Safeguarding corporate and project governance: The role of IFIs

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Introduction

This article considers some of the practical challenges and legal questions arising from the implementation of sanctions regimes imposed by the European Bank for Reconstruction and Development (EBRD) and other multilateral development banks. As these sanctions regimes have become active only recently, their operations represent a fast-growing area, giving rise to a variety of practical challenges and legal questions. Topical issues currently under consideration include the appropriate level of transparency and accountability of the systems and the application of sanctions to corporate groups.

For supranational institutions which cannot readily converge, selectively, with the jurisdictions of just some of their members, the underlying objective is to maintain a quasi-judicial administrative process for sanctioning firms and individuals in order to ensure that the projects they finance comply with the highest standards of integrity.

Background

In 2010, the impact of sanctions imposed by EBRD and several other multilateral development banks became substantially amplified as EBRD, the African Development Bank (AfDB), the Asian Development Bank (ADB), the Inter-American Development Bank (IADB) and the World Bank – each a participating institution – established a mechanism whereby a debarment decision made by one participating institution may be given effect by the others. The mechanism is set out in the Agreement for the Mutual Enforcement of Debarment Decisions (AMEDD), which was signed on 9 April 2010. Consequently, as a general rule, sanctions imposed by any participating institution will also be enforced by the other participating institutions.

For EBRD, administrative sanctions are tools used against firms or individuals that have engaged in fraud, corruption, coercion or collusion (collectively termed ‘prohibited practices’). The Agreement Establishing the European Bank for Reconstruction and Development expressly provides that EBRD has to take all necessary measures to ensure that the proceeds of its financing are used solely for the purposes for which such financing was granted. In 2009, EBRD adopted its Enforcement Policy and Procedures (EPPs), which set forth EBRD’s procedures for addressing prohibited practices in the procurement, award or implementation of EBRD-financed contracts.

This involves giving the accused party, designated as the ‘respondent’, an appropriate level of due process before it is decided whether they will be sanctioned and, if so, which sanction will be imposed.

Types of sanctions

The EPPs provide for a range of possible sanctions, including: (1) reprimand – a formal letter of censure of the respondent’s behaviour, appropriate for an isolated incident or lack of oversight or where the violation or the party’s role in it is minor; (2) conditional non-debarment, requiring a respondent to comply with certain remedial, preventative or other measures as a condition to avoid debarment from additional contracts for projects financed by EBRD; (3) debarment, whereby a respondent is debarred either indefinitely or for a specified period of time; (4) debarment with conditional release, whereby a respondent is subject to debarment but also to a conditional release under which such debarment will be terminated upon compliance with conditions set forth in the decision; and (5) restitution or remedy, whereby a respondent is required to make restitution to the borrower or to any other party, or to take actions to remedy the harm done by its misconduct.

The length of debarment is within the Enforcement Committee’s discretion and the EPPs prescribe a number of aggravating and mitigating factors. Such aggravating factors include: severity of the misconduct (e.g. repeated pattern of conduct, sophisticated means used to commit prohibited practice(s), involvement of public officials), degree of harm inflicted on the affected EBRD-financed project, the respondent’s interference with investigative process, intimidation and/or bribing of a witness, etc. Mitigating factors, on the other hand, include such circumstances as management taking all appropriate measures to address the misconduct, establishment or improvement of an effective compliance programme, assistance and co-operation with investigative process, etc. Finally, the names of sanctioned parties, together with the sanction imposed, are posted on EBRD’s external website.

Divergences of approach among IFIs

Participating Institutions’ sanctions systems differ from each other with respect to such matters as the number and type of internal bodies involved in investigating sanctionable practices, approach towards settlement of cases, ability of the parties in the proceeding to request a hearing and to appeal the relevant participating institution’s decision, deadlines for the submission of filings, composition of the sanctions (or analogous) bodies in

terms of whether the majority of their members are external members or staff members of the relevant participating institution, etc. Despite these differences, participating institutions have managed to achieve a remarkable degree of harmonisation of sanctions policies, including the mutual recognition of debarment decisions. Moreover, as participating institutions continue to develop their enforcement structures, greater harmonisation among sanctions processes is to be expected, although each participating institution will keep a system that suits its size and organisational structure. One significant area of divergence is in how and how far sanctions cases are communicated.

The EBRD’s sanction process

Allegations that a firm or individual has engaged in a prohibited practice are investigated by EBRD’s chief compliance officer (CCO). If the CCO believes there is sufficient evidence to substantiate the allegations, they prepare a report and proposed enforcement action for consideration by EBRD’s Enforcement Committee. The committee consists of at least five senior EBRD staff members, appointed by EBRD’s president. Following receipt of a report from the CCO, the Enforcement Committee may issue a Notice of Prohibited Practice to the respondent. The notice includes the allegations, the evidence and a recommended sanction.

The respondent may choose not to contest the allegations or the recommended sanction, in which case the recommended sanction will be imposed. If the respondent does contest the allegations, the case is referred to the Enforcement Committee, which considers the allegations in the notice along with any response from the respondent before taking a final decision. The committee reviews all of the evidence in the case and may hold a hearing as part of its deliberations if the respondent has requested it within the prescribed deadline.

Finally, if the Enforcement Committee determines that it is more likely than not that the respondent did engage in the alleged prohibited practice, it will prepare a report of its determination to EBRD’s president. The report will include the committee’s recommendation as to the appropriate sanction to be taken vis-à-vis the respondent. If the president accepts the Enforcement Committee’s recommendation in full, the decision of the president will be final.

In these proceedings, the initial burden of proof is on the CCO to establish that it is ‘more likely than not’ that the respondent engaged in a prohibited practice. This standard of proof is equivalent to the usual civil standard of ‘preponderance of the evidence’ or ‘balance of probabilities’. The Enforcement Committee may both consider any form of evidence, including circumstantial evidence, and draw any inferences it deems reasonable therefrom.

The EPPs also allow the Enforcement Committee to order, at any time during the enforcement proceedings, the suspension of the eligibility of the respondent to become an EBRD counterparty or to receive payment in respect of an EBRD project.

Notably, the World Bank is the only participating institution that has adopted the practice of publishing full decisions in sanctions cases. The reasons for this different approach are varied, with the main driver being concern over potential defamation claims over statements in published decisions. While EBRD, AfDB and IADB publish only a list of debarred entities, together with the committed prohibited practice that resulted in such debarment, ADB takes a rather radical stance of not publishing the names of entities or individuals that have been debarred, explaining this stance by stating, on its website, that: ‘In ADB’s view, allowing for first-time violators to improve their ethical standards and to thereby contribute to improving governance in general, rather than branding them publicly as “corrupt” after a first violation of ADB’s Anticorruption Policy and Integrity Principles and Guidelines, is a more productive and constructive approach in the fight against corruption in the medium and long term.’

Publication of World Bank’s decisions

The World Bank’s new approach was adopted in January 2011, with procedures requiring the board to issue fully reasoned decisions, including both the basic facts of the case and the legal reasoning underpinning its decision. Under the previous version of the World Bank’s Sanctions Procedures, the names of sanctioned parties, together with the sanction imposed, were posted on the World Bank’s external website, but the evidence and other considerations underlying the sanction were not made public. The choice to publish full texts of decisions was prompted by the World Bank’s management’s view that transparency acts as an important safeguard against arbitrary, blatantly unfair or inconsistent decisions. What is more, publication is seen as a powerful incentive for all actors in the sanctions process to maximise the quality of their work and as a creator of the legal certainty for the World Bank’s stakeholders by creating, over time, a body of jurisprudence that will supplement the admittedly scarce substantive legal framework for the participating institutions’ sanctions regimes.

Nevertheless, the World Bank’s management acknowledges certain pitfalls of greater transparency, amongst which are the risk that the Sanctions Board will unwittingly rely on defamatory material in the record and reputational risks associated with the potential exposure of weak cases or flawed decisions. Publication of the World Bank’s decisions represents a noteworthy contribution to the development of public international law in the context of antifraud and anti-corruption frameworks and administrative sanctions. It also sheds light on the workings of the sanctions system, the types of behaviour that will be sanctioned and the types of mitigating and aggravating factors that the Sanctions Board will consider in reaching its decision on the type of sanction imposed.

Since the adoption of the procedures for the publication of its sanctions-related decisions, the World Bank has published texts of ten decisions. They involve respondents from Thailand, Peru, West Bank and Gaza, Nigeria, India, Russia, Bangladesh and Sudan. All of them except for one involve engagement in fraudulent practices, whereas one involves engagement in corrupt practices. Most decisions impose the World Bank’s ‘baseline’ sanction of
debarment with conditional release, whereby the debarred party is required to meet certain specific, predefined conditions before it is released, after a certain minimum period of debarment (ranging from one to five years in these recent decisions). The reasoning behind debarment with conditional release rather than a ‘plain vanilla’ debarment being the ‘baseline’ sanction is that the former places greater emphasis on rehabilitation, encouraging sanctioned firms to adopt adequate, effective policies and measures that make it less likely that they will engage in such misconduct again.13

Still, of the ten recent decisions, three have imposed a ‘plain vanilla’ debarment of six months or one year,14 which demonstrates that the choice of sanction is not a mechanistic determination, but rather a case-by-case analysis tailored to the specific facts and circumstances presented in each case.

As the ten latest decisions demonstrate, the most frequently considered factors in play are the severity of misconduct, magnitude of harm caused by the misconduct, interference in the World Bank’s investigation, past history of misconduct, voluntary corrective action (which should reflect ‘genuine remorse and intention to reform, rather than a calculated step to reduce the severity of the sentence’15), co-operation in the investigation of the case and a period of temporary suspension already served by the sanctioned party.

Finally, an issue that frequently emerges in the Sanctions Board’s decisions is the respondent’s liability for the acts of its employees.16 The Sanctions Board’s stance appears to be that an employer could be found liable for the acts of its employees under the doctrine of respondeat superior. In reaching this conclusion, however, the Sanctions Board will consider specific facts and circumstances in the record.17

**Treatment of corporate groups**

All participating institutions’ sanctions procedures provide that affiliates of respondents may also be sanctioned, and that sanctions may be applied to successors and assigns of sanctioned parties. Understandably, however, a number of challenging issues surround the need to prevent circumvention of sanctions through the use of affiliates or changes in corporate forms, on the one hand, while ensuring that sanctions are commensurate with the degree of responsibility, on the other hand. In the attempt to provide a uniform guidance on these matters, in September 2012, the participating institutions adopted Harmonised Principles on Treatment of Corporate Groups, which set general criteria for the application of sanctions to affiliates and successors and assigns.18

The principles recognise that sanctions will be applied to entities within corporate groups on the basis of informed decision, based on the facts of the case and not a rigidly automatic approach. Nevertheless, the principles state a rebuttable presumption that sanctions will be applied to all entities controlled by the respondent: unless the respondent demonstrates that the entities are free of responsibility for the misconduct, application to the entities would be disproportional and is not reasonably necessary to prevent evasion. In practice, however, very few respondents focus on addressing the culpability of their affiliates in their response (and hence fail to rebut the said presumption), which results in the sanctions typically extending to affiliates controlled by the sanctioned parties.

**Latest review of the World Bank’s procedures**

At the request of the World Bank’s Audit Committee, the World Bank’s Legal Vice Presidency has undertaken a review of the World Bank Group sanctions system, which is being conducted in two phases. Some of the recommendations that the preliminary Phase I report, which was discussed at the World Bank’s Audit Committee in March 2013, identifies are: exploring ways to enhance proportionality through broader and more flexible use of sanctions; revisiting the designation of debarment with conditional release as the ‘baseline’ sanction, in particular in smaller cases involving individuals and small and medium enterprises (SMEs), which have not demonstrated much initiative in adopting effective compliance measures on which their release from debarment is conditioned; and considering listing all known sanctioned or suspended affiliates by name on the debarment and suspension lists and considering steps to make the system more accessible to SMEs and individuals who lack the means to engage legal counsel, without incurring undue costs.19

Notably, the review found that the World Bank’s sanctions regime appears to meet, and in some cases exceed, fundamental principles under general notions of due process and the emerging doctrine of global administrative law, with some recommendations aimed at the further strengthening of the fairness and transparency of the sanctions system. Curiously, the review also found a pattern of non-engagement by SMEs in the system, as more than half of respondents, most of them SMEs, are sanctioned ‘by default’ because they do not respond in any way to Notices of Sanctions Proceedings. In that context, some of the recommendations include simplifying the procedure for smaller cases and less sophisticated respondents and increasing the use of ‘plain English’ in sanctions procedures.

**Conclusion**

As participating institutions continue to develop their enforcement structures, we can expect greater harmonisation among their sanctions processes. Moreover, companies and individuals seeking finance from a participating institution should be aware of the fact that, as a result of AMEED, the profile of any single participating institution’s fraud and corruption investigation has been raised significantly and could result in sanctions not only by that participating institution, but also globally by other participating institutions.

Because of these far-reaching consequences of the participating institutions’ sanctions proceedings, these proceedings are likely to evolve towards increasingly quasi-judicial models with the development of elaborate adjudicatory processes that are more elaborate than those that typify administrative processes. At the same time, however, sanctions processes remain essentially administrative in nature. Hence, the degree to which they might continue to move towards a judicial model will depend on each participating institution’s efforts to balance standards of efficiency and effectiveness on the one hand, with rule of law and due process considerations on the other.

The content of this article reflects the personal opinion of the author and is not the official position of the European Bank for Reconstruction and Development.
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ENDNOTES
5 Ibid., § 6.8.
6 Ibid., § 5.2 (iv).
7 Anticorruption and Integrity, FAQs, available at: http://www.adb.org/site/integrity/qa (last visited on 24 April 2013).
10 Ibid., at 25.
11 Ibid.
13 See Leroy and Fariello, supra note 9, at 15.
14 See Sanctions Board Decisions No. 46, 54 and 55.
15 See, e.g., Sanctions Board Decision No. 55, at para. 76.
16 See, e.g., Sanctions Board Decisions No. 46, 47, 48, 50, 51, 52 and 55.
17 See Sanctions Board Decision No. 55, at para. 49.