-finance banks in Antwerp, Belgium, to pinpoint the link between financing rough diamond trade with conflict.<sup>24</sup>

In addition to lending to dictators, banks can act as agents for odious regimes by helping political elites stash their misappropriated funds or odious payments.<sup>25</sup> There are many cases of ex-dictators who have plundered their national treasuries.<sup>26</sup> In some instances, misappropriated funds were concealed by private banks.<sup>27</sup> Successor governments subsequently must try to recover stolen funds.<sup>28</sup> There are many examples of successor governments attempting to find stolen assets, including the Philippines after Ferdinand Marcos,<sup>29</sup> Haiti after the Duvalier family,<sup>30</sup> Nigeria after Sani Abacha,<sup>31</sup> and Zaire

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<sup>24</sup> *Id.*; see IAN SMILLIE, LANSANA GBERIE, & RALPH HAZELTON, *THE HEART OF THE MATTER: SIERRA LEONE, DIAMONDS AND HUMAN SECURITY* 46 (Partnership Africa Canada 2000), available at <http://www.pacweb.org/e/pdf/heart%20of%20the%20matter.doc>.

<sup>25</sup> JONATHAN M. WINER & TRIFIN J. ROULE, *THE FINANCE OF ILLICIT RESOURCE EXTRACTION* 18 (2003), available at [http://lnweb18.worldbank.org/ESSD/sdvext.nsf/67ByDocName/TheFinanceofIllicitResourceExtraction/\\$FILE/WinerRoule.pdf](http://lnweb18.worldbank.org/ESSD/sdvext.nsf/67ByDocName/TheFinanceofIllicitResourceExtraction/$FILE/WinerRoule.pdf); see also Anita Ramasastry, *Secrets and Lies, Swiss Banks and International Human Rights*, 31 VAND. J. TRANSNAT'L L. 325, 328 (1998).

<sup>26</sup> *Recovering Dictators' Plunder: Hearing Before the Subcomm. on Financial Institutions and Consumer Credit of the H. Comm. on Financial Services*, 107th Cong. 3-4 (2002); see Ramasastry, *supra* note 25, at 329; Jonathan M. Winer & Trifin J. Roule, *Follow the Money: the Finance of Illicit Resource Extraction*, in NATURAL RESOURCES AND VIOLENT CONFLICT 161, 167-68 (Ian Bannon & Paul Collier eds., World Bank 2003).

<sup>27</sup> Winer & Roule, *supra* note 26, at 169-70; Ramasastry, *supra* note 25, at 329.

<sup>28</sup> A summary of the legal proceedings of all the above-mentioned cases, with special mention of the participation of U.S. banks can be read in *Private Banking and Money Laundering: A Case Study of Opportunities and Vulnerabilities: Hearing Before the Permanent Subcomm. on Investigations of the S. Comm. on Gov. Aff.*, 106th Cong. 872-934 (Minority Staff Report for Permanent Subcomm. on Investigations) Nov. 9, 1999, available at [http://www.senate.gov/~govt-aff/11099\\_report.htm](http://www.senate.gov/~govt-aff/11099_report.htm).

<sup>29</sup> Ramasastry, *supra* note 25, at 430.

<sup>30</sup> GAO REP. NO. 04-1006, at 27 (2004).

<sup>31</sup> U.N. OFF. ON DRUGS & CRIME, *ABACHA AND THE BANKERS: CRACKING THE CONSPIRACY*, FORUM ON CRIME AND SOCIETY at 111, U.N. Sales No. E.03.IV.2 (2002); see also UNODC Asset Recovery Project in Nigeria, [http://www.unodc.org/unodc/en/corruption\\_projects\\_nigeria\\_project2.html](http://www.unodc.org/unodc/en/corruption_projects_nigeria_project2.html) (last visited Mar. 7, 2007).



after its dictator Mobutu Sese Seku.<sup>32</sup>

Many—if not all—corrupt dictators who have transferred money offshore for personal enrichment have done so with the aid of correspondent or private banking services. In some circumstances, political elites are selling off natural resources of “conflict commodities”<sup>33</sup> to continue to fund civil unrest and military activities.<sup>34</sup> Banks have been instrumental in laundering and concealing the proceeds of the sale of conflict commodities.<sup>35</sup> In 2005, US-based Riggs Bank was fined \$41 million for assisting former Chilean dictator Augusto Pinochet and Equatorial Guinean President Obiang conceal their assets by failing to scrutinize their suspicious transactions.<sup>36</sup>

### III. Publish What You Lend?

One of the problems with odious debt, or of payments to a non-democratic regime, is opacity. Citizens may not have an accurate accounting of the funds received by their national treasuries, adding to the difficulty of obtaining a true accounting from a despotic leader. This begs the question: how can one achieve transparency when it comes to odious payments?

Those who lend could be required to disclose both to investors and the public what types of credit have been extended to a

<sup>32</sup> Paul D. Ocheje, *Refocusing International Law on the Quest for Accountability in Africa: The Case Against the “Other” Impunity*, 15 LEIDEN J. INT’L L. 749 (2002).

<sup>33</sup> Nataliue Pauwels, *Conflict Commodities: Addressing the Role of Natural Resources in Conflict*, International Security Information Service Briefing Paper No. 27 (March 2003), available at <http://www.ciaonet.org/wps/pan01/pan01.pdf>. See generally Ingrid J. Tamm, *Dangerous Appetites: Human Rights Activism and Conflict Commodities*, 26 HUM. RTS. Q. 687 (2004).

<sup>34</sup> See, e.g., PHILIPPE LE BILLON, *THE POLITICAL ECOLOGY OF WAR: NATURAL RESOURCES AND ARMED CONFLICTS*, 20 POL. GEOGRAPHY 568-70, 561-84 (2001), available at <http://www.geog.ubc.ca/~lebillon/ecowar.pdf>.

<sup>35</sup> See Ramasastry, *supra* note 25, at 325.

<sup>36</sup> See United States Department of Treasury Financial Crimes Enforcement Network, *In re Riggs Bank*, Assessment of Civil money Penalty No. 2004-1, available at <http://www.fincen.gov/riggsassessment3.pdf>; Anita Ramasastry, *Stopping Banks from Hiding Human Rights Abusers’ Money: A Recent Settlement by Riggs Bank Highlights the Issue*, FINDLAW, Apr. 4, 2005, <http://writ.news.findlaw.com/ramasastry/20050404.html>; OPEN SOC’Y JUST. INST., *LEGAL REMEDIES FOR THE RESOURCE CURSE: A DIGEST OF EXPERIENCE IN USING LAW TO COMBAT NATURAL RESOURCE CORRUPTION* 33-36 (2005), available at [http://www.justiceinitiative.org/db/resource2?res\\_id=102966](http://www.justiceinitiative.org/db/resource2?res_id=102966).

particular sovereign. A useful model for disclosure focuses on revenue transparency in natural resource payments. Revenue transparency data could help citizens of poor countries hold their governments accountable for the management of revenues generated by state resources.

Business entities and financial institutions may be perceived to be complicit in corruption and the deterioration of social conditions in the countries where they operate, even when they provide a transitioning economy with a valuable source of investment.<sup>37</sup> In some situations, a business may operate in a weak governance zone, where the state is unwilling or unable to protect its citizens from violence.<sup>38</sup> In other situations, a business may be alleged to have aided and abetted the activities of a repressive government.<sup>39</sup> Such investment, when managed transparently and responsibly, could be a source for economic growth and development that will benefit all citizens of these poor countries.<sup>40</sup>

One existing model of payment transparency is the “Publish What You Pay” (PWYP) campaign, which has been spearheaded by the civil society organizations Open Society Institute and Global Witness.<sup>41</sup> PWYP calls for the “mandatory disclosure of

<sup>37</sup> MARGARET JUNGK, THE DANISH CENTRE FOR HUMAN RIGHTS, DEFINING THE SCOPE OF BUSINESS RESPONSIBILITY FOR HUMAN RIGHTS ABROAD 1-3 (2005), *available at* [http://www.humanrightsbusiness.org/pdf\\_files/Defining%20the%20Scope%20of%20Business%20Responsibility%20.pdf](http://www.humanrightsbusiness.org/pdf_files/Defining%20the%20Scope%20of%20Business%20Responsibility%20.pdf); UNITED NATIONS GLOBAL COMPACT, GLOBAL COMPACT BUSINESS GUIDE FOR CONFLICT IMPACT ASSESSMENT AND RISK MANAGEMENT 1-2, 5 (2002), *available at* [http://www.unglobalcompact.org/docs/issues\\_doc/7.2.3/BusinessGuide.pdf](http://www.unglobalcompact.org/docs/issues_doc/7.2.3/BusinessGuide.pdf)

<sup>38</sup> OECD, INVESTMENT IN WEAK GOVERNANCE ZONES, SUMMARY OF CONSULTATIONS 1-5 (2005), *available at* <http://www.oecd.org/dataoecd/32/45/35397593.pdf>.

<sup>39</sup> See, e.g., Anita Ramasastry, *Corporate Complicity From Nuremberg to Rangoon: An Examination of Forced Labor Cases and Their Impact on the Liability of Multinational Corporations*, 20 BERKELEY J. INT’L L. 91 (2002) (analyzing the role of Unocal in its alleged involvement in Myanmar military government’s repression of its citizens).

<sup>40</sup> IMF, GUIDE ON RESOURCE REVENUE TRANSPARENCY 4-6 (2005), *available at* <http://www.imf.org/external/pubs/ft/grrt/eng/060705.pdf>; Henry Parham, Promoting Revenue Transparency in the Extractive Industries, Issue Paper, OECD Fifth Annual Anti-corruption Conference (2005), *available at* <http://www.oecd.org/dataoecd/0/0/35592802.pdf>.

<sup>41</sup> See Publish What You Pay, <http://www.publishwhatyoupay.org/english> (last visited May 21, 2007); see also Revenue Watch Institute, <http://www.revenuewatch.org>.

taxes, fees, royalties[,] and other payments by oil, mining[,] and gas companies to governments and other public agencies.”<sup>42</sup> This is meant to help end natural resource corruption by allowing citizens to see what revenues are being paid to a government.<sup>43</sup> As the PWYP campaign notes:

[t]he call for companies to “*publish what you pay*” is a necessary first step towards a more accountable system for the management of natural resource revenues paid by extractive industry companies to governments in resource-rich developing countries . . . . If companies disclose what they pay in revenues, and governments disclose their receipts of such revenues, then members of civil society will be able to compare the two and thus hold their governments accountable for the management of revenues. This will also help civil society groups to work towards a democratic debate over the use and distribution of resource revenues.<sup>44</sup>

In addition to the PWYP campaign, international financial institutions and governments within the G-8 have also embraced revenue transparency.<sup>45</sup> The British Government has supported the Extractive Industries Transparency Initiative (EITI),<sup>46</sup> which sets forth principles relating to disclosure of payments to governments for resource extraction. EITI is supported by an International Secretariat presently based in the United Kingdom’s Department for International Development. The Secretariat works

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org/about.

<sup>42</sup> Publish What You Pay, Objectives, <http://www.publishwhatyoupay.org/english/objectives/index.shtml> (last visited May 21, 2007).

<sup>43</sup> *See id.*

<sup>44</sup> Publish What You Pay, Objectives, *supra* note 42.

<sup>45</sup> The members of the Group of Seven (G-7) are Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. Together, these countries account for nearly two-thirds of global economic output. The leaders of these countries have met annually since 1975. They discuss significant economic and political issues. The Group of Eight (G-8) includes the G-7 countries plus Russia. Russia does not participate in financial and economic discussions, which continue to be conducted by the G-7. *See* United States Department of State, What is the G-8?, [http://usinfo.state.gov/ei/economic\\_issues/group\\_of\\_8/what\\_is\\_the\\_g8.html](http://usinfo.state.gov/ei/economic_issues/group_of_8/what_is_the_g8.html).

<sup>46</sup> *See* Extractive Industries Transparency Initiative homepage, <http://www.eitransparency.org/> (last visited May 22, 2007).

closely with the World Bank and the IMF.<sup>47</sup> In addition to the implementing governments, EITI is supported by many of the largest oil and mining companies in the world, as well as investors in those companies, and by civil society groups, many of which work under the umbrella of the PWYP coalition and the Revenue Watch Institute.<sup>48</sup> A sovereign may have fewer opportunities to divert funds if there is enhanced transparency in the lending process.

Could Publish What You Lend work in the context of sovereign debt? As noted above, there are multiple ways in which regimes may be financed. Creditors and investors that provide financing to sovereigns could be required to make affirmative disclosures with respect to the amount of funds disbursed to a sovereign. Sovereign debt may consist of a loan or may come in the form of bond issuances.<sup>49</sup> In the latter case, the underwriting of sovereign debt is what could be disclosed.

It might be difficult for every entity that is an investor to disclose the nature of sovereign debt because of the nature of derivative instruments. At the same time, disclosure might be limited to situations where an initial investment leads to the disbursement of funds to a sovereign, as opposed to disclosure based on who is an investor in a sovereign debt product.

The PWYP initiative already focuses on the role of banks in lending and why transparency is important with respect to sovereign lending. For example, PWYP “calls for all private, commercial and retail banks to require transparency of revenues from extractive industries as a condition for all resource-backed

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<sup>47</sup> For information on the World Bank and its institutions, see World Bank homepage, <http://web.worldbank.org>. For information on the International Monetary Fund, see IMF homepage, <http://www.imf.org>.

<sup>48</sup> The Revenue Watch Institute is an outgrowth of the Open Society Institute. It is a nonprofit organization with a mission “to improve democratic accountability in natural resource-rich countries by equipping citizens with the information, training, networks, and funding they need to become more effective monitors of government revenues and expenditures.” RWI also “works to ensure that the revenues generated by the extractive industries contribute to sustainable development and poverty reduction, through the promotion of public finance transparency in resource-dependent countries.” Revenue Watch, <http://www.revenuwatch.org/about>.

<sup>49</sup> J. EASTON & R. FERNANDEZ, *Sovereign Debt*, in 3 HANDBOOK OF INTERNATIONAL ECONOMICS 2032 (G. M. Grossman & K. Rogoff eds., 1995).

loans to developing countries.”<sup>50</sup> These are loans which are secured against future resource revenues.<sup>51</sup> As the PWYP recommendations state: “[r]esource-backed loans are often issued to governments at high interest rates and are paid back by revenues from future resource extraction.”<sup>52</sup> These loans are characterized as possibly representing “a whole system of parallel financing, outside of public scrutiny, which supports the shadow state and provides opportunities for cash to be diverted into private pockets.”<sup>53</sup>

Because such loans are not public, information about them is not available to civil society, in whose name such debts are arranged.<sup>54</sup> Banks, therefore, may be complicit in the misappropriation of state funds unless they implement procedures to ensure that loans are being properly used.<sup>55</sup> As part of the current PWYP initiative, banks are asked to “disclose all resource-backed loans and require that the borrowers agree to be audited in a transparent fashion, as a condition of receiving the loan.”<sup>56</sup> In situations where a state oil company receives a resource-backed loan, PWYP states that “an audit would need to reveal not only the company’s receipt of loan funds but also subsequent transfers of money to the government.”<sup>57</sup>

#### IV. Banks as Agents of Politically Exposed Persons

Banks may also serve as conduits for plundered assets. High-level, large-scale corruption by public officials, also referred to as a kleptocracy, is a particular threat to nations in transition.<sup>58</sup>

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<sup>50</sup> Publish What You Pay, Banks, <http://www.publishwhatyoupay.org/englishw/objectives/banks.shtml> (last visited May 21, 2007).

<sup>51</sup> *Id.*

<sup>52</sup> *Id.*

<sup>53</sup> *Id.*

<sup>54</sup> *Id.*

<sup>55</sup> Publish What You Pay, *supra* note 51.

<sup>56</sup> *Id.*

<sup>57</sup> *Id.*

<sup>58</sup> Ramasastry, *Secrets and Lies*, *supra* note 25, at 445; see also W. Michael Reisman, *Harnessing International Law to Restrain and Recapture Indigenous Spoliation*, 83 AM. J. INT'L L. 56 (1989); NDIYA KOFELE-KALE, INTERNATIONAL LAW OF RESPONSIBILITY FOR ECONOMIC CRIMES: HOLDING HEADS OF STATE AND OTHER HIGH

Successor governments in many countries have to chase down assets that have been stolen by deposed leaders—assets that moved offshore with banks serving as critical links and, often as repositories.<sup>59</sup>

In recent years, governments have focused more on the role of banks as agents of fiduciaries for kleptocrats. While dictators may secret away large amounts of wealth, they often act in concert with family members and business associates.<sup>60</sup> Moreover, a particular regime may have elites who are moving ill-gotten gains offshore.<sup>61</sup> Thus, tracing plundered assets involves following the money trail of multiple actors—not just one dictator. News reports refer to the purloined assets of Marcos, Abacha, and Mobutu as individuals, but their networks were larger.<sup>62</sup>

The Financial Action Task Force (FATF), an intergovernmental organization composed of member governments who fund the FATF on a temporary basis with specific goals and projects,<sup>63</sup> has developed forty principles that it asks nations to implement with respect to anti-money laundering.<sup>64</sup>

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RANKING STATE OFFICIALS INDIVIDUALLY LIABLE FOR ACTS OF FRAUDULENT ENRICHMENT 20-31 (1995).

<sup>59</sup> Ramasastry, *supra* note 25 at 329-330.

<sup>60</sup> *Id.* at 430-48 (discussing role of Marcos family in moving funds offshore); see also Celia W. Dugger, *Returned Loot not Misspent*, N.Y. TIMES, Dec. 23, 2006, at A13 (discussing return to Nigeria of funds looted by Abacha and his family members); Swiss Banks to Return Abacha Loot, BBC NEWS, July 12, 2000, available at <http://news.bbc.co.uk/1/hi/world/africa/845456.stm> ("Nigeria's administration says General Abacha used a circle of family members, close aides and business associates to dispose of the cash which he plundered from the state").

<sup>61</sup> See, e.g., AFRICAN CENTRE FOR ECONOMIC GROWTH, THE LINK BETWEEN CORRUPTION AND POVERTY: LESSONS FROM KENYA CASE STUDIES 2-3 (2000) (discussing role of elites in corruption and looting); Gerald Acquah Gasie, *Grand Corruption: A Crime Against Humanity* 105 (2005), [http://www-personal.buseco.monash.edu.au/~geraldg/Temp/grand\\_corruption.pdf](http://www-personal.buseco.monash.edu.au/~geraldg/Temp/grand_corruption.pdf).

<sup>62</sup> See Dugger *supra* note 60.

<sup>63</sup> See FATF-GAFI, General FAQ, <http://www.fatf-gafi.org> (click "General FAQ" hyperlink) (last visited Mar. 22, 2007).

<sup>64</sup> See FATF-GAFI, The 40 Recommendations of the FATF on Money Laundering, <http://www.fatf-gafi.org> (click "40 Recs" hyperlink under "Site Tools") (last visited May 22, 2007) [hereinafter FATF-GAFI 40 Recommendations].

The Financial Action Task Force (FATF) is an inter-governmental body whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing. The FATF is therefore a

As part of its recommendations, it has focused on “politically exposed persons” (PEP).<sup>65</sup> This is a term of art referring to “individuals who hold prominent public functions in their own country.”<sup>66</sup> The FATF recommendation asks banks to perform heightened due diligence when opening an account for such a person.<sup>67</sup> Recommendation 6 states that:

[f]inancial institutions should, in relation to politically exposed persons, in addition to performing normal due diligence measures:

- a) Have appropriate risk management systems to determine whether the customer is a politically exposed person.
- b) Obtain senior management approval for establishing business relationships with such customers.
- c) Take reasonable measures to establish the source of wealth and source of funds.
- d) Conduct enhanced ongoing monitoring of the business relationship. In addition to lending, banks have assisted with capital flight.<sup>68</sup>

The FATF recommendations do not define the term politically exposed person, but leave interpretation to various states.

The banking industry has also taken steps toward preventing money laundering through self-regulation. These regulations attempt to deal with the concept of PEPs as a way of providing some common guidance that can apply transnationally.<sup>69</sup> The voluntary Wolfsberg Principles, created by eleven leading banks, seek to prevent the use of banking services for “criminal purposes.”<sup>70</sup> Each signatory bank “endeavor[s] to accept only

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“policy-making body” created in 1989 that works to generate the necessary political will to bring about legislative and regulatory reforms in these areas. The FATF has published 40 + 9 Recommendations in order to meet this objective.

FATF-GAFI, homepage, <http://www.fatf-gafi.org> (last visited May 22, 2007).

<sup>65</sup> *Id.*

<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> The Wolfsberg Group, <http://www.wolfsberg-principles.com/index.html> (last visited May 22, 2007).

those clients whose source of wealth and funds can be reasonably established to be legitimate.”<sup>71</sup> According to guidance promulgated by the Wolfsburg Group, the term “politically exposed persons applies to persons who perform important public functions for a state.”<sup>72</sup> The guidance provides examples of PEPs

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<sup>71</sup> See The Wolfsberg Statement Against Corruption, [http://www.wolfsberg-principles.com/statement\\_against\\_corruption.html](http://www.wolfsberg-principles.com/statement_against_corruption.html) (last viewed May 22, 2007). Certain customers identified during due diligence or enhanced due diligence (initial and ongoing) may potentially represent a greater degree of risk. Such due diligence or enhanced due diligence may include identification of negative publicly available information from credible sources that calls into question a customer's activities regarding corruption, or, indeed, that indicates that prosecutions or actions have been taken by governmental authorities and/or law enforcement. The risks and possible mitigating measures are highlighted below together with any particularly relevant red flags. Examples include:

3.1. Politically Exposed Persons - PEPs potentially represent higher risk because they either are in a position to exert undue influence on decisions regarding the conduct of business by private sector parties, or have access to state accounts and funds.

Red Flags - Substantial cash or wire transfers into or from an account of a customer identified as a PEP where such activity is not consistent with legitimate or expected activity. Particularly substantial activity over a relatively short time period and/or the improper use of corporate or other vehicles to obscure ownership may also raise suspicions.

*Id.*; see also Wolfsberg AML Principles on Private Banking (May 2002), <http://www.wolfsberg-principles.com/privat-banking.html>.

<sup>72</sup> See Wolfsberg's FAQs on Politically Exposed Persons, <http://www.wolfsberg-principles.com/faq-persons.html>. The Wolfsberg Group acknowledges that there is great deviation in the definition:

The definition used by regulators or in guidance is usually very general and leaves room for interpretation. For example, the Swiss Federal Banking Commission in its guidelines on money laundering uses the term "person occupying an important public function," the US interagency guidance uses "senior foreign political figure" and the BIS paper Customer due diligence for banks says "potentates". The term should be understood to include persons whose current or former ("Rule of thumb": 1 year after giving up any political function') position can attract publicity beyond the borders of the country concerned and whose financial circumstances may be the subject of additional public interest. In specific cases, local factors in the country concerned, such as the political and social environment, should be considered when deciding whether a person falls within the definition.

*Id.*; see also Commission Directive 2006/70/EC, 2006 O.J. (L 214) (EC), available at [http://eur-lex.europa.eu/LexUriServ/site/en/oj/2006/l\\_214/l\\_21420060804en00290034.pdf](http://eur-lex.europa.eu/LexUriServ/site/en/oj/2006/l_214/l_21420060804en00290034.pdf) ("laying down implementing measures for directive 2005/60/EC of the European Parliament and of the Council as regards the definition of 'politically exposed person'").



including:

heads of state, government and cabinet ministers; influential functionaries in nationalized industries and government administration; senior judges; senior party functionaries; senior and/or influential officials, functionaries and military leaders and people with similar functions in international or supranational organizations; members of ruling royal families; senior and/or influential representatives of religious organizations (if these functions are connected with political, judicial, military or administrative responsibilities).<sup>73</sup>

The term “families” “should include close family members such as spouses, children, parents, and siblings and may also include other blood relatives and relatives by marriage.”<sup>74</sup> Additionally, closely associated persons “include close business colleagues and personal advisors/consultants to the politically exposed person as well as persons who obviously benefit significantly from being close to such a person.”<sup>75</sup>

The Wolfsberg Guidance on PEPs acknowledges that it can be difficult to identify politically exposed persons because these individuals may exclude critical information when opening bank accounts.<sup>76</sup> To that end, the principles are a bit disappointing as they state:

[I]t is a fact that [banks] do not have the necessary powers, means no information at their disposal to detect such persons. Banks are restricted in what information they can obtain. They must rely on the information they are given by clients and that can be gleaned from business documents or from the media.<sup>77</sup>

Private companies have developed PEPs databases, which provide details about PEPs and their relatives and associates, as well as

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and technical criteria or simplified customer due diligence procedures and for exemption on grounds of financial activity conducted on an occasional or very limited basis”). The European Commission defines politically exposed persons who are entrusted with prominent public functions including: “heads of State; heads of government, ministers and deputy or assistant ministers.” *Id.* at 31.

<sup>73</sup> Wolfsberg’s FAQs, *supra* note 72.

<sup>74</sup> *Id.*

<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

photographs of these individuals.<sup>78</sup>

What is important about the emphasis on PEPs is that banks not only need to verify the identity of such high profile (and possibly high risk) customers, but must also try to ascertain the source of their funds. To date, it is unclear whether banks are truly turning away PEPs if they are unable to substantiate the source of their deposits. During the summer of 2006, for example, Wholesale Firms Division of the Financial Services Authority (FSA) visited sixteen financial firms to determine whether they were compliant with British anti-money laundering legislation focused on due diligence and PEPs.<sup>79</sup>

The FSA noted that while the firms were generally compliant, there was room for improvement.<sup>80</sup> The FSA noted, in particular that not all firms were able to produce lists of PEPs on demand.<sup>81</sup> The report further noted that, while firms did thorough checks to identify PEPs at the account opening stage, the processes used to determine if/when an existing customer became a PEP were less formal, with reliance placed on the informal relationship and knowledge of the client.<sup>82</sup>

The United Nations Convention Against Corruption (UNCAC) may also be a useful part of a global regime to stop capital flight from odious regimes. UNCAC provides a framework for international cooperation against corruption, including prevention and law enforcement measures.<sup>83</sup> A critical element in the

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<sup>78</sup> *Id.*

<sup>79</sup> Financial Services Authority, Politically Exposed Persons ('PEPs'): Good Practice, [http://www.fsa.gov.uk/pages/Library/Other\\_publications/Money/peps.shtml](http://www.fsa.gov.uk/pages/Library/Other_publications/Money/peps.shtml) (last visited May 23, 2007).

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

<sup>82</sup> The report also noted that:

the firms we visited defined the reputational risk of PEP business as the risk that a PEP might be involved in a public scandal, not that they were actually corrupt. A PEP with a high profile or impending 'whiff' of scandal might be immediately turned away. However, a PEP with lower risk of public controversy may be more likely to be accepted. This risk assessment was regardless of the source or legitimacy of the PEP's funds. Reputational risk and financial crime risk are not the same and steps to mitigate reputational risk will not always reduce financial crime risk.

*Id.*

<sup>83</sup> United Nations Convention Against Corruption, G.A. Res. 58/4, U.N. Doc.

international fight against corruption is an effort to deny kleptocrats access to the fruits of their corrupt practices.<sup>84</sup> The UNCAC provides mechanisms for targeting assets misappropriated by current and former senior foreign government or political officials, their close associates and immediate family members, or other PEPs.<sup>85</sup>

The UNCAC focuses on issues such as capital flight and plunder in several manners. Article 20 asks states to consider adopting prohibitions on illicit enrichment.<sup>86</sup> This is an effort to make it easier for states to prosecute individuals for corruption, as it is often difficult to prove corruption, bribery, or plunder directly. Article 20 states, in particular:

each State Party shall consider adopting such legislative and other measures as may be necessary to establish as a criminal offense, when committed intentionally, illicit enrichment, that is, a significant increase in the assets of a public official that he or she cannot reasonably explain in relation to his or her lawful income.<sup>87</sup>

Illicit enrichment is usually defined as a significant increase in the assets of a government official that she or he cannot reasonably explain in relation to her or his lawful earnings during the performance of her or his duties.<sup>88</sup> Many developing countries have established the crime of "illicit enrichment" as a substitute for corruption offenses because of the difficulty of proving and prosecuting cases of corruption.<sup>89</sup>

Article 26 of the UNCAC further provides that state parties should "establish liability for legal persons" (which would include

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A/58/422 (Oct. 31, 2003), *available at* [http://www.unodc.org/pdf/crime/convention\\_corruption/signing/Convention-e.pdf](http://www.unodc.org/pdf/crime/convention_corruption/signing/Convention-e.pdf) [hereinafter United Nations Convention against Corruption].

<sup>84</sup> Guillermo Jorge, Notes on Asset Recovery in the UN Convention on Corruption (2006) (online paper), <http://www.abanet.org/intlaw/hubs/programs/Annual0316.03-16.06.pdf>.

<sup>85</sup> United Nations Convention Against Corruption, *supra* note 83.

<sup>86</sup> *Id.* at 12.

<sup>87</sup> *Id.*

<sup>88</sup> *Id.*

<sup>89</sup> *Id.*

banks) for violating the convention.<sup>90</sup> Finally, Article 52 also requires states to implement measures to deal with PEPs.<sup>91</sup> Article 52 states that state parties “shall take such measures as may be necessary, in accordance with its domestic law, to require financial institutions within to . . . conduct enhanced scrutiny of accounts sought or maintained by or on behalf of individuals who are, or have been, entrusted with prominent public functions and their family members and close associates.”<sup>92</sup>

At present, it is too early to tell whether banks are changing their culture of opening accounts for PEPs. Ideally, the UNCAC and other related domestic measures are meant to help banks refuse funds that are the proceeds of corruption. Banks are meant to turn away dictators and others who cannot substantiate the source of their loot. To the extent that this is coupled with an offense focused on illicit enrichment, the international community has two powerful tools for preventing leaders from draining their treasuries and moving the funds out of the country.

Critics might assume that some countries will always serve as offshore havens for kleptocrats. Even if most nations improve their emphasis on anti-corruption and stopping corrupt PEPs from moving funds into their banks, some rogue states will offer their banks as safe havens for stolen monies. FATF engages in a practice of naming and shaming countries that are non-compliant with its forty anti-money laundering recommendations.<sup>93</sup>

Currently, there are no countries on its blacklist.<sup>94</sup> Previously there have been many.<sup>95</sup> Of course, this does not mean that all countries are currently well-behaved and vigorously pursuing anti-

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<sup>90</sup> *Id.* at 14.

<sup>91</sup> United Nations Convention Against Corruption, *supra* note 83, at 31.

<sup>92</sup> *Id.*

<sup>93</sup> The principal objective of the Non-Cooperative Countries and Territories (NCCT) Initiative is to reduce the vulnerability of the financial system to money laundering by ensuring that all financial centres adopt and implement measures for the prevention, detection and punishment of money laundering according to internationally recognized standards. See FATF, Non-Cooperative Countries and Territories (NCCT) Initiative, <http://www.fatf-gafi.org> (click “NCCT initiative” hyperlink; scroll to “About the NCCT Initiative” hyperlink).

<sup>94</sup> Non-Cooperative Countries and Territories (NCCT) Initiative, NCCT Timeline, <http://www.fatf-gafi.org> (search “NCCT Initiative”).

<sup>95</sup> *Id.*

money laundering measures. It does mean, however, that countries are improving their performance in response to being named and shamed by FATF. Why would a blacklist force a change in behavior? Perhaps due to the reputational risks involved in blacklisting. However, the fact that the banking system is global is a more likely explanation. Countries do not want to face being shut out of global financial markets because of lax anti-money laundering procedures.

Why is a focus on PEPs preferable to the cancellation of odious debt? Because this solution can be applied to all PEPs, not just those that appear to be "odious." As such, the due diligence model is not dependent on a person making the decisions. Rather, all PEPs should have to substantiate the source of their funds. Such a rule does leave some discretion in the hands of bankers, but the decision-making is tied less to whether a particular regime is corrupt. Instead, the focus is on determining whether someone is a prominent public official.<sup>96</sup> This determination is inherently less political and is one that, over time, can become more routine for bank officials.

## V. Conclusion

Even if banks can stop funds from moving offshore, odious debt and other odious payments will not disappear into thin air. The two strategies discussed in this article are meant to complement one another. First, to the extent that creditors' payments to sovereigns are disclosed (publish what you lend), kleptocrats should have less incentive to steal, recognizing that other creditors and the public know what funds have been disbursed. Second banks should be able to forestall a dictator's attempts to divert national funds for his own private gain by refusing to accept deposits whose source cannot properly be substantiated. Thus, one measure can prevent the creation of odious debt; or, if the debt is created, the other measure can keep the funds in the national treasury to be used for repayment by future governments.

The next time Bono and his friends meet at Davos, they should not focus should not be on odious debt. Rather, they should discuss how to ensure meaningful transparency in sovereign

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<sup>96</sup> See Wolfsberg's FAQs, *supra* note 72.

payments and strong implementation of the United Nations Convention on Corruption.

