Natural Resource Governance Institute

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Secretary, Securities and Exchange Commission
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CC:
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Mr. Barry Summer, Associate Director, Division of Corporation Finance
Ms. Elizabeth Murphy, Associate Director, Division of Corporate Finance
Mr. Elliot Staffin, Special Counsel, Division of Corporate Finance

Via Email (to: rule-comments@sec.gov)

16th March, 2020

Re: File Number S7-24-19 – Proposed Rule 13q-1 to implement Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act

Dear Secretary Countryman,

We welcome the opportunity to provide a submission to the Securities and Exchange Commission (the "Commission") on proposed Rule 13q-1 and amendment to Form SD implementing Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Section 1504) requiring payment disclosure by resource extraction issuers.

The Natural Resource Governance Institute (NRGI), an independent, non-profit organization, helps people to realize the benefits of their countries' oil, gas and mineral wealth through applied research, and innovative approaches to capacity development, technical advice and advocacy. NRGI is recognized for its technical expertise, and has been involved in the development of mandatory reporting requirements for the extractive industries in the United States, Europe and Canada. We have also contributed extensively to the development of the Extractive Industries Transparency Initiative (EITI), including serving on the initiative's board since its inception and contributing to the revised version of the EITI Standard adopted in 2019.

In order to better understand the patterns and problematic behaviors that indicate potential corruption in the oil, gas and mining sectors, in 2017 NRGI examined over 100 real world cases of license or contract awards in which accusations of corruption arose. The resulting report, *Twelve Red Flags: Corruption Risks in the Award of Extractive Sector Licenses and Contract* presents a list of 12 red flags which may indicate to authorities or oversight bodies that more scrutiny is required.

The warning signs presented in the report underscore the need for contract-level project data transparency, both to act as a preventative measure against the kinds of corruption cases outlined in the report, and to provide vital information to authorities, investigative journalists and other anti-corruption actors to investigate further when problematic activities are identified. As one example, flag 10 in the

report is 'A payment made by the winning company is diverted away from the appropriate government account'. Reports by both Global Witness[1] and NRGI[2] have demonstrated how contract-level project data resulting from payment-to-governments disclosures in the EU, Canada and Norway can be used to monitor and verify signature bonuses resulting from the award of a new license or contract.

We urge the Commission to ensure the final rule aligns with the contract-level project reporting requirements as laid out in the EU Accounting Directive and Canada's Extractive Sector Transparency Measures Act (ESTMA).

We appreciate the opportunity to make this submission and would welcome the opportunity to discuss the report with you in further detail. Please do not hesitate to contact us with any questions.

Sincerely,

Aaron Sayne

Senior Governance Officer
Natural Resource Governance Institute

[1] Global Witness and Resources for Development Consulting, (2018) 'Finding the missing millions A handbook for using extractive companies' revenue disclosures to hold governments and industry to account'. https://www.globalwitness.org/en/campaigns/oil-gas-and-mining/finding-missing-millions/

[2] Malden, A., and Muhammadi, F., (2019) 'Indonesia's Oil and Gas Revenues: Using Payments to Governments Data for Accountability' https://resourcegovernance.org/analysis-tools/publications/indonesia-oil-gas-revenues-payments/

Twelve Red Flags: Corruption Risks in the Award of Extractive Sector Licenses and Contracts

Aaron Sayne, Alexandra Gillies and Andrew Watkins

APRIL 2017

Natural Resource Governance Institute

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Summary

Oversight actors can detect and prevent corruption in the oil, gas and mining sectors if they ask the right questions. While corruption schemes can be complex and opaque, the players involved are not endlessly creative: clear patterns and similar signs of problematic behavior do exist across resource-rich countries.

To find these, we examined over 100 real-world cases of license or contract awards in the oil, gas and mining sectors in which accusations of corruption arose. The cases come from 49 resource-producing countries, and include the award of exploration and production licenses as well as service contracts and commodity trading contracts. For each case, we asked: what signs might have tipped off authorities or oversight bodies that more scrutiny was needed?

Based on this work, we developed a list of 12 red flags with real-world illustrations for each. Our corruption red flags list is a tool for inquiry, not prediction. Users should not interpret the presence of any individual red flag as proof of corruption. Conversely, no one should assume that a deal lacking the signs is corruption-free. The list focuses on specific attributes of the licensing transaction rather than contextual factors (e.g., levels of transparency, the rule of law) that also impact levels of corruption. As discussed below, the focus on known corruption controversies left our sample with two main biases: we did not examine cases where corruption has remained hidden or cases where accusations of corruption were entirely absent.

With these caveats in mind, when combined with country-specific analysis and adaptation, our list of 12 red flags and their illustrations can provide a concrete, practical tool to help reduce corruption risks around license and contract awards. They could inform the design of award processes by government officials, the conduct of due diligence checks by company and government actors, and the oversight activities of parliamentarians, journalists, law enforcement officials and other groups.

The red flags are:

1. The government allows a seemingly unqualified company to compete for, or win an award.
2. A company or individual with a history of controversy or criminal behavior competes for, or wins, an award.
3. A competing or winning company has a shareholder or other business relationship with a politically exposed person (PEP), or a company in which a PEP has an interest.
4. A competing or winning company shows signs of having a PEP as a hidden beneficial owner.
5. An official intervenes in the award process, resulting in benefit to a particular company.
6. A company provides payments, gifts or favors to a PEP with influence over the selection process.
7. An official with influence over the selection process has a conflict of interest.
8. Competition is deliberately constrained in the award process.
9. A company uses a third-party intermediary to gain an advantage in the award.
10. A payment made by the winning company is diverted away from the appropriate government account.
11. The agreed terms of the award deviate significantly from industry or market norms.
12. The winning company or its owners sell out for a large profit without having done substantial work.

Introduction

Oversight actors can detect and prevent corruption in the oil, gas and mining sectors if they ask the right questions. The schemes corrupt actors use can be complex and opaque, making use of complicated transactions, many legal entities and offshore secrecy jurisdictions, and a range of players. They also evolve over time—not least as accountability actors bring favored graft techniques to light. Yet the players are not endlessly creative: clear, general patterns and signs of suspect behavior do exist across resource-rich countries.

To find these, we examined over 100 real-world cases of license or contract awards in the oil, gas and mining sectors in which accusations of corruption arose. The cases came from 49 resource-producing countries. For each case, we asked: what signs might have tipped off authorities or activists that more scrutiny was needed? Based on this work, we have created a list of red flags that can guide and help prioritize the efforts of oversight actors to prevent or detect future corruption.

We examined over 100 real-world cases of oil, gas and mining sector license or contract awards in which accusations of corruption arose. The cases come from 49 resource-producing countries.

In many of the cases we analyzed, corruption led to major losses for the resource-producing country. In some, government officials selected underqualified or irresponsible companies that were unable to effectively execute the project; in others, they diverted funds that should have benefited the public. Corruption in licensing and contracting can also undermine the integrity and performance of key public institutions, weakening their overall ability to manage the sector. It can scare off risk-averse investors who do not want to be associated with scandal. The impacts of corruption on companies have been dramatic as well: high-profile lawsuits and convictions, not least under laws like the U.S. Foreign Corrupt Practices Act (FCPA); billions of dollars in fines, penalties and professional fees; falling share prices; scuttled deals; negative coverage by the media, non-governmental organizations (NGOs) or other industry watchdogs; and reputational damage.

We believe that oversight actors, both inside and outside government, and private sector players can use the list of red flags in this report as one tool to guard against these sorts of harm. When regulators, law enforcement, parliamentarians, journalists, activists or investors observe particular red flags, they should all ask further questions and gather more information. In some cases, this questioning will produce a reasonable explanation. In others, the additional scrutiny may reveal corrupt behavior.

UNDERSTANDING AND USING THE LIST

This red flags list is a tool for inquiry, not prediction. Users should not take the presence of any individual flag in an award process they are scrutinizing as *de facto* proof of corruption. Conversely, no one should assume that an award showing none of these signs is corruption-free. As discussed below, the list is not exhaustive and contains two significant biases. Nonetheless, we believe it can be a helpful, reliable tool to inform due diligence and manage corruption risks around license and contract awards.

Scope and case selection

Our list focuses only on the licensing and contracting phase of the extractives sector decision chain. When selecting cases for analysis, we looked at instances when a producing country government directly awarded an extractive sector license or contract, and when it had to approve an award by a private party—an oil services contract, for example.[1] The types of awards included the allocation of exploration and production licenses, service contracts, and licenses to engage in commodity trading and transportation. The cases we examined also involved different types of award processes, ranging from competitive tenders to first-come-first-served, single-source awards and license transfers. We chose cases that featured either proven corruption or accusations of corruption. To account for as much relevant behavior as possible, we defined corruption broadly as "the abuse of entrusted public power for personal gain."[2]

We focused on awards because they have attracted major corruption in the past, and because they can create strong incentives for corruption. Government officials select which company will receive a highly profitable business opportunity. Depending on the socio-economic and political context, the officials may have strong interests and pressures to use this power to extract benefits for themselves and their allies. Companies, for their part, may have incentives to manipulate the award proceedings, so as to gain favor with the selecting officials.

Second, and more positively: the award of licenses and contracts are discrete moments which means that in these instances oversight actors can more effectively exercise their roles. Corruption can appear across the entire extractive sector value chain, from license awards to the regulation of company behavior to the collection and expenditure of government revenues. Unlike more day-to-day regulatory decisions, the awards of licenses occur at a specific moment, and are often announced publicly, subject to established rules, receive media coverage and, in some places, are subject to approval by parliament. Therefore, award processes are concrete events that journalists, activists, parliamentarians and anticorruption authorities can scrutinize, often with the benefit of some publicly available information.

Award processes are concrete events that journalists, activists, parliamentarians and anticorruption authorities can scrutinize, often with the benefit of some publicly available information.

Appendix A to this report contains more information on our processes and rationales for selecting cases. Appendix B lists the 48 countries covered by the selected cases.

Identifying red flags

To identify red flags, we examined how the selected cases unfolded, looking for signs that oversight actors could have spotted by oversight actors and followed up with further inquiry. We included red flags that appeared in at least four case studies. The red flags varied widely in their incidence. Table 1 shows the number of cases where each red flag was present.

Table 1. Incidence of red flags, by frequency

Red flags	Total appearances in 100 cases
6 A company provides payments, gifts or favors to a PEP with influence over the selection process.	58
4 A competing or winning company shows signs of hidden beneficial ownership by a PEP.	55
1 The government allows a seemingly unqualified company to compete for, or win an award..	54
5 An official intervenes in the award process to benefit a particular company.	49
8 Competition is deliberately constrained in the award process.	38
7 An official with influence over the selection process has a conflict of interest.	36
11 The agreed terms of the award deviate significantly from industry or market norms.	35
3 A competing or winning company has a shareholder or other business relationship with a PEP, or a company in which a PEP has an interest.	30
9 The company uses a third-party intermediary to gain an advantage in the award..	28
2 A company or individual with a history of controversy or criminal behavior competes for, or wins, an award.	23
10 A payment made by the winning company is diverted away from the appropriate government account.	19
12 The winning company or its owners sell out for a large profit without having done substantial work.	12

In choosing red flags, we focused only on specific aspects of the award transactions, looking for:

1 characteristics of the companies, government bodies or individuals involved
2 conduct by the companies, government bodies or individuals involved
3 outcomes, especially those that were detrimental to the public interest

This report omits several types of red flags that have appeared on checklists produced by other organizations, such as those mentioned below in the section on related studies. We did not consider as red flags any *process weaknesses*, such as the absence of transparency or the absence of competitive bidding processes. We recognize that these attributes can help prevent corruption and they would likely feature as urgent recommendations in any effort to reform a country's award systems. However, we wanted the red flags list to apply to any type of award process, whether well-structured or otherwise.

We also did not include contextual factors, such as the country's overall levels of transparency, accountability, civic space, the rule of law and perceptions of corruption.[3] Award transactions do not take place in a vacuum, and the wider institutional, legal and political environment impacts the likelihood of corruption. In countries where transparency is limited, or where oversight actors like journalists cannot question government decisions without fear of repression, corruption becomes much easier to get away with. In the section below on the importance of context we further explain how the wider governance environment should influence the response to more specific, transaction-level red flags like the ones discussed here.

In countries where transparency is limited, or where oversight actors like journalists cannot question government decisions without fear of repression, corruption becomes much easier to get away with.

We omitted these categories of factors–process weaknesses and context– from the list of red flags in order to create a list that is widely applicable across different types of award processes and different country environments. These wider factors should, of course, still be taken into account by governments and companies when assessing corruption risks.

Biases and strengths

The cases we selected feature two significant biases. First, our research concentrated on publicly available documents and known cases. Our main types of source material were therefore court and regulatory filings, media coverage and NGO reports. We also drew almost exclusively on materials available in English, French or Spanish.[4] This means that our dataset has a bias towards the types of corruption that receive attention from law enforcement authorities or other oversight actors. Corruption schemes or behaviors that so far have escaped public notice will not be described here. These could include corruption in authoritarian countries where public scrutiny of government corruption is highly constrained, or actions by non-Western companies, which receive less attention from American and European law enforcement agencies, media and NGO actors that produced much of our source material. Finally, the overlooked cases could include some of the more effective and sophisticated corruption schemes that have to date gone undetected.

A second and related bias is that we only examined cases where suspicions of corruption have arisen, and therefore do not have a control group of non-corrupt cases against which to compare them. Our approach was to look back at a series of awards where corruption controversies occurred, and identify some red flags that oversight

actors might have observed as those award processes played out. We therefore cannot indicate the degree to which the flags on our list correlate with corruption, or are absent from cases void of corruption. A different methodology might examine a wider set of award processes that included both cases of corruption and the absence of corruption, and identify which award attributes correlate with the corrupt cases. Further research using this latter approach could be useful, if it could shed light on which of the red flags correlate more closely with corruption and therefore might hold more predictive power.[5]

These caveats noted, we believe the following factors make our red flags list sufficiently reliable as a tool to help oversight actors ask further questions about possible corruption in award processes:

- We drew our findings primarily from analysis of detailed real-world cases, not from hypotheticals, academic literature or similar sources.
- The literature review on corruption red flags we carried out listed many of the same ones as we found.
- We used a large sample of cases—in total we reviewed 124 and ultimately used 100 to build the list.
- The sample likewise has a wide geographic reach—49 countries across five continents.
- Each red flag appeared in at least four of the cases; relevant examples are summarized below, under the appropriate signs. Many showed up in far more than four cases. (See table 1, above.)
- Each red flag was also present in cases from more than one country.[6]
- In the vast majority of the cases we used, more than one red flag was present.
- Some red flags tended to appear together in familiar patterns, or "bundles." For example, red flag 6 (in which a company provides payments, gifts or favors to a PEP with influence over the selection process) tended to feature in the same cases as red flags 3 (a company shows signs of beneficial ownership by a PEP) and 5 (an official intervenes in the award process to benefit a particular company).

Inclusion of both corruption allegations and convictions

Not all of the awards described in this report led to criminal convictions. Some of the awards only prompted suspicion, controversy or lesser types of official responses. Others led to legal action, but the cases were later dropped or settled without a guilty plea. We do not suggest that the actors in these cases engaged in any illegal activity—indeed their actions may have been entirely lawful in the relevant jurisdictions. When an accused party publicly denied the charges, we present this information. However, all of the cases illustrate the kind of allegations that can arise when award processes show corruption red flags.

We also have included many cases that were subject to active investigations and legal proceedings at the time of publication. We encourage readers of this report to check the status of any of the cases for the most up-to-date and complete information.

Building on previous research and tools

Our list is meant to complement and build on previous efforts to catalog signs of corruption. Many actors, including government bodies,[7] industry analysts and anticorruption/risk management groups,[8] international financial institutions (IFIs),[9] research and policy institutions,[10] and watchdogs such as the media or NGOs[11] have compiled lists of red flags to use when assessing corruption risks. These reviews often focus on government procurement. Most of them were not specific to individual industries, or particular types of awards and award processes. A partial list of these publications is found in appendex C on selected resources.

In reviewing this literature we found many instances of overlap with our analysis, and some important differences as well. Versions of most of the red flags described in this report appear on more than one of the past lists. At the same time, some of the earlier efforts include elements that our list does not. These differences stem from choices in methodology and prioritization, rather than any one list being more exhaustive than another.

As noted above, we focused on specific attributes of the award transaction. Other lists, by contrast, include broader structural or contextual factors—for instance, respect for the rule of law and perceptions of corruption in the country where the award takes place. For example, some identified doing business in a country with a "reputation for corruption" and "low risk of sanctions" as red flags.[12] Along with national attributes, other lists considered the impact of corporate culture on corruption risks.[13] As noted above, our list does not account for contextual factors, though information about context is critical when comprehensively assessing corruption risks around an individual transaction.

Another variation across the studies concerns how the red flags were identified. Some of the studies' authors seemed to use hypothetical assessments of award processes to identify their red flags,[14] or reviewed risks in the selection processes run by particular organizations, such as the World Bank.[15] Surveying a wide set of real-world corruption cases to identify red flags was less common, though some authors illustrated their lists with (sometimes anonymized) examples.[16] For some actors, such as multilateral organizations, it can be controversial or politically difficult to explicitly mention real-world corruption cases or use these as evidence of potential problems. This may help explain why our methodology for finding red flags was relatively less common.

Finally, other researchers mention a methodological problem also encountered in our effort. As explained further below, the red flags identified here cannot be used as *predictors* of corruption, because we did not also assess their presence in award processes that apparently lack corruption. Some research has noted this challenge, suggesting that existing red flags lists may tend to overstate their value as tools for predicting the occurrence of corruption. In particular, researchers have noted that some lists seem to assume, without testing, that the appearance of a flag in future cases is a reliable predictor of corruption.[17] Accordingly, in the methodology section above, we explicitly mention that we have *not* proven the predictive power of the red flags in this report. Rather, we list red flags that appeared in several controversial award processes that oversight actors may wish to watch out for and interrogate further.

WHO COULD USE THE LIST

The aim of our red flags list is to put concrete, practical information into the hands of individuals who are well-positioned to prevent or detect corruption in the many licensing and contracting processes involved in the oil, gas and mining sector. For example, we believe the list could inform:

- **Government officials who design award processes.** The rules and procedures that govern award processes can help guard against the kinds of problematic behavior described in this report. For example, government officials could strengthen prequalification standards to better guard against underqualified or overly secretive companies. The officials charged with designing the rounds typically work for the petroleum or mining ministries, the industry regulator, or the entity that manages the sectors' licenses, sometimes called a cadaster.
- **Government officials who oversee and approve awards.** These officials, who could represent regulators, ministries, national oil or mining companies or cadasters, could use the list to detect certain behaviors as the award process unfolds, and avoid award decisions that end in controversy or other suboptimal outcomes.
- **Parliamentarians and government oversight actors.** In some countries, parliamentarians have a formal role in approving license awards; in most others, they can call the executive to answer questions about an award as part of their wider oversight powers. Members of anticorruption commissions, national Extractive Industries Transparency Initiative (EITI) multi-stakeholder groups, supreme audit institutions and other government institutions with an oversight mandate could also use the list to help prioritize and inform their monitoring functions.
- **Law enforcement officers.** Domestic or foreign law enforcement officers could use the list to help organize their investigations into a suspect award process, as a source of leads or lines of useful inquiry for them to pursue.
- **Extractive company officials.** As companies evaluate whether to participate in an award process or whether to partner with a certain company, the list can help executives to assess corruption risks—for example, as part of their anticorruption due diligence, risk management or compliance functions.
- **Financial institution staff.** Investors, including companies, banks, IFIs, and private equity firms, also need to gauge the risks of corruption from an award, and decide how and whether to finance a project.
- **Civil society actors and journalists.** NGO staff, campaigners, activists and journalists can use the list to probe the integrity and legality of ongoing or past award processes or individual awards. In particular, the list can help them to identify important lines of inquiry, and to prioritize their scarce resources.

Government officials could strengthen prequalification standards to better guard against underqualified or overly secretive companies.

This list can help executives to assess corruption risks—for example, as part of their anticorruption due diligence, risk management or compliance functions.

THE IMPORTANCE OF CONTEXT

Context is key in interpreting corruption red flags and the risks to which they could point. Corruption is always highly context-specific: it both reflects and shapes particular socio-economic and industry conditions, cultural norms and political economies of decision-making. Many broader factors affect a country's overall

corruption risk profile, such as the absence of transparency, the discretion afforded to government decision-makers, the freedom enjoyed by oversight actors like the media, and the strength of the justice system in detecting and prosecuting corruption. We do not include such underlying factors in our list, though understanding them may often be essential to using the list appropriately.

Extractives sector license and contract awards take place within these larger milieus. The red flags on our list are specific features or outcomes of award processes themselves, not attributes of the wider context. We would also note that different flags may be more likely to be indicative of corruption in different countries, regions, bureaucracies, types of transactions (e.g., an exploration license award versus a commodities trading contract), or types of award processes (e.g., a first-come-first-served mining license award versus a highly competitive oil block bid round).

When a corruption red flag appears, it is the broader context that will tell oversight actors what level of concern and scrutiny is warranted. While we advise that oversight actors ask questions about any red flag they encounter, some may manifest for entirely credible reasons. For example, red flag 11 (in which the agreed terms of the award deviate significantly from industry or market norms) could have many other causes besides corruption. When they spot a red flag, users of the list may want to start by asking such questions as:

When a corruption red flag appears, it is the broader context that will tell oversight actors what level of concern and scrutiny is warranted.

- How strong and/or how many legitimate, non-corruption-related explanations are there for the red flag?
- How close does the conduct involved come to meeting the elements of a corruption-related legal offense (e.g., bribery, conflict of interest)?
- Is the behavior involved unusual for the context?
- Has the behavior involved been a sign of corruption in that context in the past?
- What other factors in the wider context increase or decrease the likelihood that the red flag is pointing to corrupt practices?

Relying exclusively on any non-context-specific list of red flags can lead public and private actors to ignore relevant risk factors or create false impressions of certainty about the integrity of the transaction or award process they are examining. When a user spots a flag, he or she should both "zoom in" to understand more about the specific companies, individuals and processes involved, and "zoom out" to understand the broader institutional, sociopolitical, cultural, economic and industry contexts in which the licensing or contracting decision under scrutiny is made. This will allow the user to make informed judgment calls about whether the behavior is indeed worthy of concern, and what an appropriate response should be.[18] (Note that this report offers no guidance on how particular actors should incorporate the list into their work. For example, it does not say how to build diagnostic frameworks or processes to detect or evaluate red flags, or how to act on them.[19])

There is no foolproof way to detect corruption. We hope this report will serve as a resource, in combination with other tools, to inform the efforts of actors seeking to guard against and uncover costly corruption. This effort is daunting, complex and yet entirely crucial to ensuring that citizens receive full and fair benefits from their country's natural resources.

Twelve red flags

1 The government allows a seemingly unqualified company to compete for, or win an award.

A company that does not have significant technical, operational or financial capabilities either participates in an award process or wins an award. This could raise suspicions because the company is unlikely to be the best choice for effectively executing the contract, and rather was allowed to compete or prevail for some other reason – because it paid an official with influence over the award or has financial ties to a PEP, for instance. In some countries, "local content" rules may lead countries to choose unqualified firms as members of consortiums, ostensibly so that the local company can learn from its more experienced foreign partners.[20] However, in such cases, the other consortium members should have the necessary operational and financial capacities, and the working relationships between them should involve clear modalities for learning by the local partner. In mining more than in oil and gas, governments sometimes award licenses on a non-competitive, first-come-first-serve basis to companies with no real operational capacity in an effort to promote early interest in their sectors.

Specific warning signs

- The company does not meet the government's pre-qualification standards or other guidelines for the selection process, but is still selected.
- The company and/or its principals have no prior relevant work experience. For example, the company puts itself forward as an exploration and production firm but has never undertaken upstream activities before.
- The company and/or its principals have little or no industry reputation or name recognition.
- The company was incorporated or otherwise legally registered only shortly before, or even after, the award. It may appear that the company was set up specifically for the award.[21]
- The company does not have the basic capabilities or assets needed to contribute, including manpower, equipment or technical skills—for example, a purported exploration company with no geologists, engineers or project managers on staff or as consultants.
- The company lacks basic attributes that would allow it to contribute financially, either directly or by accessing outside finance. These could include a balance sheet, audited accounts, a credit rating, cash on hand, or an extended period of financial existence and operations. Additional concerns could arise if the company's finances are thin but it submitted no financial guarantee for the license or contract from a parent company or other entity.
- The company does not show other basic attributes of functioning businesses—for instance, a physical address or office space, staff or a website.

- The company appears to be a pre-existing "shelf company."[22]
- The company's website or other published materials claim relevant experience but do not include many verifiable details, including on past work or names of key personnel.
- The company submits incomplete or false materials about itself as part of the selection process—for example, during the pre-qualification or due diligence phases.
- Other consortium members agree to "carry" the company financially.[23]
- The company's main role relative to the license or contract appears to be to passively receive payments or other things of value, especially for unclear beneficiaries.

Illustrative cases

AIMROC gold mining license controversy. This case presents a strong example of a lucrative license going to a company with apparently weak qualifications but strong political ties. In 2007, the government of Azerbaijan, authorized by a presidential decree, issued a 30-year license for five gold fields to a recently incorporated company named Azerbaijan International Mineral Resources Operating Company (AIMROC).[24] The license gave AIMROC a 70 percent stake in the fields while the Azerbaijani government retained 30 percent.[25] According to a report commissioned by the Azerbaijani parliament, one of the fields held gold and silver worth about USD 2.5 billion in 2011.[26][27] Some parliamentarians complained that none of the four entities that co-owned AIMROC had a track record in the mining sector.[28] The (no longer active) website of the Panamanian entity with the largest stake in AIMROC said that it had "enormous experience in geological investigation, prospecting, and the exploration and processing" but gave few details on specific projects.[29] Journalists found that only one geologist was listed in the records of the four companies.[30] Another one of the four entities was co-owned by three other Panamanian companies that all employed two daughters of President Ilham Aliyev as senior managers according to their corporate filings.[31] Neither of these two women had evident experience in mining. To date, no formal charges, investigations or convictions have occurred. A 2013 local news report claimed that some gold had been produced from one of the fields covered by AIMROC's license, but we could not independently confirm this.[32]

See also 4

OPL 245-Malabu oil block controversy. The Malabu case shows a newly minted firm with no apparent operations or experience receiving a license that could be highly prospective. In April 1998, Nigeria's petroleum minister granted to Malabu Oil and Gas the exclusive rights to explore oil prospecting license (OPL) 245, one of Nigeria's most valuable offshore oil blocks. Malabu had been set up just five days before the award and was unknown at the time. OPL 245 sat idle for 13 years, until the Nigerian government facilitated a transfer of the rights from Malabu to Shell and Eni via a two-step transaction. In the first step, Shell and Eni paid USD 1.3 billion to the government. In the second step, the government agreed to transfer USD 1.1 billion to Malabu. Malabu later transferred most of the funds it received to several shell companies with unclear beneficiaries. The transaction has been under investigation in several jurisdictions.

See also 2 7 12

PDVSA's attempted award to Trenaco. Sometimes a selected company appears so unqualified that other companies active in the sector complain. In 2015, the Venezuelan national oil company Petroleos de Venezuela SA (PDVSA) gave a contract worth up to USD 4.5 billion to a small trucking and trading company, Trenaco. The Switzerland-registered company was to drill as many as 600 wells in the Orinoco Belt, the world's largest crude reserve. The small company started hiring staff and buying equipment months before winning. According to Reuters, the deal reportedly foundered after international oil companies active in the Orinoco Belt wrote protest letters to PDVSA, saying they were concerned about the firm's lack of qualifications and the suspicions of favoritism or corruption that its selection might provoke. Trenaco went into liquidation shortly thereafter.[33] PDVSA ultimately split up the Orinoco tender and awarded parts of it to more experienced oil services companies.[34] The Trenaco controversy broke as U.S. prosecutors investigated other bribery and money laundering allegations against other companies and officials in the Venezuelan oil sector.[35] Former and current PDVSA officials have denied these allegations, arguing they were a U.S.-led effort to damage the government's reputation.[36]

See also
5 8

NNPC sales to oil trading "briefcases." In some sectors, unqualified shell companies are regularly inserted into certain deals as a tool for distributing patronage. For years, Nigeria's national oil company, the Nigerian National Petroleum Corporation (NNPC), sold large portions of the country's crude oil production to unqualified companies, often referred to locally as "briefcase companies." These are small, little-known intermediary firms, typically connected to a political heavyweight, that lack the financial and operational wherewithal to sell oil. Instead they re-sell, or "flip," the oil they receive to larger, more experienced commodities traders, and collect a margin on the sale.[37] A 2012 Nigerian government task force noted that many buyers of NNPC oil "did not demonstrate renowned expertise in the business of crude oil trading" and had "little or no commercial and financial capacity."[38] 2015 NRGI research found that some of the briefcase companies were used to channel payments to Nigerian, and sometimes foreign PEPs.[39] These funds—estimated in 2013 at the higher end of USD 0.25-USD 0.40 per barrel[40]—could potentially have been captured by the Nigerian state. The companies therefore served a corruption or patronage purpose, rather than adding any value to the commercial transaction.

See also
2 11

2 A company or individual with a history of controversy or criminal behavior competes for, or wins, an award.

A company involved in the award process, or an individual with an ownership interest in it, has a reputation for, or a record of participation in, corruption or other misconduct. This could suggest that the company or individual has a propensity to engage in problematic business practices, or that officials treated them with favoritism. Of course, some companies may be wrongly accused by their rivals. The level of scrutiny prompted by this red flag should depend on factors such as the reliability of the evidence or how often the company or individual has been accused.

Specific warning signs

- The company or individual is under suspicion, investigation or indictment for criminal activity, in the country or elsewhere.
- The company or individual has been convicted of criminal activity or violations of other relevant laws, in the country or elsewhere.
- The company or individual has a long record of litigation or other adverse legal activity that suggests unethical business practices.

Illustrative cases

NNPC oil-for-product swaps. In this case, several companies won contracts after they were publicly implicated in an earlier scandal. Starting in 2010, NNPC sold 210,000 barrels per day of Nigeria's crude through oil-for-refined-product swap deals with private trading companies. In 2012, three of the companies that held these contracts were implicated in Nigeria's earlier USD 6.8 billion fuel subsidy scandal. A government committee ultimately cleared two of fraud,[41] though not of other alleged abuses of the subsidy scheme.[42] The third company and some of its principals were charged with nine criminal counts in 2012.[43] Nevertheless, this company continued to do oil trading business for the government under the same contract until late 2014. After the government changed hands, a Nigerian court sentenced two of its principals to prison for subsidy fraud.[44] Earlier, in 2015, Nigeria's anticorruption police opened investigations of some of the swap deals; most of the companies publicly denied wrongdoing.[45] No charges directly related to the swaps have been filed to date, though in 2016 Nigerian anticorruption police declared the managing director of another of the companies wanted on suspicion of "criminal conspiracy, diversion of funds and money laundering" in another oil-related bribery scheme. The executive replied that he was "a law-abiding citizen" and had not failed to honor any summons from the police.[46]

See also 1 11

Naftogaz oil rig procurement scandal. Other awards can involve proxies, or "fronts,"[47] for officials who have reputations for engaging in criminal or otherwise unethical behavior. When a subsidiary of the Ukrainian national oil company (NOC) Naftogaz put out a tender in 2010 to purchase an offshore oil drilling rig, it accepted bids from two companies: U.K.-incorporated Highway Investment Processing LLP and New Zealand's Falcona System Ltd.[48] The award first attracted attention when a local NGO reported that the winner, Highway Investment Processing, had purchased the drilling rig from a

See also 8

Norwegian vendor for USD 248 million—or 38 percent less than the sales price to Ukraine—just days before selling it to the Naftogaz subsidiary.[49] Ukrainian officials attributed the price difference to additional procurement and transport costs, though investigative reporting questioned the validity of these explanations.[50] Media reports later found that both Highway Investment Processing and Falcona Systems' directors and shareholders were part of a network of professional nominees who held their interests through offshore shell companies.[51] Two of the nominees were well known in anticorruption circles as linked to hundreds of shell companies, some of which allegedly played roles in government contract and bank fraud, a U.S.-based Ponzi scheme and embargoed arms sales to African rebel groups, among others.[52]

OPL 245-Malabu oil block controversy. In this case, international oil companies entered into a deal that involved a PEP with serious legal and reputational baggage. In 2011, the Nigerian government transferred the rights to a huge oil block, OPL 245, from a company called Malabu to industry giants Shell and Eni. The former Nigerian Minister of Petroleum and Malabu shareholder Dan Etete was a central player and beneficiary in the deal. Four years earlier, a French court had convicted Etete of money laundering.[53] Some Nigerian press reports claimed that the French government later granted him a pardon, but we have not been able to independently confirm that.[54] The companies moved forward with the deal despite his record and reputation. Both have denied knowing in advance that the Nigerian government would transfer most of the funds they paid for OPL 245 to Malabu, though investigations by the NGO Global Witness and others raised doubts about those claims.[55]

See also 1 7 12

Gécamines and Sodiminco asset sales to Dan Gertler entities. Between 2010 and 2012, the Congolese state-owned mining firms Gécamines and Sodiminco sold parts of their stakes in a number of valuable copper and cobalt projects to little-known offshore companies traceable to Israeli mining entrepreneur Dan Gertler, a friend of DRC President Joseph Kabila since at least the 1990s.[56] Within short periods, many of the companies sold their freshly acquired stakes for large profits to established mining sector operators.[57] The Congolese government continued to award licenses to Gertler companies after Global Witness and others publicly raised concerns about the deals—arguing, for example, that the use of opaque offshore structures could have allowed government officials in the DRC to benefit from the discounted asset sales.[58] Due diligence performed by one of Gertler's business partners found that "several compliance Watch Lists identify [Gertler] as a political [sic] exposed individual as a result of his close ties to the DRC government," and that Gertler was "named in a UN report [and] keeps what can only be described as unsavoury business associates."[59] A 2016 U.S. government investigation into DRC mining deals alleged that companies controlled by Gertler "paid more than one-hundred million U.S. dollars in bribes to DRC officials to obtain special access to and preferential prices for opportunities in the government-controlled mining sector in the DRC" from 2005 to 2015.[60] Gertler has denied findings of this kind.[61]

See also 12

3 A competing or winning company has a shareholder or business relationship with a PEP, or a company in which a PEP has an interest.

Oversight actors and investors should always take a closer look when a government does business with extractives companies that have PEPs as legal shareholders. (Red flag 4 below describes the scenario of a PEP as a hidden owner, i.e., one not listed as a legal shareholder.) They should also scan for related situations that allow PEPs to benefit through more indirect channels. A company might channel payments to the PEP via a third-party business relationship, such as a consultancy or a subcontractor. This situation requires scrutiny, as the third-party business relationship could be a conduit for transferring funds to the PEP—especially if the payments exceed the value of the service provided. In other cases, a PEP, or an entity that he or she owns or controls, is a major creditor of the winning or competing company. At worst, arrangements like these can be vehicles for bribery. (See red flag 6).

Specific warning signs

- The PEP is a shareholder in the company, and thus may be entitled to dividends or some other share of its earnings.
- The company engages a PEP or his/her firm as a consultant or service provider.
- The PEP or his/her company provides the company up for the award with a questionable-looking loan agreement,[62] promissory note or other debt instrument.

Illustrative cases

Trafigura-Cochan fuel import deals. This example from Angola also shows how governments sometimes allocate contracts to companies with PEPs as legal owners, and how those entities then partner with international companies. Starting in 2009, the Angolan NOC Sonangol tapped Swiss trading giant Trafigura to run two large fuel supply deals. The first was an oil-for-refined-products swap arrangement under which Trafigura imported millions of tons of fuel to Angola annually. Under the second, the government hired Trafigura to market billions of dollars in gasoline and other products in Angola.[63] Through networks of shell companies, the Bahamian entity Cochan Ltd. held large stakes in the two Trafigura affiliates that contracted with Sonangol for the deals. Cochan's sole shareholder was a powerful senior aide to the Angolan president.[64] A journalist filed a complaint about the matter with the Angolan attorney general, but no law enforcement action followed.[65] Together, the two deals gave Trafigura and Cochan monopolistic control over the Angolan fuel market with unclear costs to the state—terms and payments of the deals were not disclosed.[66]

Sphynx oil sale consultancy payments. In this case, PEPs owned several companies that also reportedly allocated benefits to additional individuals close to the country's leaders through consultancy contracts. In the early 2000s, the Congolese national oil company selected three companies to buy its oil: Sphynx U.K., Sphynx Bermuda and the local Africa Oil & Gas Corporation (AOGC). NGO investigations found that a senior SNPC official owned large concealed stakes in all three companies.[67] These companies sold the oil on to large international traders that then paid the government. Some evidence suggests the three intermediary companies also lent the Congolese government money at high rates of interest,[68] and distributed oil sale proceeds to politicians. For example, Sphynx Bermuda reportedly paid companies owned by a family member of the president for unknown "consulting services."[69]

See also 4

Kožený SOCAR privatization bribery scheme. In 1998, Czech-born businessman Viktor Kožený, acting for himself and other investors, transferred cash and other assets worth millions of dollars to senior Azerbaijani officials in an effort to influence them to favor his company in a planned privatization of the State Oil Company of the Azerbaijan Republic (SOCAR). Using a Swiss lawyer as a facilitator, Kožený transferred cash and privatization vouchers for the upcoming auction of SOCAR to at least 45 holding companies. He then assigned beneficial ownership of 28 of these entities to the officials.[70] In a 2009 criminal indictment relating to the scheme, U.S. prosecutors alleged that agents of shell companies linked to the officials and Kožený signed three sham loan agreements for USD 100 million each to create a false economic justification and paper trail for the transfer of beneficial ownership in the 28 holding companies.[71] Another businessman involved in the bribery scheme served a ten-month jail term under the FCPA;[72] the Swiss lawyer and a U.S. investment company each paid a USD 500,000 fine.[73] Kožený avoided the U.S. court proceedings.[74] Ultimately, the government of Azerbaijan chose not to privatize SOCAR.

See also 4

4 A competing or winning company shows signs of hidden beneficial ownership by a PEP.

Companies with PEPs as hidden beneficial owners are not uncommon in the extractive industries. Often the participation of a PEP is hidden by a company's ownership structure. Many of the corporate vehicles that can hide beneficial ownership are not illegal per se, but all should prompt close review. Some can serve legitimate legal, accounting or operational goals—or purposes such as tax avoidance that, while questionable, do not mean anything illegal has occurred. But companies with secretive attributes that might help hide the participation of a PEP should receive heightened scrutiny nonetheless, especially whenever including them in the award does not obviously promote any legitimate business or public policy interests. Oversight actors may need to scrutinize all entities in a company's ownership structure, given that PEPs sometimes hold their interests indirectly—e.g., through an offshore subsidiary or holding company structure.

Specific warning signs

- The company's shareholder structure includes a chain or network of shell companies, or a complex holding company[75]substructure, that obscures who ultimately owns or controls the company.
- The company has one or more nominee shareholders.[76] Corporate records may explicitly identify the individual as a nominee, or he/she may exhibit common characteristics of nominees—for instance, being a shareholder or director in many other entities; working for a law firm, corporate services firm or other business that specializes in creating shell companies or managing private wealth.
- Some of the company's shares are bearer shares.[77]
- The company's shareholder structure includes a name that appears to be altered or fabricated. This could be the name of a person or company for which no public records exist; a name that appears to have been deliberately misspelled; a name that no one with relevant knowledge recognizes; a name that otherwise closely resembles some other, identifiable name; or a known or suspected alias, particularly of a PEP.
- The company's shareholder structure includes a significant block of authorized but unissued shares. In some—though certainly not all—cases, this could raise suspicions that the company is holding the block of shares in reserve for a PEP.
- A list of shareholders for the company—whether contained in a corporate filing or some other official document—does not fully account for all of the company's issued shares.
- An individual with familial, personal, political, business or other close financial ties to a PEP is a shareholder, director or officer in the company. Particularly when other red flags are present, this could raise concerns that the individual is a proxy or "front" for the PEP.
- A shareholder with a significant interest in the company has a modest occupation that is unrelated to extractives, and that would not generate sufficient income to buy his/her stake or otherwise contribute financially to the company.

- When contacted, a shareholder is unaware that he or she is an owner of the company, suggesting that his or her identity may have been used without his or her knowledge or permission.
- An entity in the company's shareholder structure is incorporated in a jurisdiction that does not publicly report on shareholders, or does not collect or records shareholder information.[78]
- The company's shareholder structure contains a trust with unknown or unclear beneficiaries.[79]
- The company shares a registered or actual physical address, registered agent, office space, phone number, or other business infrastructure with another firm that is owned or controlled by a PEP, or with an individual linked to a PEP.

Illustrative cases

AIMROC gold mining license controversy. In the AIMROC case, several ownership structures – namely layers of companies and the use of offshore secrecy jurisdictions – made it more difficult to detect the presence of PEPs among the entities that held valuable mining licenses. The Azerbaijan International Mineral Resources Operating Company Ltd (AIMROC) is a joint venture between four firms. One of these, Globex International LLP, was registered in the U.K. and controls 11 percent of AIMROC.[80] Globex was in turn owned by three shell companies in Panama—a secrecy jurisdiction known for lenient taxation and corporate reporting standards.[81] Corporate filings listed two of President Aliyev's daughters as president and treasurer of each.[82]

See also 1

Cobalt oil block bribery case. In this case, several PEPs owned shares in a few small companies that became minority partners on a larger oil deal. In 2010, U.S.-listed firm Cobalt International Energy signed an agreement with the Angolan government to develop two deepwater oil licenses. Cobalt's partners on the deal were the NOC Sonangol and two little-known Angolan upstream firms: Nazaki Oil and Gas and Alper Oil.[83] Angolan regulatory filings listed Nazaki's legal owners as six individuals and a local investment firm, Grupo Aquattro Internacional (GAI).[84] A *Financial Times* journalist noticed that GAI had the same registered address as another small Angolan oil company, Sociedade de Hidrocarbonetos de Angola (SHA). SHA's records listed three top Angolan government officials as its owners: Manuel Helder Vieira Dias Junior (a.k.a. "Kopelipa"), head of the Angolan National Reconstruction Office; General Leopoldino Fragoso do Nascimento (a.k.a. "Dino"), head of telecommunications in the office of the presidency; and Manuel Vicente, then-chairman and CEO of Sonangol.[85] When the *Financial Times* questioned the officials, both Vicente and Vieira Dias admitted that they and General Do Nascimento held interests in Nazaki via the investment firm GAI.[86] Vicente claimed to have been unaware of GAI's investment in Nazaki, and that GAI pulled out of Nazaki when he became aware.[87] The U.S. government began probing Cobalt's acquisition of the blocks for violations of the FCPA in 2011; the case was later closed without public explanation.[88] Cobalt also faced a lawsuit brought by purchasers of Cobalt stock for allegedly misleading them by falsely claiming that it was in compliance with U.S. laws prohibiting bribery of foreign officials.[89] We have seen no evidence of a resolution from that lawsuit. Cobalt attempted unsuccessfully to have it dismissed in 2016.[90]

See also 5 7 11

Sphynx oil sale case. A Congolese official used multiple tools to conceal his interests in three companies that purchased oil from the NOC, including a professional nominee firm and chains of corporate ownership that led to a holding company in a secrecy jurisdiction.[91] A 2005 U.K. court judgment explained, for example, how one of the companies, Sphynx Bermuda, was wholly owned by a British Virgin Islands (BVI) holding company called Lockwood Enterprises Ltd. In corporate filings, Lockwood initially listed a professional nominee firm as its sole shareholder. This firm told Lockwood's Swiss bank that it held shares "in trust" for the official. Later, the official substituted his own name for the nominee firm's in BVI records. According to the U.K. court, the official "intended to and did run the business from abroad, treating Sphynx Bermuda as his company without any reference to the professional directors who were engaged to act as such for Sphynx Bermuda or to the friends he had appointed as directors of Sphynx U.K." The court further found that he held equity in Sphynx via a shell company in a secrecy jurisdiction because "he did not want his connection to be known."[92]

See also 3

Kožený SOCAR privatization bribery scheme. This case shows how trusts can be used by PEPs to hide their ownership. As part of a complex bribery scheme to win equity in the Azerbaijani NOC SOCAR through a planned privatization exercise, an offshore company controlled by Kožený allegedly transferred privatization vouchers it had purchased from the government to forty-five holding companies. The company then assigned beneficial ownership in 28 of these entities to three parent companies, which in turn were owned by four trusts that benefitted PEPs, some of which may have had influence over the auction process.[93]

See also 3

5 An official intervenes in the award process to benefit a particular company.

An official uses his/her formal or informal role in the award process to alter, or attempt to alter, the outcome in favor of a specific company. In some cases, the favored company will not appear to be the most qualified, or it will not offer anything that advances the public interest (see Red flag 1). This raises the suspicion that the official has intervened because he/she or someone in his/her political, social or business networks has an interest in the company, or that the company has paid the official for his/her help. Red flag 9 concerns companies that use fixers or middlemen to gain an advantage in a deal.

Specific warning signs

- An official takes unusual steps to ensure that a company is allowed to compete. For example, he/she might grant the company an exemption from the prequalification process, or insert the company's name on the list of approved bidders.
- An official with influence over the award suggests, recommends or requires that the company partner with another company to apply for the license or contract, effectively creating a "forced marriage." This can particularly be of concern when the company imposed by the official is inexperienced and non-contributory, or has apparent political connections. The forced marriage can take the form of a joint venture or partnership, or a subcontracting or third-party service provider relationship.
- An official gives a winning or competing company preferential access to confidential information—e.g., geological data—to use in crafting its bid.
- A company is granted a license or contract that it did not bid for, or allowed to swap the license or contract it won for another.
- An official with final or high-level decision-making authority overrides the outcome of the award process, or otherwise alters the decision of the officials originally charged with selecting the winners.
- The winning or highest-ranked bid is not accepted.
- The conduct of the award process departs from the government's established rules, standards or criteria, and/or exhibits a high or unusual degree of discretion and/or secrecy. This is very common in some countries, but nonetheless creates conditions amenable to influence-peddling, self-dealing, patronage and other abuses of discretion.

Case studies

Cobalt oil block bribery case. Cobalt offers an example of a forced marriage, purportedly in the interests of promoting "local content." In 2011, Cobalt International disclosed that "the Angolan government [. . .] assigned" the local companies Nazaki Oil and Gas and Alper Oil to be its local minority partners in developing two deepwater oil blocks.[94] Global Witness found that at the time of the award, both Nazaki and Alper "were obscure

See also
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companies with no visible industry track record."[95] Cobalt claimed, "We had not worked with either of these companies in the past, and, therefore, our familiarity with these companies is limited."[96] It also stressed that its due diligence around the deal did not uncover any evidence that government officials were behind their local partners.[97] But two top Angolan officials later disclosed to the *Financial Times* that they and another official each owned one-third of Nazaki via an investment firm.[98]

Starcrest oil block award scandal. In this case, decisions made after bidding closed led to a well-connected company receiving a license on favorable terms. After Nigeria's 2006 oil block licensing round closed, regulators allowed the Seychelles-registered firm Starcrest Energy International to swap the block it had won for another. The awards came at a politically charged time in Nigeria, as the president sought support—and by some accounts, funding—for his bid to amend the Nigerian constitution to allow him to run for a third term in office.[99] A government due diligence report, Chatham House and the *Financial Times* respectively described the Starcrest's principal, Emeka Offor, as a "known confidante and campaign supporter" of Obasanjo,[100] "a key financier of the ruling party [in Nigeria]"[101] and "a company . . . which industry sources say has strong political connections."[102] The regulators reportedly only started negotiating Starcrest's license swap after another firm in which President Obasanjo had an ownership stake showed interest in OPL 291 but did not finally acquire it.[103] The deal turned out to be highly lucrative for Starcrest: within months, it sold a 72.5 percent participating interest in the block to Addax Oil and Gas Limited for USD 35 million and a USD 55 million signing bonus.[104] It was Addax's announcement of this transaction that first drew public scrutiny to the deal, and three Nigerian government investigations followed. None found clear evidence of wrongdoing, though at least two may have been closed prematurely.[105] Lawyers for Emeka Offor later told Global Witness that "President Obasanjo, though a good friend of our client, never influenced (nor did any Nigerian government official), the award of [the block] to Starcrest."[106]

See also 8

PDVSA oil equipment contract bribery case. Bribery can motivate officials to intervene on behalf of certain companies. Between at least 2009 and 2014, two U.S.-based businessmen bribed officials at Venezuela's NOC PDVSA in exchange for favorable treatment in the awards of USD 1 billion in oil equipment supply contracts for their companies.[107] According to the indictment, the officials—all of whom were mid-level procurement staff at the NOC—agreed to provide the businessmen with inside information about PDVSA's bidding processes, ensure that companies owned by the two men featured on approved bidder lists for tenders, and "support" the companies' bids before internal purchasing committees. The businessmen allegedly made USD 790,000 in bribe payments to U.S. and Panamanian accounts linked to the officials, their family members and associates. They also covered the officials' travel, meal and entertainment costs, and paid off one's mortgage.[108] The two businessmen, together with an associate and three of the PDVSA officials, pled guilty to various FCPA- and money laundering-related offenses in 2016.[109] In early 2017, the U.S. justice department reported that its PDVSA bribery investigation is ongoing but did not announce new charges.[110]

See also 1 8

Petrogate bribery scandal. In this case, a company used an intermediary (see red flag 9) to allegedly bribe officials to intervene on its behalf. The "Petrogate" scandal first came to light in 2008, when a Peruvian TV station broadcast tapes of a board member at state-owned PetroPeru S.A. and a lobbyist discussing payments in exchange for the board member helping Discover Petroleum International AS (DPI) and PetroPeru S.A. win oil exploration and exploitation contracts that were up for tender.[111] DPI prevailed in the tender.[112] An official investigation subsequently found that PetroPeru officials changed the public tender requirements to favor DPI, and also qualified the company for the public tender before it even applied to participate. The PetroPeru board member and lobbyist denied wrongdoing.[113] The Petrogate tapes were widely covered in Peru, not least because they possibly implicated other high-ranking government officials besides the PetroPeru board member.[114] Several top officials resigned from office in the wake of the scandal, including the board member, the country's prime minister, minister of energy, and president of PetroPeru.[115] The government suspended the contracts with DPI.[116] In a statement, the company denied having paid bribes to Peruvian officials, though it admitted to paying the lobbyist and hiring "advisory services" from the board member, then a siting government official.[117] A prosecutor filed charges against the lobbyist and the board member in 2014, but no convictions have been secured.[118] The board member was released after spending six years in jail, on grounds that the statute of limitations in his case had run out.[119]

See also
9

6 A company provides payments, gifts or favors to a PEP with influence over the selection process.

A company pays an official or PEP to manipulate or direct the outcome of the selection process so that the company will receive some preferential treatment. In the most obvious cases, the official is the final decision-maker.[120] Often, however, he or she will have other, less direct powers to influence the outcome.[121] The "payment" can take many forms, and need not be strictly cash-based.[122] The payment also can take place either before or after the award.[123] This red flag relates closely to the previous one: here a suspicious payment is the red flag, and in red flag 5 it was a suspect intervention by an official. In reality, the distinction can be quite blurry.

Illustrative cases

Rubiandini bribery conviction. In this case, the official running the selection process received payments that were spotted by authorities. In 2013, Rudi Rubiandini, the chair of Indonesia's oil and gas regulator SKK Migas, awarded rights to the company Fossus Energy to buy oil from the government. Indonesian anticorruption police arrested him shortly thereafter, on allegations that Fossus Energy paid him an approximate USD 1.1 million bribe in exchange for the rights. He reportedly received the money via a middleman (his golf trainer) and the manager of Kernel Oil, a sister company of Fossus Energy.[124] Following a high-profile trial, an Indonesian court sentenced the Kernel Oil manager and Rubiandini to prison for bribery.[125] Rubiandini testified that the kickbacks were needed to meet demands from parliamentarians for "holiday bonuses," though lawmakers have denied the allegation.[126]

Steinmetz-Simandou bribery case. Some companies choose to influence individuals with close personal ties to the decision-maker. In 2008—two weeks before Guinea's then-head of state Lansana Conté died—the Guinean Ministry of Mines awarded Beny Steinmetz Group Resources (BSGR) exploration permits for two of the country's highly prospective iron ore concessions.[127] After U.S. prosecutors began probing the deal, written agreements between BSGR and Conté's widow Mamadie Touré surfaced in which the company promised Touré at least USD 5 million and a job for her brother in exchange for her help lobbying Conté and other officials on its behalf.[128] Touré, who cooperated with the U.S. investigation, stated that BSGR also offered her millions of dollars, jewelry, two Toyota Land Cruisers and a five percent stake in the Simandou project if she assisted BSGR with the award.[129] Investigations into the alleged bribery are ongoing in Israel, the U.S. and Switzerland.[130] Neither BSGR nor Steinmetz have been charged in any of the investigations, though the Israeli government detained Steinmetz briefly in 2016; both have denied the underlying allegations of corruption in public statements.[131] A former agent for BSGR in Guinea, Frederic Cilins, was jailed for two years in 2014 for obstructing the U.S. investigation.[132]

See also 12

Oranto Petroleum alleged payments for contract approval. At times companies make payments to officials who must merely sign off on awards, rather than those charged with making the selection. In 2005, Oranto Petroleum Limited and Broadway Consolidated PLC—later renamed Peppercoast Petroleum PLC—entered into negotiations with the National Oil Company of Liberia (NOCAL) to acquire a number of offshore blocks. However, after a tentative deal was reached, final approval of the agreements stalled in the parliament. According to a report by Liberia's General Auditing Commission and an investigation by the country's anticorruption police, members of the parliament would not approve the production sharing agreements until they received bribes.[133] In 2006 to 2007, NOCAL made four payments totaling USD 118,400 to representatives of the Liberian legislature, allegedly for the purpose of speeding the contract review process.[134] NOCAL did not have the required funds itself, so it obtained some of them as a loan from the state-owned Liberia Petroleum Refining Corporation. The Liberian auditor and Global Witness found evidence that Oranto agreed to provide NOCAL with cash for at least two of the payments; there were no signs that Broadway contributed.[135] NOCAL noted the payments on its books as "lobbying fees"—which raised the red flag causing the auditor to investigate.[136] It is not clear in all cases who the ultimate recipients of the payments were, nor how much influence they had over the contract approvals. At least USD 40,000 was paid to directly to a member of the Liberian House of Representatives; USD 1,500 went to the House's chief clerk.[137] Both men acknowledged receiving the payments. The head of NOCAL argued that the transfers were legitimate and meant to pay for computers, stationery, and other office supplies that the cash-strapped legislators needed.[138] Oranto ultimately signed contracts for three blocks; Broadway signed one.[139]

Petrobras "Operation Car Wash" bribery case. The case of Brazilian NOC Petrobras shows how officials with decision-making power over awards can simultaneously receive illicit payments themselves and help channel money to other PEPs. Beginning in 2014, allegations surfaced in the media that Petrobras officials and a cartel of companies had colluded in a massive, anti-competitive bribery and money laundering scheme, code-named "Operation Car Wash."[140] The payments involved served as key warning signs in this case, attracting the attention of Brazilian law enforcement. According to evidence compiled by U.S. prosecutors, over a period of years a group of Petrobras directors colluded with a "cartel" of at least 16 companies in multi-billion-dollar bribery and money laundering schemes. Petrobras awarded contracts to these companies, often inflating their value. Typically three percent of the contract value was shared. The excess funds were shared among the Petrobras officials, leaders of Brazil's leading political parties, and the participating companies. "Godfathers" from political parties also allegedly nominated several Petrobras directors, so as to have loyal decision-makers on the inside.[141] Once in office, the directors periodically met with cartel members to agree which companies would receive which contracts, and the details of the kickbacks required. They then split the kickbacks with party officials and private facilitators based on agreed formulas.[142] One former director testified that "this *quid pro quo* applied to all executive-level positions that were part of the patronage system and included diverting funds and resources from works and contracts falling under the control of the [responsible director]."[143]

See also 8

Several jurisdictions are still actively prosecuting, litigating and investigating the Petrobras case. Brazilian law enforcement has already questioned dozens of powerful politicians in the matter, including the speakers of both houses of parliament and at least 50 other sitting politicians.[144] By May 2015, 97 individuals had been indicted, and dozens more have followed. Brazilian prosecutors obtained at least 16 convictions by mid-2016, including several senior Petrobras executives, legislators, political party officials and company executives. Dozens of other cases are ongoing, along with investigations in the U.S. and Switzerland. Some, though not all, of the individuals implicated have denied culpability.[145] The full costs to the Brazilian government of the collusion scheme are not known, but authorities have estimated that it may be as high as USD 28 billion.[146]

7 An official with influence over the selection process has a conflict of interest.

A conflict of interest arises in an award process when an official has multiple roles or stakes in the process, and this fact potentially creates tension between the official's self-interest and his/her official responsibilities. This occurs either when the award could affect the extractives sector business interests of the official or his/her family member or associates, or when allowing the official to play multiple roles in the award process could weaken built-in checks and balances. The presence of a conflict is not a sure sign of corruption. Rather, it heightens the risks that the official could use his/her entrusted power in ways that undermine the award's integrity, fairness or potential returns to the state.

Specific warning signs

- An official involved in selecting the winner, or a close associate, holds a commercial interest in the sector in which the award is being made.
- The official or a close associate is a director, officer or owner of a company that is competing for the award.
- The official or a close associate consults for, provides services to, or otherwise does business with a company that is competing for the award.
- The official makes or influences decisions at multiple points in the selection process, either by occupying more than one decision-making role or by holding positions in more than one of the official bodies involved.
- An official at a state-owned company that seeks commercial opportunities in the sector also has influence over the award of such opportunities. Research suggests that corruption risks rise when state-owned companies have contract-awarding authority as well as acting as commercial players in the sector.[147]
- The official in situations such as those described above does not disclose the potential conflict of interest.
- An official in situations such as those described above does not recuse himself/herself from the selection process.

Illustrative cases

OPL 245-Malabu oil block controversy. In 1998 Dan Etete, then Nigeria's minister of petroleum resources, sold the rights to oil prospecting license 245 to Malabu Oil and Gas. At the time, Etete held at least 30 percent of Malabu's shares himself, under an alias.[148] An official should not be in the position to award a license or contract to a company that he/she owns; this is a very clear and problematic conflict of interest.

See also 1 2 12

See also
4 5 11

Cobalt oil block bribery case. In 2010, Manuel Vicente was the head of Angolan NOC Sonangol, and also was the beneficial owner of Nazaki Oil and Gas, a local company that was a member of the consortium that received the rights to two offshore oil blocks. The extent of Vicente's influence over the award is not clear from available information. However, he was widely seen as the most powerful decision-maker in the oil sector apart from the president, while also holding business interests in that same sector.[149]

C&K Mining shareholder issues. In 2006, Cameroon's president awarded C&K Mining Cameroon a diamond exploitation permit.[150] At the time, C&K was a joint venture between Cameroonian, Chinese and South Korean investors.[151] According to Cameroon's 2012 EITI report, C&K Mining Cameroon had six shareholders.[152] Corporate filings identified the wife of the country's minister of mines as a "representative" of one of the six.[153] Therefore, the minister had a conflict of interest because he had the opportunity to award business to a company apparently linked to one of his family members. Investigative journalism found no signs that the company made significant investments towards developing the concession area.[154]

OECD case studies. State-owned companies can create conflict of interest scenarios, as they often play both regulatory and commercial roles in the sector. In a 2016 report on corruption in extractives sector award processes, the OECD reported a case in which "a public officer was holding a position both in the operating state-owned enterprise and in the overseeing body in charge of approving extractive projects." The report also noted an instance in which the "president of a state-owned enterprise advised private companies with business activities with the state-owned enterprise and billed them for the services provided through third parties." A third case showed the "involvement in the decision-making process of high-level politicians who had previously provided consultancy services to the same companies."[155]

8 Competition is deliberately constrained in the award process.

Company executives,[156] government officials, or a mix of both collude to limit the number of companies given fair, equal opportunity to compete for a license or contract.[157] This practice should attract scrutiny particularly when it appears to favor private interests over the public interest. Governments can have good reasons for awarding extractives licenses or contracts on a non-competitive basis—for instance, the underlying assets may have high geological risk or low market interest. Many mining concessions in unexplored areas are, for example, awarded on a first-come-first-served basis. Concerns arise more when the government has committed to running competitive awards but then deviates from that promise. The warning signs listed below reflect many of the observations made by anticorruption studies of wider government procurement processes, which can provide further detail on these risks.[158]

Specific warning signs

- The government gives one or more companies rights of first refusal over a license or contract without any apparent strong commercial or public policy justification.
- Multiple companies linked to a single individual or parent company submit bids for a single license or contract.
- One or more linked companies submit bids that appear intentionally defective or uncompetitive.
- The window for bidding is unreasonably short.
- The winning company provides benefits to a losing bidder after the award takes place—e.g., makes payments to the loser or hires it as a subcontractor or other service provider—suggesting that the two companies may have colluded to favor the winner.
- Two or more competing companies win licenses or contracts in a repetitive, predictable order, suggesting they are colluding in the common anti-competitive scheme known as "bid rotation."[159]
- The government accepts a bid from a company with terms that do not favor the company, then subsequently renegotiates more favorable terms—suggesting the company and an official could have engaged in "low-balling."[160]
- The government sets aside bidders or bids that appear legitimate, for unclear reasons.
- The government awards the license or contract on a single source basis when a competition would be more typical or appropriate.

Case studies

Naftogaz oil rig procurement scandal. In this case, multiple companies bid for a contract, but turned out to be closely linked. When a subsidiary of the Ukrainian NOC Naftogaz put out a tender in 2010 to purchase an offshore oil drilling rig, it accepted bids from only two firms. The winner, a relatively unknown U.K.-registered entity named Highway Investment Processing LLP, offered a rig for USD 400 million—USD 10 million less than the other bidder, New Zealand's Falcona Systems Ltd.[161] The award first attracted attention when a local NGO noticed that Highway Investment Processing had purchased the drilling rig from a Norwegian vendor for USD 248 million—or 38 percent less than the offered price to government—just days before selling it to the Naftogaz subsidiary.[162] Media later found that both companies were represented on paper by a single network of Latvian nominee directors and shareholders who held their interests through offshore shell companies.[163]

See also 2

PDVSA oil equipment contract bribery case. In this case, two U.S.-based businessmen pled guilty in 2016 to paying up to USD 820,000 in bribes to restrict competition for high-value PDVSA contracts. U.S. prosecutors alleged that the two men made the payments to PDVSA officials in part so they could "propos[e] bidding panel lists that contained more than one company owned by [them] to create the false impression that the bidding process was competitive."[164] Thereafter, the businessmen would tell the officials, who sat on the bidding panels, which of the companies to select. They also concealed their overlapping stakes in multiple companies by assigning the companies nominee owners and managers.[165]

See also 1 5

Petrobras "Operation Car Wash" case. Anti-competitive behavior formed an integral part of the Petrobras scandal. According to extensive evidence uncovered by Brazilian prosecutors and police (summarized in U.S. court documents), executives at Petrobras awarded a range of valuable service contracts to cartel members in which project costs were inflated by as much as 20 percent.[166] Cartel members and Petrobras officials—often directors nominated by political party heads—allegedly met regularly to choose which firms would receive which contracts. After the awards happened, the winners, via intermediaries, allegedly would pay up to three percent of the contract's total value as kickbacks to Petrobras executives, Brazilian politicians and other parties, including the scheme's facilitators.[167]

See also 6

Nigerian 2006 oil block awards. This case illustrates well how officials initially set up a competitive process, but later constrained it in order to advance their narrow, short-term political goals. The bid round came at a politically charged time in Nigeria, as the then-president canvassed support—and by some accounts funding—from bid round winners,[168] for his (unsuccessful) bid to amend the Nigerian constitution to allow him a third term in office.[169] Only invited companies—most of them Asian firms picked by the president or his main petroleum aide—were allowed to compete; some received rights of first refusal on certain blocks, if they made often-unrealistic promises to build infrastructure that largely did not materialize.[170] Companies linked to the same well-connected individual won equity in three licenses.[171] A later parliamentary probe found other red flags. Officials awarded several blocks without requisite approvals. They awarded other blocks, after the round closed, to companies that did not submit timely offers for them. One block was awarded despite being actively held by a state-owned company under unclear circumstances.[172] The parliamentary probe concluded that, "regardless of its pretensions, [the 2006 bid round] was a purely discretionary award of oil blocks to whomsoever the operators of the bid round desired."[173]

See also
5

9 A company uses a third-party intermediary to gain an advantage in the award.

A competing or winning company hires a third-party entity or individual to act as an intermediary between the company and influential government officials.[174] In some cases, the company makes payments to the intermediary which are then forwarded to the PEP, either in the form of money or gifts.[175] The payment to the PEP can be for purposes of influencing the award itself, or serving broader patronage goals. In other cases, the intermediary uses connections to provide the company with access to key officials. The corruption is less clear in this situation, but such arrangements require scrutiny as this type of preferential access can facilitate bribery or other quid pro quo negotiations, or otherwise provide the company with an unfair advantage in the award process.

Specific warning signs

- The intermediary or hired by a competing company has political, social, familial or business ties to an official.
- An official or government body recommends or requires the company to retain the intermediary.
- The contract between the company and intermediary describes the services the intermediary must perform in vague, non-descriptive terms.
- The contract between the company and intermediary calls for the intermediary to perform a long laundry list of services for which the intermediary lacks capacity or resources.
- The intermediary or service provider requests unusually high commissions or fees.[176]
- The intermediary helps the company arrange meetings with high level officials, or other types of access that other companies competing for the award do not receive.
- The intermediary appears to perform little if any substantive work.
- The intermediary or service provider requests unusual, or unusually complex, payment patterns, including payments in cash, into offshore accounts or accounts in different names or countries.
- The intermediary creates documentation saying it performed services under the contract that it has not performed—e.g., false invoices or reports.
- The winning or competing company creates a false paper trail showing payments to non-existent companies, suggesting the paper trail has been used to conceal payments to a PEP.

Illustrative cases

Statoil Rafasanjani bribery case. The Statoil Iran case is a relatively straightforward example of a corrupt intermediary at work. In 2003, a Norwegian newspaper—using information from company whistleblowers—published a series of articles alleging that Statoil had signed a suspect consulting contract the prior year with a U.K. entity named Horton Investment.[177] Horton's beneficial owner—represented on paper by a proxy shareholder—was Mehdi Hashemi Rafsanjani, a director at a subsidiary of Iran's national oil company and a son of a former Iranian president.[178] Under the agreement, Horton promised to assist Statoil in its bid to acquire contracts to develop parts of Iran's highly prospective South Pars gas field in exchange for several million dollars in payments.[179] According to U.S. court filings, Rafsanjani delivered messages from Statoil to Iran's then-oil minister. He also allegedly provided Statoil employees with non-public information and copies of bid documents from competing companies.[180] Both the Norwegian and Statoil investigations concluded that Rafasanjani did not influence the Iranian decision making process.[181] Nonetheless, U.S. prosecutors found that Statoil paid Horton at least USD 5.2 million, most of it after Statoil and the Iranian government signed a contract for three phases of the South Pars project.[182] Statoil canceled the South Pars contract after the newspaper stories emerged; three of its top executives resigned.[183] In 2004, Norwegian prosecutors fined the company USD 3.5 million for violating prohibitions on trading in influence.[184] Statoil reached a settlement with the U.S. Department of Justice two years later, agreeing to a USD 10.5 million fine for violating the Foreign Corrupt Practices Act.[185] The U.S. SEC assessed a second USD 10.5 million fine.[186]

Griffiths oil block facilitator case. Some intermediaries seem to do little for their payments beyond opening doors. In 2008, two executives at Griffiths Energy began cultivating a relationship with Chad's then-ambassador to the U.S. and Canada in hopes that he would use his influence to help Griffiths gain access to oil exploration licenses in southern Chad.[187] In early 2009, Griffiths offered to pay the ambassador a USD 2 million fee for "advisory, logistics, operational and other assistance."[188] Shortly thereafter, the ambassador facilitated a meeting in Washington, DC to discuss possible license awards between a former Canadian prime minister, the Chadian president and oil minister, and Griffiths executives.[189] Once Griffiths signed an memorandum of understanding and production-sharing contract with the government of Chad, a U.S.-based law firm, acting on Griffiths' behalf, paid the promised USD 2 million to a Nevada-registered entity owned by the ambassador's wife.[190] Griffiths also sold four million of its shares to associates of the ambassador at steeply discounted prices.[191] When new management at Griffiths later discovered the transfers during due diligence for an initial public offering in 2011, they self-reported them to Canadian and U.S. authorities.[192] In 2013, Canada's PPSC found Griffiths guilty of one count under the country's Corruption of Foreign Public Officials Act and levied a USD 10.35 million fine.[193] The U.S. Department of Justice filed a USD 34 million civil forfeiture claim in 2015, equivalent to the cash value of the four million shares.[194]

Unaoil bribery scandal. Sometimes companies use multiple layers of fixers to influence top-level officials. According to documents from the 2016 Unaoil leak, Monaco-based Unaoil—itself an intermediary—paid a well-connected Iraqi national tens of millions of dollars in "commissions" between at least 2009 and 2011 to help win Iraqi oil services contracts for U.S., European and Australian firms. In particular, the documents showed the Iraqi national discussing plans with Unaoil executives to deliver large bribes for the companies to two successive oil ministers, whom Unaoil referred to by the codenames "Teacher" and "M."[195] Unaoil's clients did win several of the contracts they sought, though the leaked emails do not definitively show that payments reached Iraqi officials. In addition to the Iraqi national mentioned above, Unaoil paid retainers to at least two other senior Iraqi oil officials who promised to help its clients win bids.[196] The documents also suggest that Iraqi officials passed non-public tender information to Unaoil clients and interfered in government negotiations on their behalf.[197] Asked about the allegations, the Iraqi national claimed that he never worked for Unaoil and did not know the two ministers.[198] Unaoil and one of the ministers publicly claimed innocence.[199] Several of Unaoil's implicated clients have also denied knowledge of its alleged actions on their behalf.[200] U.S., U.K. and Australian police opened probes of Unaoil's operations in mid-2016.[201]

10 A payment made by the winning company is diverted away from the appropriate government account.

Governments often require that companies make certain payments to take part in a selection process, or to finalize an award once they are chosen as the winner. A red flag arises when a company makes one such payment, but then some or all of the funds are re-routed outside of government coffers. In some cases, the company pays funds directly into a non-government account that is owned or controlled by a PEP, or a PEP's associate. At other times, the company will make the payment into a government-owned account, but then officials will transfer some or all of the funds to a PEP or his/her associates. In these latter cases, the government body itself effectively acts as an intermediary, or conduit for handing over public wealth to a PEP. Signature bonus payments may be especially vulnerable to diversion.[202]

Specific warning signs

- The government agency in charge of collecting payments issues unclear, confusing or unusual payment instructions.
- A single payment is broken into pieces and wired to multiple accounts.
- Payments from the selection process are transferred to, or collected in, a large number of different accounts.
- A company makes a single payment in multiple forms—for example, the company wires a portion and pays the balance by physically delivering cash.
- Some or all of a payment that a company makes does not appear on the financial reports of the government body in charge of collecting the payments.
- The government does not use the funds it receives from the company for their intended or required purpose—for instance, as stated in law, regulations or policy.
- The government does not report details about payments made—for example, size, reasons, recipients, bank account inflows and outflows.
- The award is structured so that payments from the company flow from into government accounts and then quickly out to private accounts.

Case studies

Marathon signature bonus controversy. Media reports suggest that signature bonuses in this case eventually found their way into private pockets. In July 2000, Marathon Oil Company sent one-third (or approximately USD 13.7 million) of a signature bonus it had agreed with the Angolan government to an account in Jersey owned by the NOC Sonangol. Shortly thereafter, according to official documents reviewed by investigative journalists, Sonangol transferred portions of the funds from its Jersey accounts to a private security company owned by a former Angolan minister and a charitable foundation run by the Angolan president. The NOC did not explain the reasons for the transfers.[203]

Global Witness allegations about CNPA signature bonuses. Sometimes confusion around the amount and destination of payments leads to suspicion and corruption inquiries. Global

Witness in 2009 published a report noting that several international oil companies paid multi-million dollar bonuses to the Cambodian National Petroleum Authority (CNPA) in exchange for prospecting rights. Investigations by the NGO found that the amounts supposedly paid were not recorded in relevant government financial reports. It was not clear that all of the bonus payments were legally required or authorized. Generally, neither the CNPA nor the winning companies disclosed payment amounts, recipients and accounts, or otherwise explained what happened to the bonuses. None of the parties responded to Global Witness's requests for further information.[204]

Oil-for-food scandal. In this case, the diversion of payments developed into a large-scale and systematic practice. Between 1996 and 2003, certain oil traders that won rights to buy Iraq's crude oil through the United Nations-monitored Iraq Oil-for-Food Program (OFFP) negotiated secret side payments to the Iraqi government. Actors involved in the scheme used shell companies, disguised corporate ownership, and offshore banking services to facilitate the payments. This system of kickbacks generated over USD 1.8 billion for the Saddam Hussein regime.[205] The payments eventually led to at least six formal investigations. Most of the resulting law enforcement action, for bribery and related financial offenses, took place in the U.S. The investigations found serious gaps in United Nations oversight of the OFFP. For instance, one firm, the Africa Middle East Petroleum Company, admitted to wiring USD 160,000 to the personal account of an OFFP director in exchange for contracts—a claim the director denied.[206] The probes also found that the Hussein government spent much of the kickbacks it received on extravagant palaces and weapons, including a missile program that exceeded limits imposed by the UN Security Council.[207]

Turkmenistan gas sales foreign accounts controversy. In highly autocratic political systems, where one or a few officials have sole control over public revenues, the bulk of payments from extractives awards can be diverted outside of normal public financial management systems. Beginning in the 1990s, the government of Turkmenistan received and kept nearly all of its earnings from its oil and gas exports in foreign accounts, many of them with Deutsche Bank. The government published no information about the accounts' balances, management or outflows. However, investigations found that these funds fed 75 percent of government spending, much of it on an off-budget basis. In 2006 Global Witness estimated that the foreign accounts together contained roughly USD 3 billion.[208] Bafin, Germany's financial supervisory authority, investigated the matter and concluded there was no reason to believe that Deutsche Bank itself had broken international rules.[209] Turkmenistan's then-"president for life" Saparmurat Niyazov reportedly maintained effective control over the accounts. His government spent large sums of oil and gas sale revenues on national prestige projects that were of little use to the general public and reinforced the president's "personality cult."[210] These included an opulent presidential palace and a golden statue of the president that rotated so that it always faced the sun. Maintaining sole, secretive and discretionary control over the accounts, and the petroleum sale revenues they contained, helped the Niyazov regime, widely seen as one of the world's most authoritarian and repressive, to consolidate power.[211]

11 The agreed terms of the award deviate significantly from industry or market norms.

If the terms of licenses or contracts depart significantly from expectations, past examples or industry norms, this may warrant extra scrutiny from oversight actors. There is no global rule for how much deviation is too much; only close scrutiny of the underlying industry and country context can support informed judgment calls in that regard. Judging whether a country received fair value for an award is rarely easy. Most deals—especially the larger, more valuable ones—are products of negotiation. Corruption is by no means the only possible reason why final terms may favor the winning company more than the government. For example, officials might not have done a good job managing the award process. They may have set terms too low or negotiated poorly, based on limited experience, information or negotiating power. Or, for similar reasons, they may have set their initial expectations too high, or prioritized short term gains over longer term returns. External shifts in the market also can force officials to take less attractive deals or offer companies investment incentives with high costs to government. Corruption risks related to this red flag are higher when none of the above reasons are evident, and when other red flags are present—for example, if an unqualified company with signs of hidden PEP ownership won a contract with highly preferential terms.

Specific warning signs

- The winner's bid is substantially higher or lower than government's own assessed value for the license or contract up for grabs, or it deviates widely from the bids made by other companies. Suspicions may be stronger whether the government's value assessment appears realistic and based on sound technical analysis rather than simply an opening position in negotiation.
- The final award shows significant deviations from existing law or regulation, or from the model contract, term sheet or other roster of terms used during the selection process. This is potentially problematic particularly if the proposed terms appear reasonable.
- The terms of the final award are significantly more favorable to the company than those that it and the government initially agreed.
- One or more terms of the license or contract are changed only shortly before signing, in a manner that favors the company.
- The terms of the award are significantly more favorable to the company than those from other, similar deals signed by the government—yet market conditions have not significantly changed.
- The responsible government agency makes no effort to assess the value of the license or contract it is awarding.
- The final terms include prices that are substantially lower or higher than market price—e.g., a contract that allows a company to buy hydrocarbons from the government at steep discounts, or sell them to the government for premiums not otherwise obtainable in the market.

- The final terms include other non-standard provisions that reduce the winner's obligations or make the deal more valuable to the winner. These could include excessive tax holidays, unclear or skewed currency conversion formulas or rates; unusually long payment windows; or concessionary credit lines, debt guarantees, or other non-standard financial support from the government to the winner, either as terms of the sale or in side deals with the winner.

Illustrative cases

Skanska case. Often a red flag of this type concerns the cost of a good that has been procured by a government entity. In 2004, the Argentine Ministry of Planning opened a bidding process for the construction of two natural gas pipelines and compressor stations. The bidding process was managed by a private company, Transportadora Gas del Norte (TGN).[212] Skanska's initial bid for the projects was ARS 26.3 million, far above TGN's estimated cost estimate for the project.[213] A higher contract value would have made the project significantly more expensive for the government. TGN informed ENARGAS, Argentina's regulatory agency for the gas sector, that Skanska's bid was significantly above TGN's reference price and asked for guidance, but ENARGAS approved the cost increase and Skanska was awarded the contract. After construction began, a judicial investigation found Skanska had received and paid 118 fake invoices to at least 23 fictitious companies. Money reportedly went to bribe officials and assist the construction firm in evading taxes. A Skanska internal investigation found that roughly USD 4 million was spent on "improper payments" to unidentified third parties.[214] Individuals suspected of accepting bribes have not been publicly identified, but several officials did face charges of fraud, unfaithful public management and bribery for choosing the more expensive Skanska bid.[215] In 2011, however, an Argentinean federal court discontinued the trial for lack of evidence that the contract was overpriced.[216]

NNPC oil for product swaps. 2015 research by NRGI found that some of Nigeria's oil-for-refined-product swap contracts contained unbalanced or inadequately defined terms that allowed the traders to profit at the government's expense. NRGI estimated that losses from three technical provisions in a single "offshore processing" contract could have reached USD 381 million in one year (or USD 16.09 per barrel of oil sold).[217] Some of the unbalanced provisions dealt with the measures used to convert volumes of crude into volumes of refined products. Another gave the company an excessive allowance for the value of oil lost during the refining process. The contracts were awarded at a time of strong competition for Nigeria's oil trading business, and other companies proved willing to sign contracts with much less profitable terms. After a change in government, NNPC canceled three such contracts in mid-2015, stating that they were "skewed in favor of the companies such that the value of product delivered is significantly lower than the equivalent crude oil allocated."[218]

See also
1 2

Gazprom use of intermediaries. Other deals offer benefits to certain companies, but may not be commercially necessary at all. Majority state-owned Gazprom contracted with politically connected firms to transport natural gas through its own pipelines. These companies appeared to benefit greatly from the deals, sometimes at the Russian state's expense. Gazprom has provided some of them with large loans, debt guarantees and other financial support—USD 880 million to one firm in a single year.[219] Analysis by the firm Hermitage, based on Russian Audit Chamber data, found that the Russian state-owned company lost an estimated USD 5.5 billion in pre-tax profit from a 2002 deal.[220] One of the intermediaries, OstChem, reportedly made more than USD 3.7 billion over two years.[221] The large profits drew the attention of NGOs, journalists and law enforcement who asked questions about the purpose and necessity of these deals.

Cobalt oil block bribery case. In some cases, payments made by a company may appear small when compared to similar payments made under similar market conditions. When the Angolan government awarded offshore blocks 9 and 21 to Cobalt Energy and its local partners in 2010 on a non-competitive basis, it accepted a signature bonus of only USD 10 million.[222] Other companies paid much higher sums in the country's earlier licensing rounds for blocks with similar geology, during times of much lower oil prices.[223] For example, international oil companies paid USD 870 million for three ultra-deepwater blocks a decade earlier, in 1999.[224]

See also

4 5 7

12 The winning company or its owners sell out for a large profit without having done substantial work.

This final red flag has two main variations. In the first, a company that won a license or contract for a relatively low upfront cost resells, or "flips" it for a big return without having worked to develop the underlying asset. In such instances, observers of this red flag should ask why the government didn't just award the license to the ultimate recipient in the first place. In the second, the company's shareholders sell their equity for large profits shortly after the award, suggesting they acquired the license or contract merely to boost the sales price. Of course, there is nothing inherently suspect about companies unloading their assets for profit.[225] Corruption risk may be higher when the company's return on investment is exorbitantly high, or other red flags are present—for example, the company was unqualified or has a PEP as a legal or beneficial owner.

Illustrative cases

OPL 245-Malabu oil block controversy. Malabu Oil and Gas acquired a 100 percent equity interest in OPL 245 in 1998 with only a USD 2 million up-front payment to the Nigerian government. The company sold its interest for USD 1.1 billion in 2011 after doing nothing substantial to develop the block over the preceding thirteen years.[226]

See also 1 2 7

Steinmetz-Simandou bribery case. After acquiring lucrative exploration permits for the Simandou Blocks 1 and 2 iron ore blocks in 2008, BSGR reportedly invested only USD 165 million in exploration costs before selling 51 percent of its Simandou license to Vale, a Brazilian mining company, in 2010 for USD 2.5 billion.[227] This transaction gave the company a roughly 3,000 percent return on investment in two years—or, profits equal to 2.4 times Guinea's government budget for 2011.[228]

See also 6

Gécamines and Sodiminco asset sales to Dan Gertler entities. In the Gertler case, the Congolese state-owned mining firms Gécamines and Sodiminco sold parts of their stakes in a number of valuable copper and cobalt projects to little-known offshore companies traceable to Israeli mining entrepreneur Dan Gertler.[229] Within short periods—sometimes as little as one month—the buyers sold their freshly acquired stakes for large profits to established mining sector operators. A 2013 report estimated that the DRC lost USD 1.36 billion in public revenues between 2010 and 2012—an amount equal to twice the country's combined health and education budgets for one year—from five such deals.[230] The Gertler-associated companies meanwhile made an average margin of 512 percent.[231]

See also 2

Uranex stock sale. In June 2007, the Australian-listed company Resource Generation Limited (ResGen) announced it had purchased 80 percent of the shares of the Cameroonian entity Uranex SA (Uranex).[232] Only a few months earlier, Cameroon's Ministry of Mines, Industry and Technological Development had granted Uranex exclusive rights to three uranium exploration licences that together covered 2,935 square kilometres.[233] As payment for the sale, ResGen gave Uranex's shareholders a total of 40 million ResGen shares—worth about USD 5.6 million on the day.[234] The shareholders included a former parliamentarian and a mayor who headed the country's ruling party in the area where the mining site was located; and the son of a prominent general.[235] A 2016 investigative report found that the Uranex shareholders earned a 37,900 percent one-year rate-of-return on their upfront capital invested.[236] The investigative report found no evidence that either Uranex or ResGen spent substantial funds developing the mines. Neither had obvious experience as concession operators: before the 2007 buy-out, ResGen had supplied telephone, data, facsimile, and internet to remote mining sites.[237] In 2008, soon after it bought into Uranex, ResGen wrote off the three uranium concessions in its annual report, stating that it needed to focus on another project in South Africa.[238]

Conclusion

These 12 red flags certainly do not capture the wide range of forms that corruption can take. If oversight actors asked questions whenever they encountered these attributes, they would detect more corruption. Incremental changes of this kind could, over time, help resource-producing countries to save valuable public revenues, and help companies active in the extractive sector to avoid reputational damage and costly law enforcement action. A further step would be to design an award process hardwired with vigilance for these red flags, and thereby systematically diminish the threat of corruption.

Even in the harshest political environments, actors can ask questions – either quietly from the inside, or loudly from afar. Exploring past corruption cases helps identify the right questions to ask.

This red flags list represents a contribution to a wider effort to understand how best to identify and prevent corrupt transactions. Further research on this topic could help to deliver additional tools. For instance, if the presence of red flags was assessed across cases where corruption accusations arose *and* cases where corruption was most likely absent, the resulting list would hold greater predictive power. Studies such as these, along with further examination of real-world corruption cases and their lessons, can generate better-informed policy decisions and oversight activity.

Appendices

APPENDIX A. PROCESS FOR CASE SELECTION

To identify the list of possible oil, gas and mining sector licensing cases for analysis, we surveyed the following sources:

- Databases of filings from litigated corruption cases in several jurisdictions—for example, LexisNexis, PACER and the U.S. DOJ and SEC websites
- Publicly accessible databases that track and describe alleged instances of corruption, including Ethixbase, Trace Compendium and World Bank's StAR compendium
- Corruption case compendiums published by law firms, trade periodicals and other industry bodies
- Reports from NGOs, IFIs and international policymaking bodies on corruption and other poor management of extractives license and contract awards—e.g., by Global Witness, the World Bank, OECD and Public Eye
- Media reports, reviewed using a series of keyword searches in Google
- Academic literature
- Colleagues and experts, including NRGI staff and advisory board members and corruption practitioners from multiple NGOs and international organizations

We then reviewed the prospective cases, and chose among them using the following set of questions:

- Do the available materials contain a clear and consistent description of the mechanics of the alleged corruption?
- When did the alleged corruption occur? *(Preference for newer cases)*
- Where did the alleged corruption occur? *(Attempt at wide regional distribution)*
- Does the source material read as reliable and come from multiple sources?

After applying the questions, we were left with a group of 100 cases of license and contract awards where corruption accusations were present, and we analyzed these to identify potential red flags.

APPENDIX B: COUNTRIES COVERED IN THE REVIEWED CASE STUDIES (49 TOTAL)

- Afghanistan
- Algeria
- Angola
- Argentina
- Azerbaijan
- Benin Republic
- Burkina Faso
- Burundi
- Brazil
- Cambodia
- Cameroon
- Chad
- China
- Colombia
- Côte d'Ivoire
- Democratic Republic of Congo
- Equatorial Guinea
- Ghana
- Guinea
- Indonesia
- Iran
- Iraq
- Jamaica
- Kazakhstan
- Liberia
- Libya
- Mexico
- Mongolia
- Mozambique
- Myanmar
- Niger
- Nigeria
- Peru
- Portugal
- Republic of Congo
- Russia
- Sao Tome and Principe
- Senegal
- Sierra Leone
- Somalia
- South Africa
- Tanzania
- Tunisia
- Turkmenistan
- Ukraine
- United States of America
- Venezuela
- Zambia
- Zimbabwe

APPENDIX C. ADDITIONAL RESOURCES ON DETECTING CORRUPTION RISKS

Australian Trade Commission, *Red Flags for Bribery,* 1-2.

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1 While the focus here is on license and contract award processes, similar red flags can crop up in other stages of a license or contract's life, such as contract or license reviews, renewals, extensions, assignments or revocations. They could also apply at other points along the extractive sector decision chain, such as when the government enforces regulations or how it makes investment and spending decisions with oil, gas or mining revenues. Our selection of case studies did not include examples like these, however. Lesser types of awards—e.g., of permits or waivers—may also carry some similar red flags, but our cases did not focus squarely on these either.

2 Because each jurisdiction has different laws, acts that count as corrupt under this definition might be illegal in one country and legal in another. Note that under this definition, an act can be corrupt even if it does not result in direct financial gain for the public official involved. An official could behave corruptly by abusing his/her authority in order to benefit someone else—for example, a political ally or business partner.

3 A number of measures exist for these contextual factors. The Resource Governance Index measures how well a country governs its oil or mineral sector. More broadly, the Corruption Perception Index and the Governance Matters Indicators measure a country's overall governance and corruption environment.

4 Many of the cases were drawn from an existing in-house library of corruption case studies that NRGI has developed over the past 18 months. We also identified cases by reviewing databases of existing cases other sources. For more on the case selection process, see Annex A to this report.

5 We would note, however, that a reliable control group of "non-corrupt" extractives sector license and contract awards could be difficult to compile—for example, because it would be hard to establish whether corruption was not present or simply not detected, and because "clean" processes may tend to receive less scrutiny and reporting from oversight actors than those where corruption occurs.

6 The requirement that a red flag appear four times and in more than one country eliminated some candidates that we think could be important and commonplace. For example, our sample did not contain enough cases in which the winning company defaulted on its license or contract obligations but suffered no consequence as a result, appeared to pay fees required for the award with proceeds of crime, or captured a large share of available business through the award.

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22 A shelf company is a corporation that is set up for later purchase and takeover by a third party. Typically, the company will have no operations or clear business purpose at the time of formation, and the third party will re-purpose it to meet its needs. It is distinct from a "shell company," but can have the attributes of a shell company.

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