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# UNDUE DILIGENCE

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How banks do business with corrupt regimes

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# SUMMARY

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Economic crisis:  
banks have damaged  
the world's richest  
economies, but by  
facilitating corruption  
they help perpetuate  
poverty in the world's  
poorest countries.

## What is the problem?

The world has learnt during 2008 and 2009 that failures by banks and the governments that regulate them have been responsible for pitching the global economy into its worst crisis in decades. People in the world's richest countries are rightly angry at the increasing job losses and house repossession.

What is less understood is that for much longer, failures by banks and the governments that regulate them have caused untold damage to the economies of some of the poorest countries in the world.

By doing business with dubious customers in corrupt, natural resource-rich states, banks are facilitating corruption and state looting,

which deny these countries the chance to lift themselves out of poverty and leave them dependent on aid.

This is happening despite a raft of anti-money laundering laws that require them to do due diligence to identify their customer and turn down illicitly-acquired funds. But the current laws are ambiguous about how far banks must go to identify the real person behind a series of front companies and trusts. They fail to be explicit about how banks should handle natural resource revenues when they may be fuelling corruption. And if a bank has filed a report on a suspicious customer as required by the law, but then the authorities permit the transaction to go ahead, the bank can legally take dirty money. So it may be

possible for a bank to fulfil the letter of its legal obligations, yet still do business with these dubious customers.

By accepting these customers, banks are – directly or indirectly – assisting those who are using the assets of the state to enrich themselves or brutalise their own people. Corruption is not just done by the dictator who has control of natural resource revenues. He needs a bank willing to take the money. It takes two to tango.

This report presents a series of case studies about bank customers in Equatorial Guinea, Republic of Congo, Gabon, Liberia, Angola and Turkmenistan. In these countries, the national resource wealth has or had been captured by an unaccountable few, whether for personal enrichment, to maintain an autocratic personality cult that violated human rights, or to fund devastating wars.

The banks doing business with these customers include Barclays, Citibank, Deutsche Bank, and HSBC. Nearly all of the banks that feature in this report are major international banks and all of them make broad claims about their commitments to social responsibility. Yet there is a grotesque mismatch between rhetoric and reality. Their customers are heads of state or their family members, state-owned companies used as off-budget financing

mechanisms by their parent government, central banks in states that have been captured by one individual, and companies trading natural resources out of conflict zones. Banks should have been extremely wary about doing business with any of them.

## Why does it matter?

Natural resource revenues offer a potential way out of poverty for many developing countries. But too often, resource revenues that could be spent on development are misappropriated or looted by senior government officials, or are used to prop up regimes that oppress their own people. Banks have a crucial role to play as the first line of defence against corrupt funds, but they are not doing a good job of it.

The key step banks are already required to perform to prevent corrupt funds entering the international system is due diligence, to find out who their customer is and where his or her funds have come from. But the current system is full of loopholes, whether in the anti-money laundering laws themselves, or the way that they are enforced. The result is that the international banking system is complicit in helping to perpetuate poverty, corruption, conflict, human suffering and misery.

This is a serious matter of public interest, both in the countries whose natural resources ought to be paying for development but are

An Angolan mother mourns the death of her child. Angola is Africa's largest oil producer, but has the highest rate of child mortality relative to its national wealth in the world.  
Credit: J. B. Russell/  
Panos



not, and in the countries whose taxpayers are funding aid to the developing world to fill the gap that is left by corruption and other forms of illicit capital flight. Global Witness is publishing this report in order to provide a tool for productive debate and, hopefully, to contribute to an improvement in banking regulation and enforcement that will have a positive impact on development outcomes for the world's poorest countries. In the current climate of banking meltdown, the report's focus on transparency and the need for assurance that the financial regulatory system is working effectively is of particular public interest.

## **What can be done?**

The changes in financial regulation that are on the way as a result of the global financial crisis also present a chance to tackle the financial industry's ongoing facilitation of corruption.

While the multiple causes of a complex banking crisis are different to the relatively straightforward factors which allow banks to do business with corrupt regimes, there are two identical underlying themes. The first is that when it comes to sticking to the rules, bankers are doing the minimum they can get away with. They aggressively exploit the loopholes and ambiguities in regulations and arbitrage their responsibilities to the lowest level. The second is that regulation by individual national governments is too fragmented to be effective, is hindered by bank secrecy laws, and is not backed by political will.

Global Witness is making the following recommendations, which need to be adopted globally, with effective information sharing across borders. There would be no point in tightening anti-money laundering rules only in Europe and the US if that meant that dirty money then flowed, for example, towards Asia.

**1. Banks must change their culture of know-your-customer due diligence, and not treat it solely as a box-ticking exercise of finding the minimum information necessary to comply with the law.** Banks should adopt policies so that if they cannot identify the ultimate beneficial owner of the funds, or the settlor and beneficiary if the customer is a trust, and if they cannot identify a natural person (not a legal entity) who does not pose a corruption risk, they must not accept the customer as a client. They should adopt this standard even if they are not legally required by their jurisdiction to do so.

**2. Banks must be properly regulated to force them to do their know your customer due diligence properly, so that if they cannot identify the ultimate beneficial owner of the funds, or the settlor and beneficiary if the customer is a trust, and if they cannot identify a natural person (not a legal entity) who does not pose a corruption risk, they must not accept the customer as a client.** Anti-money laundering laws must be absolutely explicit, and consistent across different jurisdictions, that banks must identify the natural person behind the funds, investigate the source of funds, and refuse the customer if they present a corruption risk. Regulators are in the front line of ensuring that this is enforced, and should treat the prevention of corrupt money flows as a priority.

This is the scandal at the heart of the system, because customer identification has been the crucial element of money laundering laws since their inception in the 1980s. Yet inconsistencies and a failure by many jurisdictions to be sufficiently explicit about what is required from banks in practice mean that there are still too many loopholes that can be exploited.

While it is important that banks develop their own effective know-your-customer policies, as per the previous recommendation, leaving banks to do it on their own without regulatory oversight will not work, because the avoidance of corrupt funds inevitably involves turning down potential business, and not all banks are willing to do this. The subprime crisis and ensuing credit crunch have shown, among other things, that allowing banks to self-regulate does not work. They consistently claim that they employ the cleverest people in the world and can be allowed to manage their own risk. But if, as they have shown, they cannot safely manage the task that is of greatest importance to them – making a profit – then it seems clear that they cannot be expected to self-regulate when it comes to ethical issues.

**3. International cooperation has got to improve.** A necessary first step is to overhaul and strengthen the workings of the Financial Action Task Force (FATF), a little known and opaque inter-governmental body that sets the global standard for the anti-money laundering rules that are supposed to prevent flows of corrupt funds. FATF must use its powers to name and shame more effectively, open itself up to external scrutiny, and cooperate with other organisations and government agencies working on corruption.

G20 leaders discuss how to mend the global financial system. November 2008. Credit: Brooks Kraft/Corbis



FATF's members – which include the states that are home to the world's major economies – also need to get their own houses in order before they lecture the small island tax havens who have frequently been FATF's targets. For example, of 24 FATF member states evaluated in the last three years, none were fully compliant with Recommendation 5, which requires countries to have laws in place obliging banks to identify their customer and none had legislation in compliance with FATF's Recommendation 6 which says countries must require their banks to perform enhanced due diligence on politically-exposed persons (PEPS: senior government officials or their relatives and associates, who because of their access to state resources are a heightened money laundering risk). Only four countries were 'largely compliant,' two were 'partially compliant,' eighteen, including the UK, were non-compliant.<sup>1</sup> (See table on page 107)

#### **4. New rules are needed to help banks avoid corrupt funds.**

- Each country should publish an online registry of the beneficial ownership of all companies and trusts, and an income and asset declaration database for its government officials.
- National regulators should be required by FATF to assess the effectiveness of the commercial databases of PEPs on which banks rely to carry out their customer due diligence.

- Banks should not be permitted to perform transactions involving natural resource revenues unless they have adequate information to ensure that the funds are not being diverted from government purposes; should be required to publish details of loans they make to sovereign governments or state owned companies, as well as central bank accounts that they hold for other countries; and should develop procedures to recognise and avoid the proceeds of natural resources that are fuelling conflict, regardless of whether official sanctions have yet been applied.

(See page 116 for a full explanation of these and other recommendations.)

The governments of the world's major economies must stand up to make these things happen. If they do not, no other jurisdictions will either. Governments that have bailed out banks and whose taxpayers now own a stake in them have even more incentive to do so. Those governments that have committed themselves to making poverty history, and that claim to be pushing good governance and accountability through their aid interventions, are guilty of hypocrisy if they fail to take responsibility for how their financial institutions and the financial system which they regulate are contributing to corruption and therefore poverty.

# INTRODUCTION

01

## Breaking the links between banks, corruption and poverty

On 28 May 2005, Denis Christel Sassou Nguesso, son of the president of Republic of Congo, went shopping in Paris. He spent €2,375 in Dolce & Gabbana, followed by €6,700 in Aubercy Bottier, a high-end bootmaker. Less than three weeks later, on 14 June, he was back: another €4,250 on shoes at Aubercy and €1,450 at a designer handbag shop. A month later, on 15 July, he burned another €2,000 at Aubercy, apparently his favourite shoe shop at the time.

*How are we going to make poverty history if we can't make corruption history?*

Sorious Samura, Sierra Leonean journalist<sup>4</sup>

Most of the population of Congo cannot afford beautiful handmade Parisian shoes. This is because they can barely afford to live at all. Seventy per cent of the population live on less than a dollar a day, and one in ten children dies before their fifth birthday. Yet Congo is rich in oil, and in 2006 oil revenues reached around \$3 billion.<sup>2</sup> It was the proceeds of Congo's oil sales which appeared to be paying for Denis Christel's designer shopping sprees. His personal credit card bills, along with those of another Congolese official, were paid off by offshore companies registered in Anguilla which appear to have received, via other shell companies, money related to Congo's oil sales.

Denis Christel is not only the president's son, he is also responsible for marketing Congo's oil. Yet he was able to open a bank account at one of Hong Kong's largest

banks, into which the proceeds of oil sales were deposited, and out of which these personal credit card bills were paid.<sup>3</sup>

This is one of a number of stories covered in this report in which the wealth of a nation has been captured by those who run it.

The report shows how, despite a raft of anti-money laundering measures which should prevent flows of corrupt money, banks are finding ways to do business with dubious customers in corrupt, resource-rich states. The current laws are ambiguous about how far banks must go to identify the real person behind a series of front companies and trusts. They also fail to be explicit about how banks should handle natural resource revenues when they may be fuelling corruption. So it may be possible for a bank to fulfil the letter of its legal obligations, yet still do business with these dubious customers.

The report focuses on a particular cluster of states in West Africa and Central Asia which see some of the most egregious examples of the 'resource curse' in action. In these countries, the national resource wealth has or had been captured by an unaccountable few, whether for personal enrichment, to maintain an autocratic personality cult that violates human rights, or to fund devastating wars – or some combination of these. All of them are countries whose natural resources – oil, gas and timber – are in great demand by the world's developed and rising economies.

By doing business with these customers banks are – directly or indirectly – assisting

Are banks prepared  
to turn down  
corrupt money?  
Credit: Simon Vardy/  
StockphotoPro



those who are stripping their state of its assets and their people of an economic future. Corruption is not just done by the dictator who has control of natural resource revenues. He needs a bank willing to take or process the money. It takes two to tango.

The key step banks must perform to prevent corrupt funds entering the international system is due diligence to find out who their customer is and where his or her funds have come from. But the current system is full of loopholes, whether in the laws themselves, or the way that they are enforced.

The result is that the international banking system is complicit in helping to perpetuate poverty, corruption, conflict, human suffering and misery.

The case studies in this report show how:<sup>5</sup>

- **Barclays** was holding a personal account for Teodorin Obiang, son of the president of oil-rich but dirt-poor Equatorial Guinea, one of the world's worst kleptocracies. Despite his \$4,000 a month salary as a minister in his father's government, Teodorin owns a \$35 million mansion in Malibu and a fleet of fast cars, and claimed to a court hearing in South Africa that in Equatorial Guinea it is normal for ministers to end up with a sizeable

chunk of government contracts in their pockets.

- **HSBC** and **Banco Santander** hid behind bank secrecy laws in Luxembourg and Spain to avoid revealing the owners of accounts they held which received suspicious transfers of millions of dollars of Equatorial Guinea's oil money.
- Despite the fact that the US bank **Riggs** collapsed and was sold at a discount after a Senate inquiry investigated its handling of Equatorial Guinea's oil funds (which included numerous payments into the president's personal accounts), unknown commercial banks are still holding the Equatorial Guinea oil funds, with no transparency over their location and use. When Riggs collapsed in 2004 the oil funds were at \$700 million; they are now at more than \$2 billion.

- **Citibank**, through correspondent banking relationships, enabled Charles Taylor, the ex-president of Liberia now on trial for war crimes, to use the global banking system to earn revenues from timber sales, which were fuelling his war effort as well as being diverted into his personal bank account. Fortis was also involved in processing payments for timber that was fuelling Liberia's brutal conflict.



Much of Africa's oil wealth has not been used to alleviate poverty, but has disappeared into the pockets of its kleptocratic rulers.  
Credit: Sven Torfinn/  
Panos Pictures

- **Deutsche Bank** was the banker for the late President Niyazov of Turkmenistan, whose regime was notorious for human rights abuses, repression and impoverishment of the population. Deutsche Bank held the central bank accounts for gas-rich Turkmenistan for 15 years, despite the fact that the money was being kept out of the national budget and was effectively under the personal control of Niyazov.
- **Bank of East Asia**, Hong Kong's third largest bank, and offshore companies in Hong Kong and the UK Overseas Territory of Anguilla helped funnel Republic of Congo's oil money into an account controlled by the president's son, Denis Christel Sassou Nguesso, which he used to pay his personal credit card bills after frequent luxury shopping sprees.
- Huge oil-backed loans from large consortia of banks to Angola's state-owned oil company Sonangol helped to fuel corruption and support a system of parallel financing, beyond public scrutiny, which provided opportunities for cash to be diverted to the shadow state and into private pockets. While there have been some limited improvements to Angola's provision of information about its oil revenues, huge transparency concerns remain. Yet the oil-backed loans continue, in new forms, with

no parliamentary or civil society oversight to prevent potential diversion of funds.

These are nearly all major international banks and all of them make broad claims, to a greater or lesser extent, about their commitments to social responsibility. Six of the banks mentioned in this report – Banco Santander, Barclays, Citigroup, Deutsche Bank, HSBC and Société Générale – are among the eleven members of the Wolfsberg Group, which has developed a set of voluntary principles to help banks fulfil their anti-money laundering requirements.<sup>6</sup> This report will show that the Wolfsberg Principles are little more than a statement of intent and have no real power to prevent banks doing business with dubious customers.

There is a grotesque mismatch between rhetoric and reality. The customers that feature in this report are heads of state or their family members, state owned companies used as off-budget financing mechanisms by their parent government, central banks in states that have been captured by one individual, and companies trading natural resources out of conflict zones. Banks should have been extremely wary about doing business with any of them.

### **Supporting the shadow state**

For many of the poorest countries in Africa, South America, and Asia, the biggest

inflow of wealth from the rich world for the foreseeable future will be payment for oil, minerals, and other natural resources. In 2007 exports of oil and minerals from Africa were worth roughly \$260 billion, nearly eight times the value of exported farm products (\$34 billion) and nearly six times the value of international aid (\$43 billion).<sup>7</sup>

This huge transfer of wealth could be one of the best chances in a generation to lift many of the world's poorest and most dispossessed citizens out of poverty. Yet so far it has not worked out that way. Economist Paul Collier recently noted that of the world's poorest one billion people, one-third live in resource-rich countries.<sup>8</sup>

None of this is news to Global Witness, which has been working to expose the links between conflict, corruption and natural resources for the past twelve years, and was a driving force behind the Kimberley Process, to control the trade in conflict diamonds, and the Extractive Industries Transparency Initiative, which sets a global standard for extractives companies to publish what they pay and for governments

to disclose what they receive.<sup>9</sup> During this time we have worked in some of the world's most resource-rich countries: Angola, Sierra Leone, Liberia, Republic of Congo, Democratic Republic of Congo, Cambodia, Kazakhstan and Turkmenistan. These are countries which by rights should have significant natural resource revenues to spend on development. Instead they are impoverished, institutionally corrupt, and prone to violent instability.<sup>10</sup>

What binds these resource-rich countries is the emergence of a 'shadow state'; one where political power is wielded as a means to personal self-enrichment and state institutions are subverted to support those needs. Behind the façade of laws and government institutions of such states is a parallel system of personal rule. Through the wholesale subversion of bureaucratic institutions and control of force, the leaders of such states are able to exploit their country's resources in order to enrich themselves, and to pay for the means to stay in power, both through patronage and a bloated military and security apparatus.<sup>11</sup>

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Are banks going far enough to investigate the identity of their customer and the source of their funds?



Where self-enrichment becomes the overriding aim, the style of government can be described as a kleptocracy.

*A small minority of bankers are living on the profits from holding deposits of corrupt money. We have a word for people who live on the immoral earnings of others: pimps. Pimping bankers are no better than any other sort of pimp.*

**Paul Collier**, Professor of Economics at Oxford University, in 'The Bottom Billion: why the poorest countries are failing and what can be done about it'<sup>15</sup>

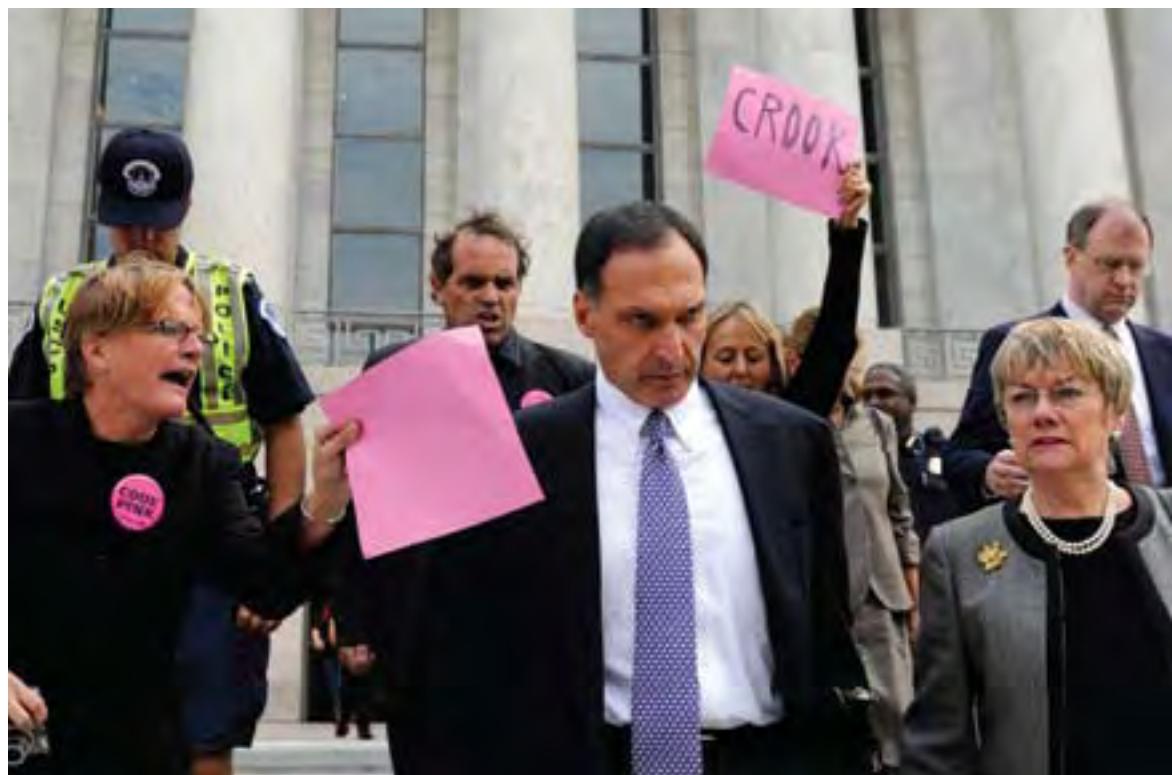
A shadow state's kleptocratic elite generates much of its illicit wealth via the expropriation of national assets, particularly the natural resources which should belong to the country's people and should be utilised for the common good. The amounts involved are catastrophic for the country's economy. However, asset stripping at this level is not just an economic crime. Its real effect occurs in the social destruction that follows when such vast amounts of capital are siphoned off into overseas private bank accounts.

It is a poverty problem in Angola, which has now overtaken Nigeria as Africa's biggest oil

producer but where, six years after the end of the war, life expectancy is still 42 and one in five children die before their fifth birthday.<sup>12</sup> It is a poverty problem in Democratic Republic of Congo, a country blessed with most of the minerals that mankind finds useful, but where 45,000 people are still dying every month from appalling deprivation brought by years of resource-fuelled conflict.<sup>13</sup> It is a poverty problem in Cambodia, where the current regime and its cronies control access to all the state's resources, but where an estimated 35% of the population live below the poverty line, and the vast majority without electricity or mains water.<sup>14</sup>

In short, mismanagement and outright looting of natural resources fundamentally undermines the ability of the state to provide basic services for its people, diverts funds intended for development, and destabilises whole societies. In the worst cases, it leads to conflict and failed states. The consequence is extreme poverty and human suffering, and in this context, it needs to be understood as an assault on fundamental human rights.

This much is known, and has been given names: the paradox of plenty, the resource curse. But the crucial point, less well recognised, is that the leaders of shadow states cannot loot the national coffers without help from outside. They need companies to pay for the extraction of



**Dick Fuld**, chief executive of failed bank Lehman Brothers, is heckled after testifying at a Congressional hearing in Washington. The banking crisis has revealed the gaping holes in the financial regulatory system. Credit: Susan Walsh/AP

Protesters in Reykjavik in January 2009. People are angry about the current banking crisis but developing countries have already been suffering for years from a failure to regulate banks properly.



natural resources, and they need banks to look after their money and to borrow from. Power confers both the ‘resource privilege’ – the right to strike deals for resource extraction – and the borrowing privilege – the right to borrow in the name of the country you lead.<sup>16</sup> But these privileges conferred by the international legal order can be subverted towards personal enrichment. The rulers of shadow states are abusing the badge of state legitimacy in order to build their personal fortunes at the expense of their impoverished citizens, yet the financial sector appears unable or unwilling to differentiate, and appears happy to do business with them regardless. This needs to change, and this report discusses how it can be done.

When running such a shadow state system it is helpful to keep funds well away from the national budget and the national treasury, by whatever means. A parallel financial system, held offshore or operated through a state-owned enterprise is what allows rulers to keep funds to pay people off when necessary, maintain control of favours, and in many cases to take funds for their own luxurious lifestyles. In addition, the calculated chaos created by shadow state leaders in order to maintain their own rule also makes their own countries highly unsuitable venues for the safekeeping of their stolen wealth, which is why they prefer to keep it offshore.

Therefore by doing business with such regimes and their state owned companies, banks

are aiding and abetting the survival of the shadow state. Corruption is not just something that happens in developing countries when bribes are paid and money is looted: it is also something that happens in the world’s major financial centres and offshore financial centres when financial institutions and corporate service providers do not care enough about who they are doing business with.

### The rules don’t work

In each case, the report examines what has happened from three perspectives: the bank’s ethics (which are essentially a voluntary matter), the bank’s regulatory obligation to know its customer, and the duty of the bank’s regulators to enforce these obligations.

The available evidence leads to one clear conclusion across each of the cases: the end result is that the bank has done business with a high profile customer who is involved in some way with the capture of the state’s resource revenues. This casts immediate doubt over the bank’s ethical decision making. The other two perspectives – the bank’s obligation to know its customer, and the regulator’s duty to enforce this obligation – are harder to disentangle, given the available evidence. It is not clear that by doing business with these customers the banks have failed in their regulatory obligation to ‘know their customer,’ because the standard set by the regulation may be insufficient, even if met,

to prevent banks doing business with such dubious customers.

In some examples, such as the Turkmenistan and Angola cases, it is clear that the regulations – both at national level and the international standard – do not yet extend to these situations, and there is a need for new guidance. The banks are treating these customers as, respectively, central bank accounts and a state-owned commercial enterprise, without considering the fact that the governments behind them cannot – or will not – publicly account in full for their country's natural resource revenues.

In other cases, the bank does have a regulatory obligation to 'know its customer.' In most countries, with national variations in the detail, the current anti-money laundering legislation puts a legal or in some cases supervisory requirement (an obligation set by the regulator, without legal force) on banks to find out about their customer, a process known as 'due diligence', and to make a suspicious activity report (SAR) to the authorities if they suspect tainted money. (See Box 2 on page 24 on how anti-money laundering laws are supposed to work).

The question posed in this report is whether fulfilment of these regulatory requirements – to tick the customer identity box and file a SAR if there are suspicions – is enough, in reality, to prevent banks doing business with potentially corrupt customers. The answer is that it does not seem to be.

Without reference to any particular case, a bank may not have found the ultimate customer behind a chain of ownership, or have made sufficient enquiries into their source of funds. Or, if a bank has suspicions and files a SAR, the authorities may not respond, or may allow the transaction to proceed for intelligence or political reasons. Global Witness understands that some governments are struggling to respond effectively to the volume of SARs filed. Industry insiders have also suggested to Global Witness that as well as law enforcement, there may be political and diplomatic issues behind some decisions to permit transactions to take place after a SAR has been filed.

While the SAR regime does produce useful leads for law enforcement, it can also allow a moral cop-out. It allows everyone to feel like they're doing something, but not actually necessarily to

address the problem. A bank suspects the money is dirty, it tells the authorities the money may be dirty, but if they give the go-ahead, the dirty money ends up in the bank and corruption has been facilitated. If law enforcement immediately kicks into action, the system has worked. But too often it does not.

*From my professional experience, if you speak up as a compliance officer they listen to you but at the end of the day what's going to happen is the business is accepted. There are so many ways to get around and make it look like the funds are not criminal... you set up companies worldwide and move the money around so you can't see where it came from or the business behind it.*

Former compliance officer, 2008<sup>17</sup>

The report also poses other questions. Are banks really prepared to turn down profitable business? How strong is the culture of compliance within banks? How much influence do the compliance officers have on decisions made by the relationship managers? And crucially, what is the point of due diligence if not to weed out who you shouldn't do business with?

By asking banks to identify their customers, and to file suspicious activity reports where they suspect dirty money, the anti-money laundering laws are effectively asking banks to be whistleblowers. This is very difficult for banks when their main purpose is making money. This is what sets up the appalling tension in banks between the compliance function, whose job is to ensure that due diligence is done, and the dealmakers, who of course want to complete the deal if it will be profitable. This is why Global Witness argues that while banks must change their culture of due diligence so that it is not just a box-ticking exercise, they also require strong regulatory oversight to ensure that they are doing it properly, and to provide more support to the compliance function within banks.

Compliance too often is solely about avoiding reputational risk, rather than a concern not to take corrupt business. The UK's regulator, the Financial Services Authority, noted this in 2006 with a survey of 16 banks' systems

to deal with Politically Exposed Persons (PEPs – the senior government officials or their family members and associates who as a result of their position present a higher corruption risk). It found that banks were far more interested in the likelihood that there might be a public scandal which might affect the bank's reputation, than in the likelihood that their customer was corrupt.<sup>18</sup> What this may show, in Global Witness's view, is that banks are operating on the basis of: if the customer is corrupt, we don't care; what we do care about is being found out to have done business with them.

Global Witness believes that there are certain circumstances in which banks should not do business with a person or entity because they cannot sufficiently minimise the risk that natural resources revenues and government funds are being mismanaged or misappropriated, however many due diligence boxes are ticked. If the mechanisms of government have been hollowed out by the corrupt shadow state behind it, or indeed if grotesque human rights violations are being committed, the argument that a bank has ticked the box by doing its due diligence, or that it is dealing with a sovereign entity, should not be enough.

Global Witness wrote to the world's top fifty banks (as of July 2008) to ask them if they had a policy of prohibiting accounts for heads of state or senior officials or their families from countries with a reputation for large-scale corruption, or even – for what might seem obvious to banks that claim to take their human rights commitments seriously – for heads of state of the world's most repressive regimes.<sup>19</sup> Sixteen of them wrote back: none of these banks have taken a policy decision to prohibit accounts from heads of state or senior officials from the most corrupt states, or from the world's most repressive regimes.

The establishment and constant expansion of anti-money laundering regulations has been inextricably linked with the framing of money laundering as a problem for global security. Anti-money laundering measures were deemed to be essential in order to combat drug trafficking, organised and serious crime such as the trafficking of women and children and, most recently, terrorism. Underlying this threat discourse has been the goal of protecting the stability of the international financial system. The irony behind banks' failure to adequately know their customers from corrupt shadow states is that it is precisely these environments that

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Soldiers in Turkmenistan. None of the banks that responded to Global Witness's survey have a policy of not taking accounts from the heads of state or senior officials from the world's most corrupt or repressive regimes.  
Credit: Sipa/Rex Features



*The only purpose of all of this is to make it extremely complicated for law enforcement agencies to follow the trail, as each step serves as a filter to hide the track of the client's money.*

**Heinrich Kieber**, a whistleblower now in a witness protection programme, in testimony to the US Senate Permanent Subcommittee on Investigations, talking about shell company structures used by the Liechtenstein bank LGT, 17 July 2008<sup>20</sup>

provide an ideal breeding ground for all of the above.

So the huge effort – backed by political will – that has gone into tracking down terrorist funds now needs to go into recognising – and curtailing – potentially corrupt funds.

### The need for reform?

In certain inter-governmental and policy-making circles, there is currently a lot of talk about asset recovery: the means by which countries whose rulers have looted state assets and deposited them in banks elsewhere can trace, freeze and repatriate the funds. It is a fiendishly difficult and expensive process, for reasons which will become clear throughout this report but not least of which are the facts that (a) it usually takes a change of regime before a government is willing to ask for the money back, and (b) the many ways that ownership of money can be hidden in the financial system means that it is very hard to see where the funds are. Organisations such as the World Bank's Stolen Asset Recovery Initiative (StAR), which aim to help by providing technical and financial assistance to requesting nations, are proliferating.

The very fact that these asset recovery efforts exist is testimony to the fact that corrupt money ends up in banks through loopholes in the regulatory and enforcement system. While Global Witness supports these asset recovery efforts we believe it would be far cheaper, easier and more effective to focus on tightening up the holes in the system which allow dirty money to enter banks in the first place.

The term 'moral markets' has been used by British Prime Minister Gordon Brown when talking about solutions to the financial crisis. 'Moral markets' can refer to a number of aspects of cleaning up the financial system, but it certainly applies to this issue. While dealing, as they must, with the problems that banks have created in the developed world, governments are also being presented with a chance to help lift millions of people

out of poverty in the developing world, in a way that aid flows will never achieve.

It is vital to understand that one of the key aspects of the international financial system that has contributed to the current banking crisis is also what allows corrupt money to circulate and disappear, and that is asymmetric information: knowledge that is held by one party but not the other. Banks (and their regulators) did not have enough information to understand the liabilities inherent in the complex derivatives packages they were buying, and the consequences for the economy have been terrible. The answer, many commentators agree, is more disclosure, more transparency.

Meanwhile, the moving and disappearance into the financial system of corrupt (and indeed, other criminal, as well as terrorist funds) is facilitated by the many jurisdictions that peddle secrecy for a living and do not require disclosure of the beneficial ownership of companies or trusts, as well as by the banking secrecy rules that hinder the few subsequent investigations that do take place. The answer to this problem, too, is more disclosure, more transparency.

Economists will agree that markets function most efficiently when there is symmetrical disclosure of key information, and that problems always arise from non-disclosure.

In the case of the banking crisis, it has been the investors, pension funds and subsequently the companies and populations of rich countries (as well, of course, as the banks themselves) that suffer as a consequence of lack of information about the bad debts. In the case of the stories in this report, it is the impoverished populations of the countries whose rulers are looting their state coffers who bear the brunt of this lack of transparency.

In the rich countries, the consequence will be some years of belt tightening, job losses, house repossession. Nobody is saying it will be pretty. But the populations of some of the poorest countries in the world already suffer far more every day, with no

Malabo, the capital of Equatorial Guinea. The country's oil revenues should make it one of the richest countries in the world, per capita; instead its people are among the poorest.  
*Credit: Robert Grossman/  
Africaphotos.com*



hope of respite unless the international community intervenes to change the rules.

As banks tumble, there is growing recognition that if you provide an enabling environment, one in which secrecy can flourish, you create an environment that encourages and stimulates bad practice.

During 2008, two interesting developments reignited the question of whether a minority of jurisdictions can continue to help those from other countries avoid their obligations. Both situations concerned tax evasion, but the arguments are equally applicable to corrupt funds, since both tax evasion and corruption involve depriving a government of its legitimate sources of funds.

Last year an employee of the Liechtenstein bank LGT, which is owned by Liechtenstein's ruling family, leaked details of 1,400 account holders who were evading tax in their home countries; eleven countries including Germany and the UK are now pursuing tax investigations.<sup>21</sup>

In February 2009, the Swiss bank UBS was fined an extraordinary \$780 million by the US authorities for facilitating tax evasion.

The bank was forced to hand over some of the names of its US customers who had knowingly concealed \$20 billion from the American tax authorities.<sup>22</sup> Meanwhile a US Senate committee called both UBS and LGT to account for helping US citizens hide billions from the taxman.<sup>23</sup>

These moves are starting to make dents in the walls of banking secrecy that have been used to shield those with ill-gotten gains.

In the run up to the G20 summit in early 2009 the leaders of key G20 states were starting to make strong statement that a global crackdown on tax havens would be essential in the reshaping of the financial regulatory system.<sup>24</sup>

Finally the truth is on the front pages: light touch regulation has not worked. This is the right time to throw in a new question about the regulation of banks: is enough being done to prevent banks helping corrupt officials who impoverish their countries? The answer is no, and as the financial regulatory architecture is rebuilt in the aftermath of the current crisis, the opportunity to do something about it has arrived.

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# WHO IS YOUR CUSTOMER?

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02

Banks make their profits performing a vast array of services these days, some involving financial instruments so complex that, as the banking crisis has shown, not even senior figures in the bank fully understood them. But at the heart of it all, banks are, and always have been, enablers and agents. By providing funds, they enable businesses to develop. By guaranteeing a transaction, they allow trade payments to be made. By holding accounts, they help money to be stored safely and marshalled for use when and where required.

Without a bank providing these services, business would not be able to develop, payments for goods would not be made, money could not be kept safely for later use. In this sense, banks are like other agents that do not produce goods themselves but help the business deals of others to go ahead.

Global Witness argues in this report that without the involvement of banks, large-scale diversion of natural resource revenues would not be able to take place. Of course, banks are not the only enablers of corruption. Auditors, lawyers, trust and company service providers and the regulatory structures in secrecy jurisdictions are all part of the system that is able to exploit regulatory and enforcement loopholes to move dirty money around the world, and some will play a part in the stories that follow. But for now, in this publication, Global Witness is focusing primarily on the role of banks – and the governments that regulate them.

Of course, like other agents and enablers, banks have a choice in which customers they

provide these services for. These choices can be made on at least two levels: the country, and then the individual person or company.

## Which country?

The country choice, except in extreme cases where sanctions have been applied, such as North Korea, is up to the bank.<sup>25</sup> ‘Country risk’ is one of the key types of risk that is taken into account when banks decide where to do business. It includes an analysis of the economic, political and social factors that may affect the willingness or ability of a government to meet its obligations, or the policy decisions made by a government which may impact on the ability of private individuals or companies to do business in that country. Country risk, as with all of the other types of risk that banks analyse before taking on a client, is about making sure that the bank’s loans are repaid and that its profit stream is assured. While regulators are interested in country risk in the context of its impact on ‘credit risk’ – the risk that money will not be repaid, affecting the bank’s capital ratio – it is not a matter that carries criminal penalties.

What country risk does not include, however, is an analysis of the ethics of doing business with a particular regime, one that, for example, abuses human rights, or one that fails to use its oil windfall to benefit the vast majority of the population. Banks are free, of course, to choose the countries in which to operate based on the ethics of dealing with particular regimes. As this report will show, ethics do not always win when banks make decisions about where to do business, despite the

The most important question that bankers must answer: Who is your customer?



claims in their corporate social responsibility materials to take ethical decisions seriously.

As Chapter 8 will show, for example, some of the banks that have provided oil-backed loans to Angola's state oil company are proud of their relationship with the country, despite the fact that this is a government presiding over the highest levels of child mortality relative to national income in the world, and which persists in refusing to provide transparent and audited information about the fate of its oil revenues.

Global Witness wrote to the world's top 50 banks (as of July 2008) to ask them if they had a policy of prohibiting accounts for heads of state or senior officials or their families from countries with a reputation for large-scale corruption, or even – for what might seem obvious to banks that claim to take their human rights commitments seriously – for heads of state of the world's most repressive regimes.<sup>26</sup>

Only sixteen banks responded: Barclays, Bayerische Hypo-und-Vereinsbank, BNP Paribas, Calyon, Commerzbank, Credit Agricole, Credit Suisse, Danske Bank, Fortis, HSBC, ING, JP Morgan Chase, National Australia Bank, Rabobank, Royal Bank of Scotland, and UBS.<sup>27</sup> Of these, all but one did not explicitly answer this question. Rabobank said that it did not have such policies. Those who replied all elaborated at length about how their policies were of course in line with the anti-money laundering regulations, which require them

to identify accounts of potential corruption concern and perform enhanced checks, and a number mentioned their compliance with sanctions regimes which prevent anyone doing business with certain countries.

But none of these banks have taken a specific policy decision to prohibit accounts from heads of state or senior officials from the most corrupt states, or from the world's most repressive regimes.

### **Which company or individual?**

Then there is the decision about which individual or company to do business with.

**Due diligence** is the process that banks go through in order to decide whether to do business with somebody. It means finding out who your customer is, whether you're loaning them your money, or banking their money. It has always been in banks' interest to do due diligence when making loans and investments, because they need to strictly control the risk that they will not get their money back.

Since the 1980s, however, increasingly stringent anti-money laundering regulations have required banks to do due diligence before accepting customers' money, in an attempt to prevent the proceeds of crime from entering the global financial system. The requirement to do 'know-your-customer' due diligence forms the core of anti-money laundering regulations: who is this customer, can they prove who they say they are, and how did they make their money? If a bank cannot find answers to these questions – which might suggest that the customer is trying to hide their identity, and thus has something to hide – then it should not accept the business. Nor should a bank accept the funds if it suspects that they have been illicitly earned.

The compliance function within banks is responsible for making sure that this happens. As the complexity of the regulations has increased, so has the amount that banks have to spend on compliance systems: specialised compliance staff, training for all other bank staff, database systems to screen potential customers. Meanwhile a huge and lucrative industry of commercial databases, newsletters, conferences and consultants has sprung up around the requirement to know your customer (which now also applies to lawyers, insurers, estate agents and casinos as well as banks). Banks' corporate social responsibility materials all make a big deal out of their compliance with anti-money laundering regulations.

Global Witness has had conversations with a number of compliance officers currently working in banks and the message is usually the same. ‘Compliance officers are paid so that senior management doesn’t receive any surprises,’ one told us. ‘My job is to prevent the sky falling on our heads,’ said another. They clearly understand their importance to the bank.

But the conversations Global Witness has had with other professionals in the industry – external anti-money laundering consultants, lawyers and law enforcement officials, as well as ex-compliance officers – add a different dimension to the story, one which contrasts with the banks’ own public messages. The message that comes through in these conversations is that the compliance function is too far down

the food chain within many banks:

- while the head of compliance may – sometimes – report to a member of the bank’s board, they do not sit on the board;
- it is usually the relationship manager’s job, rather than the compliance officer’s, to ensure that due diligence is done;
- research done by the compliance officer may be overridden by a relationship manager wanting to go ahead with the business.

Too often, they tell us, the pressure not to do due diligence is enormous, and if the bank can find a way to pretend it is not doing business with a politician but with his crony, it will do. In the words of one former insider, ‘as long as senior management is not

Compliance officers say that they are under pressure from the dealmakers in their banks.



told that you're dealing with a scumbucket through his lawyer in, say, Malta, that's ok.'

One former compliance officer told Global Witness: 'From my professional experience, if you speak up as a compliance officer they listen to you but at the end of the day what's going to happen is the business is accepted. There are so many ways to get around and make it look like the funds are not criminal... you set up companies worldwide and move the money around so you can't see where it came from or the business behind it.'

Global Witness has itself been in the extraordinary position of being asked by a major global bank to retract its previously published statements about a businessman with whom the bank wished to do business, but over whom its compliance team had raised concerns.

Global Witness wrote to the world's top 50 banks (as of July 2008) to ask:

- whether the relationship manager or compliance officer is responsible for ensuring that due diligence is done;
- to whom their head of compliance reports;
- what access the head of compliance has to the board;
- what mechanisms are in place for reviewing compliance procedures.

Sixteen banks responded (see page 18).

Of the seven that explicitly answered the first question, six said that the relationship manager was responsible in the first instance for ensuring that due diligence was done and only if there were concerns was it escalated to the compliance function; one of them, Commerzbank, said that the compliance department was responsible.

Of the nine that explicitly answered the second question, two said that the head of compliance reports directly to the CEO, one to the chair of the Executive Board, three to the group general counsel, one to the CFO, one to the Chief Risk Officer, and one to the Group General Manager. Only six banks responded to the question of whether the head of compliance had a seat on the board; the answer from all was no. Twelve of the responding banks answered the question about mechanisms for reviewing compliance procedures: these involved banks' own internal audit functions. Four banks mentioned that their external auditors are involved in reviewing compliance procedures. Thirty four banks did not reply.

### **Is compliance working?**

Global Witness is concerned that even if all the systems are in place as required by the regulations, compliance may too often be a box ticking exercise rather than a real attempt to weed out business that should not be done. 'Due diligence is a lifesaver,' said a finance professional at an offshore industry conference during 2007, in the context of explaining that if you do your due diligence then you'll be in compliance with the growing

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During cross-examination  
**Jean-Didier Maille**, seen here (centre) arriving at court for an 'Angolagate' (see pages 93-94) hearing, commented that "when you're a banker, you have to know how to have blinkers".





Where's the money?  
These dictators (L-R, **Suharto, Marcos, Mobutu and Abacha**) used private bank accounts to hide the profits of their corruption.  
Credits: (L-R) Thierry Orban/Corbis; Bettmann/Corbis; Walter Dhladhla/AP; Reuters/Corbis

### Box 1: Private banking and some of its clients

Private banking is the provision of financial services to wealthy individuals and families. Its watchwords are discretion and personalised service. The whole point of it is secrecy: these are clients that do not want their wealth to be known. This is all very well, but what if the client is in fact a corrupt politician? Private banking poses a particular risk for money laundering partly because it attracts rich clients some of whom will have obtained their money illicitly, but also because the nature of the service is one of close relationships between the client and the private banker, which could potentially result in the banker being unwilling to probe too deeply into the source of funds.

The old systems of international private banking, set up over decades to attend discreetly to the finances of the very rich, had by the 1980s also become a route for the laundering of criminal and corrupt proceeds.<sup>34</sup> From the 1990s the news started to come out: the millions, and perhaps billions, stolen by Ferdinand Marcos in the Philippines, Suharto in Indonesia, and Mobutu Sese Seko in former Zaire, which had made their way into banks in Europe and the US.<sup>35</sup> In 2001, the UK banking regulator, the Financial Services Authority (FSA), found that 23 banks in London, including UK banks and London branches of foreign banks had handled \$1.3 billion of the \$3-5 billion looted from Nigeria by the late dictator Sani Abacha. The FSA did not name the banks involved.<sup>36</sup> Other Abacha funds were located or had been

transferred through banks in Switzerland, Luxembourg, Liechtenstein, Austria and the US.<sup>37</sup> As a consequence, the anti-money laundering regulations now explicitly recognise private banking as a specific risk.

But despite the scandals associated with it, and the ongoing risks posed by some clients, private banking remains an attractive business, particularly when other sources of banking income may be drying up: a 2007 survey of European private banks by McKinsey found that average pre-tax profit margins are 35%.<sup>38</sup> The private banking industry grew by 44% globally during 2007, a year in which the banking industry overall began to take huge hits as the subprime loan market started to unravel. A survey of 398 private banking and wealth management institutions by Euromoney in January 2008 found that private banking assets under management worldwide were up 120% on the previous year to \$7.6 trillion which, as Euromoney pointed out, was equivalent to:

- The combined GDP of France, Germany and the UK
- More than one and a half times the market capitalisation of all the companies listed on the London Stock Exchange in January 2008
- 20 million Ferrari 599s.<sup>39</sup>

If the private banking industry is growing compared to the rest of the banking sector, then the potential risks that it poses become proportionally greater, and require ongoing attention from banks.

flood of overlapping and headache-inducing regulations that apply to the financial industry, and avoid the fines that are meted out in some jurisdictions to banks that do not have a compliance system in place.

Too often, compliance is solely about avoiding reputational risk, rather than a concern not to take corrupt business. When the UK's financial regulator, the Financial Services Authority, visited 16 financial institutions in 2006 to assess their systems to deal with politically exposed persons (PEPs – those who hold public office and therefore could potentially be in a position to divert public funds), it found that banks were defining the reputation risk of PEP business as 'the risk that a PEP might be involved in a public scandal, not that they were actually corrupt. A PEP with a high profile or impending 'whiff' of scandal might be immediately turned away. However a PEP with a lower risk of public controversy may be more likely to be accepted. This risk assessment was *regardless of the source or legitimacy of the PEP's funds.*' It went on to warn: 'Reputational risk and financial crime risk are not the same and steps to mitigate reputational risk will not always reduce financial crime risk.'<sup>28</sup> [emphasis added] What this may show, in Global Witness's view, is that banks are operating on the basis of: if the customer is corrupt, we don't care; what we do care about is being found out to have done business with them.

Compliance provides a safety net: if you can say you've done your due diligence, procured the client's passport, ticked the boxes to say you know your customer, then

you're in compliance with the law, and you're covered. What this means in reality, though, is once the boxes are ticked, you've covered your back, and the question of whether the business in question actually contributes to corruption is of much less interest.

Certainly, the cases outlined in this report – which ought to have raised serious questions at the time of due diligence – suggest, perhaps, that there is strong pressure from the deal-makers and relationship managers to go ahead, even if the research of the compliance department has thrown up concerns.

The story behind the recent fine imposed on Lloyds TSB in the US clearly illustrates the desire by banks to keep doing the business if at all possible, even if concerns have been raised within the bank. In January 2009, Lloyds was fined \$350 million by the American authorities for deliberately 'stripping' customer information from dollar wire transfers made on behalf of Iranian, Libyan and Sudanese banks into the US. Between the mid-1990s and 2007 Lloyds systematically violated US sanctions by removing all information such as customer names, bank names and addresses, on outgoing payments so that they would not be blocked by the US. In the case of Iran, Lloyds had a unit dedicated to manually removing this information.

In 2002 bank staff raised concerns that this process might violate US law. In response Lloyds itself stopped stripping customer information. However, the bank then trained its Iranian customers how to

Oil pipelines near a village in the Niger Delta, whose citizens have seen little benefit from the wealth under their feet. Anti-money laundering regulations haven't prevented rampant looting of Nigeria's oil wealth.  
Credit: George Osodi/  
Panos Pictures



bypass US sanctions for themselves. Between 2002 and 2007 Lloyds transferred \$350 million of Iranian, Libyan and Sudanese money in contravention of US law.<sup>29</sup>

*I would say that one of the things we need to do is make sure that financial institutions, world, global financial institutions... are called to task and held accountable for their role in this criminality ... These people, with their striped suits and their high incomes... are accomplices to criminals... the financial institutions that take that money are accomplices to that crime.*

Dana Rohrabacher Republican Congressman,  
May 2007<sup>32</sup>

In April 2003 Lloyds' Group Executive Committee decided to suspend the US dollar service it provided for Iranian banks. But the bank continued to strip customer information on behalf of Sudanese banks until September 2007.<sup>30</sup> According to press reports there are another nine banks, including Credit Suisse and Barclays, under investigation for violating US sanctions.<sup>31</sup> This case highlights the pressures on banks to continue doing lucrative business if at all possible: Lloyds continued to process payments for sanctioned banks for five years after staff had first questioned the legality of these transfers.

A bank is not a monolith, it consists of many people with different duties. How many people have to NOT say something in order for business such as this to go ahead? It should only take one person to put up their hand and say let's not take this business; but that person has to be empowered to say no, and has to be listened to.

So there are two levels at which banks can make decisions to avoid involvement with corruption – by choosing not to do business with a corrupt or human rights-abusing country, or by choosing not to do business with an individual or company that might be involved in corruption. The country-based decision concerns the ethical character of the bank, and is set – or in some cases, it seems, not set – at director level. In addition, it is determined by current sanctions regimes. Meanwhile the day-to-day frontline decisions about individuals are backstopped by an assessment by a compliance officer in the bank.

The compliance officer does not get into a macro level judgment about doing business with a country per se, but deals with individual names that come up. The compliance officer's job is already difficult, because he or she may have to argue against the relationship manager, whose career benefits if the deal goes ahead. But if there is no culture being set from the top of the bank on avoiding business with unethical regimes that refuse to account transparently for their natural resource revenues, then it becomes even more difficult for the compliance department to argue against a particular piece of business.

This brings us to the final perspective from which the cases in this report will be analysed. Each case looks at not only the bank's ethical policy about what kind of regimes it will deal with, and the likelihood that the bank has sufficiently investigated the identity of its customer and their source of funds as required by its regulator, but also examines whether the regulators have themselves taken action. With the example of Riggs, there was a clear dereliction of the regulator's duty. In many other stories presented here, such as the account held in Hong Kong by Denis Christel Sassou Nguesso's shell company (see Chapter 5), the regulator concerned has not been permitted to tell Global Witness whether or not it has taken any action. And in some cases, such as Deutsche Bank and its Turkmenistan accounts, there has been no unprompted action from regulators because the regulations that they are responsible for enforcing do not yet cover the issue in question: in this case, the question of state accounts from a state that has been captured by one person.

Now we are going to go on a journey, to the oil-producing countries of the Gulf of Guinea as well as to Central Asia, to witness the corrosive and devastating effects of banks being willing to do business with corrupt regimes. With each story, the effectiveness of the bank's ethical standards, compliance with due diligence requirements, and regulatory action will be examined, as far as the available evidence permits. Many of the examples in this report raise serious questions about how well a bank really knew its customer, even if it had been able to tick the regulatory box to say it had done its due diligence; and about whether compliance with the letter of regulations that require identification of the customer is sufficient to prevent banks doing business that contributes to corruption.

## Box 2: How the anti-money laundering laws are supposed to work

Money laundering is the process by which the proceeds of crime are disguised so that they can be used without being detected. In order for money laundering to take place, there needs to have been a crime in the first place, which has produced a profit: the proceeds of crime. This initial crime is referred to as the predicate offence. In the case of corruption, the predicate offence is usually stealing or misappropriating state funds, or accepting a bribe.

Money laundering involves three stages: placement, where the money is moved into the financial system; layering, where it is moved via a series of transactions to break the link with its origins and make it harder to trace; then integration, where it is used or invested by the criminal once its origins have been disguised. The easiest of the three stages to detect is the placement stage, when the money is moved into the financial system for the first time.

This is why financial institutions have been put in the front line of money laundering prevention. Because the money has to be introduced to the financial system, often through them, they have been given the responsibility of checking where it comes from.

The principle behind the anti-money laundering laws which, with national variations, exist in most countries is that banks and other financial institutions (and these days, lawyers, estate agents, and insurers too) are required to find out the identity of their customer, and the source of their customer's funds. If the customer is a company or a legal entity such as a trust, they must do due diligence to find out who is the 'beneficial owner' – the person at the top of the ownership chain (as opposed to another company) who really controls the funds. If they cannot do this, they should not accept the customer. If they have concerns that the funds might be the proceeds of crime, they should submit a 'suspicious activity report' (SAR) to the national law enforcement authorities – without tipping off the customer that they are doing so.

Certain categories of customer are deemed higher risk. Those who pose the greatest risk of bringing corrupt funds to a bank are 'politically exposed persons' or PEPs. A PEP is a senior government official, as well as his or her family members and associates, who could, as a result of his or her position, potentially have access to state funds or could be in a position to take bribes. To say that somebody is a PEP is not to say that they are corrupt; the head of every state in the world is a PEP, for example. It simply means that there is potentially a greater risk that this customer could have acquired their funds corruptly.

Anti-money laundering regulations require banks to take measures to identify PEPs, then subject them to 'enhanced due diligence' on their source of funds and to ongoing scrutiny of transactions through their account, with senior management approval required within the bank in order for the account to be opened.<sup>33</sup> This means that banks are not prohibited from taking PEP accounts, but they should establish whether there is a risk of corruption associated with that person, and should not accept the account or a particular transaction (and should file a SAR) if they believe the funds may be corruptly acquired.

Anti-money laundering laws were not originally designed to stop the proceeds of corruption. They were initially imposed in the 1980s, led by the US, as part of the 'war on drugs', in an attempt to prevent drug traffickers moving their profits through the financial system. They were later broadened to include other organised crime and corruption, and after 9/11, terrorist finance.

Anti-money laundering laws are imposed in each jurisdiction by national governments, and compliance with them is monitored by national regulators. But at the international level, an inter-governmental body called the Financial Action Task Force (FATF) sets the global standards for what anti-money laundering laws should look like, in the form of its 40 Recommendations, last updated in 2003. The latest version is called the 40+9 Recommendations, and includes nine recommendations specifically on avoiding funds destined for terrorist finance.

Broadly, the FATF recommendations cover five basic obligations for states:

- Criminalise the laundering of the proceeds of serious crimes and enact laws to seize and confiscate them
- Oblige financial institutions to identify all clients, including all beneficial owners of financial property, and to keep appropriate records
- Require financial institutions to report suspicious transactions to national authorities
- Put into place adequate systems to control and supervise financial institutions
- Enter into agreements to permit each jurisdiction to provide international cooperation on exchange of financial information and other evidence in cases involving financial crime

FATF members perform ‘mutual evaluations’ on each other, to assess whether each jurisdiction is in compliance with the 40+9 Recommendations. FATF also produces ‘typologies’, or analyses of particular money laundering techniques, based on real case studies, to help banks identify when such techniques are being used.

FATF has 34 members, largely the world’s richest countries. Other countries are members of ‘FATF-style regional bodies’ for Europe, Eurasia, the Middle East and North Africa, Asia/Pacific, Eastern and Southern Africa, West Africa, the Caribbean and South America.

Outside of finance ministries, FATF is a little-known organisation with a tiny secretariat based at the OECD in Paris. Driven by its key members, particularly the rich OECD nations that are home to some of the world’s largest financial centres, it is largely responsible for the fact that there are now anti-money laundering laws of some form or another in the majority of countries in the world – although, as this report will discuss, the question of whether they are effectively implemented is quite another matter.

FATF is the best option available to the international community for ensuring



A US drug enforcement agent and her haul. Anti-money laundering laws were originally designed to fight the ‘war on drugs’, not to tackle corruption.  
Credit: J. Pat Carter/AP

that the money laundering laws in each jurisdiction are of a sufficient standard – and, crucially, are being implemented and enforced to a sufficient standard – in order to prevent flows of corrupt funds out of the developing world.

But it has four serious weaknesses that must be tackled before it can do this effectively. None of these weaknesses are inherent in FATF’s structure. They can be tackled with the political will of its member states.

1. FATF has no legal enforcement powers of its own, due to its status as an intergovernmental body that consists of its member states. But although it has no official sanction powers, it is not even sufficiently using the non-legal powers that are at its disposal: naming and shaming, and public pressure.
2. FATF appears to operate in isolation from many of the other actors who are working on anti-corruption efforts.
3. FATF’s focus on terrorist financing has not been matched by equal attention to the fight against corrupt funds, and might even have distracted from it.
4. There are loopholes in the standards that FATF promotes, which means that the anti-money laundering framework that it is promoting is not sufficient to curtail the flows of corrupt money.

These weaknesses – and Global Witness’s proposed solutions – are discussed in more detail in Chapter 9 on page 105.

# 03

# RIGGS BANK AND EQUATORIAL GUINEA

## Doing business with heads of state

(Plus: Where did Equatorial Guinea's oil money go after the demise of Riggs?)

"How best we can serve you": Riggs bosses, seen here testifying before a Senate committee, were obsequious in their treatment of Equatorial Guinea's dictator, Teodoro Obiang. They failed their due diligence responsibilities in their eagerness to bank Equatorial Guinea's oil wealth.  
Credit: Denis Cook/AP



Riggs Bank provides the ultimate textbook example of failure to conduct due diligence on politically exposed persons. The Washington bank, an august institution which had banked for Abraham Lincoln and billed itself as the bank of presidents, fell apart in 2004 after a US Senate committee investigation and federal criminal investigators found it had been holding accounts for President Obiang of Equatorial Guinea, his family members, and his corrupt government, as well as for Augusto Pinochet, the former Chilean dictator.<sup>40</sup>

Riggs was hit with a \$25 million civil fine from its regulators in May 2004 for failure to implement money laundering regulations, and pleaded guilty in January 2005 to federal criminal charges of failing to file suspicious

activity reports, agreeing to a \$16 million criminal fine.<sup>41</sup> In 2005 the bank was sold off, at a discount, to PNC Financial Services Group in Pennsylvania, and the Riggs name disappeared. Between PNC's first offer in 2004, and the final agreed discounted price in 2005, twenty per cent of shareholder value, or about \$130 million, was lost.<sup>42</sup>

The story of what happened – of how Riggs ignored recently-tightened money laundering regulations, turned a blind eye to evidence of foreign corruption, and allowed suspicious transactions to take place without reporting them to law enforcement – is the bogeyman story now used worldwide to train bank compliance officers about the risks of doing business with politically exposed persons.

The oil wealth of Equatorial Guinea has made little difference to the country's grinding poverty. Credit: Robert Grossman/Africaphotos.com



### Box 3: Equatorial Guinea

Equatorial Guinea is a tiny coastal country in West Africa, sandwiched between Cameroon and Gabon, with a population of only half a million. Over the last decade it has become Africa's third largest oil exporter, with an economy that until 2006 was growing at an average rate of 37% per year<sup>43</sup> and annual oil revenues of around \$3.7 billion.<sup>44</sup> Per capita, it should be one of the richest countries in the world. But this is far from the case: the majority of the population still lives in miserable poverty. 'An urgent priority is to ensure that... an emphasis is placed on human resource development. Progress in alleviating poverty and meeting the Millennium Development Goals has been slow,' wrote the IMF in May 2008.<sup>45</sup> Life expectancy was only 50 in 2005.<sup>46</sup>

Management of the country's vast oil wealth remains a 'state secret' according to President Teodoro Nguema Obiang. He has ruled since 1979 when he executed his brutal uncle to seize power, and has maintained his power through repression and human rights abuses. Members of Obiang's family control key government ministries. Opposition parties are banned, and political prisoners are beaten and tortured in custody.<sup>47</sup>

In March 2008, Saturnino Ngogo Mbomio, a member of a banned political party, died in police custody after being tortured. Other political detainees were held without charge.<sup>48</sup> Mass forced evictions have been carried out when the government wants access to land. Hundreds of homes were destroyed in the capital Malabo in 2006, with no consultation or compensation.<sup>49</sup>

Freedom House rates Equatorial Guinea near the bottom of its survey of repressive countries, above only Burma, Cuba, Libya, North Korea, Somalia, Sudan, Turkmenistan and Uzbekistan, for offering 'very limited scope for private discussion while severely suppressing opposition political activity, impeding independent organising, and censoring or punishing criticism of the state'.<sup>50</sup>

Meanwhile, the ruling family continues to enrich itself. At the end of 2006 Global Witness revealed that the president's playboy son had bought a new \$35 million dollar home in California. He has been reported as earning a \$4,000 a month salary as the country's Minister of Agriculture and Forestry.<sup>51</sup>

The rest of the banking industry tends to view Riggs as a special case, because of the high number of foreign embassy accounts which led to high risk business, and therefore does not see it as particularly applicable to other banks.

With its high number of embassy accounts, Riggs was indeed in some ways a special case, but that does not mean it should be relegated to the 'history' section at the back of compliance handbooks. The first reason for this is that the Riggs case is a startling illustration of failures at each of the levels examined throughout this report: the bank's ethical culture; the bank's compliance system; and the action of the regulators. It is unusual to be granted a view inside a bank, to see how records are kept – or not – on high profile customers, how decisions are made and who makes them. As a result of Riggs' meltdown, it all came out: a detailed anatomy of how a bank helped members of corrupt resource-rich government to siphon off oil funds for their own benefit.

But this is not the main reason that we are revisiting the Riggs story here. Despite the huge scandal caused by Riggs banking for Equatorial Guinea and its rulers, significant

and disturbing questions still linger about where the Equatorial Guinea oil money has gone, how banking secrecy laws have impeded the tracking of its progress, and whether the regulators have since upped their game. These questions are relevant for other banks and their regulators, as well as governments.

### **Failures at Riggs: no ethical culture, a complete failure of compliance systems, and breaking its own rules**

News that Riggs was holding Equatorial Guinea's oil money, in accounts under the personal control of the president, was first broken by the *Los Angeles Times* and Global Witness in January 2003.<sup>52</sup> In March 2004, the Global Witness report *Time for Transparency* reported a conversation with the Equatoguinean ministers of the Treasury, and Departments of Justice and Energy, in which they said that the oil money was indeed held offshore, partly because the Treasury building is not secure and lacks a safe. The report also showed that Simon Kareri, the account manager at Riggs, had helped Obiang and his family members to buy two mansions in Maryland and a townhouse in Virginia.<sup>53</sup> Neither Riggs nor Kareri responded.

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Riggs Bank in Washington DC was brought down as a result of accounts it held for President Obiang of Equatorial Guinea and Augusto Pinochet, the former Chilean dictator.





One of the houses near Washington DC that the Obiang family bought with the help of **Simon Kareri**, the Equatorial Guinea account manager at Riggs.

*Credit: Global Witness*

Four months later, in July 2004, the US Senate Permanent Subcommittee on Investigations released a damning report into the failures at Riggs. With subpoena powers, the Senate investigators had sifted through boxes of paperwork from the bank to find out the real dimensions of its relationship with Equatorial Guinea. The contents of the report were incendiary, complete with picaresque details such as the Equatorial Guinea account manager, Simon Kareri, carrying suitcases of cash into the bank for deposit. Kareri himself later pleaded guilty to fraud and conspiracy after diverting more than a million dollars into his own accounts, and was sentenced to 18 months' imprisonment.<sup>54</sup>

Between 1995 and 2004, Riggs Bank administered over 60 accounts for senior members of the Equatoguinean government with total deposits of between \$400 and \$700 million at any one time.<sup>55</sup> Without conducting any due diligence to ascertain how state officials had acquired such enormous wealth, Riggs opened personal accounts for President Obiang himself, his wife, and other relatives. The bank also helped establish offshore shell companies for Obiang and his sons. Over a three year period, from 2000 to 2002, Riggs accepted nearly \$13 million in cash deposits into accounts controlled by the president and his wife.<sup>56</sup>

On one occasion, the bank accepted without due diligence a \$3 million cash deposit into an

account of one of Obiang's offshore shell companies.<sup>57</sup> On another, Riggs opened an account for the Equatoguinean government to receive funds directly from oil companies, allowing withdrawals with only two authorising signatures – one from Obiang and another from his son or his nephew. Riggs then allowed \$35 million to be wired from this account to two unknown companies which had accounts in jurisdictions with bank secrecy laws.<sup>58</sup>

This was not a case of junior staff failing to do their job properly. The senior management were well aware of the Equatorial Guinea accounts, and met with Obiang or his officials on a number of occasions. A letter to Obiang in May 2001, signed by Riggs' chairman, CEO, another bank president and the Equatorial Guinea account manager, says:

‘We would like to thank you for the opportunity you granted to us in hosting a luncheon in your honor here at Riggs Bank. We sincerely enjoyed the discussions and especially learning about the developments taking place in Equatorial Guinea... Following your request to us to serve as Financial Advisors to you and the Government of Equatorial Guinea, we have formed a committee of the most senior officers of Riggs Bank that will meet regularly to discuss our relationship with Equatorial Guinea and how best we can serve you.’<sup>59</sup>

Other internal bank documents that emerged from the investigation included:

- A memo between bank staff from 2001 calling for a meeting to discuss the growing funds in the Equatorial Guinea accounts. ‘Where is this money coming from? Oil – black gold – Texas tea!’ one of them gloats.<sup>60</sup>
- A memo from Simon Kareri, who handled the Equatorial Guinea accounts, to Larry Hebert, his boss, following a media article about President Obiang’s corruption. Kareri claims:

‘Regarding the issue of the President of Equatorial Guinea being corrupt, I take exception to that because I know this person quite well. We have reviewed... the transactions of Equatorial Guinea with Riggs since inception and not once did Riggs send money to any ‘shady’ entity or destination.’<sup>61</sup>

Karerri wrote this on 12 December 2002, by which time the majority of the transfers from the Equatorial Guinea accounts that were later identified by the Senate report as suspicious had already taken place.

- Documents relating to President Obiang’s personally-owned offshore shell corporation, Otong SA, which received deposits of \$11.5 million. Currency transaction reports filed by the bank, in accordance

with regulations requiring them to be submitted for any transaction over \$10,000, mis-characterised Otong as making its profits from timber, although bank staff knew that it belonged to the President himself.<sup>62</sup> No suspicious activity reports were ever filed despite millions of dollars being paid into the accounts of an offshore corporation owned by Obiang.<sup>63</sup>

Belatedly, once the Senate investigators were already on its back in January 2004, Riggs did file a suspicious activity report relating to Otong, which Global Witness has seen. It reveals the extraordinary after-the-fact reason given by the bank to justify suspicious money movements into the Otong account. The SAR reports seven cash deposits between September 1999 and April 2002, totalling \$11.5 million. They had been made by the Equatoguinean ambassador in Washington, and the explanation given by Michael Parris, of Riggs’ embassy banking division, was that ‘the cash deposits were made with funds the president received from closing CD’s [certificates of deposit] in foreign banks, and not wanting those banks to know where he was re-depositing the money, he opted not to conduct wire transfers, rather, maintain the funds in cash to avoid calls from would-be marketers looking for reinvestment opportunities.’<sup>64</sup>

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According to US Senate investigators **President Obiang**, pictured here, may have owned companies whose bank accounts at HSBC in Luxembourg and Banco Santander in Spain received suspicious transfers of millions of dollars from the Equatorial Guinea oil accounts at Riggs.

*Credit: International COVER*





Despite the collapse of the US bank Riggs in a huge corruption scandal, the people of Equatorial Guinea still do not know which bank now holds most of the country's offshore oil funds.

It seems highly unlikely that Riggs had an organisational ethical culture of not doing business with unpleasant regimes such as Equatorial Guinea's. At the regulatory compliance level, the bank also failed miserably. The Senate investigators concluded that the Equatorial Guinea accounts were not aberrations but 'the product of a dysfunctional AML program with long-standing, major deficiencies,' including an inability readily to identify all the accounts associated with a particular client, absence of any risk assessment system to identify high risk accounts, and inadequate client information.<sup>65</sup> Any know-your-customer policies the bank did have were not implemented; the bank did not even follow its own rules.

### **Failures by the regulators**

The bank's internal systems were not the only controls that failed in the face of a powerful client. The next line of defence should have been the regulators. Located in the centre of Washington, Riggs was about as close as it was possible to be to the centre of regulatory power, in the country that has done most to push banks' anti-money laundering responsibilities. Yet it was able to get away with having deficient systems for several years. From 1997, examiners from its primary regulator, the US Office of the Comptroller of

the Currency (OCC) had repeatedly reported major anti-money-laundering deficiencies at Riggs, which Riggs repeatedly failed to correct. Yet no further action was taken.<sup>66</sup>

Even more seriously, they were overruled by their superiors. The senior OCC Examiner-in-Charge for Riggs, R. Ashley Lee, was found by the Senate investigators 'to have become more of an advocate of the bank than an arms-length regulator.'<sup>67</sup> In 2002 Lee ordered colleagues not to include a memo on the Pinochet investigation in the OCC's database. After failing to take action during 2001 and 2002 for anti-money laundering deficiencies at Riggs, he was then hired by the bank, creating an obvious conflict of interest. The OCC acknowledged 'there was a failure of supervision' and 'we gave the bank too much time'.<sup>68</sup>

The Senate investigators concluded that this was not just an isolated failure by federal regulators. The General Accounting Office (the US government's audit office) had identified a number of other occasions where regulators had failed to take action despite persistent and repeated failure to address anti-money laundering failures at other banks.<sup>69</sup> In July 2005 an internal OCC review also criticised the fact that the OCC directed insufficient resources to anti-money laundering compliance.<sup>70</sup>

Riggs bosses (from left), Lawrence Hebert, Raymond Lund, and R. Ashley Lee, testify before a Senate committee. Credit: Dennis Cook/AP



Global Witness asked the OCC if the Riggs debacle had changed the way it oversaw banks' anti-money laundering systems. A spokesperson said that the OCC had performed a 'top down scrub internally', and that 'we've really changed, we're almost a different organisation, it was a priority of the new comptroller' [John Dugan, who came in during 2005]. All bank examiners, whether or not they are money laundering experts, have received extra training on anti money laundering issues, to enable them to spot problems and bring an expert examiner in if necessary. There is also a mandatory 'cooling off' period of one year before regulators can take up a post with a bank. Other changes to how the OCC supervises banks, however, are part of the broader tightening up of regulations as a result of the 2001 US Patriot Act, and are not so much a result of Riggs. Banks are now provided each year with the latest Bank Secrecy Act manual, which clearly sets out their regulatory obligations and how their regulators expect these to be met, whereas before, said the OCC spokesman, 'all the different regulatory agencies were going at this unilaterally, which was perplexing for the banks'.<sup>71</sup>

### Failure to find the money 1:

#### **What happened to the Equatorial Guinea money left in Riggs when it closed the accounts?**

However, the question of what happened to Equatorial Guinea's oil money remains. When the accounts were closed there was about \$700 million left in the Equatorial Guinea accounts at Riggs.<sup>72</sup> This could make a huge difference to development in Equatorial Guinea; for example, it would take only \$17 million to provide essential medical care for the whole population.<sup>73</sup> But where is this \$700 million of state funds now?

Riggs closed the Equatorial Guinea accounts shortly before the publication of the Senate report in July 2004. *Harpers* magazine reported two years later that they had been taken by Independence Federal Savings Bank in DC.<sup>74</sup> However, Global Witness sources in a position to know have said that this did not in fact go ahead. Global Witness wrote to Independence Federal Savings Bank asking if it could confirm if it took the Equatorial Guinea accounts; it did not reply. Other sources, unconfirmed, have suggested that the money went to banks in France, Germany, Switzerland or South Africa.

That \$700 million has now grown threefold. And despite what happened to Riggs, it is still being kept in commercial banks outside of Equatorial Guinea. According to a recent IMF report, as of 2006 Equatorial Guinea was keeping \$2.1 billion of its government revenues in commercial banks abroad, some in actively managed accounts and some in conventional deposit accounts. This figure was projected to rise to nearly \$3 billion in 2007, and to \$5.4 billion by 2011.<sup>75</sup>

Other funds are kept in the Bank of Central African states (BEAC, in its French acronym), a regional bank in Cameroon that holds treasury accounts. According to the IMF, the Equatoguinean authorities are concerned about the low rate of interest their deposits receive at the BEAC, and have said they will remit the funds currently held abroad once CEMAC (Economic and Monetary Community of West Africa) undertakes reforms that would increase the amounts that BEAC deposits can earn.<sup>76</sup>

But in the meantime, what due diligence are these commercial banks, wherever they are, doing on payments from the accounts, in order to ensure that state funds are not continuing to be diverted? Who are the signatories on the accounts? Crucially, which and where are these banks? How well are they regulated? How are their regulators ensuring that sufficient due diligence is being done?

It seems quite extraordinary that despite a credible investigation publicly identifying corrupt oil funds in a bank, and the bank having foundered as a consequence, that the people of Equatorial Guinea still do not know where a large chunk of their oil money is being held, and whether there is sufficient oversight. While the IMF has publicly reported that more than \$2 billion of Equatorial Guinea's oil money is held abroad in commercial banks, it has not identified these banks. Given the history of poor management of Equatorial Guinea's oil funds, if the IMF knows where this money is, it should say so. This would help to increase public pressure for accountability over the funds.

## Failure to find the money 2:

### **What happened to the suspicious transactions made out of the Equatorial Guinea accounts at Riggs?**

Further serious questions relate to the destination of funds that had been transferred

out of the Equatorial Guinea accounts by Riggs. These 'suspicious' wire transfers, as the Senate investigators put it, included three transfers totalling more than a million dollars to the account of a company called Jadini Holdings, owned by the wife of the Equatorial Guinea account manager at Riggs, and three transfers totalling nearly \$500,000 that were sent to the personal bank accounts of a senior Equatoguinean official. They also included suspicious transfers to accounts of companies unknown to Riggs:

- 16 transfers worth \$26.5 million to the account of a company called Kalunga Co. SA at Banco Santander in Madrid, between June 2000 and December 2003;
- Another ten transfers worth \$8.1 million to the accounts of a company called Apexside Trading Ltd, nine of them at Credit Commercial de France in Luxembourg, and one at HSBC in Luxembourg, between July 2000 and August 2001.
- Transfers had also been made to the account of another company (which remained unnamed by the Senate report) at HSBC in Cyprus.<sup>77</sup>

These transfers were suspicious because they raised the possibility that Obiang or his associates were moving millions of dollars of Equatorial Guinea's oil money out of Riggs.

The Senate investigators said they had 'reason to believe' at least one of Apexside and Kalunga 'may be owned in whole or in part' by President Obiang.<sup>78</sup>

The first question is: what due diligence did Banco Santander, HSBC and Credit Commercial de France (owned by HSBC since July 2000, the date of the first Apexside transfer) do in order to identify the ultimate beneficial owners of these companies when the accounts were opened? Did they find out who the beneficial owners were? If not, why did they open the accounts? The next question is: did they submit suspicious activity reports related to these huge payments from the Equatorial Guinea oil accounts at Riggs? Global Witness wrote to HSBC and Banco Santander to ask these questions; HSBC said it could not answer them because of confidentiality; Banco Santander did not reply to this letter, although it did reply to a subsequent letter that posed related questions, see below.<sup>79</sup>

Global Witness wrote to Luxembourg's regulator, the Commission du Surveillance du Secteur Financier, to ask whether it had investigated this matter and if so what action was taken, and whether Credit Commercial de France or HSBC made any suspicious activity reports regarding these transfers. It replied to say that it could not respond.<sup>80</sup>

The Spanish media reported in April 2005 that an investigation by the Spanish public prosecutor for anti-corruption into alleged money laundering by Banco Santander's president Emilio Botín and its CEO Alfredo Saénz relating to the Kalunga transfers from Riggs had been closed due to lack of evidence. According to the media reports, Banco Santander had on its own initiative made suspicious activity reports about the transactions to SEPBLAC, the Spanish financial intelligence unit, and had subsequently responded to requests from SEPBLAC for further information. It also, according to the reports, provided the necessary information so that SEPBLAC could respond to a request for information from the New York District Attorney in September 2004.<sup>81</sup>

The public prosecutor's office confirmed to Global Witness that this investigation had

indeed been closed.<sup>82</sup> Global Witness asked SEPBLAC to confirm if Banco Santander had, as reported in the media, filed suspicious activity reports to SEPBLAC, responded to a request for further information about Kalunga, and provided information so SEPBLAC could respond to enquiries from the New York District Attorney's office. We also asked SEPBLAC if it had investigated the matter and if so, what action had been taken. SEPBLAC replied to say that it could not respond to these questions.<sup>83</sup>

In October 2008, a criminal complaint was submitted to the public prosecutor in Spain by the NGO Asociación Pro Derechos Humanos de España (APDHE), alleging money laundering by senior Equatoguinean officials and their family members. The complaint summarised the findings of the US Senate Subcommittee's report on Riggs, and alleged that the money paid to the Kalunga account was used to buy properties in Spain:

'The Subcommittee concluded that Riggs Bank had failed to comply with its anti-money laundering obligations in connection with certain transactions relating to the accounts held by Equatorial Guinea and that, without any room for doubt, such transactions had their criminally unlawful

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Ordinary citizens are still waiting for development. One in five children in Equatorial Guinea dies before their fifth birthday.  
Credit: Christine Nesbitt/AP



origin in corruption practices (embezzlement) in that country.

'During the course of the investigation, it was discovered how, over a period of three years, various transfers had been made from the Equatorial Guinea Oil Account at Riggs Bank... to an account in the name of the company Kalunga Company S.A. held at a branch of Banco Santander in Madrid, in the amount of 26,483,982.57 U.S. dollars.

This "laundered" money was apparently used by the Equatorial Guinean personalities and their families for their own benefit, for the acquisition of properties in various Spanish provinces.<sup>84</sup>

Global Witness offered Banco Santander the opportunity to comment on the media reports about the closure of the case in 2005 as well as the new complaint submitted by APDHE, and asked if it could confirm whether it had made any suspicious activity reports. It did respond to this letter, saying that it was aware of these media reports and did not have any comment or clarification, and that Spanish law prevented it providing any other confirmation. It added, 'I reassure you that in connection with the transactions investigated by the US Senate Permanent Subcommittee, Banco Santander complied in full not only with all its internal manuals and procedures but also with all Spanish Anti Money Laundering laws and regulations, before, during and after the investigations by the Subcommittee.'<sup>85</sup>

The second question is: what due diligence were these banks required to do by their regulators? Global Witness has a number of concerns about the effectiveness of FATF (see Chapter 9 on page 105), but even by FATF's current standards, Spain and Luxembourg's regulatory regimes have failed to achieve compliance with FATF's Recommendations.

In 2006, Spain was found only partially compliant with the crucial FATF Recommendation 5 on customer due diligence, which is what is at issue here. The comment on 'identification of beneficial owners' was that 'financial institutions are left with very general and imprecise requirements (this raises the issue of effective implementation of the requirement)'. It also noted that 'there is no legislation that requires reporting financial institutions to refuse to establish a customer relationship or carry out a transaction if customer identification

(including beneficial owner identification) cannot be carried out'.<sup>87</sup>

When Luxembourg's anti-money laundering controls were evaluated by the IMF in 2004, the legal requirement to identify customers was found to be 'generally in line with international standards,' but that 'given the variety of structures operated in and from Luxembourg to legally separate the apparent from the real ownership of bank accounts and other assets managed by financial professionals there, identification of the true beneficial owner in each case, as required by law, can present a difficult challenge... this is an important risk factor ... and a threat to the reputation of Luxembourg.' There were also ongoing risks with customer due diligence on accounts opened by 'lawyers, notaries, accountants, auditors and other such professionals... given the scale and importance in Luxembourg of business sourced through these professionals...'<sup>88</sup>

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*I'm not sure that banks understand just how much corruption money there is. They don't want to understand, they don't want to find out.*

Anti-money laundering expert, 2008<sup>86</sup>

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So there are question marks hanging over the issue of customer due diligence standards in Spain and Luxembourg. But that is not the only problem. Even more disturbing is the impact of bank secrecy in these jurisdictions.

Once the questioning from the Senate investigators started, Riggs wrote under Section 314 of the Patriot Act to Banco Santander and HSBC USA, asking them to share information about the beneficial owners of these accounts.<sup>89</sup> But both banks said they could not provide this information, because the accounts were opened at their affiliates in Spain, for Banco Santander, and Luxembourg and Cyprus, for HSBC. Bank secrecy laws in these jurisdictions, they both said, barred disclosure of information not only to third parties, but to staff of the same bank who were outside that country.<sup>90</sup>

So banks which have received transfers identified in another jurisdiction as suspicious are able to shelter behind bank secrecy laws and refuse to identify the account owners, even to their own branches elsewhere. This is an extraordinary situation.

These secrecy laws do not only impede the tracking down of money that has already gone. As the Senate investigators commented, ‘The position taken by Banco Santander and HSBC USA means, in essence, that banks in the United States attempting to do due diligence on large wire transfers to protect against money laundering are unable to find out from their own foreign affiliates key account information. This bar on disclosure across international lines, even within the same financial institution, presents a significant obstacle to US anti-money laundering efforts.’<sup>92</sup>

This raises a disturbing question, applicable not just to US anti-money laundering efforts, but globally. How can banks say they are doing their due diligence, as required by anti-money laundering laws, when their subsidiaries operate in jurisdictions with banking secrecy laws?

It means that not only can they not find out the identity of account owners in other jurisdictions to whom they might be requested to transfer funds, as identified in the quote

from the Senate investigators above, but also that they cannot ensure that their foreign branches are upholding sufficient standards.

Effectively, a bank has a correspondent relationship with each of its branches in other jurisdictions.<sup>93</sup> A correspondent bank is one which holds an account for another bank, allowing the second bank to provide services to its customers in a country in which it does not itself have a presence. A bank cannot know who all of its correspondent bank’s individual customers are, which makes correspondent relationships a higher risk for money laundering. The regulations therefore recognise this: FATF Recommendation 7 requires countries to require their banks to collect enough information to fully understand their correspondent’s business, and to assess the quality of its anti-money laundering controls and how well it is supervised.<sup>94</sup>

Under US law the responsibility of a US bank is to assure itself that its correspondent banks have appropriate due diligence procedures.<sup>95</sup> So to take the example of the Apexside transfers from the Equatorial Guinea account at Riggs:



- HSBC USA has accepted HSBC Luxembourg as a correspondent client.
- HSBC Luxembourg has a client, Apexside, over whom serious questions have been raised in the US regarding the source of its funds (ie a state's oil revenue, potentially diverted by its president), and the identity of its beneficial owner (potentially the president of Equatorial Guinea) to the point where HSBC USA might not be able to accept this client.
- HSBC USA cannot, however, find out about this client, and who its ultimate owner is, from its own branch in Luxembourg.

How, then, can HSBC US claim to know its correspondent bank HSBC Luxembourg – which is effectively a correspondent client because HSBC US holds accounts for it – if it has no means of finding out who HSBC Luxembourg's clients are? And how can it assess how effective HSBC Luxembourg's due diligence is when it cannot find out anything about the clients that it chooses to take? They're playing the jurisdiction game with

their own branch standards,' one US banking expert told Global Witness. 'When you have cases that indicate different sets of standards, how can you accept their standards, yet say you're upholding the higher standards?'

Global Witness wrote to HSBC to ask on what basis HSBC USA can claim to know its correspondent customer HSBC Luxembourg, when, according to bank secrecy laws which prevent the sharing of information, it has no means of finding out who HSBC Luxembourg's clients are.

HSBC did not answer this, stating only that 'We did [...] cooperate fully with the relevant Senate Subcommittee. This cooperation included providing guidance to them as to how to make cross-border information requests in respect of non-US accounts. It is a common principle of banking relationships worldwide that banks are subject to strict duties of confidentiality and can supply information to third parties only with customer consent or pursuant to a formal request from legally competent authorities.'<sup>96</sup> The equivalent question was posed to Banco Santander,



Gagged by bank secrecy: laws in some jurisdictions prevent bankers revealing the owners of accounts – including to their colleagues in overseas branches of the same bank. This prevents effective cross border due diligence being done.

which did not reply to that letter.<sup>97</sup> The standards articulated by the Wolfsberg Group, a voluntary grouping of 11 banks which sets standards for customer due diligence, and of which HSBC currently holds the chair – say nothing about this problem.

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*As the ability to move capital has speeded up the ability of tax collectors and law enforcement has not kept pace. The regulators are in the position of police on a freeway without a speed limit using bicycles to stop Ferraris.*

Jack Blum, lawyer and money laundering expert, in testimony before the US Senate Committee on Finance, 24 July 2008<sup>98</sup>

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Interestingly, FATF Recommendation 4 requires countries to ensure that financial institution secrecy laws do not inhibit implementation of the FATF recommendations – which include the requirement to do due diligence on your correspondent banking clients. When Luxembourg was evaluated in 2004 (against the previous version of the FATF recommendations, which were updated in 2003), it was found to be ‘largely compliant’ with the equivalent recommendation, although it was noted that ‘further steps are needed to ensure that secrecy laws do not inhibit effective implementation of AML/CFT measures.’<sup>99</sup> When Spain received its latest FATF mutual evaluation in June 2006, it was found to be compliant with Recommendation 4.<sup>100</sup>

What is going on here? Global Witness wonders how seriously FATF is taking its responsibilities to create an effective global network of anti-money laundering laws. It has given full marks on banking secrecy laws to one key member state, Spain, in which a bank has recently invoked these laws to hinder an inquiry into evident corruption. Buried deep in a report, it has rapped another key member state, Luxembourg, lightly over the knuckles for needing ‘further steps’ when it too plays host to a bank that has done the same. FATF claims to evaluate both the laws and their implementation,<sup>100</sup> but in these cases, the implementation part of the story seems to have fallen by the wayside.

Of course, requests from one branch of a bank to another branch abroad are not the only way for information to travel across borders, although they are perhaps the most important for prevention of money laundering. Other

processes are available when money needs to be tracked down. Financial Intelligence Units (FIUs) – the national agencies responsible for receiving suspicious activity reports from banks and passing them on to law enforcement – are able to exchange intelligence internationally, and the Egmont Group, their membership organisation, has a set of principles for them to do so.

Meanwhile, law enforcement officers seeking evidence for prosecution or asset forfeiture can request information from other jurisdictions in a process known as Mutual Legal Assistance. This can be facilitated either by bilateral mutual legal assistance treaties (MLATs) or through multilateral treaties such as the UN Convention against Corruption and the OECD Convention on Combating Bribery, both of which prohibit their signatories from denying mutual legal assistance on the grounds of bank secrecy.<sup>101</sup> However, anecdotal stories abound of the practical difficulties of gaining evidence through mutual legal assistance.

Global Witness has spoken to contacts in the US Treasury and US Department of Justice who have not been able to confirm or deny if any of these other processes have been used by the US authorities to follow up on the transfers from the Equatorial Guinea accounts at Riggs to Luxembourg and Spain after the Senate investigators hit a wall. The only information about a possible US investigation has come from the Spanish media reports about the closed investigation into Banco Santander (see above), which suggested the New York District Attorney’s office had made enquiries of the Spanish authorities. Global Witness asked the District Attorney’s office if any such investigation had taken place; it could not confirm or deny this.

So a high profile investigation has taken place in the US, a bank has failed as a result – and yet the money has effectively been able to flee. Not only is this an extraordinary situation, it also makes any bank’s claim to be a good facilitator of cross-border business seem, at best, extremely ironic. HSBC, for example, advertises its HSBC Premier service, for wealthy private customers, under the heading ‘Banking without Boundaries’.<sup>102</sup>

But ‘banking without boundaries’ clearly does not extend to chasing the money after it has gone. So that’s ‘banking without boundaries’ if you’re a customer or a banker wanting to move money around. But as soon as anyone

needs to find out where the money has gone and who it belongs to, banks hide behind the shield of national jurisdictions which use the force of their laws to permit banking secrecy. This is the fundamental dislocation at the heart of the financial industry and the way it is regulated: modern instant globalised movement for money, and old-fashioned jurisdictional obstacles to following it after the event.

If secrecy laws such as these are not tackled, attempts by any single jurisdiction to deny use of the banking system to the corrupt will only ever be temporary, because the money can just go elsewhere.

## Conclusion

Riggs was an example of a bank that appeared to have no ethical culture determining which types of regimes it would deal with, whose compliance system failed and, despite it being situated at the heart of regulatory power in Washington DC, whose regulators were asleep at the wheel for far too long. It was left to a legislative committee to unravel the mess. The story demonstrated that oil money, in the immense volumes in which it can descend on a small state with poor governance, can potentially affect bankers' judgment.

Riggs repeatedly assured its regulators that everything was in order, and the regulators failed to take action when they did find failings. In the end, the truth only came about because journalists and NGOs including Global Witness started asking difficult questions about where Equatorial Guinea's oil money was going, which ultimately helped prompt the Senate subcommittee to do its laudable investigation into the bank.

Now that the Riggs story has revealed the potential gap between assurances and reality, on what basis are the people of resource-rich but desperately poor countries supposed to believe other banks, and their regulators, when they are told now that the systems are in place to prevent the movement of corrupt money? Whenever banks say that everything is in place to prevent them taking corrupt money, they will think of Riggs.

The problems have not gone away though. HSBC pointed out to Global Witness that the anti-money laundering regulations have moved on since these events occurred. Indeed, they have. But many of the important issues highlighted in this chapter have still not been solved. Banking secrecy laws that are

incompatible with the modern anti-money laundering regime meant that millions of dollars worth of suspicious transactions, paid into accounts that might be controlled by Obiang, could not be traced by the Senate investigators. It is not clear if any other official investigation has taken place.

Meanwhile the \$700 million that was in Equatorial Guinea's Riggs accounts at the point when Riggs closed them has now grown to at least \$2.1 billion. The IMF knows the money is offshore in commercial banks; if it does know which banks these are, it is not saying so. So the people of Equatorial Guinea still do not know where their oil money is being kept.

It also appears that other banks have not learnt the lesson about the risks of holding accounts for members of the Obiang family, as the next chapter will show. As soon as the money moves beyond the US, nobody seems to care. Riggs may be held up as an example to scare compliance officers, but is anybody listening?

### Action needed:

- The IMF should find out and disclose the names of the commercial banks that are holding Equatorial Guinea's oil revenues and ensure that there is proper oversight of the funds held in them.
- Banks should be required by regulation to respond to requests for information from other banks or their own overseas branches that are subject to supervision by any regulator from a country that is broadly in compliance with FATF standards without falling foul of banking secrecy laws, whether the request is being made in connection with an inquiry relating to money laundering, terrorist finance, or tax fraud risk.
- Each jurisdiction should publish information annually detailing the number of requests for cross-border legal assistance in financial investigations that it has received, specified by the country of origin, the type of offence to which the investigation relates, the total amount of funds involved for each country making a request, and the proportion of these requests that it has been able to fulfil.

# 04

# BARCLAYS AND EQUATORIAL GUINEA

## Doing business with the sons of heads of state, Part I

(Plus: Who banks for President Bongo of Gabon since Citibank closed its doors to him?)

President's son  
**Teodorin Obiang**  
splashes out on  
expensive cars  
and luxury houses  
while the people  
of Equatorial Guinea  
live in poverty. As  
of November 2007,  
a Barclays branch  
in Paris still held  
an account for him.



Despite the huge questions raised by the US Senate report about the source of the Obiang family's wealth, a branch of Barclays in Paris continued to hold a current account for Teodorin Obiang, one of president Obiang's sons. Account number 30588 61204 61483680101 was still open as of November 2007.<sup>103</sup>

This account information emerged after three French non-governmental organisations – Sherpa, Survie and Fédération des Congolais de la Diaspora – filed a legal complaint in France alleging that the ruling families of Angola, Burkina Faso, Congo Brazzaville, Equatorial Guinea, and Gabon had acquired millions of euros of assets in France that could not be the fruits of their official salaries.<sup>104</sup>

An initial police investigation took place during the second half of 2007, undertaken in response to the complaint. It uncovered evidence in France of tens of millions of dollars worth of luxury properties and cars, and dozens of bank accounts belonging to the rulers of Congo, Equatorial Guinea and Gabon, as well as their family members and close associates. Teodorin Obiang's car purchases alone came to €4.5 million (\$6.3 million) over the last decade.<sup>105</sup>

Teodorin is minister for agriculture and forests in his father's government, for which he earns a salary of \$4,000 a month.<sup>106</sup> However, he spends much of his time jetting around the world as a wannabe international playboy, running a hip hop

record label, reportedly dating glamorous rap stars, and collecting fast cars.

In 2006 Global Witness revealed that he had bought a \$35 million dollar mansion in Malibu, California, complete with its own golf course and extensive ocean view.<sup>107</sup> It would have taken him 730 years on his salary – or at the very least, extremely advantageous mortgage terms – to purchase the house, which raises questions about where, in oil and timber-rich Equatorial Guinea, he did find the money.

*[We] discovered that bank secrecy was not only for money laundering, tax evasion, drugs and corruption, but also for terrorism; we have since circumscribed the use of bank secrecy for terrorism – and thus we have shown that it can be done. But we have chosen not to deal with the problems of corruption and tax evasion which are so enervating to the developing countries and deprive them of so much needed money.*

**Joseph Stiglitz**, Testimony to the House Financial Services Committee, 22 May 2007<sup>110</sup>

Further evidence of institutionalised corruption in Equatorial Guinea emerged when Teodorin testified to a South African court in 2006, during a commercial case relating to the seizure of other luxury properties. He stated to the court that public officials in Equatorial Guinea are allowed to participate in joint ventures with foreign companies bidding for government contracts and, if successful, receive ‘a percentage of the total cost of the contract.’ He outlined that this means that ‘a cabinet minister ends up with a sizeable part of the contract price in

his bank account.’<sup>108</sup> (This was even more blatant than his father, the president, pointing out in TV interviews in 2003 that the country’s oil money was indeed under his personal control because that was the only way that he could be 100% certain that it was safe.<sup>109</sup>)

While a corrupt state such as Equatorial Guinea may have failed to make such behaviour illegal, this does not mean that it is an environment with which banks should want to be associated.

Yet despite these disturbing indications of corruption, and despite the public meltdown of Riggs, which should have been a terrifying reminder to the banking world of the risks of doing business with Equatorial Guinea’s ruling elite, Teodorin’s Barclays account was still open as of November 2007. The account was originally opened in September 1989, before Equatorial Guinea’s current oil boom had taken off. But what ongoing due diligence has Barclays done on its customer Teodorin Obiang in the years since the oil money has been flowing? Riggs collapsed largely because of the accounts held by Teodorin’s father, in a case now used to warn banks about the risks of PEPs, so on what basis had Barclays reassured itself that these were manageable risks?

Global Witness and Sherpa asked Barclays what due diligence it had done on its customer Teodorin Obiang and whether it had ever filed any suspicious activity reports in relation to transactions through the account. Barclays responded that its legal obligation of customer confidentiality precluded it from ‘commenting on any specific relationship or transaction or, indeed, whether we have entered into a transaction or provide financial services to a person or entity.’ It did, however, helpfully enclose a copy of its policy positions on bribery, corruption and anti-money laundering.<sup>111</sup>



Malibu, California, not to be confused with Malabo, Equatorial Guinea. Teodorin Obiang bought this \$35 million dollar mansion in 2006, despite earning a salary of \$4,000 a month as a minister in his father’s government.

One of Teodorin's bankers: **John Varley**, CEO of Barclays. The bank was not able to tell Global Witness what due diligence it had done on its client and his source of funds.



Barclays is a member of the Wolfsberg Group, which has published statements on fighting misuse of the financial system through corruption, and principles on anti-money laundering for private banking.<sup>112</sup> It is unclear how Barclays' membership of Wolfsberg squares with its holding an account for Teodorin Obiang.

Global Witness and Sherpa have seen the 200-page dossier from the French police investigation which resulted from the NGOs' complaint. It makes for extraordinary reading. The Barclays account was just one of several bank accounts used by Teodorin to pay for his extravagant collection of luxury cars. In June 1998, he wrote a cheque from the Barclays account for 200,000 francs (€30,490<sup>113</sup>) towards the purchase of a Ferrari 550 Maranello.<sup>114</sup>

The remaining payment of 812,639.87 francs (€123,886) for this car was drawn from another account (number 00825/00083719) at BNP Paribas.<sup>115</sup>

He also had an account at CCF Banque Privée Internationale, which has been owned since July 2000 by HSBC.<sup>116</sup> Teodorin wrote a cheque from this account (number 01931200002) for 1.2 million francs (€182,938) to pay for a Ferrari 512M on 7 December 2000.<sup>117</sup>

Of course, the fact that someone is a PEP does not in itself mean that a bank cannot open an account for them. But Teodorin is not just a PEP, he's a PEP from a country with a significant and well-documented history of corruption, whose family's accounts have already brought down an American bank. So the question is whether the banks who hold or have held accounts for him have been able to reassure themselves that he does not present a corruption risk.

Global Witness and Sherpa asked BNP Paribas and HSBC about the due diligence they had done on their customer Teodorin Obiang and whether they had ever filed any suspicious activity reports in relation to transactions through the accounts. HSBC responded that it was unable to answer questions about specific third parties, accounts and transactions, and said that 'global standards and practices to counter the now well-known risks associated with providing banking services to politically exposed persons have advanced significantly since the time of the incidents about which you have written, and HSBC has more than kept pace with these developments.' BNP Paribas said it could not respond, as 'over and above our bonds of professional confidentiality certain of your questions fall within our banking secrecy obligations.'<sup>118</sup>

More recently, during 2006 and 2007, Teodorin has been a reliable customer to the luxury car manufacturer Bugatti, purchasing two Veyrons for a million euros apiece and putting down a deposit on a third.<sup>119</sup> The Bugatti Veyron was built to be the fastest production car in the world, a record which it briefly held during 2006–7 (although it has recently been overtaken), with a top speed of 253.8 miles per hour.<sup>120</sup>

For less than the cost of just one of these Bugatti Veyrons, a long-lasting insecticide-treated mosquito net could be provided for every child in Equatorial Guinea. This could cut deaths from malaria by up to 44 per cent.<sup>121</sup>

Teodorin's Bugattis were paid for by wire transfers, some of them through French banks, from a company belonging to Teodorin. A subsequent investigation into these specific payments by Tracfin, the French anti-money laundering service, concluded in November 2007 that: 'the financial flows [...] are [...] likely to be the laundered proceeds of misappropriated public funds'.<sup>122</sup>

## Teodorin Obiang's car shopping in France



### Bugatti Veyron

Teodorin bought three of these. At the top speed of 407 km/h the tires burn out in 15 minutes. But this doesn't matter as you empty the fuel tank in 12 minutes.

**BOUGHT:**  
10/02/2006  
20/02/2006  
**DEPOSIT:**  
16/05/2007

**€1,196,000 (x3)**



### Maserati MC12

The car entered production in 2004. Only 25 models were made that year, and another 30 in 2005.

**BOUGHT:**  
02/07/2005

**€709,000**

Credits (clockwise from top left)  
**Bugatti Veyron:** Jorge L./Creative Commons  
**Maserati MC12:** Kevin White/Creative Commons  
**Ferrari 512M:** Creative Commons  
**Maserati Coupe F1 Cambiocorsa:** Clinton Davin/Creative Commons  
**Ferrari 550 Maranello:** Wikicommons  
**Rolls Royce Phantom:** Simon Greig/Creative Commons



### Rolls Royce Phantom

The first Rolls Royce produced under the guidance of BMW, reviving a name used on Rolls Royces since 1925. It now comes with a BMW assembled 6.75L, 48-valve, V12 engine and stands at almost six metres long.

**BOUGHT:**  
11/02/2005

**€381,000**



### Ferrari 512M

Only 500 of these were produced. It replaced the 512TR, which itself had replaced the legendary Testarossa.

**BOUGHT:**  
15/12/2000

**€182,938**



### Ferrari 550 Maranello

This replaced the 512M as the company's upmarket model. Unlike any other Ferraris since the Daytona, it had a front mounted V12 engine, which basically means you can still get your golf clubs in the back.

**BOUGHT:**  
16/12/1998

**€152,201**



### Maserati Coupe F1 Cambiocorsa

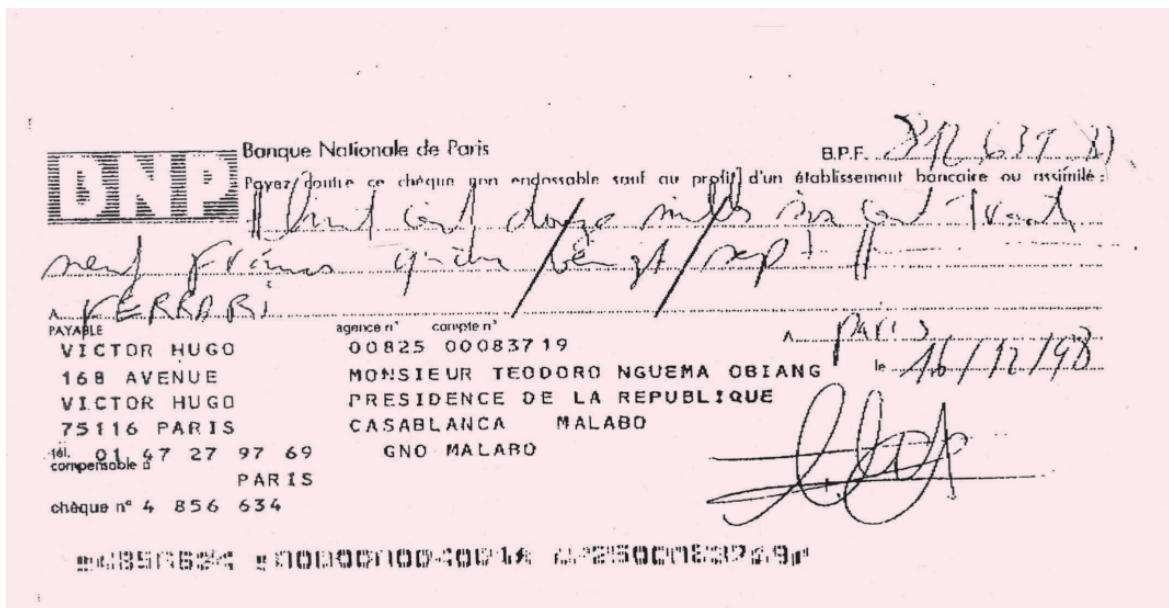
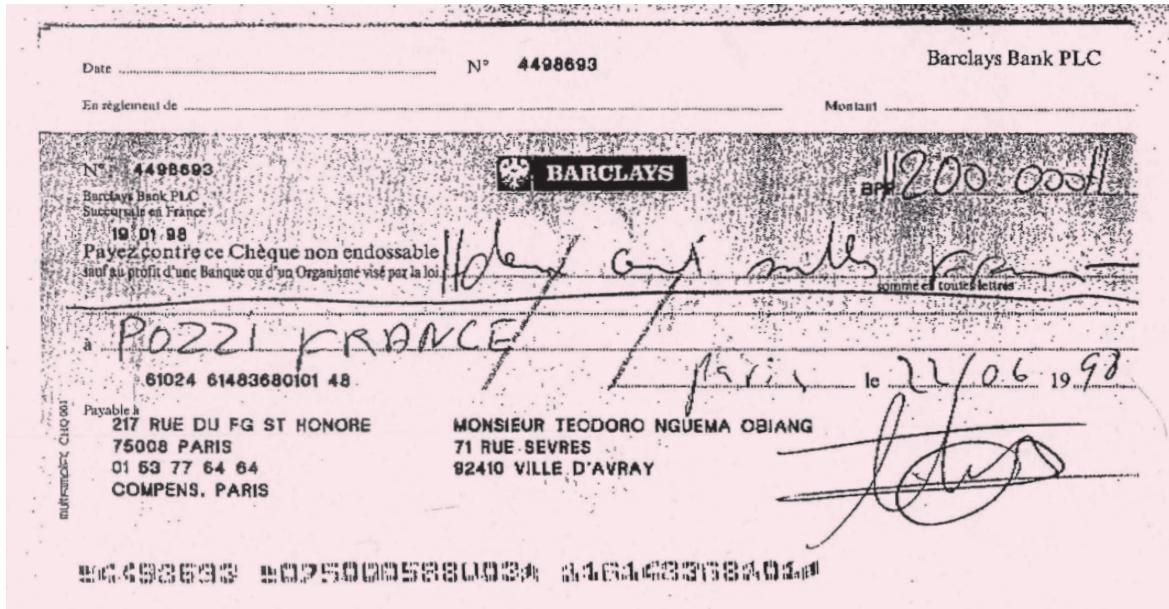
The cheapest of Teodorin's car purchases in France, coming in at less than €100,000.

**BOUGHT:**  
15/02/2005

**€82,000**

Euro values taken from French police file

**Teodorin Obiang**  
used money from  
his Barclays and  
BNP Paribas accounts  
to pay for a Ferrari  
550 Maranello.



**Michel Pébereau**  
was the CEO of BNP  
Paribas from 1993  
until 2003. In 1998  
Teodorin partly paid  
for a €152,202 Ferrari  
with funds from his  
BNP Paribas account.  
*Credit: Elipsa/Corbis  
Sygma*



Yet it was only a week later that the investigation initiated as a result of the NGOs' complaint was closed. The Public Prosecutor found that the offences were insufficiently substantiated and the case was not allowed to go further.<sup>123</sup>

This investigation, the first of its kind in France, should have been a key test of President's Sarkozy's call for a new 'partnership between equal nations' with Africa, and France's global commitments against corruption.<sup>124</sup> This new partnership seems to have failed at the first hurdle. Sherpa, together with Transparency International France, and with the cooperation of citizens of Gabon and Congo, is now launching a civil party petition calling for a more detailed investigation.<sup>125</sup>

French banks have not just been banking for the Obiang family. The police file that resulted from the investigation also lists more than 20 banks in France as holding nearly 200 separate accounts for family members of President Omar Bongo of Gabon and President Sassou Nguesso of Republic of Congo.

### Bongo accounts

In 1999, Citibank in New York closed its accounts for President Bongo after a Senate subcommittee investigation used them as a case study to illustrate its concerns about the risks of private banking being used for money laundering (See Box 4 on following page). Yet the French police file shows that as of October 2007, President Bongo had at least six accounts at BNP Paribas in Paris, and another four accounts, two in Paris and two in Nice, at Crédit Lyonnais. The Crédit Lyonnais accounts and two of the BNP Paribas accounts had been open since before the US Senate investigation; four of the BNP Paribas accounts were opened after it, two in 2001 and two in 2006.<sup>126</sup>

It seems that use of government funds for private spending may still be occurring in Gabon. According to the same French police file that resulted from the NGOs' complaint, in 2004 President Bongo's wife, who is not a government official, purchased a €326,000 Maybach luxury car that was entirely paid

for by the Gabonese Treasury.<sup>134</sup> Meanwhile Gabonese anti-corruption activists continue to face harassment from the authorities, including being arrested on trumped-up charges.<sup>135</sup>

So once again, despite huge questions having been raised in the US about the source of Bongo's funds following which his accounts at Citibank were closed, French banks have continued to hold accounts for Bongo.

The French police dossier does not reveal the source of funds into Bongo's private accounts at BNP Paribas and Crédit Lyonnais. Global Witness and Sherpa asked these banks what due diligence they had done on their client Omar Bongo and his sources of wealth, particularly given the concerns raised over Bongo's accounts by the US inquiry eight years ago. BNP Paribas said it could not respond; Crédit Lyonnais did not reply.<sup>136</sup>

Global Witness asked the French regulator, the Secrétariat Général de la Commission Bancaire, if it was aware of any of these accounts at French banks, if it had ever monitored them, or if any suspicious activity reports had ever been filed that related to them. It replied that it could not answer questions about individual matters.<sup>137</sup> Given that one of the banks, Barclays, is a UK bank, Global Witness asked the Financial



**Presidents Sarkozy of France and Bongo of Gabon.** France did not pursue an investigation into allegations that ruling families of a number of African countries including Gabon had acquired millions of euros of assets in France that could not be the fruits of their official salaries. Credit: Michel Euler/AP

### **Box 4: Citibank's Bongo accounts**

In 1999, Citibank in New York had suffered severe embarrassment when the US Senate Permanent Subcommittee on Investigations published a report and held a hearing on private banking and money laundering risks, focusing on Citibank's accounts for high profile clients including President Bongo of Gabon.<sup>127</sup>

Between 1985 and 1999, funds moving through the Bongo private bank accounts exceeded \$130 million, as well as multiple, multi-million dollar loans collateralised by his deposits.<sup>128</sup>

The Senate investigators made it clear that their primary concern was the apparent acceptance by the bank that government funds were a legitimate source of funds for the private bank accounts of a president.

Citibank's initial client records on Bongo's source of wealth did not elaborate beyond the fact that the country was an oil producer and the president had oil interests. When pushed by its regulator to do so, Citibank then said it understood that \$111 million, or 8.5% of the Gabonese government budget, was available to be used at the discretion of the president.<sup>129</sup> As the subcommittee noted, 'the plain meaning [...] is that the private bank was identifying Gabon government funds as a primary source of the funds in the Bongo accounts.'<sup>130</sup> But Gabon budget experts at the IMF and World Bank rejected the suggestion that the President received \$111m for his personal use.<sup>131</sup>

The Senate report also highlighted how the OCC, in its role as regulator, did not question the bank over the alleged source of funds in the accounts – government funds and oil revenues – and gave its approval to the bank's management of the accounts.<sup>132</sup>

The accounts were closed in 1999, but Citibank management told the Subcommittee that this was decided because of the cost of answering questions about them, rather than because of specific concerns about the source of funds or the reputational risk.<sup>133</sup>

Services Authority, the UK regulator, if it was responsible for regulating overseas branches of UK banks. It said it was not, this is the responsibility of the local regulator.<sup>138</sup>

Global Witness asked the banks named in this chapter what kind of documentation they obtain to establish the source of funds in a client's account when that client is a politically exposed person from an oil-rich state, and whether they consult international financial institutions about budgetary transparency in resource-rich countries when PEPs state that some of their income is derived from resource revenues. BNP Paribas's response did not acknowledge these questions; Barclays' letter indicated its policy positions document and sustainability report, which do not mention these issues; Crédit Lyonnais did not respond. HSBC did not answer these specific questions, but pointed to HSBC's 'comprehensive and robust policies, principles and procedures... developed to counter the use of its services for corrupt practices.'<sup>139</sup> So none of these banks chose explicitly to answer this crucial question.

### **Conclusion**

This chapter shows how it has been possible for investigators in the US to raise huge concerns about the source and destination of funds in accounts controlled by the Obiangs and Bongos, resulting in the closure not only of accounts but of an entire bank – and for British and French banks to hold accounts for them regardless. What kind of due diligence are these banks doing on their obviously high-risk clients? And are their regulators in France actively monitoring what they are doing, or passively waiting for the next scandal to strike?

In the case of Equatorial Guinea and the Obiang family, a high-profile US investigation resulted in criminal charges, fines, and the sale of the bank with huge loss of shareholder value. Anything to do with the Obiangs should be hugely high risk for other banks as a consequence. It would of course be interesting to know what due diligence CCF and BNP Paribas did on their client Teodorin Obiang and his source of funds. But the French police file provides a snapshot of which banks held accounts for him in 2007, and by this point, they no longer did. While Teodorin used his accounts at CCF, now owned by HSBC, and BNP Paribas to pay for some of his luxury car purchases in 1998 and 2000, and while this of course should have raised huge due diligence questions for the banks, the fact that these accounts were no longer



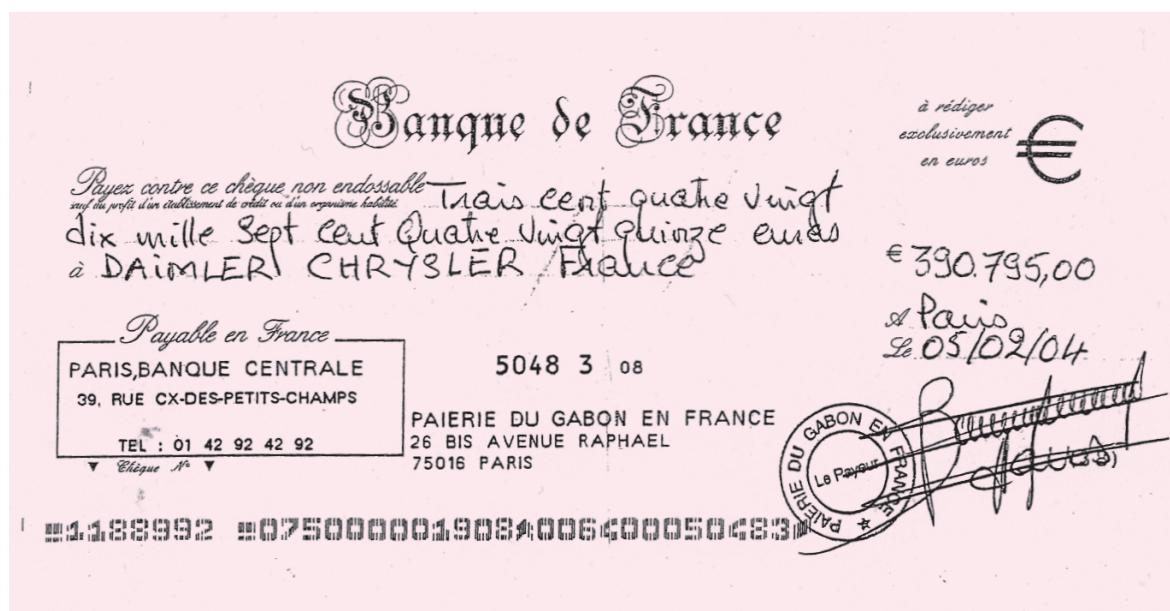
One of President Bongo's properties in Paris, on rue Laurent Pichat, according to a French police investigation that was later dropped.  
Credit: Global Witness

open at the time of the 2007 French police investigations means that we do not know when they were closed, nor whether they remained open after Riggs' collapse in 2004-5.

The account which raises the most questions, therefore, is Teodorin's Barclays account, which was still open as of the end of 2007. This was three years after Riggs collapsed. Here is a British bank continuing to hold an account for Obiang's son, someone who has publicly declared that it is normal to take a cut from government contracts, and when the Riggs debacle has already decisively

demonstrated that banking for Obiang is appallingly high risk. But Barclays will not say what due diligence it has done on its client.

In the case of Gabon and the Bongo family, nearly ten years after Citibank gave up its Bongo accounts, the French banks BNP Paribas and Crédit Lyonnais were still banking for Omar Bongo. Four of the accounts at BNP Paribas were opened after the Citibank accounts were closed. So banks can be steered away from high risk clients in one jurisdiction, and the banks in other jurisdictions don't have to know. There is nothing requiring



Presidential perks?  
**Edith Lucie**, wife of President Bongo, was bought a €326,000 Maybach luxury car. The Gabonese Treasury paid the cheque. It overpaid: the difference was used to buy a Mercedes for the President's daughter.

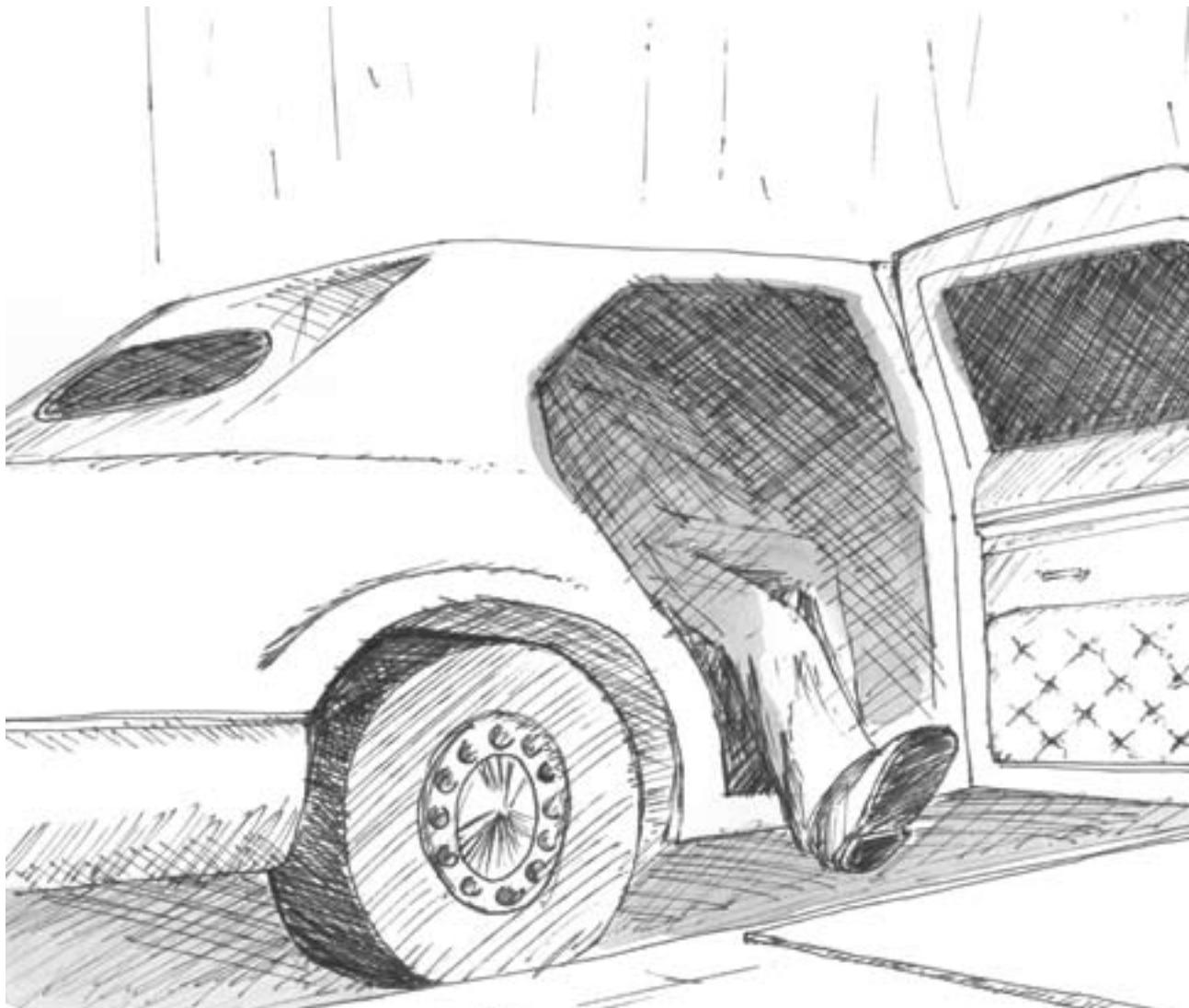
banks to know about action taken in other jurisdictions regarding their clients.

Meanwhile, another set of accounts revealed by the French police file were, as of late 2007, four accounts at Société Générale in Paris that appear to belong to Denis Christel Sassou Nguesso, son of the president of Congo-Brazzaville and a government official responsible for marketing Congo's oil.<sup>140</sup>

As the next chapter will show, creditor court judgments from 2005 onwards have raised significant questions about Mr Sassou Nguesso's handling of Congo's oil receipts. A separate judgment in the UK High Court in July 2007 said: 'It is an obvious possible inference that [Sassou Nguesso's]

expenditure has been financed by secret personal profits made out of dealings in oil...' and that documents relating to one of his companies, 'unless explained, frankly suggest' that Mr Sassou Nguesso and his company were 'unsavoury and corrupt'.<sup>141</sup> Yet a Hong Kong bank and a company services provider had allowed him to move these 'secret personal profits' around the world without hindrance.

Global Witness asked Société Générale what due diligence it had done on its client Mr Sassou Nguesso; it did not respond. Société Générale is a member of the Wolfsberg Group, whose document on PEPs highlights the potential risk presented by PEPs at the helm of state-owned companies.<sup>142</sup>

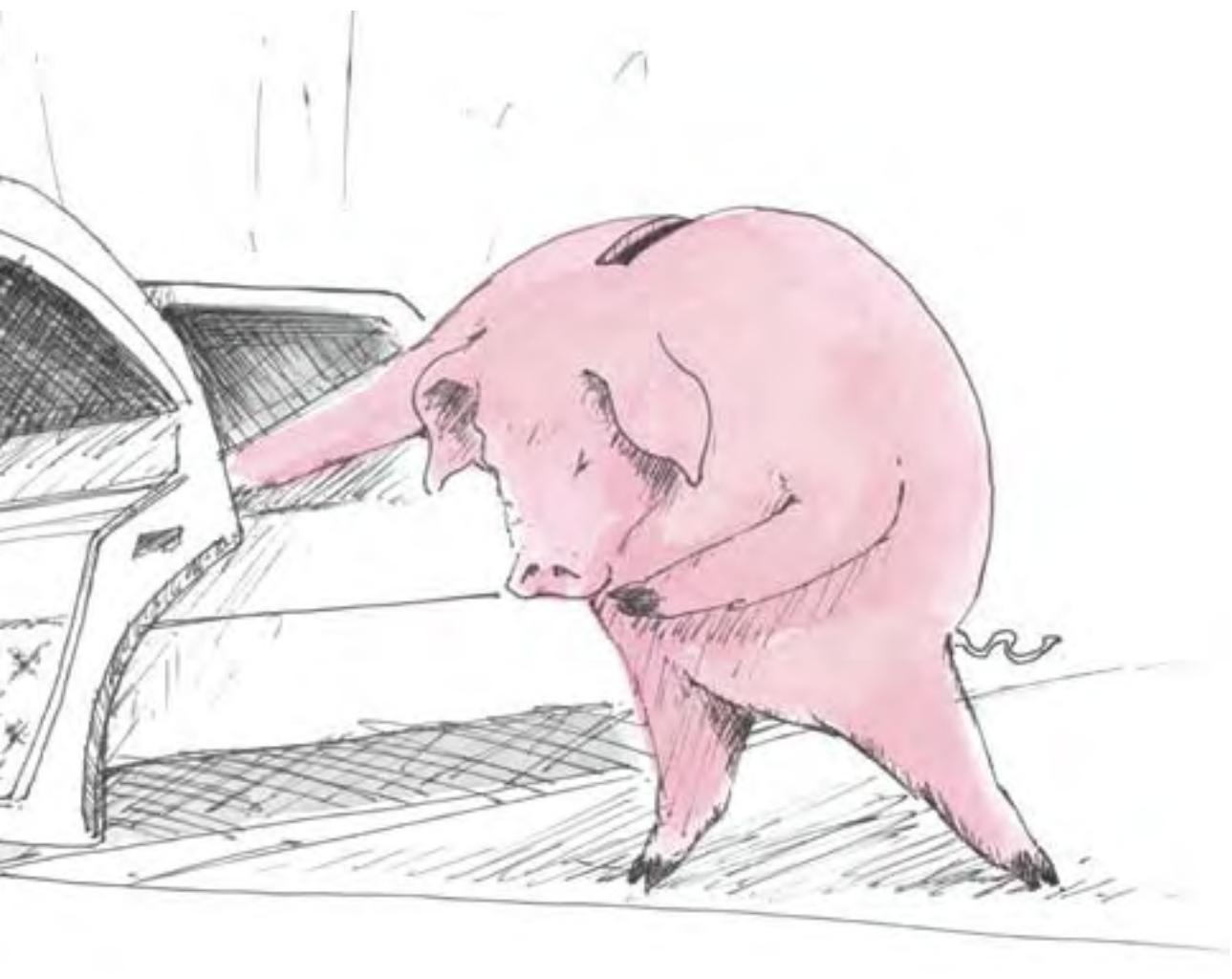


**Action needed:**

- The French government should reopen the investigation into the French assets of foreign rulers that could not have been purchased with their official salaries.
- Banks wishing to handle transactions involving natural resource revenues should be required by regulation to have adequate information to ensure that the funds are not being diverted from government purposes.

In cases where no such information exists, they should not be permitted to perform the transaction.

- FATF should set up a taskforce specifically to tackle the proceeds of corruption, including the prominent role played by natural resources in corrupt money flows. External experts including law enforcement officials who are at the coalface of fighting corruption and money laundering should be invited to take part.



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# 05

# BANK OF EAST ASIA AND REPUBLIC OF CONGO

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Doing business with the sons of heads of state, Part II

The President of the Republic of Congo, Denis Sassou Nguesso

**Nguesso.** Evidence obtained by Global Witness suggests that his son spent thousands of dollars of the country's oil money on designer clothes and shoes.

Credit: Patrick Robert/Corbis



Between February 2004 and August 2006, Denis Christel Sassou Nguesso, son of the president of Republic of Congo, went shopping. Many times. Mostly in Paris, but also in Hong Kong, Monaco, Dubai and Marbella. He spent hundreds of thousands of dollars on designer names including Lacroix, Gucci, Escada, Louis Vuitton, Christian Dior and Roberto Cavalli.

In addition to being the president's son, Mr Sassou Nguesso is head of Cotrade, a public agency which sells Congo's oil on behalf of the government.<sup>143</sup> His personal credit card bills, along with those of another Cotrade official, were paid off by offshore companies registered in Anguilla which appear to have received, via other shell companies, money related to Congo's oil sales.

Oil accounts for around 80 per cent of Congo's income and in 2006 oil revenues reached around \$3 billion.<sup>144</sup> Despite this, Congo remains one of the poorest and most indebted countries in the world, and its oil wealth has contributed to several bloody civil wars. But while the majority of the population remains mired in poverty, the president's family are able to live in luxury.

Mr Sassou Nguesso's credit card spending in just one month, June 2005, came to \$32,000. This could have paid for more than 80,000 babies to be vaccinated against measles, which is a major cause of child death in Congo. A third of Congolese babies are not vaccinated against measles, and a single dose of measles vaccine costs as little as 40 cents.<sup>145</sup>



Ordinary Congolese see very little of their country's oil wealth, while the president's son Denis Christel has splashed out on luxury shoes and clothes in Paris.  
Credit: Robert Grossman/  
Africaphoto.com

This chapter tells the story of how the ultimate politically exposed person – the son of the president of an oil-rich yet indebted and poverty-stricken country – was able to open a Hong Kong bank account at Bank of East Asia, from which his credit card bills were paid, apparently from funds derived from Congo's oil money. A London High Court judge would later go on to find, in a court case brought against Global Witness by Mr Sassou Nguesso, that documents concerning his spending ‘frankly suggest,’ unless proven otherwise, that he and his company were ‘unsavoury and corrupt.’<sup>146</sup>

The story raises three significant questions about what Bank of East Asia – which describes itself as ‘the largest independent local bank in Hong Kong’ – should, and could, have known.

1. Did Bank of East Asia know that it had opened an account for the son of the president of Congo? If not, why not?
2. Did Bank of East Asia know that the account was receiving questionable transfers of funds derived from Congolese oil payments? If not, why not?
3. Did Bank of East Asia know that the account was being used to pay the personal credit card bills of the son of the president of Congo? If not, why not?

Denis Christel Sassou Nguesso’s account at Bank of East Asia was opened in the name of his Anguilla-registered company, Long Beach. So the first big question arrives immediately:

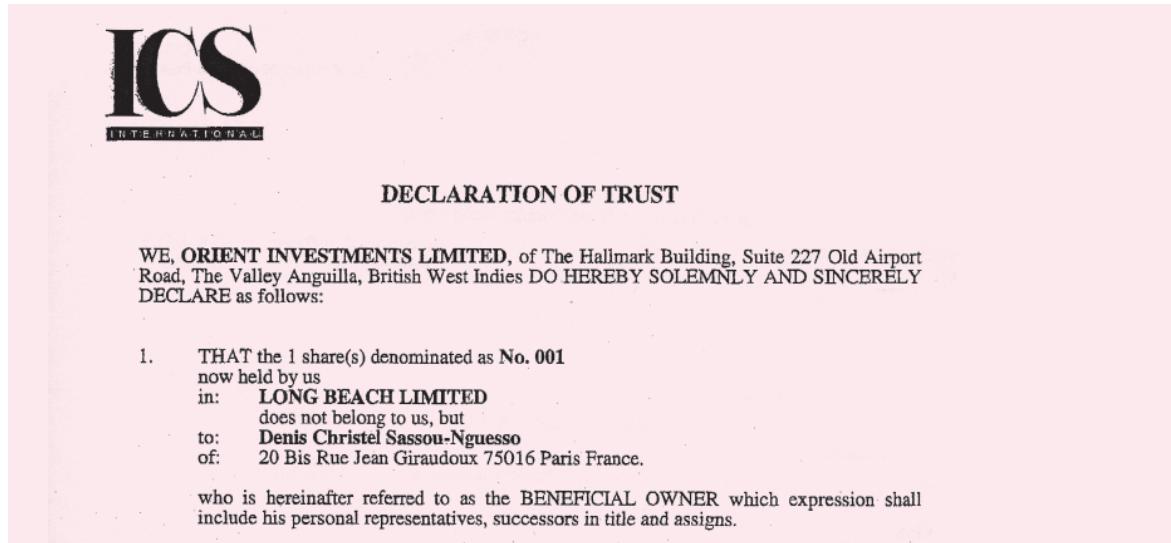
### **Did Bank of East Asia know, or attempt to find out, who really owned Long Beach?**

Long Beach was incorporated in the Caribbean secrecy jurisdiction of Anguilla in March 2003, although its business address is stated as being in Hong Kong, the same address as a company services provider called ICS.<sup>147</sup> According to a company information sheet seen by Global Witness and evidence given in Hong Kong court proceedings, Long Beach’s shareholders and directors are Orient Investments Ltd and Pacific Investments Ltd, which are both Anguilla-based companies in the ICS group that provide nominee services.<sup>148</sup>

When Long Beach opened a bank account at Bank of East Asia in Hong Kong in November 2003, account number 015-514-25-10518-6, it was Orient Investments which acted as the sole signatory.<sup>149</sup> However, a Declaration of Trust document seen by Global Witness shows that Orient and Pacific were actually holding the shares in trust for Mr Sassou Nguesso, who was the ultimate beneficial owner of Long Beach.<sup>150</sup>

As of November 2003, Hong Kong anti money laundering guidelines (which, largely, did not and still do not have the force of law, but are merely supervisory requirements set by the regulator; see page 63) required banks to identify the directors and shareholders of companies opening accounts, and specifically required banks to identify the beneficial owners of shell companies such as Long Beach.<sup>151</sup> The ultimate beneficial owner of a company is the person at the top of the

**Denis Christel**  
registered a company  
called Long Beach in  
the British tax haven  
of Anguilla, then put  
his shares in trust to  
hide his ownership.



chain of ownership; it cannot be a trust and company services provider such as Orient or Pacific Investments, because such a provider is always acting on behalf of a client. A shell company is a legal entity that does not do any actual business but through which financial transactions are conducted.

In situations where a company is introduced to the bank by a professional intermediary acting on its behalf, as was the case with Long Beach, Hong Kong requires the bank to establish whether the applicant is acting on behalf of another person as trustee, nominee or agent, and the bank should obtain information on the identity of the trustees or nominees and the persons on whose behalf they are acting.<sup>152</sup>

Global Witness asked Bank of East Asia if Orient Investments, as the signatory on the account, had disclosed that it was acting as an intermediary on behalf of a third party

client, but it declined to answer. Its answer to Global Witness's 48 questions was: 'The Bank of East Asia, Limited is regulated by the Hong Kong Monetary Authority ('HKMA') and we have established relevant internal procedures in accordance with the requirements on prevention of money laundering and terrorist financing set forth by HKMA. These internal procedures are for internal circulation only. Moreover, due to the secrecy owed to our customers, our Bank should not disclose any information of our customers without their prior written consent or unless it is obligated to do so under relevant court order or laws.'<sup>153</sup>

The Hong Kong anti-money laundering guidelines permit banks to rely on intermediaries who introduce customers to perform the due diligence on that customer themselves, however, 'the ultimate responsibility for knowing the customer always remains' with the bank.<sup>154</sup> If a bank

Long Beach opened an account at Bank of East Asia in Hong Kong. Did the bank find out who was really behind Long Beach?  
*Credit: Global Witness*



does rely on an intermediary to do the due diligence, it should be using standards equivalent to Hong Kong's, and it is 'advisable' for banks to rely on intermediaries which are regulated by the Hong Kong regulator or an authority performing equivalent functions, or that are incorporated in or operating from a jurisdiction that is a member of the FATF or an equivalent jurisdiction, which it defines as EU, Netherlands Antilles and Aruba, Isle of Man, Guernsey and Jersey.<sup>155</sup>

So Bank of East Asia was required either to carry out its own due diligence on the owner of Long Beach, or to rely on Orient Investments to do so. But neither Bank of East Asia nor Orient Investments was willing to say whether or not they had actually done this. Bank of East Asia declined to answer any specific questions and Orient Investments and its related companies Pacific Investments and ICS did not respond to queries from Global Witness about what due diligence they had done on their customer Denis Christel Sassou Nguesso.

Hong Kong anti-money laundering guidelines also require banks to carry out enhanced due diligence if they are dealing with a PEP. The guidelines suggest that risk factors to consider when doing business with a PEP should include 'any particular concern over the country where the PEP is from, taking into account his position'.<sup>156</sup> But in order to do this, of course, they must first know that they are dealing with a PEP. Global Witness asked Bank of East Asia if it had established whether the owner of the Long Beach account was a PEP, but it declined to answer.

Global Witness notes that Republic of Congo was placed 113 out of 133 countries in Transparency International's Corruption Perception Index in 2003, the year in which the account was opened.<sup>157</sup> The IMF and World Bank have also expressed 'serious concerns about governance and financial transparency' in Congo, focused on mismanagement of Congo's oil sector.<sup>158</sup>

So the Hong Kong guidelines required Bank of East Asia to know who its customer was. In other words, the bank should have known that it was effectively opening an account for the son of the President of Congo, who was indisputably a PEP simply by connection with his father, let alone the fact that he also was in charge of marketing the state's oil.

The guidelines suggest that knowing this, Bank of East Asia should have carried out enhanced due diligence, considering his position and concerns about Congo itself. These concerns ought to have included the question of corruption, which had been explicitly raised by the World Bank and Transparency International, in reports which were published and easily available on the internet.

But it is unclear whether or not Bank of East Asia knew who its customer was, whether it knew if he was a PEP, and whether it conducted enhanced due diligence on him, because the bank did not answer questions on this point when asked by Global Witness. Just because a bank can hide behind customer confidentiality and refuse to answer our questions does not, of course, mean that it did not do its due diligence. It does mean, though, that neither Global Witness, nor the people of Congo – who have the real interest in this matter – can see what happened, and whether the bank did do its due diligence. All that we can see is what the documents show: that an offshore shell company of which the son of the President of Republic of Congo was the beneficial owner was able to open an account.

This leads to the second question:  
**How much did Bank of East Asia know about the source of funds (ie oil money) into the account?**

Bank of East Asia was in a position to know that the money in the account was likely to come from trading in Congolese oil because,



**Elizabeth L Thomson**  
 founder and president  
 of ICS Trust (Asia)  
 Ltd, the Hong Kong  
 provider of company  
 services and wealth  
 management which  
 set up Denis Christel  
 Sassou Nguesso's  
 offshore company  
 structure. 'Ms  
 Thomson has been  
 respecting the unique  
 and confidential  
 requirements of our  
 clients for more  
 than 25 years  
 through the provision  
 of discreet and  
 highly personalised  
 services,' her profile  
 on the company's  
 website says.  
*Credit: South China  
 Morning Post.*



**Biondini**  
78 Avenue Champs  
Elysées, Paris 7500

18/06/2005 €543

Credit: Global Witness



**Louis Vuitton**  
22 Avenue Montaigne,  
Paris 75008

08/01/2005	€2,860
09/04/2005	€4,090
18/11/2005	€3,245
22/04/2006	€2,960
22/04/2006	€3,077
03/06/2006	€10,225

Credit: Soyoung Park/  
Creative Commons



**Lancel**  
127 Avenue des  
Champs Elysées

08/07/2004	€560
20/07/2004	€1,090
25/09/2004	€1,300
01/10/2004	€9,500
20/06/2005	€1,458

Credit: Nicolas/  
Creative Commons



**Hotel Bristol**  
112 Rue Fbg St Honoré,  
Paris 75008

19/02/2004	€1,513
02/05/2004	€1,190

Credit: Global Witness



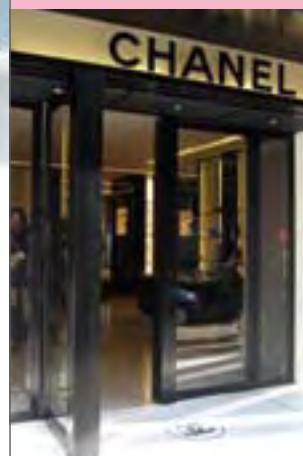
**D&G**  
54 Avenue Montaigne,  
Paris 75008

28/05/2005 €2,375



**Chanel**  
40 Avenue Montaigne,  
Paris 75008

22/04/2004 €900



**Christian Dior**  
30 Avenue Montaigne,  
Paris 75008

22/04/2004	€3,023
18/11/2005	€605



Credit: Global Witness

Credit: Wally Gobetz/  
Creative Commons

## A selection of Denis Christel Sassou Nguesso's favourite shopping haunts in Paris

(not including his shopping sprees in Monaco, Marbella and Hong Kong)



Global Witness has seen Denis Christel Sassou Nguesso's credit card statements from Online Credit Card Limited, dated 2 March 2004 to 3 October 2006, which provide the Parisian arrondissement for each shop he visited, but not the exact address. There is more than one outlet of some of these shops in the 8th arrondissement, so this map is therefore an approximation of some of his shopping sprees.

according to Hong Kong court documents, the bank held a customer information sheet on Long Beach, signed by Orient on behalf of Long Beach, describing the company's main business activities as 'Trading crude oil, gas and products (mogas, jet, gasoil, kerosene) in Congo'.<sup>159</sup> From this it is reasonable to infer that the bank knew that its client's source of revenue was Congolese oil.

Bank documents show that specific transactions through Long Beach's account related to Congolese oil proceeds and sometimes to specific oil cargoes.

A Bank of East Asia 'Daily Transaction Journal' appears to show that on 12 April 2005 the Long Beach account received a transfer of \$149,944.19 from a named individual unknown to Global Witness; the payment details referenced 'MT Genmar Spartiate B/L 17.1.05'. On 31 May 2005 the Long Beach account received another transfer of \$322,132.84 from the same individual; the payment details referenced 'MT Tanabe B/L 19 Mars 2005'.<sup>160</sup>

Bills of lading in Global Witness's possession indicate that 'MT Genmar Spartiate' and 'MT Tanabe' were vessels carrying oil cargoes.<sup>161</sup> It is therefore reasonable to infer that Long Beach was receiving transfers of money relating to particular oil cargoes. On the basis that the bank knew the source of funds in the account was Congolese oil, its ongoing due diligence might reasonably be expected to investigate these particular sources of income.

Another Bank of East Asia 'Daily Transaction Journal' appears to show that on 10 November

2004, Long Beach received a payment of \$299,967 from a company called AOGC.<sup>162</sup>

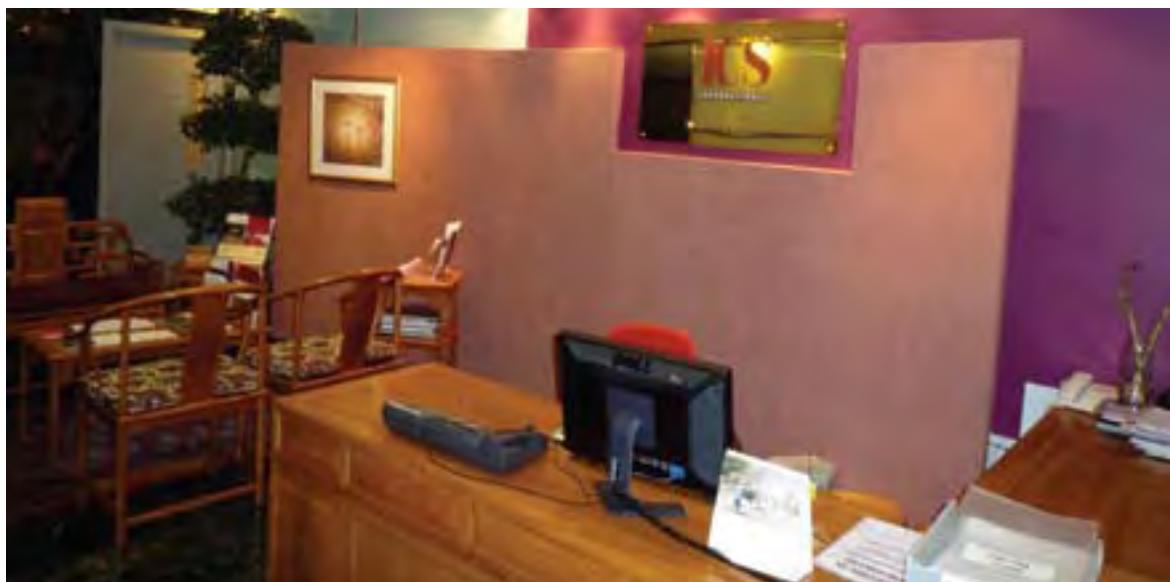
A London High Court judgment on 28 November 2005 found that AOGC (Africa Oil and Gas Corporation), a private company, was owned by a person who is also the head of Congo's state oil company, who had used AOGC in a series of 'sham' transactions to stop creditors of the Congolese state from attaching state assets such as oil revenues. The court also found that Mr Sassou Nguesso was a party to these sham transactions.<sup>163</sup>

*The international banks remain home to corrupt African money under a veil of secrecy. If the money is linked to terrorism the banks are legally required to report it, but if it is merely money looted from the poorest countries in the world the banks can remain silent.*

**Paul Collier**, Professor of Economics at Oxford University and author of *The Bottom Billion: why the poorest countries are failing and what can be done about it*<sup>170</sup>

Since November 2001, Hong Kong anti-money laundering guidelines had required banks to perform 'ongoing monitoring of accounts and transactions.' In June 2004, before these transfers into the Long Beach account were made, these guidelines were updated to require banks to 'perform on-going scrutiny of the transactions and account throughout the course of the business relationship to ensure that transactions being conducted are consistent

The offices of ICS, the Hong Kong company services provider to whose address Denis Christel's credit card statements were addressed after his designer shopping sprees.  
Credit: Global Witness



# DEBIT BEACH LIMITED

8/F Henley Bldg., 5 Queen's Rd., Central, Hong Kong  
Tel No. (852) 2854-4848 Fax No. (852) 2543-4080

11 September 2006

**Record of terrorists checked**

The Manager  
The Bank of East Asia, Limited  
10 Des Voeux Road Central,  
Hong Kong

Dear Sir/Madam,

**RE: LONG BEACH LIMITED**  
**ACCOUNT NO.: 015-514-25-10518-6**

Upon receipt of this letter, please immediately transfer from the above captioned account to the following:-

<b>AMOUNT</b>	: USD 35,313.36*** (United States Dollars Thirty Five Thousand Three Hundred Thirteen and Cents Thirty Six Only.)***
<b>BENEFICIARY BANK</b>	: Standard Chartered Bank (HK) Limited Hong Kong
<b>BENEFICIARY NAME</b>	: Online Credit Card Limited
<b>ACCOUNT NO</b>	: 317-1-008609-7
<b>MESSAGE</b>	: Payment of Online CC: Denis Christel Sassou Nguesso A/C # 5430 9600 6810 1330

'Record of terrorists checked': Bank of East Asia checked whether Denis Christel was a terrorist, but did it manage to identify him as the son of the president of Republic of Congo?

with the... [bank's] knowledge of the customer, its business and risk profile, including, where necessary, identifying the source of funds.<sup>164</sup>

Global Witness asked Bank of East Asia if it had performed any due diligence on AOGC or the named individual as the source of these payments into the Long Beach account; whether it was made aware of the UK High Court judgment on 28 November 2005, which found that AOGC was used in a series of 'sham' transactions, and whether it accepted transfer of further payments from AOGC to Long Beach's account after this date. The bank declined to answer.

So to recap for a moment: Bank of East Asia opened an account for a shell company owned by the son of the president of a country where corruption was known to be a serious problem. According to Hong Kong anti-money laundering guidelines, the bank should have checked to find out who its customer was, whether directly or indirectly via Orient Investments, but the bank would not tell Global Witness whether it did this or not. The guidelines also require the bank to perform ongoing scrutiny of transactions through the account, but again, it would not tell Global Witness whether this happened. What is clear from the available documentation, though, is that the bank was in a position to know that the

funds in the account were likely to come from Congolese oil sales, because the bank's own records showed that oil was the main business of Long Beach and transfers into the account appear to have come from sales of specific oil cargoes carried in named oil tankers.

This raises the third question: **Did Bank of East Asia know that an account for a company that traded Congolese oil was being used to pay the personal credit card bills of the son of the president of Congo?**

Four letters on Long Beach letterhead, between May 2004 and September 2006, request that Bank of East Asia arrange for payment, from the Long Beach Limited account, of Mr Sassou Nguesso's monthly credit card bill. The letters are signed by Orient Investments on behalf of Long Beach.<sup>165</sup>

The credit card bills themselves, seen by Global Witness, card numbers 5430 9600 6810 1330 and 5411 2340 4010 1039, are in Mr Sassou Nguesso's name and are addressed to the Hong Kong address of ICS Trust (Asia) Ltd, one of the ICS group companies.<sup>166</sup> It is reasonable therefore to infer that the credit card bills were sent to ICS Trust (Asia), which saw the bills, then instructed its sister company Orient Investments to arrange for

*In a recent speech on terrorism and its financing, the Chancellor of the Exchequer made a clear commitment that HM Treasury will work more closely with the financial sector in identifying suspicious transactions. He compared the forensic accounting measures required to tackle terrorist financing with the groundbreaking achievements at Bletchley Park during the Second World War. This is welcome and should also be applied with the same vigour and supportive resources to the proceeds of corruption as well as the financing of terrorism. After all, if a country's health budget is misappropriated, for example, the results can also threaten safety.*

Africa All Party Parliamentary Group, *The Other Side of the Coin: the UK and Corruption in Africa*, March 2006

payment from the Long Beach account of which it was signatory. Global Witness wrote to ICS and to Orient Investments to verify this but they did not reply. ICS Trust (Asia) Ltd appears to have had a clear opportunity to identify its customer and observe that the credit card bills were for personal spending.

The instructions for payment, sent on Long Beach letterhead by Orient Investments to Bank of East Asia, mention Mr Sassou Nguesso by name as the owner of the credit card. This was the point at which the bank itself had a very clear opportunity to see that it was dealing with the son of the president of Congo: a quick Google search could have established as much.

The payment instructions have been stamped, most likely by Bank of East Asia, 'Record

of terrorists checked', suggesting that Mr Sassou Nguesso's name had been run through at least one due diligence database. This would have been another opportunity to verify his identity as a PEP. However, having established that he was indeed not a terrorist, the bank proceeded to arrange for payment of his credit card bills, out of a bank account which it should have known was receiving the proceeds of Congo's oil.

As described above, by 2004 Hong Kong's banks were required to scrutinise transactions through accounts. Interpretative notes to the June 2004 anti-money laundering guidelines suggested that banks refer to Transparency International's Corruption Perceptions Index when trying to identify risky PEP business.<sup>167</sup>

In December 2005 Global Witness published information alleging that the head of the Congolese state oil company, Denis Gokana, had sold government oil to his own companies at prices below the market rate in order to profit from subsequent sales to independent traders, and that these deals had been overseen by Denis Christel Sassou Nguesso.<sup>168</sup> This information was reported in the media, including by Dow Jones on 13 December 2005.<sup>169</sup> Information was therefore in the public domain raising questions over Mr Sassou Nguesso's role in the dubious sales of Congolese oil. Yet Bank of East Asia was arranging for payment of his credit card bills out of the account of a company that it knew to trade Congolese oil until at least September 2006.

Global Witness asked Bank of East Asia if it had done due diligence into the identity of the credit card owner named on the payment instructions that it received from Long Beach, if it established whether he was a politically exposed person, and what due diligence it had done in order to be able to stamp the

**Sir David Li Kwok-po,** former Hong Kong politician, and CEO and Chairman of Bank of East Asia (BEA). Until February 2008 Sir David was a member of Hong Kong's Executive Council. He resigned after paying \$8m to the US Securities and Exchange Commission to settle an insider trading case against him. Sir David still represents the financial sector in the Legislative Council. BEA is the largest independent local bank in Hong Kong, and made \$542m profit in 2007.<sup>172</sup>  
Credit: Uden Graham/Redlink/Corbis



payment instructions ‘record of terrorists checked.’ The bank declined to answer.

Global Witness also asked ICS Trust (Asia) and Orient Investments if their own due diligence had revealed that some of Mr Sassou Nguesso’s transactions from the Long Beach account appeared to be in payment of personal expenditure by Mr Sassou Nguesso himself, and that this personal expenditure appeared to involve extensive and regular purchases of luxury goods; and whether this due diligence, against the backdrop of their knowledge that Long Beach’s source of income was Congolese oil, prompted any further investigation into the apparent payment, by a company set up to trade oil and gas products, in respect of luxury personal expenditure by its beneficial owner. They did not reply.

### How these documents came to light

The documentation referred to in this chapter came into the public domain in mid-2007 through creditor litigation by a so-called ‘vulture fund’ in Hong Kong. Vulture funds are so described because they buy up distressed debt from poor countries and litigate to gain creditor judgments forcing repayment. In Congo’s case, there have been legal attempts by several companies that bought Congolese debt to attach Congolese oil cargoes as repayment. Global Witness obtained some of the documents and, struck by the fact that litigation for commercial ends had produced information of great significance

to those interested in corruption and governance, published the documents on its website. They showed the payment chain all the way from the oil cargoes, through Long Beach, to Mr Sassou Nguesso’s credit card shopping in Paris and elsewhere.

Mr Sassou Nguesso attempted to force Global Witness to take this evidence of his personal spending off its website. A UK High Court judgment in August 2007 dismissed this attempt, saying that ‘it is an obvious possible inference that [Sassou Nguesso’s] expenditure has been financed by secret personal profits made out of dealings in oil sold by Cotrade.’ Mr Justice Stanley Burnton continued that the documents, ‘unless explained, frankly suggest’ that Mr Sassou Nguesso and his company were ‘unsavoury and corrupt’, and that ‘the profits of Cotrade’s oil sales should go to the people of the Congo, not to those who rule it or their families.<sup>171</sup>

So to summarise, here is a situation where a president’s son, who is responsible for marketing his country’s oil, is apparently using proceeds from government oil sales to pay for luxury personal expenditure to the tune of hundreds of thousands of dollars, and has been described by an English judge as unsavoury and corrupt. Meanwhile the majority of the population of Congo languish in dire poverty.

### How did this happen?

What does this example involving Bank of East Asia tell us about how the requirement



The IMF criticised Hong Kong for its failure to regulate corporate services providers.  
Credit: Michael McDonough/  
Creative Commons

to do customer due diligence is interpreted in practice? There are four possibilities, all of which are legitimate interpretations of the available evidence. Without further information, Global Witness does not know which, or indeed if any, of these happened.

**Possibility 1:** Bank of East Asia did carry out its own due diligence on Long Beach, discovered that its beneficial owner was Mr Sassou Nguesso, opened the account anyway, and allowed him to use it to pay his private bills with what appears, unless proven otherwise, to be corruptly misappropriated Congolese public money.

**Possibility 2:** Bank of East Asia accepted that the owners of Long Beach were Orient Investments and Pacific Investments. Both Hong Kong's regulation and the FATF recommendations on which they are based require banks to establish the identity of the ultimate beneficial owner.

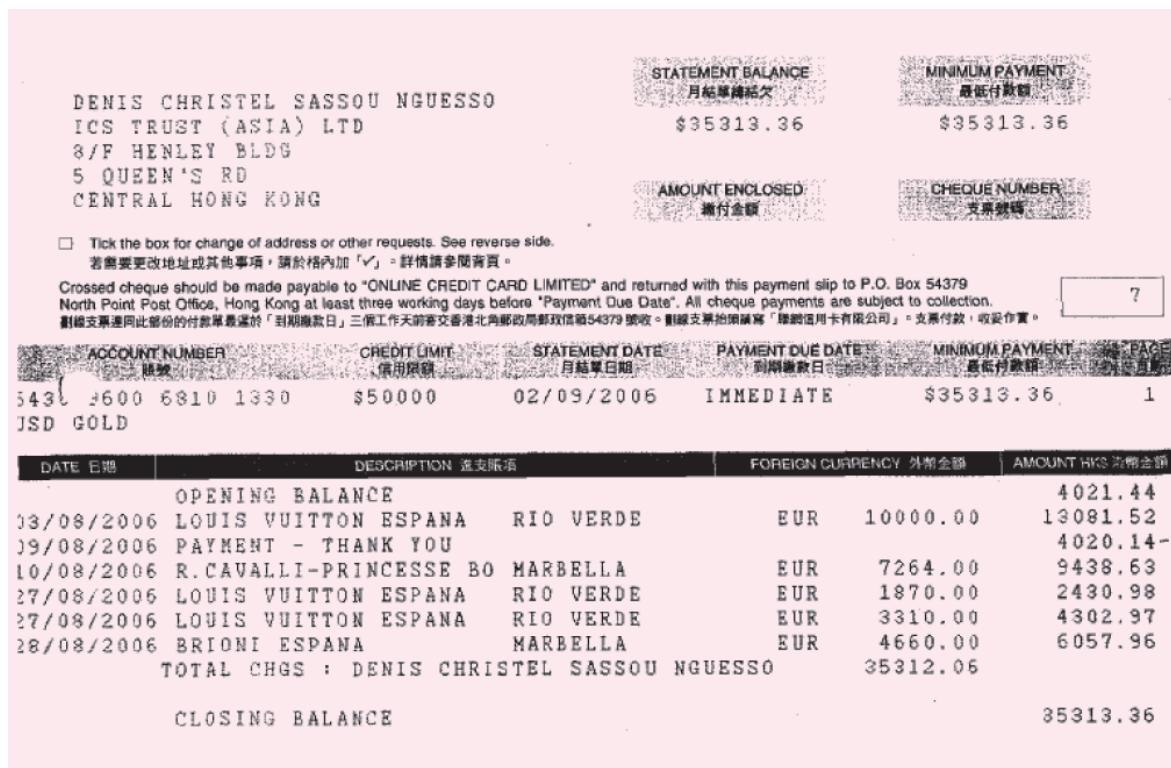
If Bank of East Asia took this course, it would not necessarily be breaking any of the rules. According to international anti money laundering and offshore finance experts consulted by Global Witness, the interpretation of this requirement varies from jurisdiction to jurisdiction. As one expert told Global Witness: 'Strictly speaking, they should find the ultimate beneficial owner. But in many

cases they settle for the trustees to be accepted as the owners. I've been talking to compliance officers about this for a long time and they've never given me a satisfactory answer.' This means that banks in some jurisdictions are ticking the box to say that they have found out the 'owner', even though that owner is just another company in an offshore haven standing in the way of the real owner. This is an empty gesture, sufficient maybe to tick a regulatory requirement but powerless to prevent politically exposed persons using the financial system to move the proceeds of corruption.

**Possibility 3:** The bank did know that the ultimate beneficial owner was not 'Orient Investments and Pacific Investments', the owners of the shares in Long Beach, but then relied on assurances from Orient Investments, the signatory on the account, that it had verified the identity of the beneficial owner of Long Beach. While it was permitted to do this by Hong Kong money laundering regulations, as long as Orient Investments is itself properly regulated, the bank retains the ultimate responsibility for knowing its customer.

However, if this last option was the case, then Bank of East Asia would have been relying for its customer due diligence on a company services provider that seems to have ignored even more red flags than the bank itself. The ICS companies, including Orient

Denis Christel Sassou Nguesso's credit card statement, showing his designer shopping in Spain during August 2006. His credit card bills were paid from an account at Bank of East Asia that received Congo's oil revenues.



Investments and Pacific Investments, could see the entire payment chain – much more than the bank could. They set up Long Beach, held its shares in trust for Mr Sassou Nguesso, arranged for its bank account to be opened, knew that Long Beach's source of income was Congolese oil, saw the credit card bills with their evidence of personal expenditure, and arranged for them to be paid from the Long Beach account. They could see the entire chain of payments. Yet they went ahead to do business with Mr Sassou Nguesso anyway.

**Possibility 4:** The bank identified its customer as the son of the President of Congo and the source of funds in his account as Congolese oil, filed a suspicious activity report to the Hong Kong authorities, who either did not respond, or gave the go-ahead for the relationship or transaction. Global Witness does not know if this was the case, because the SARS regime is kept secret by law.

This story did not come out through regulatory action, but through an unlikely combination of a vulture fund and a campaigning NGO. But have the regulators taken any action as a consequence?

## Where were the regulators?

### Hong Kong regulator

When it came into possession of the documents in 2007, Global Witness wrote to the Hong Kong Monetary Authority (HKMA), which regulates Bank of East Asia, to draw its attention to the transactions.<sup>173</sup> There was no response. In July 2008 Global Witness followed up to ask if the case had been investigated or if any other action had been taken. The HKMA responded that it was unable to comment on whether the case had been investigated, but commented: 'In light of your earlier email, we have looked into the matter and have taken appropriate actions to ensure that our guidelines are being followed by the bank concerned.'<sup>174</sup>

Global Witness also asked the Hong Kong Department of Justice if it had investigated the role of Bank of East Asia or ICS. It said that it was 'not in a position to advise on the matter you raised, as it involves investigation by law enforcement agencies. You may wish to consider writing to these agencies to make enquiries.' Global Witness did so, writing to the Hong Kong Police and the Independent Commission Against Corruption (ICAC). The Hong Kong police said they could not confirm or deny



The Hong Kong Monetary Authority allows the banks it regulates to rely on third parties such as company service providers to verify the identity of their customers. Credit: Kay Poon/Creative Commons

that any enquiries had been made; the ICAC said 'we have looked into the circumstances including examination of relevant court papers... We have arrived at a decision of taking no further action as the matter does not reveal any allegation of corruption which comes under Hong Kong jurisdiction.'<sup>175</sup>

In June 2003, five months before the Long Beach account was opened at Bank of East Asia, the IMF had criticised Hong Kong's anti-money laundering standards on precisely the issue that may be at stake in this case: **can a bank rely on intermediaries such as company service providers to verify beneficial ownership of a company opening an account?** The IMF's regular Report on Observance of Standards and Codes<sup>176</sup> for Hong Kong's anti-money laundering system found that while 'with respect to the customer identification framework... the rules are adequate and are generally well implemented,'<sup>177</sup> there were particular problems:

- '...identification of beneficial owners of shell companies, especially within the banking sector. Some domestic banks may use intermediaries who may not undertake adequate customer identification.'<sup>178</sup>
- 'Some compliance officers, especially in the domestic banks, are not as expert as they could be in recognising suspicious transactions.'<sup>179</sup>
- 'In general there is little investigation of, or enforcement action taken, with

Do the Congolese people know that their oil revenues are being siphoned off via Anguilla and Hong Kong?

Credit: Laudes Martial Mbon/IRIN



respect to AML/CFT requirements of corporate formation/secretarial services companies... Consideration should be given to focus additional law enforcement efforts on the corporate formation/secretarial companies sector'.<sup>180</sup>

At the time, the Hong Kong authorities' official response to this aspect of the 2003 evaluation was that 'In HKSAR, corporate formation/secretarial services generally consist of accountants and lawyers who are already subject to AML/CFT requirements. HKSAR conducts investigations on these services providers in line with its established enforcement policies'.<sup>181</sup> In effect, what this appears to be saying is that existing regulation is adequate – in other words, a reluctance to acknowledge the IMF's concerns. But the entity that set up and attended to Long Beach was not a lawyer or an accountant, it was a trust and company services provider that did not fall under the purview of Hong Kong's anti-money laundering regulation.

That was in 2003. In late 2007, there was another evaluation of Hong Kong's anti-money laundering regime, this time by FATF. Global Witness considers that some of FATF's standards are too lax (see Chapter 19 on page 105), but even by these standards, it is clear that the problems identified by the IMF four years earlier had not been fixed. Three key problems still stood out:

1. 'The scope of permissible reliance on third-party introductions within the banking and securities sectors is broad in terms of the type of introducer from whom the introduction may be accepted, and the country of origin of the introducer. In the banking and securities sectors, reliance may be placed on introducers who are not regulated for AML/CFT purposes.'<sup>182</sup>

FATF Recommendation 9 does allow banks to rely on third parties (such as, in this case, Orient Investments) to do the customer due diligence, as long as the third party is regulated and supervised. It is left to each country to decide in which countries the third party can be based, using information about which countries adequately apply the FATF Recommendations. A footnote to the FATF Methodology for Assessing Compliance elaborates only that 'countries could refer to reports, assessments or reviews concerning AML/CFT that are published by the FATF, FSRBs, the IMF or World Bank'.<sup>183</sup> But there is no specific guidance on how many 'non compliant' or 'partially compliant' ratings a country has to get in order to be considered not to be 'adequately' applying the FATF recommendations. In this case, Anguilla, where the business came from, had, at the point when the Long Beach account was opened, received a number of criticisms in its latest evaluation (even by the less-than-rigorous standards of the current FATF evaluation system), as will be seen later

in this chapter. Banks relying on third parties from Anguilla to do their client due diligence should, therefore, have been especially wary.

2. Key customer due diligence provisions are not required by law, and guidelines do not specifically say that senior management approval is required to continue a business relationship with a customer subsequently discovered to be a PEP.<sup>184</sup>

This means that in 2003, when the Long Beach account was opened, it was not a legal requirement in Hong Kong for banks to do customer due diligence, but merely a ‘supervisory requirement,’ ie one set by the regulator.<sup>185</sup> According to the latest FATF mutual evaluation published in June 2008, this is still the case.<sup>186</sup>

The HKMA told Global Witness that ‘breach of the regulatory guidelines is a serious matter and may lead to severe supervisory consequences. Having said that, the Government is actively considering the need to enshrine these requirements in legislation in order to be in line with the recommendations of the Financial Action Task Force.’<sup>187</sup>

What are these ‘supervisory consequences’ that, in the absence of hard law, are imposed if banks failed to do their due diligence? The HKMA said they included imposing a restriction on the institution’s business; bringing in external auditors to review the systems; downgrading the institution’s supervisory rating; withdrawing the consent

given to the responsible senior bank officials; requiring the institution to seek advice from an Advisor appointed by the HKMA; and, in an extreme case, suspending or revoking the institution’s authorisation. Global Witness then asked how often each of these sanctions had been imposed over the past five years; and whether any of them had been imposed on Bank of East Asia. The HKMA provided a series of figures about the 342 on-site examinations of banks’ AML controls it had undertaken since 2004, the 21 written warnings to senior management, the 13 cases where internal or external auditors were brought in, and the three cases in which it invoked its statutory powers to require the bank to follow its instructions or risk fines and imprisonment for the directors and chief executive. It could not, however, say whether Bank of East Asia had faced any of these consequences.<sup>188</sup>

But although it wasn’t a legal requirement to do customer due diligence when the Long Beach account was opened in 2003, it was a legal requirement to report suspicious transactions.<sup>189</sup> Global Witness asked Bank of East Asia if it had filed any suspicious transaction reports relating to the Long Beach account, but it declined to answer. The same question to ICS Trust (Asia) and Orient Investments went unanswered. Banks are not legally permitted to disclose information about SARs (the so-called ‘tipping off’ provision), so it is impossible for anyone beyond their regulators to know whether they are fulfilling their requirements. Of course, the regulators



Anguilla peddles secrecy: it does not publish details of company ownership. It is home to a number of company and trust service providers, including Orient Investments and Pacific Investments, whose clients included Denis Christel Sassou Nguesso. Credit: Atlantide Photo Travel/Corbis

The Anguilla regulator was slow in taking action after a UK judge called Sassou Nguesso and his Anguilla-regulated company “unsavoury and corrupt”.



will not say anything either, which leaves the public in countries affected by corruption none the wiser about whether anything effective is really being done to stop the banks and company service providers who assist those public officials that are ripping off the public purse. If Hong Kong’s regulatory system was getting full marks from FATF evaluations (which it clearly is not), if FATF was rigorously investigating countries’ enforcement of their laws rather than just their existence (which it is not), and if there were no loopholes in the existing standards pushed by FATF (which there are), then perhaps the interested public might be able to trust the regulators to ensure that dirty money stays out of the financial system. As it is, though, the public is left with the knowledge that somehow, money is getting through, and that not enough is being done about it.

3. As in 2003, the 2007 FATF evaluation of Hong Kong found that trust and company service providers were still not regulated on anti-money laundering and counter terrorist financing issues.<sup>190</sup>

The HKMA confirmed to Global Witness that: ‘As in many jurisdictions, company and trust service providers in Hong Kong are not currently supervised for AML/CFT purposes.’ It tried to sweeten the pill by pointing out that ‘the Hong Kong Government has made substantial efforts to promote the AML/CFT awareness of designated non-financial businesses and professions including trust and company service providers. Both the Law Society of Hong Kong and the Hong Kong Institute of Chartered Secretaries have issued comprehensive guidance to their members on AML/CFT. The Government will continue to monitor the situation and consider the need for a formal regulatory framework for these businesses and professions.’<sup>191</sup> While professional associations issuing

guidance to their members is a start, it is clearly no substitute for proper regulation.

This means that a Hong Kong company, ICS, which took part in setting up a structure which was apparently used to loot state funds in Congo, is unregulated for anti-money laundering purposes. Meanwhile, a Hong Kong bank is permitted to rely for its customer due diligence on a third party as long as that third party is in a jurisdiction that is adequately regulated. But there is no clear definition of what adequately regulated means and, in fact, the home jurisdiction of Orient and Pacific Investments, Anguilla, has faced a barrage of criticisms of its regulatory system, as will be seen below. Meanwhile there is no law in Hong Kong requiring customer due diligence to be done. These are gigantic loopholes in the Hong Kong regulatory system.

Internationally, company service providers have been covered by the FATF regulations since 2003, so by failing to regulate its company service providers, Hong Kong is failing to meet this requirement. However, Hong Kong is not alone. The US, for example, does not currently require its company formation agents to verify customer identity, although a proposed ‘Incorporation Transparency and Law Enforcement Assistance Act’ introduced in May 2008 by senators Barack Obama, Carl Levin and Norm Coleman would change this.<sup>192</sup> As one international money laundering expert put it to Global Witness, ‘outside the EU, there is considerable ambivalence about their inclusion [in the anti money laundering requirements].’ So this is not just a Hong Kong loophole, it is a global loophole.

### **Anguilla regulator**

Half way round the world in Anguilla, a small Caribbean island whose financial services industry consists primarily of company and

trust services, the anti-money laundering regulations do theoretically apply to such service providers, including Orient and Pacific Investments, the companies that set up Long Beach and held its shares in trust.<sup>193</sup>

When it obtained the documentation in 2007 Global Witness wrote to the Anguillan regulator, the Financial Services Commission (FSC), to alert it to these transactions.<sup>194</sup> In June 2008, alerted by a third party to Global Witness' continuing interest in the case, Niguel Streete, the FSC's director, emailed Global Witness to assure us that it had 'conducted a review of operations of the local agent representing the referenced companies to ensure that adequate due diligence was and continues to be conducted on the companies principals and its operations. We will continue to monitor the companies operations via our regulatory relationship with the local agent.'

Surprised that Long Beach had still been allowed to continue its operations, Global Witness wrote in July 2008 to Mr Streete to ask if the FSC considered that, following the decision of the UK High Court that unless proved otherwise, the documents showed that Mr Sassou Nguesso and his company were 'unsavoury and corrupt', it was appropriate that Anguillan companies were continuing to provide services for Mr Sassou Nguesso and his company.

Mr Streete responded six days later to say that measures had been taken to 'strike the referenced companies off the register of companies operating in Anguilla.' While it is welcome that Long Beach, a vehicle apparently used by Mr Sassou Nguesso to divert Congolese oil revenues for his own personal spending, has now been closed down, it is unclear why Mr Streete should have delayed a year after Global Witness first alerted the FSC to these transactions to do so. Global Witness asked Mr Streete whether Orient and Pacific Investments, the Anguilla-based companies that set up Long Beach and held its shares in trust for Mr Sassou Nguesso, would face any disciplinary action for having done so; and about whether Anguilla had any policies regarding sanctions for its trust and company service providers; he did not respond to these questions.<sup>195</sup>

A 2007 report by the UK's National Audit Office (NAO) into the UK's management of risk in the Overseas Territories for which it is responsible, including Anguilla, noted

that only two suspicious activity reports were filed in Anguilla during 2005.<sup>196</sup> In 2003, the IMF had called on the Anguillan authorities to 'investigate the reasons for the small number of suspicious activity reports filed to date.'<sup>197</sup> While regulators do not want to encourage financial institutions to engage in trivial suspicious activity reporting to cover their backs, the NAO noted that 'global experience shows that as tougher requirements are imposed and enforced, and effective awareness programmes implemented, the number of valid suspicious transaction reports rises substantially.'<sup>198</sup> The NAO report also noted that:

- 'Anguilla has not created a separate agency to market its financial services overseas, freeing the regulator from involvement in this potentially conflicting activity.'
- 'An IMF report in 2003 referred to the need to broaden the professional and managerial capacity of the Anguilla Commission, and to the absence of sufficient skilled persons to analyse and investigate suspicious transaction reports.'
- 'There are doubts over the extent of compliance with "know your customer" requirements. The IMF's 2003 review of Anguilla identified difficulties obtaining customer information from overseas sub agents and recommended a tightening of procedures. When the Anguillan Regulator conducted on-site checks in 2004 most agents did not have copies of the code of practice issued by the professional association, and there were numerous instances of deficient or incomplete documentation.'
- 'The Anguillan regulator's policy towards non-compliance in anti-money-laundering practice has been to encourage raised standards through education, rather than to apply sanctions on the most deficient agents. It is not evident that this has been a successful strategy. Police and Industry sources in Anguilla expressed the view to us that there are still a minority of financial service providers in the Territory which they believed would accept "any business".'<sup>199</sup>

Global Witness asked the FSC if the concerns raised in the 2003 IMF report had been addressed. It did not respond to this question.<sup>200</sup> In Global Witness's view, the IMF's concerns have been made

manifest in the story of Denis Christel Sassou Nguesso and his credit cards.

Regulation of the Anguillan financial services industry is the direct responsibility of the UK-appointed Governor, and thus is also the responsibility of the UK.<sup>201</sup> By failing to ensure that Anguilla is enforcing appropriate anti-money laundering regulations on its company and trust service providers, the UK also bears some responsibility for Mr Sassou Nguesso's apparent spending of Congo's oil money on designer shopping sprees.

## Conclusion

This story shows that the PEP provisions, which require banks to do extra due diligence if they are dealing with a PEP, are meaningless if the initial due diligence fails at the first hurdle to identify that the customer is indeed a PEP. This is why the identification of the ultimate beneficial owner of an entity such as Long Beach is so important. If banks cannot do this themselves, all the way to the natural person at the top of the chain, they should not be taking the business in the first place. Banks should not be able to rely solely on intermediaries to do their due diligence for them.

This story also shows that FATF was able to identify some of the failings in the Hong Kong and Anguilla regulatory systems which may have contributed to these transactions taking place. This is one of the things that FATF is able to do: identify problems relating to the current form of the 40 Recommendations.

But then there are two problems. Firstly, Hong Kong, despite the criticisms in 2003, had not raised its game on the most concerning issues by the time of its next evaluation four years later. Had FATF applied enough public pressure to make this happen?

Secondly, the story in this chapter is an example of a loophole that FATF is well aware of, but is not prepared to tackle properly. A FATF typologies exercise on PEPs, carried out in 2003-4, at the time the Long Beach account was being opened, identified precisely the mechanisms used by Mr Sassou Nguesso. It began by commenting that 'PEPs that come from countries or regions where corruption is endemic, organised and systemic seem to present the greatest potential risk,' then noted that 'PEPs involved in moving or concealing illegal proceeds generally do so by funnelling the funds through networks of shell

companies... in locations outside his or her country of origin that are not likely to divulge details of relevant transactions. In other cases, their financial operations may be concealed behind various other types of opaque legal arrangements such as trusts. Again, the ability of a financial institution to conduct full due diligence and apply know-your-customer principles to PEPs in this instance is severely restricted.'<sup>202</sup>

This could be a description of the Long Beach story. FATF knows what the problem is.

But FATF does not seem prepared to do what is necessary to tackle it. The typologies report continued: 'According to one FATF member, there are two principal ways in which to detect the illegal financial activities of a PEP. The first is when there is a change in government in the home country of the PEP, and his or her illegal activities are revealed by the successor regime. ...The second way... is through suspicious or unusual transactions in which persons acting on his or her behalf may be involved.'<sup>203</sup>

Global Witness would suggest that there is a third, much more powerful way to detect the illegal financial activities of a PEP, and that is our favourite word: transparency. If all jurisdictions published registries of beneficial ownership and control of companies and legal arrangements such as trusts, it would be clear even to the population of the PEP's country that he, a family member or one of his close advisers was opening shell companies to move money around. The current rules are not sufficient to deal with a problem that FATF itself has identified.

This story therefore also illustrates that FATF needs to do much more, at both levels – what it requires from member states for compliance, and how it ensures that they are enforcing their regulations.

Each chapter of this report so far has dealt with the misappropriation of natural resource revenues, with examples of poor countries' patrimony being squandered for the benefit of their ruling elite. The next chapter takes the ultimate example of this, one which led to vicious conflict: Liberia. In this next story, Global Witness investigates the involvement of what was until recently the world's biggest bank with one of the world's – at the time – most damaged countries.

### Action needed:

- Hong Kong should regulate trust and company service providers to ensure that they comply with anti-money laundering regulations.
- Hong Kong should make it a legal, rather than supervisory, requirement to perform customer due diligence.
- The Anguillan authorities should investigate the role of Orient Investments and Pacific Investments in setting up a corporate structure for Denis Christel Sassou Nguesso, if they have not done so already, and ensure that these companies officers pass an appropriate fit and proper person test to hold a corporate service provider licence.
- The UK should take responsibility for ensuring that its Overseas Territories do not provide services that facilitate corruption.
- Every jurisdiction should publish an online registry of beneficial ownership of companies and trusts. Such transparency should become a mandatory criterion for jurisdictions to be in compliance with FATF Recommendations 33 and 34, which require countries to prevent misuse of corporate vehicles and legal arrangements such as trusts.
- FATF should undertake a new name and shame list focusing on countries – including its own members – that are not implementing their regulations, rather than on the existence of a legal framework.
- FATF should publish a clearly accessible roster of each country's compliance status with each of the FATF recommendations, and the date by which that country has to comply, in order to increase the public pressure for compliance.



# 06

# CITIBANK, FORTIS AND LIBERIA'S LOGS OF WAR

Doing business with natural resources that are fuelling conflict

Ethical banking?  
Citibank and Fortis  
continued to do  
business with a  
country in meltdown.  
*Credit: Patrick  
Robert/Corbis*



There are few more stark examples of a country's wealth being pillaged and squandered by its ruler than Liberia under Charles Taylor. This one-time warlord, who launched an uprising in the west African state in 1989, became its elected president in 1997 after a devastating civil war. Civil conflict erupted again in 2000.

Taylor stepped down as president in 2003 and is now on trial in the Hague for crimes against humanity in neighbouring Sierra

Leone, where he backed a rebel group notorious for savage violence against civilians.<sup>204</sup> The war in Sierra Leone is estimated to have cost 50,000 lives.<sup>205</sup>

The history of Taylor's rule reveals a loophole in the regulation of banks, through which the funding for appalling war crimes can flow. This chapter will show that at a time when Taylor was fomenting war and atrocity, funded by Liberia's timber, he and his cronies were able to access the global banking system via



President of Liberia, **Charles Taylor** was able to route timber revenues that fuelled Liberia and Sierra Leone's conflict through Citibank in New York.  
Credit: Patrick Gardin/AP

Citibank, until recently the world's largest bank, and the Dutch/Belgian bank Fortis.

Citibank did not hold an account directly for Taylor or his government. But it acted as a correspondent bank for a Liberian bank, Liberian Bank for Development and Investment (LBDI), that did both these things. As noted previously in the Riggs chapter, a correspondent bank is one which holds an account for another bank, allowing the second bank to provide services to its customers in a country in which it does not itself have a presence. Citibank also acted as a correspondent bank for another Liberian bank, Ecobank, that was receiving payments for the timber that was fuelling the war. A branch of Fortis in Singapore received these payments directly.

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*The history of Taylor's rule reveals a loophole in the regulation of banks, through which the funding for appalling war crimes can flow.*

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So this is a story about how Citibank held correspondent relationships with banks in a country that was in absolute meltdown. Correspondent relationships are normal and legitimate in the banking industry. But in this case, they enabled a vicious warlord to use the global banking system to earn revenues from timber sales, which were then ploughed

into his war effort, as well as into his own bank account.

The question raised by this story is: what should Citibank and Fortis have known about Liberia, and about the nature of their clients there? And what should regulators do to prevent the abuse of the banking system by warlords like Taylor?

From January 2001 onwards, Global Witness as well as other NGOs and the UN repeatedly documented how Liberia's timber exports were being used to pay for weapons and ammunition. Taylor used these arms to support a campaign of terror waged in Sierra Leone by the rebels of the Revolutionary United Front. Timber profits were also used to pay for Taylor's own security forces in Liberia, which were implicated in numerous human rights abuses.<sup>206</sup>

At the centre of this trade was the Oriental Timber Company (OTC), run by Dutch national Guus Kouwenhoven, a close associate of Taylor. OTC had been granted the rights to manage a massive 1.6 million hectare logging concession, 42% of Liberia's total productive forest, and also controlled the port of Buchanan through which arms shipments were entering Liberia. OTC used logging roads to bring the timber out of Liberia, and to move the weapons in and across the border with Sierra Leone. Like other logging companies in Liberia, OTC maintained notorious private

The Liberian Ministry of Finance under Taylor's rule instructed logging company OTC to pay timber revenues into Taylor's personal bank account in lieu of forestry taxes.

Credit: Global Witness



militias which committed human rights violations against Liberian civilians.<sup>207</sup>

OTC (also known to Liberians as 'Only Taylor Chops') was one of the key props of Taylor's shadow state, which whittled away the bureaucracy of national government to almost nothing in favour of strategic economic alliances with external actors. These actors included both multinational companies, such as those trading rubber, as well as those operating in the black market such as arms dealers and gem smugglers. These economic alliances with willing international partners – forged before 1997 when Taylor was a warlord, and after the 1997 election with the full weight of sovereignty behind him – were to a great extent the source of Taylor's strength, affording him

the means to sponsor atrocities at home and in neighbouring countries in order to pursue his ambitions of regional destabilisation.<sup>208</sup>

### Citibank, the correspondent account and Charles Taylor

In July 2000, the Liberian Ministry of Finance sent a letter to the general manager of OTC, instructing him to transfer \$2 million 'against forestry-related taxes' to an account at the Liberia Bank for Development and Investment (LBDI). Global Witness has a copy of this letter which gives the number of the account at LBDI as 0020132851-01. The letter said that the transfer was to be made through Citibank, 399 Park Avenue, New York.<sup>209</sup>

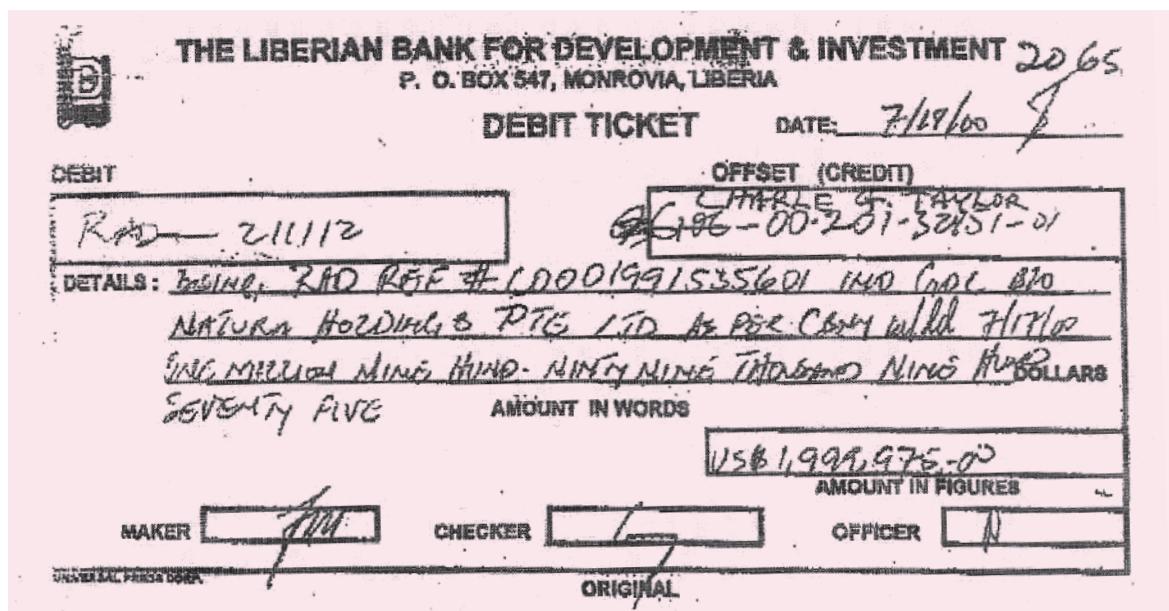
A UN Panel of Experts on Liberia, mandated by the Security Council to 'investigate sanctions on arms, diamonds, and individuals and entities deemed a threat to regional peace,' revealed in a 2007 report that this bank account at LBDI belonged to Charles Taylor. The panel published a bank statement issued by LBDI which identifies the holder of account 0020132851-01 as 'Taylor, Charles G.' and describes it as 'US dollar checking accounts – personal,' as well as a debit ticket for the deposit of the funds into the account.<sup>210</sup> In other words, Citibank was processing a payment of government timber revenues to a personal account at a Liberian bank in Taylor's name.

The role of OTC and timber revenues in propping up Taylor's brutal rule may not have been well known in mid-2000 when this \$2 million transfer took place.

**Sanford Weill,**  
Citigroup CEO  
1998-2003. At this time Citibank held a correspondent account for the Liberian Bank for Development and Investment, allowing its clients – including Charles Taylor – access to dollar payments.

Credit: Michele Asselin/Corbis





Debit ticket showing payment of nearly \$2 million on 18 July 2000 from Natura Holdings, a company associated with OTC, into Charles Taylor's personal bank account at Liberia Bank for Development and Investment.

Statement of Account							
LIBERIAN BANK FOR DEVELOPMENT AND INVESTMENT							
HEAD OFFICE BRANCH (US DOLLAR)				For Correspondents Call us at 22211 or Fax us Bank Sort Code: 000-000			
<b>00.201-32851-01 (32851-01)</b>				<b>CHARLES G. TAYLOR CONGO TOWN MONROVIA, LIBERIA</b>			
THIS STATEMENT COVERS 01 Jul 2000 THROUGH 31 Jul 2000							
Trx Date	TxRef	Details	Ghq No	Value Date	Debits	Credits	Balance
<i>Jul 2000</i>							<i>Payee</i>
01 0000		BALANCE 8/0				2,274.32	
11 19377		COMM ON TOD			-2,000.00		274.32
11 19380		T6 CHECK CASHED	033532		-100,000.00		-99,725.88
11 19389		PER DEBIT CHARGE			-1.10		-99,726.78
17 20571		T2 CHECK CASHED	033636		-250,000.00		-349,726.78
17 20571		PER DEBIT CHARGE			-1.10		-349,727.88
18 20856		RAD ING C.G.T. B/O NATURA HOL			1,998,975.00		1,650,247.12
18 20883		COM ON RAD DD 7/17/00			-26,990.66		1,623,247.46
18 20883		PER DEBIT CHARGE			-1.10		1,623,246.36
18 20792		T6 CHECK CASHED	033551		-240,000.00		1,383,246.36

Statement for Charles Taylor's personal bank account showing the deposit.

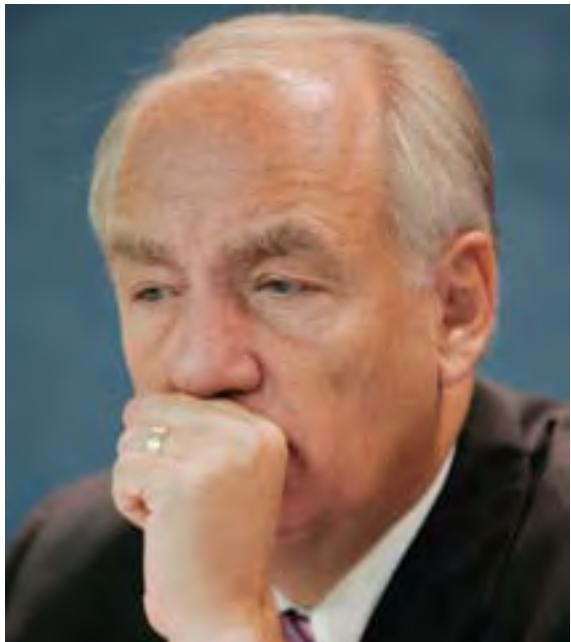
Nor was it well known at this point that, as the Panel of Experts was later to report, Taylor's government hid extra-budgetary income and spending by instructing OTC to make payments to various bank accounts around the world (including those of alleged arms dealers), rather than to the government's own account for tax receipts.<sup>211</sup>

But it was well known at the time that Taylor was a former warlord who had plunged his country into a devastating civil war. A series of articles in the *Washington Post* in 1999 and the first half of 2000 reported

on Taylor's reign of chaos in Liberia as well as his support for the vicious rebels in neighbouring Sierra Leone.<sup>212</sup> The US State Department's annual human rights report for 1999 painted a damning picture of the human rights record of Taylor's regime.<sup>213</sup>

Banks that hold correspondent accounts cannot be expected to know who all of their correspondent banks' individual clients are. This is why correspondent banking is recognised as presenting a high risk of money laundering. The best defence that banks have against correspondent risk is careful due

**Stephen Rapp,**  
Chief Prosecutor for  
the Special Court for  
Sierra Leone, is on  
the hunt for Taylor's  
reputed billions.  
*Credit: Shawn Thew/  
EPA/Corbis*



diligence of the correspondent bank itself. What are its know your customer procedures? What type of customers does it accept? How well does it keep customer records? How well is it regulated? In other words, if the major bank cannot do due diligence on every single customer of its correspondent, it should at least understand its correspondent's ability to do so, and the environment in which it is operating.<sup>214</sup> Given the well-known and well-reported state of mayhem in Liberia, it is not clear how Citibank could have reassured itself that its correspondent bank, LBDI, had good anti-money laundering systems in place.

At the time of this payment there was no explicit legal requirement to do due diligence on the correspondent client. (This changed in July 2002 when the correspondent banking provisions of the Patriot Act came into force.<sup>215</sup>) However, under the 1970 Bank Secrecy Act, US banks were already required to do due diligence on their customers, and guidance on how to meet these requirements, published in 1993 by the OCC, Citibank's regulator, highlighted that banks needed to know their correspondent banks' business.<sup>216</sup> In its response to a survey of US banks' correspondent relationships by the US Senate Subcommittee on Investigations, published in February 2000, Citibank said that it did determine an applicant bank's primary lines of business.<sup>217</sup>

Global Witness wrote to Citibank in July 2008 to ask what due diligence it had done on LBDI and its know your customer procedures, and whether it had ever filed any suspicious activity

reports in relation to LBDI. Global Witness also asked if Citibank knew that one of its correspondent's customers was the president of Liberia, and whether it knew that government timber revenues were being diverted into his account. Citibank replied but declined to answer these questions: 'In accordance with Citi policy and general principles underlying applicable law, I am unable to confirm or deny whether a person is a Citi customer or to provide the other information requested.'<sup>218</sup>

The correspondent account held by LBDI at Citibank in New York featured in another of the letters from the Liberian Ministry of Finance to OTC. Global Witness has a copy of the letter which shows that on 10 April 2001, OTC was instructed to pay US \$1.5 million in lieu of forestry taxes 'to Liberia Bank for Development and Investment through: Citibank, 399 Park Avenue, New York, NY 10043, A/C#36006105.'<sup>219</sup>

Stephen Rapp, Chief Prosecutor of the Special Court for Sierra Leone, where Taylor is currently on trial, has spoken to the press about his search for Taylor's wealth. Quoted in a Sierra Leonean newspaper, Rapp mentions 'two accounts in the US in which there were \$5 billion of activity... but a lot of it was money moving back and forth between the two accounts in order to maximise daily interest payments. But at least \$375 million we've identified as moving out of those accounts into other banks in the US and elsewhere around the world...' <sup>220</sup> Mr Rapp subsequently confirmed this information to Global Witness.

The accounts were closed, according to Reuters, in December 2003, four months





Liberian Bank for Development and Investment confirmed its correspondent account at Citibank in New York to Global Witness.  
Credit: Tim A. Hetherington/Panos

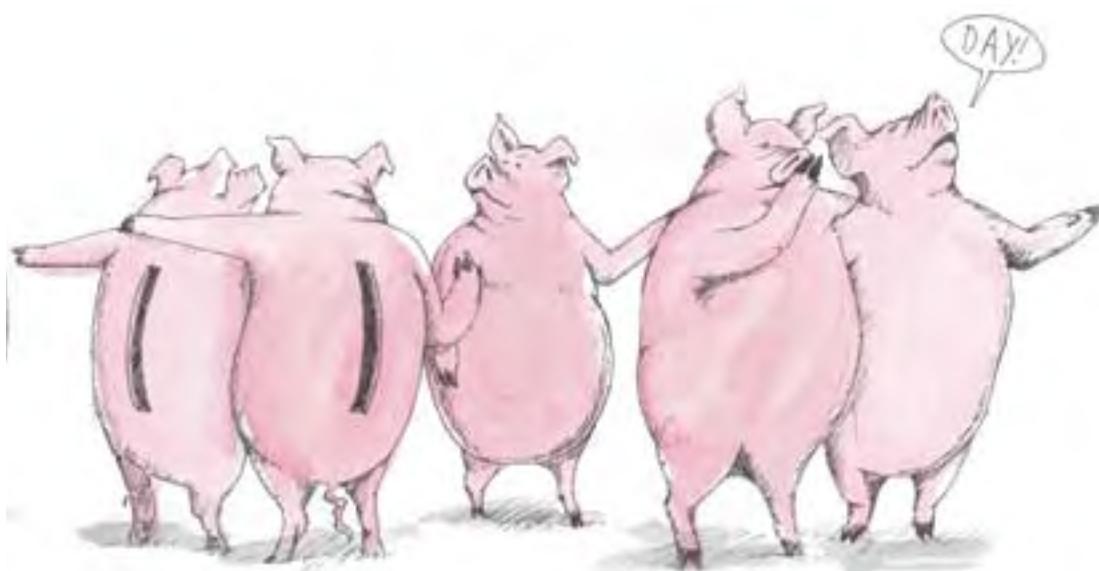
after Taylor stepped down as President.<sup>221</sup> According to Global Witness sources, at least one of the accounts Mr Rapp is referring to is this LBDI account at Citibank.<sup>222</sup>

A third letter from the Ministry of Finance to OTC, dated 29 May 1999, instructs OTC to pay \$2.5 million in lieu of forestry taxes to 'GOL Tax a/c #111-000043 through ABA-021-000089 Citibank NA, 399 Park Ave, New York NY 10043, A/C#36006105 FFC.'<sup>223</sup> FFC is likely to mean 'for further credit,' and this last account number is the same as the LBDI account above, suggesting that this payment for the Government of

Liberia tax account was also destined for the same LBDI account at Citibank.

Global Witness asked Citibank what due diligence it had done to identify the beneficial owners and source of funds of these accounts; whether it had monitored ongoing transactions through the accounts; and whether it had ever filed any suspicious transaction or suspicious activity reports relating to these accounts. Again, Citibank said it could not answer.<sup>224</sup>

Over in Monrovia, however, LBDI was rather more forthcoming. In response to Global Witness's enquiries, it confirmed



Do banks have reliable information about the standard of their correspondent banks' customer due diligence?

Citibank ended its correspondent relationship with Liberia Bank for Development and Investment in 2003, after Taylor had gone. In May 2008, it attempted to restart the relationship.

*Credit: Global Witness*



that it did hold account number 36006105 at Citibank, and that it was opened in the 1960s. The authorised signatories were LBDI 'Executive Managers'. Global Witness asked LBDI what due diligence it had done on the ultimate beneficiaries of the account, that is, its own customers. It responded: 'LBDI followed its Know Your Customer special operating procedure to the extent possible. The account is a correspondent banking relationship and the ultimate beneficiaries are LBDI customers who are diverse.'<sup>225</sup>

LBDI enclosed a know-your-customer profile checklist used for new customers, dated 2003 (long after the account was opened). While it asks if a customer's identity and a transparent source of funds have been identified and verified, there is no mention of politically exposed persons. It does, however, require that customers be informed that 'their account could and will be monitored from time to time in compliance with the CBL provisions, LBDI regulations and the Patriot Act at the request of our correspondent bank, Citibank' and that 'Citibank may cease any transfer deemed to be suspicious [sic] by Citibank'. LBDI did not make it clear if this policy was in operation before 2003, and did not respond to further requests from Global Witness to clarify this point.

LBDI said it had never filed any suspicious activity reports relating to the account, as 'there was never any suspicious activity observed.'

LBDI said that this correspondent account at Citibank was closed in November 2003, and provided correspondence between LBDI and Citibank about the closure. It appeared to have nothing to do with the change of government in Liberia: Citibank was withdrawing from 14 countries for strategic reasons. A representative of Citigroup in Johannesburg wrote to LBDI saying: 'Citigroup is repositioning its NPC Africa operations to focus on customers in specific countries which we can best serve given our product offering and infrastructure located in Johannesburg. As a result of this repositioning, Citigroup will no longer be able to service customers in Liberia in an appropriate manner. It is for this reason that we are advising you that we will no longer be able to continue maintaining your above-noted account(s) and are requesting that you make alternative banking arrangements.' The accounts referred to are US dollar accounts 36006105 and 36071783.<sup>226</sup> Global Witness does not have any other information about this second account.

This means that Citibank kept its correspondent relationship with LBDI open all the way through Liberia's worst years, at a time when the last thing the country needed was a US bank willing to process dollar payments into Taylor's account, and during which Liberian banks had very little ability to find out who their customers were and keep appropriate records. It then ended the relationship just as Liberia was entering a potentially more stable post-Taylor transitional period and was most in need of access to international financial markets in order to rebuild itself.

In May 2008, however, Citibank's Johannesburg office wrote to LBDI to 'reiterate our desire as an institution to re-establish correspondent banking activities with LBDI.' The letter continued, 'The relationship we had in the past over approximately a 12-13 years period was strong and without any major incident. Unfortunately, as explained in our mails due to a strategic decision linked to our inability to best serve clients [sic] needs in Liberia, we were forced to end our relationship with your bank... We hope that this letter gives you enough comfort and enables us to rekindle what was once a great partnership.'<sup>227</sup>



Ecobank said its offices were 'looted a number of times' during Liberia's conflict. So how did Citibank carry out adequate due diligence on its correspondent bank?  
Credit: Global Witness

Global Witness asked LBDI if it planned to renew its relationship with Citibank; it did not reply.

### Citibank, another correspondent relationship, and payments for 'conflict timber'

As well as the letters from the Liberian Ministry of Finance instructing OTC to make various payments in lieu of forestry taxes, Global Witness also has copies of the invoices OTC sent to its timber-purchasing clients in Europe, Asia and America.

Between November 2001 and April 2002, operating under the name Evergreen Trading Corporation, OTC instructed its timber-purchasing clients around the world to make at least 37 separate payments for timber through a branch of Citibank at 111 Wall Street in New York. OTC was requesting that its clients settle their bills to Evergreen's dollar account

at Ecobank Liberia, account number 1021-0022-81201-7, routed through the Wall Street branch of Citibank in New York, swift code CITIUS33, 'For credit to Ecobank Liberia Limited, Account Number 36147565.'<sup>228</sup> Given the number of separate invoices with the same bank details, it is reasonable to assume that these payments were indeed being made.

This means that Citibank, through its correspondent relationship with Ecobank, was processing timber payments that were fuelling West Africa's wars. Global Witness wrote to Citibank to ask about these payments, but it said it could not answer.

As with the LBDI relationship, Citibank cannot be expected to know every single one of its Ecobank's clients. However, by the time these payments began in November 2001, new guidance had been issued to US banks on knowing their correspondent banks. In



'Only Taylor Chops': the Oriental Timber Company was a key prop in Taylor's shadow state.  
Credit: Global Witness

September 2000, Citibank's regulator, the OCC, published the Bank Secrecy Act / Anti-Money Laundering Handbook to help them meet their AML obligations under the 1970 Bank Secrecy Act and the 1986 Money Laundering Control Act. Recognising that correspondent banking relationships represented a higher risk, particularly if they were conducting wire transfers, it said: 'Information should be gathered to understand fully the nature of the correspondent's business. Factors to consider include the purpose of the account, whether the correspondent bank is located in a bank secrecy or money laundering haven... the level of the correspondent's money laundering prevention and detection efforts, and the condition of bank regulation and supervision in the correspondent's country.'<sup>229</sup>

Even if Citibank was not able to see the beneficiaries of individual wire transfers

through Ecobank's account in New York, basic research into the type of clients that Ecobank was serving in Liberia might have revealed the importance of timber to Liberia's economy. By the time of these payments, the following information was in the public domain linking Liberian timber to funding for the war in Sierra Leone and Liberia:

- In September 2001, Global Witness published *Taylor-made: The pivotal role of Liberia's forests and flag of convenience in regional conflict*, which showed how the Liberian timber industry, with OTC at the fore, was being used to fund Taylor's support for the rebels in Sierra Leone, and which called for sanctions on Liberian timber.<sup>230</sup>
- In October 2001, a UN Panel of Experts report said that Liberian timber production

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Children were recruited as soldiers in the conflicts that Taylor ignited in Sierra Leone and Liberia.  
Credit: Patrick Robert/Corbis



was a source of revenue for sanctions busting, and said that a payment for weapons delivery was made to an arms trafficking company by the Singapore parent company of OTC, Borneo Jaya Pte.<sup>231</sup>

- In March 2002, Global Witness published *The Logs of War: The Timber Trade and Armed Conflict*, which elaborated the ways in which timber companies, and specifically OTC, were deeply involved in supporting the violence in Sierra Leone and Liberia. The report said that ‘the industry cannot claim to be unaware that timber is coming from a country gripped by armed conflict. It is our assertion, that in situations of armed conflict these companies should not be permitted to pursue business as usual.’<sup>232</sup>

Global Witness asked Ecobank what due diligence it did on its client OTC, and whether it could confirm its correspondent relationship with Citibank. Ecobank responded that ‘our records indicate no activity on that account during the period in question.’ However, it continued, ‘the period to which your enquiry refers was an extremely difficult time in Liberia and, as one might expect, Ecobank was not completely insulated from the crisis. Our offices were looted a number of times, and several of our files and computer systems were taken away or destroyed. This has created significant problems with information retrieval, and made transaction cross-referencing virtually impossible... Ecobank maintains KYC procedures that are in line with international standards, and is proactive in dealing with anti-money laundering matters.’<sup>233</sup>

The fact that Ecobank’s record-keeping system was so compromised during the conflict raises questions as to how Citibank could possibly be confident in its correspondent’s ability to monitor its clients.

Global Witness wrote to Citibank to ask what due diligence it did on its client Ecobank in Monrovia and its customers. We asked if it knew what measures its Liberian correspondent banks were using to assess their personal and corporate clients, and how it could be sure that the Liberian banks knew who their clients were given the instability of the situation in Liberia and the almost complete vacuum where effective government should have been, let alone appropriate financial regulation.

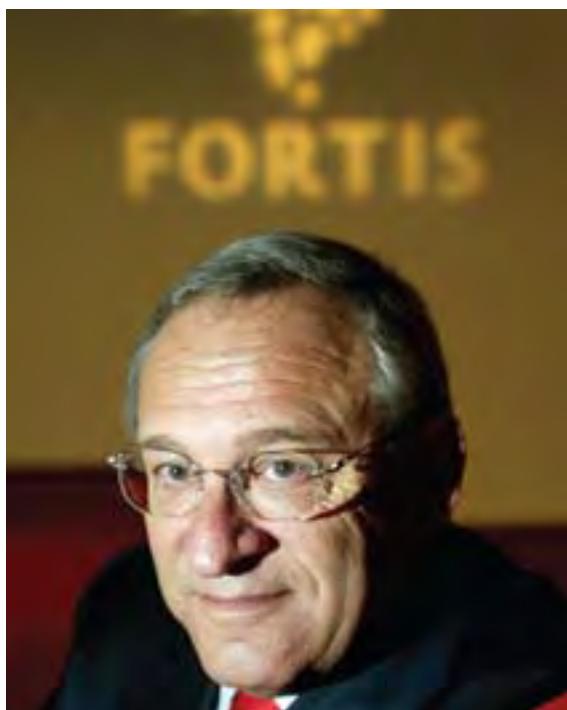
Citibank said it could not answer, adding that ‘Citi takes seriously its obligation to combat money laundering and terrorist financing.... Citi has adopted a Global Anti-Money Laundering and Anti-Terrorist Financing Policy that requires all Citi businesses worldwide to develop and implement effective programs to comply with applicable laws.’<sup>234</sup>

When Citigroup, the owners of Citibank, were contacted in July 2003 by Greenpeace, which was working with Global Witness on the environmental impact of OTC’s logging, Citigroup responded that ‘We have conducted an extensive search of our records and were unable to identify any relationships with the Oriental Timber Company or any of the other associated companies.’<sup>235</sup>

This would appear to indicate a disturbing inability to trace information relating to correspondent banking relationships at Citibank. Global Witness asked Citibank if it had searched its correspondent banking records, as well as its records of direct banking relationships, when it replied to Greenpeace in 2003, and what action it had taken regarding the accounts after receiving the letter. Citibank said it could not respond.<sup>236</sup>

### **Fortis: receiving direct payments for conflict timber**

OTC’s invoices also show that prior to November 2001, the company instructed its timber-



**Anton von Rossum,**  
CEO of Fortis until  
2004. Fortis accepted  
payments for timber  
that was fuelling  
Liberia's conflict.  
*Credit: Francois  
Lenoir/Reuters/  
Corbis*

purchasing customers to make their payments directly into an account at Fortis in Singapore.

Between December 2000 and September 2001, OTC instructed its timber purchasing clients in Europe, Asia and America to make at least 20 separate payments, worth at least \$2.36 million, to a branch of Fortis in Singapore.

OTC was requesting that its clients settle their bills to an account of Natura Holdings PTE Ltd at Fortis in Singapore, account number NSO190 and Swift code MEESSGSGTCF.<sup>237</sup> Global Witness has previously documented some of the complex corporate history of Natura Holdings and its relationship with OTC.<sup>238</sup>

Again, given the number of separate invoices with the same bank details, it is reasonable to assume that these payments were indeed being made. However, there was no indirect correspondent relationship here; these were payments made directly into an account at Fortis.

This means that Fortis was processing timber payments that were fuelling West Africa's wars. Global Witness wrote to Fortis to ask about these payments, but it said it could not answer.

At the time of these payments to Fortis, banks in Singapore were required by their regulator to do customer due diligence.<sup>239</sup>

As the UN Panel of Experts was already publicly documenting money from timber

sales was being used to purchase weapons that were being used against civilians, and OTC had been named as being involved. At the time of the payments to OTC's dollar account at Fortis, the following information about the links between timber and the Liberian conflict was publicly available:

- In December 2000, a UN Panel of Experts highlighted the active role of the Liberian timber industry in arms shipments that were fuelling the civil war in Sierra Leone, and named the Oriental Timber Company as being involved in this trade.<sup>240</sup>
- In March 2001, the UN Security Council placed Liberia under an arms embargo and imposed sanctions on the sale of rough diamonds from Liberia.<sup>241</sup>
- From June 2001 until December 2008, Gus Kouwenhoven, OTC's boss, was put on a UN travel ban list.<sup>242</sup>

Global Witness wrote to Fortis to ask what due diligence it had done on its client Natura Holdings Pte and its sources of income, and whether it filed any suspicious activity reports relating to the account. Fortis responded to say that 'following the strict rules for client confidentiality, more specific those rules that we are subject to under Singapore law,' it could not comment.<sup>243</sup>

Even if Fortis did identify its client and its source of income, however, there was not then – and still is not now – any requirement to turn down funds that derive from sales of natural resources that are fuelling conflict.

Global Witness asked the OCC, Citibank's regulator in the US, and the Monetary Authority of Singapore, which regulates Fortis's Singapore branch, if their attention had been drawn to these accounts or transactions, and if any action had been taken. The OCC responded that it was unable to comment on the scope, knowledge or extent of its confidential supervisory activities, but added that it would review the information concerning the OTC transactions at Citibank and would 'forward it to the Examiner-in-Charge of Citibank for supervisory consideration.'<sup>244</sup>

The Monetary Authority of Singapore pointed out that as part of its supervisory responsibilities it had implemented the 2004 Taylor asset freeze, and commented:

**Gus Kouwenhoven,**  
Oriental Timber  
Company's boss,  
was put on a UN  
travel ban list  
from June 2001  
to December 2008.



'when the allegations against a Singapore company, Borneo Jaya Pte Ltd,<sup>245</sup> with apparent links to a sanctioned Liberian company, Oriental Trading Company, were first made, Singapore's Ministry of Foreign Affairs had asked both the UNSC's Panel of Experts of the Liberia Sanctions Committee and the Sanctions Committee itself for more specific information that would allow Singapore to properly investigate the matter. Unfortunately we did not receive specific information that would have enabled us to investigate the matter further.'<sup>246</sup>

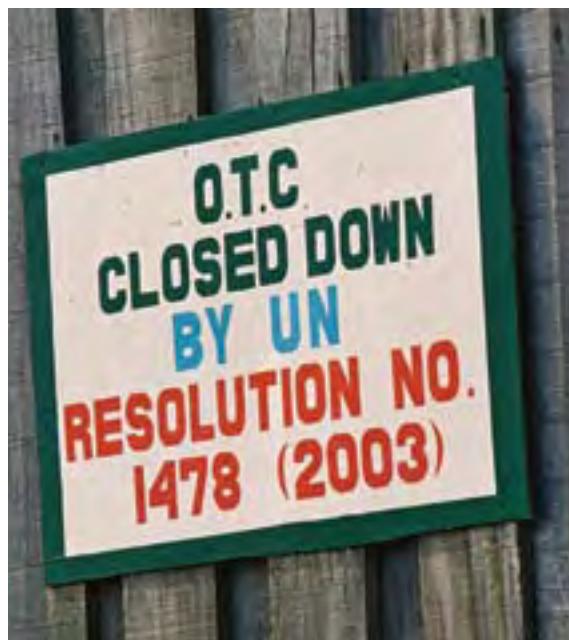
### What happened next?

Global Witness's concerns about Charles Taylor and his use of Liberia's timber have since been vindicated.

- Charles Taylor is currently on trial for war crimes at the Special Court for Sierra Leone, sitting in the Hague.
- Timber sanctions were finally imposed on Liberia in July 2003 – after several years of opposition from France and China, both significant importers of Liberian logs.<sup>247</sup> Sanctions were lifted in June 2006 despite concerns from Global Witness and other experts that there were not yet sufficient safeguards in place to prevent predatory logging practices.<sup>248</sup>
- On 7 March 2003, the Special Court for Sierra Leone called on all states to locate and freeze any bank accounts linked to Taylor and others under investigation for war crimes in Sierra Leone.<sup>249</sup>
- In March 2004, the UN called on all states to freeze the assets of Charles Taylor, his family members and associates, and other individuals associated with his regime including alleged arms dealers. The freeze was implemented in the US through Presidential Executive Order 13348 of 22 July 2004.<sup>250</sup> Global Witness asked Citibank if, in addition to checking its own accounts for these individuals, it scrutinised its correspondent accounts with Liberian banks at this point, in order to ensure that the individuals on the asset freeze list were not able to obtain indirect access to the global financial system. Citibank declined to respond.<sup>251</sup>
- A multi-stakeholder review of Liberia's forests concessions in 2005 (which concluded that none of the concessions



Taylor is currently on trial for war crimes.  
Credit: Patrick Robert/Sygma/Corbis



Oriental Timber Company's operations in Liberia were finally shut down in July 2003, when the UN put sanctions on Liberian timber following campaigning by Global Witness and other NGOs.  
Credit: Global Witness

were in compliance with the minimum legal criteria) found that after Taylor took office in the late 1990s, less than 14% of all timber taxes assessed were actually paid into government accounts and used to fund governmental functions or development.<sup>252</sup>

As a result of some of these revelations, Guus Kouwenhoven, OTC's president, was prosecuted in the Netherlands for war crimes and breaking a UN arms embargo. He was initially convicted at trial in June 2006 of breaking the UN arms embargo on Liberia,<sup>253</sup> however his conviction was subsequently overturned at appeal in March 2008 on grounds of contradictory witness testimony.<sup>254</sup>

In 2004 Citibank announced an anti-illegal logging initiative, whereby it requires timber firms seeking loans to make representations about their compliance with logging laws, and bankers managing relationships with companies involved in logging to conduct an annual risk assessment.<sup>255</sup>

As a result of the US Patriot Act, which belatedly recognised the inherent risks of correspondent banking (which are that a bank cannot know who all of its correspondent bank's individual clients are), Citibank should since July 2002 have been compelled to implement the new regulatory standards on correspondent banking, which focus on ensuring that the foreign correspondent bank wanting access has got sufficient customer due diligence systems in place and is sufficiently regulated itself. These standards require banks to understand the ownership structure of their correspondent bank and whether it provides correspondent services to other foreign banks, and to conduct enhanced scrutiny of the account and report any suspicious transactions.<sup>256</sup> These are similar to the standards set out in FATF Recommendation 7. Global Witness wrote to Citibank to ask how it does customer due diligence on correspondent accounts these days; and whether it still maintains correspondent relationships with Liberian banks; it declined to respond.<sup>257</sup>

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*The conflict in Liberia is over. But resource-driven conflict has reigned once again in Democratic Republic of Congo (DRC). Which banks are handling the profits of the minerals that are fuelling Congo's war?*

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Global Witness understands from its sources that some major banks in the US have terminated some of their correspondent relationships as a result of the new rules.<sup>258</sup>

Global Witness also asked Citibank and Fortis, as well as LBDI and Ecobank, if they have systems in place to recognise the proceeds of conflict resources, even if they have not directly been embargoed, in order to prevent themselves from being embroiled in such a situation in the future. Citibank, Fortis and Ecobank did not answer the question; LBDI said it did not have such systems in place.<sup>259</sup>

Global Witness then asked the OCC and the Singaporean and Belgian regulators about the due diligence requirements for a financial institution doing business with a company operating in a conflict zone, and what guidance is provided to financial institutions doing business in conflict zones. The Monetary Authority of Singapore did not respond to this question. The Belgian regulator – the Banking Finance, and Insurance Commission – which is one of Fortis's home regulators, replied: 'there is to our knowledge no requirement or guidance, either at the international or at the national level, specifically applicable to operations or activities of credit institutions in conflict zones. Nevertheless, the specific risks linked to such operations and activities are included, at a more general level, within the scope of the standards concerning customer due diligence and the prevention of the use of the financial sector for the purpose of money laundering.' The OCC responded in a similar vein.<sup>260</sup>

Although banks are already required to do customer due diligence and all claim to have put systems in place in order to comply with their regulators, Global Witness fears that this may not be enough to steer banks away from the devastating and largely unregulated trade in conflict resources, particularly where the international community has been slow to impose sanctions. Specific guidance should be given to financial institutions so that they can identify and avoid doing business with those that are trading natural resources that are fuelling conflict. At the moment, there is no regulation in place that would prevent this situation happening again.

## Conclusion

It ought to have been common sense. It was known internationally that Liberia was in a mess of epic proportions, and that the UN was involved. A bank with ethics would not have been doing business with timber traders at a time when concerns were being raised about timber fuelling the war. Once again, however, it was UN investigators and NGOs who brought attention to this situation, rather than the regulators, who were not required to keep a watch for situations like this. Meanwhile, the banks have allowed their reputations to be besmirched.

The conflict in Liberia is over. But resource-driven conflict has reigned once again in Democratic Republic of Congo (DRC). Which banks are handling the profits of the minerals that are fuelling Congo's war? The provinces of



A woman is consoled by her neighbour after her son, a teacher, was killed near Goma in the Democratic Republic of Congo on 6 November 2008. Which banks are handling the profits of the minerals that are now fuelling Congo's war?  
Credit: Kate Holt

North and South Kivu, in eastern DRC, are rich in cassiterite (tin ore), gold and coltan. The desire to gain or maintain control of these mines and the resulting trade has been a central motivating factor for all the warring parties since 1998. Ten years on, rebel groups as well as units and commanders of the Congolese national army continue to enrich themselves directly from the mineral trade and are able to access international markets. Some groups dig the minerals themselves, others force civilians to work for them, or extort 'taxes' in minerals or cash. The profits they make enable them to keep fighting, exerting an unbearable toll on the civilian population, just as the profits from timber supported Taylor's wars in Sierra Leone and Liberia.<sup>261</sup>

Global Witness has already called on the companies that are buying Congolese minerals to exercise stringent due diligence on their mineral supplies.<sup>262</sup> But the banks that facilitate payments for these minerals and bank the profits that companies make from them should also exercise stringent due diligence to avoid handling the proceeds of minerals that are fuelling this conflict.

When a country is unstable, there should be an extra duty of due diligence on banks doing business in that country – whether directly or through a correspondent relationship – to ensure that they are not

dealing in any way with natural resources that are fuelling conflict. When setting up, or maintaining, a correspondent relationship in such circumstances, they must take rigorous steps to satisfy themselves that their potential correspondent bank is not fronting for or doing business with warlords or those who are funding conflict.

The anti-money laundering regulations might have been developed since this time, but they still do not explicitly tackle transactions that may be fuelling conflict. Nor do the standards of the Wolfsberg Group, of which Citibank is a member.

The next chapter moves onto another bank in a relationship with one of the worst regimes in the world: Deutsche Bank and Turkmenistan. However, this is hardly a correspondent relationship, but a major relationship worth billions of dollars.

### Action needed:

- Banks should be required to develop systems to recognise and avoid the proceeds of conflict resources, regardless of whether official sanctions have yet been applied.

# 07

# DEUTSCHE BANK AND TURKMENISTAN

Doing business with a human rights abuser

A shining example?  
Turkmenistan's late  
dictator, Niyazov,  
spent millions on  
pet projects such  
as this golden  
statue of himself.  
*Credit: Global Witness*



This chapter turns to Turkmenistan, and the relationship between Deutsche Bank and the late dictator and president-for-life, Saparmurat Niyazov, who died in December 2006. The story raises a question that is not currently addressed in the regulation of banks, but should be: how should banks treat a nominally sovereign government when in reality, that government has been captured by a single individual who uses the powers and the funds of the state to oppress his own people? It also raises the question of what information about state

accounts should be available in the public domain.

Whilst investigating the destination of Turkmenistan's prodigious natural gas wealth, Global Witness was intrigued to discover that Deutsche Bank was holding accounts of the Turkmen Central Bank which appeared to be under the effective control of the late president Saparmurat Niyazov.

Under Niyazov's disastrous 15-year rule, which ended with his death in



While Niyazov spent money on vanity projects, 58% of the population are estimated to live in poverty.  
Credit: Global Witness

December 2006, Turkmenistan became one of the most repressive, corrupt and secretive regimes in the world.

Niyazov came to power in 1991. Deutsche Bank held Turkmen state funds since 1995, according to a former governor of the Turkmen Central bank in an interview with Global Witness.<sup>263</sup> The *Financial Times* has reported that Deutsche Bank held Turkmen accounts since the early 1990s.<sup>264</sup>

In other words Deutsche Bank, was, for most of the time that Niyazov was in power, serving as a banker to his regime. This was not a hands-off relationship. Niyazov made a visit to Germany in 1997 which was to include meetings with top officials at Deutsche Bank.<sup>265</sup> From 1998, if not earlier, Deutsche Bank had an office in the Turkmen capital Ashgabat.<sup>266</sup> In 2000, Deutsche Bank board member Tessen von Heydebreck visited Ashgabat to meet Niyazov.<sup>267</sup>

The Niyazov regime was not only totally secretive in its handling of the country's natural resource wealth. It also committed appalling human rights violations, with regular reports of systematic torture, and total censorship of the media.

Amnesty International had repeatedly described how Niyazov's regime had 'ruthlessly repressed any form of peaceful dissent. Dissidents were tortured and imprisoned

after unfair trials or forced into exile. People were dismissed from their jobs and barred from travelling abroad simply because they were related to a dissident while the authorities targeted human rights defenders, portraying their activities as 'treason' and 'espionage.' Amnesty reported on the case of Ogulsapar Muradova, a human rights activist, who was detained in June 2006, sentenced to six years' imprisonment in an unfair trial in August and died in suspicious circumstances shortly afterwards.<sup>268</sup>

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*Turkmenistan is the only country that Global Witness has ever come across where none of the natural resource wealth appeared to be making it on to the government's budget.*

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Freedom House, an American non-governmental organisation, has each year since the mid 1990s given Turkmenistan the lowest possible score for political rights and civil liberties. It reserves such scores for countries where 'state control over daily life is pervasive and wide-ranging, independent organisations and political opposition are banned or suppressed, and fear of retribution for independent thought and action is part of daily life.' The 2007 report, which rated countries for 2006, the last year that

A gas export contract between Ukraine and Turkmenistan shows the Central Bank of Turkmenistan's account at Deutsche Bank in Frankfurt.

#### 6.6. Платежи по валютной части осуществляются путем перевода денежных средств на валютный счет Продавца по следующим реквизитам:

Центральный Банк Туркменистана, г. Ашгабат, Туркменистан,  
account № 949924500 with DEUTSCHE BANK AG, Frankfurt-am-Main, Germany TAUNUS ANLAGE 12-21,60262, SWIFT:  
DEUTDEFF

Niyazov was in power, ranked Turkmenistan alongside Burma, Cuba, Libya, North Korea, Somalia, Sudan and Uzbekistan.<sup>269</sup>

It was also a country where government budgets were completely opaque. Turkmenistan is the only country that Global Witness has ever come across where none of the natural resource wealth appeared to be making it on to the government's budget. Turkmenistan has some of the largest gas reserves in the world, and earned \$5 billion from the lucrative gas trade during 2007.<sup>270</sup> The country's GDP in 2006 was \$10.5 billion, so it was a huge proportion of national income that was not appearing on the budget.<sup>271</sup> Under Niyazov's shadow state Turkmenistan's human development indicators were low and falling, health and education budgets were being cut, and there was every indication that this wealth was not benefiting the population.

By 2005 Turkmenistan had plumbed the depths of the Transparency International

Corruption Perceptions Index, ranked as the joint third most corrupt country in the world.<sup>272</sup> Fifty eight per cent of the population is estimated to live in poverty,<sup>273</sup> and infant mortality rates are similar to those of Pakistan and Democratic Republic of Congo, despite the fact that Turkmenistan's per capita income is more than twice that of Pakistan and nearly five times that of Congo.<sup>274</sup>

There was no way that the Turkmen population – or indeed anyone else – could see how the billions of dollars of national gas revenues were being spent... except, perhaps, for the evident proliferation of Niyazov's vanity projects, including a huge gold statue of himself that rotated to face the sun, and an artificial lake in the middle of the desert.

Meanwhile, at least \$2 billion to \$3 billion of gas revenues were being kept in Turkmen central bank accounts and foreign reserve accounts at Deutsche Bank. A gas export contract signed on 14 May 2001 between Ukraine and Turkmenistan, obtained by Global Witness, shows that the Central Bank of Turkmenistan holds account number 949924500 at Deutsche Bank in Frankfurt, Germany.<sup>275</sup>

According to sources in the financial community, Deutsche Bank was reported to manage Turkmen foreign currency assets, such as the Foreign Exchange Reserve Fund (FERF). Sources told Global Witness that 50 per cent of the gas revenues which were deposited in the main Central Bank account at Deutsche Bank were being transferred to the FERF, although Global Witness has not been able to get Deutsche Bank to confirm this.<sup>276</sup>

A former chairman of the Turkmen Central Bank, Khudaiberdy Orazov, told Global Witness that these funds were under the effective control of President Niyazov himself, and were effectively Niyazov's 'personal pocket money.' This was backed up by other independent sources from the international

President Niyazov may have been smiling but his people weren't.  
Credit: Alexander Zenianichenko/AP



financial institutions.<sup>277</sup> The FERF did not appear under the national budget; an extraordinary 75-80% of government spending was taking place off-budget from such funds, which meant that billions of dollars of national revenue were disappearing into a black hole with no accountability whatsoever.<sup>278</sup>

The European Bank for Reconstruction and Development (EBRD) was refusing to fund projects related to the FERF because of the opacity of its operations, and had explicitly called on the Turkmen government to make the FERF more transparent and accountable.<sup>279</sup> Yet Deutsche Bank appeared to be happy to hold accounts for the FERF despite these serious concerns raised by a multilateral institution.

Global Witness first wrote to Deutsche Bank in July 2005 to express its concerns and ask about the accounts and any due diligence measures taken. The reply was as follows:

'As a financial services provider active worldwide Deutsche Bank is aware of possible impacts of its activities on the environment and society. Therefore we consider environmental and sustainable aspects through our sustainability management system and in specific cases of lending decisions we carry out environmental risk assessment.'

This was interesting, given that Global Witness had not asked Deutsche Bank about its impact on the environment or about its lending decisions. The letter continued, again failing to answer our question about the Turkmenistan accounts:

'Acting in line with sustainability criteria is an important part of our business activities and corresponds with our role as a corporate citizen. On the basis of the UNEP statement and the 10 principles of the UN Global Compact, principles behind Deutsche Bank's sustainability policy have been developed that are translated into action through various activities. Deutsche Bank works according to national laws and regulations and the relevant guidelines published by international organisations like the UN and the World Bank or national organisations like BaFin-Federal Supervisory authority. Due to data protection laws we cannot give you information regarding specific client relationships.'<sup>280</sup>

The real client, of course, should have been the people of Turkmenistan. The letter did not engage with the point, which is that the



The Turkmen Central Bank in Ashgabat. Nominally the \$2-3 billion of Turkmen gas revenues kept at Deutsche Bank were under the control of the Turkmen Central Bank. However, Niyazov had effective control.  
Credit: Global Witness

money concerned consists of state revenues derived from natural resources, which belong to the people of Turkmenistan. (Even the *Rukhnama*, the 'holy' book written by Niyazov, which became the central text in the Turkmen education system during his rule, says that 'within the borders of Turkmenistan the natural resources... are the people's national wealth and property,'<sup>281</sup> although of course



A tuberculosis patient in Turkmenistan. Under Niyazov health budgets were cut.  
Credit: Wayman Richard/Corbis Sygma

by keeping the gas revenues offshore and off the national budget, Niyazov was far from honouring his own principles.) In a situation involving state accounts, information about these accounts and the money in them should be available in the public domain.

In October 2006 Global Witness wrote again, asking about the Turkmen central bank account and the nature of Deutsche Bank's relationship with Turkmenistan. The reply was exactly the same as the two paragraphs above, except the word 'environment' in the second sentence had been replaced by 'human rights.' The letter directed Global Witness to two websites about corporate social responsibility and the environment, neither

investigated the accounts early in 2007. Deutsche Bank reassured BaFin that the Turkmen accounts are indeed state accounts, and that Deutsche Bank had fulfilled its regulatory obligations with respect to PEPs.<sup>285</sup> However, Global Witness notes that BaFin only carried out a random sample investigation ('stichprobenartige') of the accounts, and did not perform a complete investigation.

In response to a third Global Witness letter to Deutsche Bank in October 2006 – and following the random sample investigation by BaFin – Deutsche Bank finally confirmed to Global Witness that it held an account for the Central Bank of Turkmenistan to handle its international payment transactions, but

Did Deutsche Bank CEO Josef Ackermann know that his bank was doing business with a human rights abuser?  
Credit: Kai Pfaffenbach/Reuters/Corbis



of which answered our concerns about the Turkmen accounts.<sup>282</sup>

On 21 December 2006, Niyazov died, reportedly of heart failure. Concerned about what might ensue in the resulting power vacuum, Global Witness publicly called on Deutsche Bank to ensure that no transfers were made out of these accounts until an internationally recognised government was in place.<sup>283</sup> Global Witness has asked Deutsche Bank what happened to the accounts following the death of Niyazov, and whether any special measures were put in place to ensure that the money was not being used for corrupt ends in the changeover to the new regime. It has also asked whether Deutsche Bank holds or has held accounts for members of Niyazov's family, or for senior Turkmen government officials. Deutsche Bank declined to answer.<sup>284</sup>

Prompted by Global Witness, BaFin, Germany's financial regulator, finally

denied that it had an account for Niyazov.<sup>285</sup> Global Witness has now requested that BaFin undertake a thorough investigation of the accounts, rather than just spot checks, but has received no reply.

The new government of Gurbanguly Berdymukhammedov which succeeded Niyazov's regime has made various commitments to clean up Turkmenistan's public finances. It was reported in June 2007 that he had set up a commission to audit the activities of one of Niyazov's foreign currency funds. According to *Associated Press*, the 'International Fund of Saparmurat Niyazov', founded in 1993, is managed by German banks.<sup>287</sup> Deutsche Bank told Global Witness in July 2007 that it had no relationship with such a fund.<sup>288</sup> Berdymukhammedov has also reportedly said that the spending of government funds will now be audited.<sup>289</sup> If this does indeed take place, it would be a welcome development.<sup>290</sup> But until this occurs there will be no tangible evidence

of change. Interestingly the EBRD which, under Niyazov, refused to do any business that was connected with the FERF, has still not changed its stance, which is that it will not do so while there is no transparency about these extra-budgetary funds.<sup>291</sup>

Meanwhile, the revenues continue to increase. In addition to the gas revenues examined by Global Witness in its report *It's a Gas*, Turkmenistan is on the verge of exploiting its offshore oil and gas, with new interest from Western oil companies that will increase overall extractive revenues.<sup>292</sup>

There is nothing inherently wrong with a government keeping public funds in

overseas bank accounts, and Global Witness does not suggest that Deutsche Bank has broken any laws by taking the deposit of Turkmen public funds. However, there are serious problems with Deutsche Bank's relationship with Niyazov's Turkmenistan.

At the first level, there are the bank's ethics. As a member of the UN Global Compact – something it cited in its letters to Global Witness – Deutsche Bank has committed to the Compact's 10 Principles, including respect for human rights and working against corruption in all its forms. The Global Compact is one of the largest and best known voluntary frameworks for corporate behaviour, with over 4,700 businesses in 130 countries having

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Deutsche Bank in Frankfurt held Turkmen gas revenues of up to \$3 billion. These funds were described by a former chairman of the Turkmen Central Bank as Niyazov's 'personal pocket money'. Credit: Deutsche Bank



signed up to its ten environmental and social principles as of January 2009.<sup>293</sup> Global Witness investigated submitting a complaint to the Global Compact, but the most that it could offer was to facilitate a dialogue with the bank, with whom we were already having such an unsatisfactory correspondence.

Global Witness is baffled by Deutsche Bank's claim to be supporting human rights by holding an account for a regime that was universally perceived to be repressive and corrupt. When it joined the Compact in 2000, Deutsche Bank said 'It is our belief that it is possible to be both profitable and moral; doing more than the law requires because it is not just correct policy, but it is our moral obligation and conviction,' and that 'Our business partners and respective business transactions must meet moral and ethical standards deemed to be exemplary.'<sup>294</sup>

Yet Deutsche Bank had been in Turkmenistan since at least 1996, when it reportedly signed a cooperation agreement with the government. This was renewed when Deutsche Bank board member Tessen von Heydebreck visited Ashgabat to meet Niyazov in 2000. Deutsche Bank cannot reasonably claim to have been unaware of the kind of repressive regime Niyazov was running.

It is important to note that the services Deutsche Bank was providing to Niyazov, allowing him to keep the gas revenues offshore and off the national budget, were not incidental to the type of regime that he was running.

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*These might officially be 'state' accounts – but what if the state has been completely captured by one person?*

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Too often offshore money is thought of as the reward for being a dictator, a by-product of the problem in repressive countries. But it is not just the bonus for having seized control of the state: it is what enables a dictator to maintain his position. Dictatorships and shadow states are not just about coercion, they are also about control of the money. A dictator is an effective arbiter of who gets what among competing factions, which are constantly kept in balance so as not to threaten his power. It is much easier to do this if the money being used to pay these

competing factions is kept offshore, where nobody else has access to it. It's a zero sum game: if he doesn't keep access to all of the money himself, somebody else might gain access to it and start making inroads on his power.

By allowing Niyazov's regime to keep Turkmenistan's gas revenues off the budget and out of the country, Deutsche Bank was helping Niyazov to stay in power and run his appalling regime.

How significant are Deutsche Bank's profits from its Turkmenistan business? Given that there were cooperation agreements signed between the bank and Turkmenistan, and that the relationship was important enough for a Deutsche Bank board member to make an official visit, it is likely that there were more profits from other associated deals than just those derived from holding the central bank accounts. What kind of money did it take for Deutsche Bank to willingly override its ethical statements?

Secondly, there is the compliance issue. Global Witness asked Deutsche Bank what due diligence it had done when the Turkmen government was first accepted as a client, and what monitoring had continued on an ongoing basis, to ensure that the money was not being used for corrupt purposes. Deutsche Bank said that it could not answer: 'As stated previously, as a bank we are not authorised to comment on account relationships. Similarly, information concerning activities and measures in connection with the statutory requirements for monitoring accounts and the movement of accounts is, as a strict rule, disclosed only to the relevant competent bodies or the bodies specified by law, in particular the criminal law enforcement authorities.'<sup>295</sup>

Global Witness notes that Deutsche Bank is a member of the Wolfsberg Group, a group of major banks that have drawn up voluntary due diligence standards, as a complement to FATF's, to help in the fight against corrupt money. The Wolfsberg Group's document on PEPs addresses the question of whether state-owned enterprises, including central banks should be treated as a PEPs (its answer is no, although those who run them could be). However, it does not address this specific situation of state accounts that are under the effective sole control of a dictator.<sup>296</sup>

Thirdly, there is the question of regulation. BaFin has confirmed that Deutsche Bank has not broken any of its regulatory obligations. But for Global Witness, the question remains: are these current regulatory obligations enough to prevent a bank doing business with a corrupt and abusive regime such as Niyazov's? These funds were considered sufficiently untransparent that a multilateral bank such as the EBRD would not go near them, yet they did not trigger any regulatory concerns, and once again this disturbing story did not come out through action of a regulator, but through the research of an NGO.

These might officially be 'state' accounts – but what if the state has been completely captured by one person? Niyazov was the modern personification of Louis XIV's famous 'Etat, c'est moi' ('I am the state'). Niyazov had de facto control over Turkmenistan's Central Bank, with the power to sack its chairman at will – five people occupied the position between 2002 and 2006, of whom three were subsequently jailed, along with other ministers jailed for embezzlement in a series of trials that were regarded as Niyazov's way of getting rid of potential opponents.<sup>297</sup>

In a country where none of the income from natural resources appears in the budget but remains under the discretionary control of the president, and where the president has effective control over the Central Bank, where is the distinction between the state and the head of state, and what effect does this have on how a bank deals with that country's state accounts?

State accounts from countries with high levels of corruption and poor transparency, or where the state has effectively been captured by an individual or group, should be subjected to the same red flags in the money-laundering regulations as private or correspondent banking relationships. Banks should not be able to hide behind the shield of holding 'central bank accounts' in order to do business with a corrupt and abusive regime.

Speaking to the Economist Intelligence Unit in 2006, Deutsche Bank's global head of compliance Henry Klehm talked about how the board and senior management must emphasise the importance of ethical behaviour and accountability: 'The compliance department can help prepare those messages and do a lot of prompting, but everybody expects the compliance guy to stand up in front of the audience and be a goody two shoes. However,

the most effective is when senior business line management says that he has zero tolerance for this type of risk.'<sup>298</sup>

It appears, however, that Deutsche Bank has failed to exercise zero tolerance for the risk posed by doing business with Turkmenistan.

### Action needed:

- Deutsche Bank should explain how its membership of the Global Compact was consistent with a relationship with Niyazov's Turkmenistan.
- Banks should be required to be transparent about central bank accounts they hold for other countries, so that populations of those countries know where their national wealth is being held.



# 08

# OIL-BACKED LOANS TO ANGOLA

Doing business with an opaque national oil company

Deutsche Bank was hiding behind the shield that it was dealing solely with 'central bank accounts' in order to do business with Niyazov's horrifying regime in Turkmenistan. Meanwhile, a host of banks have been hiding behind the shield of providing trade finance for an oil company in order to do business with Angola, a country which earns billions from its oil yet the majority of whose population continues to live in conditions of appalling poverty.

By providing oil-backed loans to Sonangol, the Angolan state oil company, large consortia

of banks have allowed Angola to mortgage its future oil wealth in return for instant cash with no transparency about how the money is being used.

Resource-backed loans are not an unusual way of raising finance, and Angola is not the only country doing this. So why does this matter? It is because Angola is a key example of resource revenues being misused and put to the service of a shadow state where the only real outcome for the majority of people is poverty and, once again, banks are part of the structure that has allowed it to happen.

Angola is now one of Africa's two largest oil producers, but is still near the bottom of the UN's Human Development Index.  
*Credit: Thomas Havisham/Panos*



As with Deutsche Bank and Turkmenistan, the issue here is not a regulatory one. There is no suggestion that the banks involved have breached any of their regulatory obligations. The questions this story raises are: could the banks have exercised a higher level of responsibility? Should they be required to exercise a higher level of responsibility?

Government in Angola broke down completely during its long civil war, then once the conflict ended with government victory in 2002, remained highly secretive. For a few years, the subject of corruption was top of the agenda, with vocal criticism from the IMF and donors, and billions of dollars going missing from the budget, as publicised by Global Witness and others.<sup>299</sup> Now the criticism is more muted. The corrupt environment has not changed significantly, nor have the living conditions of the majority of the population, as this chapter will show. A democratic election has recently taken place, won by the existing government by a huge majority which, observers have noted, is not unrelated to the oil funds at its

disposal. Independent media operates under restrictions and civil society organisations are being threatened with closure.<sup>300</sup> What has changed is demand for Angola's oil. Everyone wants some of it, and the government is now trying to convert itself, in terms of perceptions, into a respectable business partner.

Angola's economy revolves around oil, which accounts for over 80% of government income.<sup>301</sup> In April 2008 it overtook Nigeria as Africa's largest producer of oil.<sup>302</sup> The IMF said that Angola's GDP grew 21% in 2007, and based on an oil price of \$90 a barrel it estimated in October 2007 that Angola was due to earn tax revenues from oil of \$22.8 billion in 2008.<sup>303</sup>

But a continuing lack of transparency and proper budgetary oversight means that much of this vast influx of wealth is being squandered with no improvements to the lives of its population. According to recent research by Save the Children UK, Angola has the highest rate of child mortality relative to national wealth in the world.<sup>304</sup> The average Angolan



The Luanda headquarters of Sonangol, Angola's state oil company. It reportedly cost \$131 million to build and has a heliport and two gyms. Sonangol has still not published audited accounts. Credit: Jose Carlos Costa/Flickr

can expect to live only to 41.7, one of the lowest rates in the world; 31% of all Angolan under-fives are malnourished and almost half of Angolans do not have access to safe water and sanitation.<sup>305</sup> Seventy per cent of Angolans still live on less than \$2 a day.<sup>306</sup> So despite now being the largest oil producer in Africa, Angola still ranks at only 162 out of 177 on the UN's Human Development Index; barely moved from its position at 160 out of 174 a decade and billions of dollars of oil revenue ago.<sup>307</sup> Even as the oil flowed throughout the 1990s, income inequality rose, making Angola one of the most unequal countries in the world.<sup>308</sup>

Yet for the last ten years, the amounts lent by commercial banks – mostly European but increasingly also Chinese – in oil-backed deals to Sonangol have steadily increased and now involve regular new loans of billions of dollars each. The trade press is full of praise for Sonangol as a reliable borrower – a borrower which has in recent years been rewarded for its reliable repayments with increasingly large loans, diminishing interest rates, and longer ‘tenors’ (length of loan).

In the last couple of years, oil-backed loans are no longer the sole source of external funding for Angola, as China has opened extensive credit lines, followed by a couple of European banks. But the oil-backed loans have continued. Global Witness and Angolan civil society are concerned that by forward-selling future output, these loans have allowed the Angolan government to convert future oil revenues into cash today, with no clarity or accountability about how those revenues are being used. By making such loans, banks may be making themselves complicit in the activities of a government that continues to resist full transparency over its resource revenues.

This chapter shows how accepting deposits is not the only way that banks can help to fuel the engine of the corrupt shadow state; they can also do it by providing untransparent loans. But whether accepting money or loaning it, the need for due diligence is the same. If the bank doesn't check where the money is from, it might be the proceeds of corruption; if it doesn't check how the money will be used, there is a risk that it may contribute to corruption.

### **What is an oil-backed loan?**

Businesses need finance from banks. Resource extraction businesses, particularly oil, have significant financing needs, because of the high initial cost of extracting the commodity from

the ground before it can be sold. One way of doing this is to borrow money using the oil as security. Another – which can be more secure for the banks in uncertain environments – is pre-export financing. The loan is not just secured against oil revenues, but is repaid directly in specific future oil cargoes, whose proceeds can be paid straight into an offshore account or ‘special purpose vehicle’, with specific provisions in the loan contract for how the future oil cargoes will be ‘lifted’ and sold, to whom, and how often, in order to replenish the offshore account or special purpose vehicle from which the bank takes its repayment. This was, until recently, the structure used for many of the commercial oil-backed loans to Sonangol.

The interest rates on such loans are not always the cheapest way of raising finance for the borrower, but because the lender has a very secure way of getting its money back, it is an attractive option for the bank. Effectively, from the bank's point of view, none of the money with which the bank is repaid goes anywhere near the company or indeed even the country with which they are making the deal. An international oil company might lift the oil in Angola, a western oil trader then buys it, and the money that the trader pays for the oil goes straight into an offshore account from which the bank is paid back.

A 2001 report by UNCTAD (the UN body dealing with trade and development) about the potential uses of structured commodity financing – of which pre-export finance is one technique – notes that, unlike more traditional forms of financing, it is all based on a specific transaction, or set of transactions, allowing the circumvention of risks associated with a company's balance sheet or a country's risk profile. ‘In many parts of the world, accounting standards are not truly satisfactory from a financier's point of view. With structured finance the role of the balance sheet is fairly minor; what matters more are the transactions for which finance is sought – if the profitability of these transactions can be reliably ascertained, they could be financed, even if the company has a poor balance sheet.’<sup>309</sup>

It is this set-up that has allowed banks to manage the risk of making loans to a state-owned company in a country that was for decades at war, and which since the end of the conflict has continued to maintain a significant reputation for corruption. However, while the banks may be able to separate themselves from the financial risks, by making these loans they are actually



**Arkadi Gaydamak** (left), by his own admission to Global Witness, was a signatory on French bank accounts used for oil-backed loans that paid for weapons for Angola.  
Credit: REA

contributing to the very situation that makes Angola a risky investment in the first place.

The extraordinary series of huge oil backed loans to Sonangol has made it the poster-child of pre-export finance to the developing world, and the number of banks joining each syndicated deal has grown as more banks become comfortable with doing business there. But as Angola's oil production increases, promising ever more lucrative deals for the banks making loans, Global Witness believes it is important to take a clear look at how oil-backed loans came about in Angola, and how much has really changed since the end of the war.

### Oil backed loans – a dirty history

Oil-backed loans to Angola come with a disturbing history, with origins that are mired in arms dealing and corruption on a massive scale. When the Elf scandal – the story of how the Elf Aquitaine oil company systematically paid kickbacks, peddled influence and encouraged government indebtedness in order to maintain its control over the oil of several African countries – reached the French courts in 2003, the provision of oil-backed loans was revealed to be a key component of the 'Elf system'. Future oil revenues in Congo-Brazzaville, Angola and Gabon were mortgaged for ready cash, with handsome kickbacks for African leaders and Elf's secret accounts. The trial ended in November 2003 with the conviction of 30 former senior Elf executives.<sup>310</sup>

Jack Sigloet, who was not charged with any offences, was the Elf executive in charge of

arranging oil-backed financing for African leaders. He testified that the loan system was conceived 'in such a way that the Africans were only aware of the official lending bank and were ignorant of the whole system which Elf rendered particularly and deliberately opaque.' His testimony said that he arranged several oil-backed loans of between \$50 million and \$200 million for the Angolan government in the first half of the 1990s, during the civil war.<sup>311</sup>

Global Witness raised the issue of oil-backed loans to Angola's opaque and corrupt wartime government in its 1999 report *A Crude Awakening*, which first sounded the call for transparency over oil revenues.<sup>312</sup> Its 2002 follow-up, *All the Presidents' Men: The devastating story of oil and banking in Angola's privatised war*, showed how the civil war provided a cover for the full-scale looting of the country's oil money by national and international business and political elites, typified by the Angolagate 'arms-to-Angola' scandal that broke in France in 2000.

During the civil war against UNITA in the 1990s, the Angolan President dos Santos had turned for help to sympathisers in the French establishment. Introductions were made via Jean Bernard Curial, who ran a humanitarian aid company that worked on behalf of French government ministries, and Jean-Christophe Mitterrand, son of the then French president. As a consequence, two businessmen, Pierre Falcone (an advisor to Sofremi, a security export company run by the French interior ministry under Charles Pasqua) and Arkadi Gaydamak, a Russian émigré, were provided

Pierre Falcone is currently standing trial in France in criminal proceedings arising from 'Angolagate.' According to the Angolagate indictment, between 1993 and 2000 Falcone ordered bank transfers worth more than \$54 million in favour of Angolan officials. Credit: SIPA/Rex Features



with Angolan diplomatic passports and went to work on behalf of dos Santos.<sup>313</sup>

As Gaydamak told Global Witness in 2000, they were 'made signatories on the accounts' that they had set up with Banque Paribas (now BNP Paribas) for generating oil-backed loans. He at first stressed that the purpose of his and Falcone's role was the provision of oil-backed loans only, and only later admitted that arms had also been supplied.<sup>314</sup> The Angolan government did not have the money to pay for weapons directly, so a system of high-interest loans against future oil production was devised. Those arranging the arms deal would be paid a sum up front, then an oil-backed loan was raised from French banks and disbursed out of Paris to cover the other costs and fees.<sup>315</sup>

In testimony to the Angolagate investigators, Jean Bernard Curial said that he distanced himself from these deals after beginning to see them as 'une gigantesque escroquerie' – a gigantic fraud. He alleged that this offshore procurement process outside the national budget became a 'huge money making machine' for Falcone, Gaydamak and Angolan leaders. He also testified that kickbacks were so common from these deals that Jack Sigolet, the Elf finance executive, had begun to refer to Angolan officials by the percentage of their cut: there was Mr Thirty Percent, and Mr Twenty Percent.<sup>316</sup>

Falcone is currently standing trial in France in criminal proceedings arising from 'Angolagate'.<sup>317</sup> The trial is expected to be deeply embarrassing, exposing the dirty laundry of the French political establishment. Falcone has already been given a four-year prison sentence

for tax fraud and sentenced to a further year by French courts for receiving commissions in a case involving misappropriation of public funds via Sofremi.<sup>318</sup> According to the Angolagate indictment, seen by Global Witness, between 1993 and 2000 Falcone ordered bank transfers totaling a minimum of \$54,569,520 in favour of Angolan officials.<sup>319</sup>

Meanwhile, more oil-backed loans were raised, supposedly to pay off \$1.5 billion of Angola's debt to Russia. The funds were moved through the bank account at UBS in Geneva of a company set up by Falcone and Gaydamak called Abalone Investment Limited. Between 1997 and 2000, out of a total of \$773.9 million paid into Abalone's account by Sonangol, only \$161.9 million was passed into an account marked Russian Ministry of Finance.

Around \$600 million was transferred to accounts belonging to Falcone, Gaydamak and a series of obscure companies, with millions ending up in the private accounts of high-ranking Angolan officials, including President Dos Santos, according to a memo reproduced in the French newspaper *Le Canard Enchaîné* and documents seen by Global Witness. Falcone was investigated for 'money laundering, support for a criminal organisation' and 'corruption of foreign public officials' in a Swiss criminal inquiry into these suspicious transactions. Gaydamak was never formally charged. Both men deny any misappropriation of funds.<sup>320</sup>

The investigation was suspended at the end of 2004 by the Public Prosecutor of Geneva, Daniel Zappelli. In 2006, a group of Angolan citizens called for the case to be reopened, but despite renewed pressure from Global Witness and Swiss civil society organisations, there has been no further action from the Swiss authorities.<sup>321</sup>

This system of oil backed loans was in operation from 1993-4 onwards. So when banks consider the long history of Sonangol as a reliable loan customer that pays back on time, they are also including the many years in which oil-backed loans were being used to line pockets and purchase weapons.

The Global Witness report *All the Presidents' Men* highlighted a series of newer oil-backed loans from a variety of commercial banks to Sonangol during 2000 and 2001 which provided a minimum of \$1.1 billion beyond the IMF-imposed limit of \$269 million in new credit to the conflict-stricken government,<sup>322</sup> thus undermining the

international community's efforts to bring some accountability to Angola's use of its oil revenues.

In 2004's *Time for Transparency*, published two years after the end of the war, Global Witness showed how Angola was continuing to borrow against future oil revenues while the country's oil income remained completely opaque; revealed the diversion of oil revenues to offshore bank accounts, and raised the 'major concern that the mechanisms of embezzlement entrenched during the war will simply be redirected towards profiteering from the country's reconstruction'.<sup>323</sup>

What had begun as an emergency measure under the fog of war, a structure to get around the restraints of the civil war when nobody else would lend to Angola, had became a cash cow for government officials. When peace came in 2002, there was no sign of it being given up.

### An opaque present

The Angolan conflict may now have ended, but the loans have continued. However, the fundamental problem remains the same: the murky management of oil revenues which flourished under the cover of war has not yet been satisfactorily cleaned up, and it is still not clear how these loans are being used.

Mismanagement and corruption in Angola's public finances, and particularly in the oil sector, are well documented. Transparency International currently ranks Angola 158th out of 180 countries on its Corruption Perceptions Index<sup>324</sup> and the OECD, in a 2007 economic outlook, referred to a business climate characterised by 'major bottlenecks due to endemic corruption, outdated regulations and rent-seeking behaviour'.<sup>325</sup>

Historically, analysis by Global Witness of IMF reports showed that an annual average of about \$1.7 billion (or 23 per cent of GDP) went unaccounted for from the Angolan Treasury between 1997 and 2001.<sup>326</sup> According to the UNDP in 2005, about 17% of the country's budget was still earmarked for 'special use', with no clarity over where it goes.<sup>327</sup> In 2007 the OECD said that 'much remains to be done to align fiscal policy actions with the priorities of poverty eradication'.<sup>328</sup> A few improvements have now been made; in May 2008 the OECD remarked that 'recent years have seen progress regarding the transparency of oil revenue management' then continued, 'although much remains to be done'.<sup>329</sup>

Such progress has included the fact that the Ministry of Finance now publishes some oil export figures on its website. But these figures serve scant purpose when set against the ongoing bigger picture of lack of transparency, because they cannot be put in sufficient context to tell the full story. There is still too much muddiness about what happens between Sonangol and the Ministry of Finance, as the World Bank and IMF continue to point out.

The fundamental problem with transparency over Angolan oil revenues centres around the multiple roles of Sonangol, the state oil company. Its roles as both a tax-paying oil company and a concessionaire for the government, handling oil revenues accruing for the government, constitute a significant and much-commented on conflict of interest.<sup>330</sup> As a fiscal agent for the government, it collects revenues and makes expenditures on the state's behalf, but as of 2007, the World Bank noted that the government still did not have effective control and monitoring over these quasi-fiscal operations.<sup>331</sup> The 2007 IMF Article IV report commented that several of the actions required to effectively ring-fence Sonangol's activities had still not been initiated; and that Sonangol's quasi-fiscal activities were not being executed through the central budgeting system, SIGFE.<sup>332</sup> Sonangol's activities are only recorded in the budget with a 3-month delay.<sup>333</sup> Crucially, while Sonangol has now apparently been audited, it still does not publish any audited accounts and thus remains without effective public oversight.<sup>334</sup>

In reality, Angola's public finance system still maintains two spending tracks. One is the official budget managed by the Treasury; the other is the 'non-conventional' system via Sonangol, which is not subject to public scrutiny.<sup>335</sup> In 2007, the World Bank noted that Sonangol has in the past reduced 'the tax and profit oil payments it owes to the Government by the amount of the costs it has incurred on Government's behalf. Disputes arise because in the past there has not been clarity on which activities qualify for offset treatment, and because expenditures under qualifying categories have not been audited'.<sup>336</sup>

A recent article by Ricardo Soares de Oliveira at the University of Oxford described Sonangol as 'the centerpiece in the management of Angola's "successful failed state", highlighting the extent to which a nominal failed state can go on surviving and indeed thriving amidst widespread human destitution.' Instead of

leading to development, Sonangol's success had 'primarily been at the service of the presidency and its rentier ambitions'.<sup>337</sup>

What this all means is that a bank lending to Sonangol is lending into a financial system that has never explained its black holes, and in which it is still unclear exactly where the line is drawn between Sonangol and the state budget.

Yet the oil-backed loans have continued, including the following loans which have been reported in the trade press. It should be noted that this may not be complete information on each loan, and that there may be other loans not listed here. Banks release only selected information about loans into the public domain.

- June 2003: **\$1.15 billion**, arranged by BNP Paribas, Belgolaise, Natexis, SG CIB. Other banks included Commerzbank, Crédit Lyonnais, KBC, Standard Chartered, RBS and West LB. The loan was made and repaid via a special purpose vehicle called Nova Vida. The rate was 2.25 per cent over LIBOR for four years and then 2.5 per cent thereafter.<sup>338</sup>
- August 2004: **\$2.35 billion**, coordinated by Standard Chartered. Other banks out of a total of 35 in the syndication included Banco Espírito Santo, Barclays, Calyon, Commerzbank, Deutsche Bank, KBC, Natexis, RBS. The loan was structured through a special purpose vehicle called Esperanca Finance. The rate was 3.125 to 3.37 per cent over LIBOR.<sup>339</sup>
- November 2005: **\$3 billion**, coordinated by Calyon. Other banks in the syndication included Banco BPI, BNP Paribas, Commerzbank, Deutsche Bank, DZ Bank, Fortis, HSH Nordbank, KBC Bank, Natexis, Nedbank, RBS, SG, Standard Bank, SMBC, UFJ, West LB. This loan was described as a 'structured commodity export finance facility.' The rate was 2.5 per cent over LIBOR.<sup>340</sup>
- March 2007: **\$1.4 billion** loan to Sonangol Sinopec International, a joint venture of Sonangol and Sinopec, the Chinese oil company. This was a new structure: a borrowing base facility (ie a revolving credit line) secured against oil reserves. Coordinated by Agricultural Bank of China, Bank of China, Bayern LB, BNP Paribas, Calyon, China Construction Bank, China

Development Bank, China Exim, ING, KBC Finance, Natixis, SG CIB, and Standard Chartered. The rate was 1.4 per cent over LIBOR for the first three years and then 1.5 per cent.<sup>341</sup> Some bankers reportedly expressed concerns about the status of the joint venture to which they were lending, suspecting 'it might belong in part to local interests too close to the ruling elite'.<sup>342</sup>

- April 2007: **\$500 million** from Standard Chartered, at a low interest rate (only 1% over LIBOR) and for a long term of ten years.<sup>343</sup>
- August 2007: **\$3 billion** arranged by Standard Chartered, with Commerzbank, Natixis, and Banco Espírito Santo, at the same low interest rate, for seven or eight years. It was reported that this would be used to repay the November 2005 loan and provide funds for capital and operating expenditure. The loan was reportedly unsecured.<sup>344</sup>
- November 2008: **\$2.5 billion** arranged by Standard Chartered, Absa/Barclays, Sumitomo Trust & Banking Company and Millennium bcp, with a similar structure to the previous year's loan and paying 1.6% over LIBOR, up slightly on the previous year's rate. The trade press article commented, 'Debate rumbles on over how hard the global financial turmoil will hit Africa, but some things apparently never change.'<sup>345</sup>

That's at least \$13.9 billion in slightly over five years. It is unclear whether each of these loans represents entirely new money, or whether they are being used to refinance earlier borrowing. It is also unclear how they are being used: spent on developing oil infrastructure? Passed to the government? Repaying other loans? Because Sonangol does not publish independently audited accounts, it is not known how much it needs to spend on capital expenditure, and whether that is really what these massive and repeated loans are being used for. This matters because of the continued opacity of the relationship between Sonangol and the Ministry of Finance, as documented by the World Bank and IMF; because of the history of missing oil revenues; because of the current lack of evidence that Angola's oil revenues are benefiting its population.

Certainly there are now other sources of finance available in Angola. The major oil

companies which are exploiting Angola's offshore oil will already be ploughing large amounts into the country's oil infrastructure themselves, and the Angolan government also has a revolving credit facility from China, reported to be anything between \$2 billion and \$7 billion, to use for rebuilding the Angolan economy.<sup>346</sup> This was reported in July 2008 to have been extended, to finance construction of a new airport as well as roads and railways.<sup>347</sup> Concerns have been raised by civil society and donors about the opacity of arrangements for disbursement of the Chinese loans, which have raised the spectre of potential diversion of funds.<sup>348</sup>

In addition, a consortium of Angolan banks is reported to have opened a line of credit worth \$3.5 billion to the government for reconstruction;<sup>349</sup> in 2003 Deutsche Bank signed a framework agreement with the Ministry of Finance for infrastructure loans which have so far totaled more than €800 million (\$1.1 billion);<sup>350</sup> in June 2008 Société Générale signed a framework credit agreement for infrastructure development.<sup>351</sup> So with all this other funding available, the question of how the upfront cash borrowed against Angola's future oil sales is being used remains open.

The IMF and World Bank, at various stages of their troubled relationships with Angola, have put pressure on the government to quit its commercial oil-backed loans habit, and have repeatedly criticised the loans being made.<sup>352</sup> The IMF offers far better terms for long-term loans than commercial banks, yet for years Angola chose to opt for short-term, high-interest loans from private lenders in order to avoid the scrutiny of public finances that comes with IMF engagement. Promises to stop the loans were repeatedly broken, as Global Witness documented in its reports *All the Presidents' Men* and *Time for Transparency*.

However, Angola's increasing confidence as its oil output increases (and, until recently, as the price of oil continued to rise) means that it no longer has to listen. In late 2006 the Angolan government paid off \$2.3 billion in debt to Paris Club creditors, instead of negotiating a rescheduling or partial write off, which would have required an IMF-approved programme.<sup>353</sup>

### **The problem with oil-backed loans**

There is nothing wrong with using assets as security to access finance in itself. The problem is if state assets are used without

public or parliamentary debate and oversight, and if there is no transparency about the loans themselves or the fees associated with them; the problem is if it is done in order to run a parallel financial system that may be fuelling corruption, as the Angolagate and Abalone cases (see: Oil backed loans – a dirty history, on page 93) have suggested. Global Witness research in Angola has shown that, as in other corrupt countries, state-owned enterprises are used to provide hidden off-budget financing, and therefore can constitute a significant corruption risk for those banks that do business with them.

As far as the banks are concerned they are making commercial loans, from their trade finance departments, to an oil company. In Angola, the oil-backed loans have



The oil industry has heaped accolades on banks who brokered loans for Sonangol.

been made to Sonangol, not the Angolan government, and that has been the basis on which the banks are prepared to make them. For years, Sonangol has successfully presented itself to the international oil majors and big banks with which it does business as separate from the chaos of the rest of Angola's finances. Ricardo Soares de Oliveira's article shows how Sonangol was deliberately protected from Angola's chaotic political economy from the outset, becoming 'a paradoxical case of business success in one of the world's worst governed states.'<sup>354</sup>

But, as shown above, the Angolan authorities are having their cake and eating it, because Sonangol has been used by the authorities as an off-budget system, one which has in the past allowed billions of dollars of national oil wealth to simply disappear from the state's opaque finances. Loans to Sonangol have also been used to pay off some of the bilateral debt run up by an opaque state. For example, \$800 million of the \$2.35 billion 2004 oil-backed loan arranged by Standard Chartered was used to pay off Portuguese creditors.<sup>355</sup>

*Box 5: Talking different languages*

Year	What the bankers and trade press said	What the international community said
2001 – 2002	<p><b>'Angola's performance has been impeccable and it has great potential...'</b>            Jean-Louis Salas, deputy head of energy and commodities, Africa and the Middle East at BNP Paribas in Paris, December 2001<sup>359</sup></p>	<p><b>'There is virtually no public information on fiscal and external public borrowing, the state owned oil company manages the country's oil related receipts through a web of opaque offshore accounts ... reported revenues from Sonangol cannot be easily reconciled with its share of the oil receipts... Sonangol has never been independently audited, and its accounting procedures are not in line with international accounting standards.'</b>            Unpublished IMF report, March 2002<sup>360</sup></p>
2004	<p><b>'Sonangol has an impeccable record and good name.'</b>            Andy Lennard, managing director, Texel Finance<sup>361</sup></p> <p><b>'Sonangol is a major landmark for 2004. It has traditionally been the big beast of the trade finance market, and the \$2.35 billion four/six year volume commitment-based transaction signed this year helps it retain that lead.'</b>            John MacNamara, managing director, head of structured trade and export finance, Deutsche Bank in Amsterdam<sup>362</sup></p>	<p><b>'Reliance on expensive oil-backed loans from commercial banks has burdened the economy with heavy debt servicing commitments and Angola's external position will continue to be very difficult for the remainder of this decade.'</b>            Statement by IMF Staff Mission to Angola, July 2004<sup>363</sup></p>
2005	<p><b>'Angola, sub-Saharan Africa's second largest oil producer, has become the benchmark borrower, building a strong repayment record after many years of export-backed deals.... Sonangol stands out for its exemplary payment record...'</b>            Trade Finance, May 2005<sup>364</sup></p>	<p>The World Bank described Angola's oil-backed loans as the core obstacle to the country's development: 'the need to service the country's large commercial, oil-guaranteed debt, with an annual cost estimated at around US \$750 million, has taken a heavy toll on the country's disposable resources.'<sup>365</sup></p> <p><b>'Fiscal discipline is undermined by... less than firm control of oil revenues by the Finance Ministry...'</b><sup>366</sup></p> <p><b>'...The central government remains without effective control and monitoring of the quasi-fiscal operations of Sonangol.'</b><sup>367</sup></p>
2006	<p><b>'Angola's Sonangol continues to draw a crowd...'</b>            Trade Finance, May 2006<sup>368</sup></p>	<p><b>'The role of Sonangol should be reassessed with a view to eliminate the conflict of interest and improve the quality and effectiveness of public finance management in Angola.'</b> World Bank, <i>Angola Country Economic Memorandum</i>, October 2006<sup>369</sup></p>
2007	<p><b>'Five or six years ago all the oil was under a nice separate trust fund. Now the structures are looser, the prices are lower and the tenors are higher. The country risk premium may have fallen so Angola is certainly perceived a better risk..'</b>            Jan de Laat, Rabobank<sup>370</sup></p>	<p><b>'Despite some improvements on the revenue side, a great deal more progress is needed to achieve full transparency concerning the expenditure side and oil revenues (especially concerning Sonangol's quasi-fiscal operations)...'</b>            Africa Development Bank/OECD, <i>African Economic Outlook</i>, May 2007<sup>371</sup></p>
2008	<p><b>'Such a scheme was achievable thanks to the excellent track-record of Sonangol over its numerous structured finance transactions in the past.'</b>            Michel Jay, head of energy upstream and structured commodity finance at Natixis, March 2008<sup>372</sup></p>	<p><b>'Although SIGFE [Angola's new integrated system for expenditure management] has been extended to all provinces, it does not include the quasi-fiscal activities of Sonangol... Angola has not yet become a member of the Extractive Industries Transparency Initiative.'</b>            Africa Development Bank/OECD, <i>African Economic Outlook</i>, May 2008<sup>373</sup></p>

This is a loan that was made to an oil company by the commercial trade finance departments of banks, yet it was used to pay off sovereign debt. If it had been a sovereign loan, the banks would have had to do proper due diligence on Angola's fiscal systems, and it is unclear, given the concerns which have been raised by the international financial institutions about these systems, how the banks could have mitigated their risks. The oil backed loan to Sonangol, however, allows the Angolan government to circumvent this problem.

This means that the banks are also having their cake and eating it. They do business with Sonangol as if it were a commercial outfit like any other. But in fact it is a state owned company whose functions overlap with its opaque parent government. If the banks are not prepared to do business with the state as a sovereign entity – and in Angola, until very recently, they were not (despite some effort, Angola has not been able to achieve a sovereign credit rating which would allow it to access cheaper finance on world markets) – then they should not be comfortable doing business with a state oil company which operates as a shadow off-budget financing system.

Commercial oil-backed loans to Sonangol have therefore allowed the Angolan government to continue to:

- bypass its own treasury's central financing system;
- run parallel black-box financial systems which are not open to public scrutiny, and are potential vehicles for corrupt activities;
- use its state oil company to access trade loans from commercial banks, yet use the money to pay off sovereign debt with no transparency or parliamentary oversight;
- resist the emerging global consensus among civil society, donors and investors that where natural resource revenues are the main source of government income, managing those revenues more transparently and equitably is the key to sustainable development and poverty reduction.<sup>356</sup> Although it is no longer the case that commercial oil backed loans are undermining the international community's efforts to pressure Angola into more transparency, given that alternative sources of funding such as the Chinese credit lines are available, there is still the huge problem of lack of

transparency and oversight over the loans, their fees, and what they are used for.

There is also a striking gap between, on the one hand, the accolades heaped on the shoulders of the banks and bankers in the structured commodity finance business who have set up the loans for Sonangol (such as *Trade Finance's* Deal of the Year for the Standard Chartered \$2.35 billion loan in 2004<sup>357</sup> and *The Banker's* country Deal of the Year for the \$1.4bn loan in 2007<sup>358</sup>), and the praise from these bankers for Sonangol as a good loan bet, and on the other hand, the despairing reports from the IMF and World Bank about Angola's failure to account fully and publicly for government revenue.

Then, beyond the purely ethical concern is the due diligence aspect of the issue. What due diligence did these banks do before making the loans? Global Witness asked each of the banks which had been involved in arranging these oil-backed loans since 2003:

- to confirm if the press reports of their involvement were correct
- to provide details of all the loans to Sonangol or the Angolan Government in which they had participated, including the purpose of the loan
- what information it sought about its client and the use to which the loans would be put
- how it reconciled its relationship with Sonangol with the repeated concerns expressed by international financial institutions about conflicts of interest



**Peter Sands**, the current CEO of Standard Chartered, joined the bank in 2006. By that time it had been doing business with Sonangol for more than 30 years.  
Credit: Shanghai Daily/AP

and off-budget financing relating to the role of Sonangol in public finance management in Angola

- how it evaluates country, credit and reputational risk in Angola, given that Angola earns the vast majority of its revenue from oil, and given these well documented concerns regarding the utilisation of oil revenues in Angola
- what safeguards are built into the loan documentation regarding the use of loans
- what monitoring is performed of the use of loan funds disbursed to Sonangol or the Angolan Government in order to police these safeguards.

Nineteen of them did not respond. Of the 12 that did reply, Royal Bank of Scotland, Bayern LB, Deutsche Bank, Barclays, BNP Paribas and ABSA were not able to provide any information about whether they had participated, saying that they could not comment on individual deals or relationships. All except BNP Paribas added that all deals were subject to risk and compliance procedures.<sup>374</sup>

Calyon said it is subject to AML rules and also complies with its group policies, and said: ‘We acknowledge that the wider economic and political issues raised in your letter may be in the public interest, however the specific information you are seeking on the provision of financing to our client and the structure of such financing is information which Calyon may not disclose due to its legal obligations of confidentiality to the client.’<sup>375</sup>

Others, such as Standard Bank and Fortis were able to briefly confirm that they had participated in loans to Sonangol in the past and, as with the others, said the loans had been subject to their compliance and know-your customer standards. Standard Bank, for example, said: ‘as both a policy and a principle’ it ‘will not knowingly provide funding for any unlawful or socially deleterious purpose and will require repayment of any loan that is found to have been used for anything other than a stated, lawful purpose.’<sup>376</sup> Bayern LB, WestLB and Fortis pointed out that, the loans in which they were involved having been repaid, they no longer have any exposure to Sonangol.<sup>377</sup>

Standard Chartered, which has arranged a number of the loans, wrote to say ‘while

it is not appropriate for us to comment on the specifics of client deals as we owe a legal duty of confidentiality to our clients, it is in the public domain that we have a business relationship with Sonangol. Standard Chartered is committed to working with each of its clients to promote international standards of disclosure and governance ... The purposes of loans are outlined as a condition of the relevant loan agreements. We do not lend in circumstances where the Bank believes the borrower will breach that contractual obligation.’<sup>378</sup>

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*Securing supplies of oil has always been a factor but is now more important than ever, and it is now happening in ever-sexier countries. So it boils down to country risk appetite of the bank for these sexier environments. Those that have this appetite are going to be the winners.*

**Andy Bartlett**, global oil and gas director, corporate finance at Standard Chartered, quoted in *Trade Finance*, May 2007<sup>380</sup>

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Standard Chartered invited Global Witness to a meeting to discuss the decision-making process for its loans. None of the dealmakers were present, although an executive who sits on one of the committees that assesses potentially controversial loans was. They were not able to talk about any specific deals, but said they could talk about how decisions were made. They confirmed that Standard Chartered has had a relationship with Sonangol since 1975, and described how the wholesale banking reputational risk committee assesses loan decisions that get referred to it. Each of the Sonangol loans has been discussed by the committee, and has also been referred up to the group risk committee. ‘There’s a process to make sure these things aren’t glossed over by guys whose primary interest is to sell the deal; there are many others concerned,’ they said. There is also training for all staff, to ensure that they know when to refer deals to the risk committees, and ‘to overcome the mentality of the traders’ “if it’s legal, I will do it” attitude.’

They emphasised that there were very clear terms attached to the loans, but could not say specifically what these were, except that ‘the loan structure had elements in it that encouraged transparency.’ The wholesale banking reputational risk committee reviews

the use of loans annually. They added that the bank's guiding principle was to be able to make a positive difference, and that they did so in this case by putting their weight behind the reformers within Sonangol who wanted to make it more transparent. They did not provide any specific details on how use of loan funds is monitored.<sup>379</sup>

Fortis, while not commenting beyond acknowledging its involvement in the 2005 \$3 billion loan, pointed out that its procedures for client due diligence have 'evolved rapidly', that it is strengthening its sustainability risk assessment framework, and 'in this context, the eligibility of new clients and deals outside high-income OECD countries will be subject to enhanced ESG [environmental, social and governance] due-diligence.'<sup>381</sup>

ING noted that it is 'currently not involved in providing financing to Sonangol Sinopec International,' the loan which it is reported to have participated in during 2007. It elaborated on the policies which it uses to guide its loan decisions, and added: 'In addition to the sensitivities that we generally acknowledge for the oil and gas sector... we acknowledge that financing oil and gas transactions involving Angola is – for a number of financial and non-financial reasons – prone to higher risks than in a number of other countries. In that respect we have designated Angola as a high risk country. Transactions involving activities in a high risk country such as Angola are treated with great care; as described above we will only consider such financings if sufficient mitigants are in place.'

'The proper application of funds and control mechanisms is part of our considerations.'

ING went on to say that 'Sonangol has made progress in achieving better transparency and improving its standards, and progress seems to be made with developing Angola's economy to the benefit of the population.' As evidence for this, it pointed to factors including the audits of Sonangol's financial statements by an international firm, the improvement of the macro-economic situation in Angola, and the implementation by Angolan authorities of an economic programme to address the consequences of the war.<sup>382</sup> Global Witness remains concerned, however, as stated previously, that these audits have not been published, that the international institutions have continued to raise concerns relating to Sonangol, and that development indicators for Angola are still dire.

KBC and Natixis were among those who did not reply. However, they had responded to Global Witness's public criticism of the 2005 \$3 billion loan. KBC said it 'has adopted and implements stringent ethical rules for the approval of loan transactions.' Natixis said that 'our formal approval process for all facilities is extensive, involving several committees and transaction reviews, including compliance, legal and credit risk due diligence.'<sup>383</sup>

The German bank WestLB provided perhaps the most specific information about the loans in which it participated, confirming that it first took part in an oil-backed loan to Sonangol in



Angola's government is not accountable to its people for how it uses the country's oil wealth.

Credit: Sam Seyffert/Creative Commons

1997, and participated in further loans in 2003 and 2005. It provided an insight into the 2003 Nova Vida facility, arranged by BNP Paribas, in which it participated along with other banks. WestLB said: 'In this pre-export financing, the funds were used to finance a prepayment to Sonangol, which was subsequently repaid by proceeds from the delivery of crude oil. It is common in such financings, that the facility documentation states a specific utilisation of the disbursed funds and even explicitly prevents the Borrower(s) from using the funds for any military purposes. We also requested and obtained confirmation by respective official institutions that the application of the funds would not contravene any obligations of Angola towards the International Monetary Fund, World Bank or any other supranational organisation. If misappropriation of funds had become evident, this would have triggered a default under the facility, which did not happen.'<sup>384</sup>

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*It should no longer be acceptable to hide behind the secrecy of commercial confidentiality to make untransparent resource-backed loans to governments or state-owned companies*

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It is interesting to see that the funds cannot be used for military purposes, which was the reason for some of the original oil backed loans during the war. It is also interesting to see that misappropriation of funds would have triggered a default as part of the loan contract. The question then, of course, is how much monitoring is performed of the use of the loan funds in order to identify any such misappropriation? While WestLB's letter did talk about its 'comprehensive due diligence process before entering into a business relationship with a client,' and noted that 'our due diligence did not provide evidence of incidents preventing us from sustaining a business relationship in the past,' it did not answer the specific question posed by Global Witness: 'what monitoring did WestLB perform of the use of loan funds disbursed to Sonangol?' None of the other banks that replied to us answered this specific question either.

So it is difficult to know how much effort was put into searching for evidence of misuse of funds. The regulatory requirement, as WestLB points out, emphasises knowing your customer and their business at the

opening of the relationship, not after the funds have been disbursed. It would not appear to be in any bank's interests to enquire too deeply, if it was not required to do so by regulations, into the use of funds loaned in case it endangered its own profits.

So it is unclear how much practical effect all this due diligence is having with oil backed loans to Angola. What effect did due diligence have on the oil-backed loan that was supposed to pay off \$1.5 billion of Angola's debt to Russia, but of which only \$162 million was passed to the Russian finance ministry amid huge backhanders to Angolan officials? (see Oil backed loans – a dirty history, on page 93)

What exactly do the 'rigorous risk and compliance procedures' to which so many banks refer actually entail? None of the banks explicitly answered the crucial questions: exactly what information they sought about their client and the use to which the loans would be put; how they reconciled their relationship with Sonangol with the repeated concerns expressed by international financial institutions about the conflicts of interest and off-budget financing relating to the role of Sonangol in public finance management in Angola; how they evaluate country, credit and reputational risk in Angola, given that Angola earns the vast majority of its revenue from oil, and given the well documented concerns regarding the opacity over utilisation of oil revenues in Angola.

Instead those who responded to our letters, and Standard Chartered whom we met, told us about how their own policies are sufficient to control the risks presented by doing business in Angola. The subtext to this is 'trust us, we have systems in place.' But the global banking crisis, in which banks have been shown to have insufficient systems in place to control the extent of their own liabilities, has demonstrated the hollowness of such claims.

There is no information in the public domain about the specific assurances that banks require from trade finance clients that are state-owned companies. If there isn't a sufficiently clear distinction between Sonangol and central government, as the World Bank and IMF continue to point out, then how can a bank claim to know precisely who it is lending to, and how the use of funds will be firewalled?

Of course a bank's primary motivation is commercial, to get its money back, along

with interest and fees. On this basis alone, then Sonangol, with its access to the second largest oil reserves in Africa, positioned safely offshore away from any potential political instability, can be perceived as an excellent customer. With an agreed mechanism through which the oil is sold and, up until 2007, a ring-fenced structure such as a trust fund or offshore special purpose vehicle to collect the oil revenues and pay them back to the lenders, it looks like a great deal for the banks making the loans.

But banks have recently begun to admit that, in their position of global influence, profit cannot be their sole concern when making loans. The 65 major and second-tier banks that have adopted the Equator Principles since 2002 have agreed to consider the social and environmental issues of new developments before making project finance loans, and not to provide loans for the worst offending projects.<sup>385</sup>

Some of the banks who responded to Global Witness's letters – WestLB, ING, Fortis, Standard Bank – cited their adherence or, in the case of Standard Bank, planned adherence, to the Equator Principles.<sup>386</sup> Other banks cited their own sustainability policies or their adherence to the UN Global Compact, including Deutsche Bank, Barclays, Bayern LB, WestLB, RBS and Fortis.<sup>387</sup> Standard Bank pointed out its membership of the Johannesburg Stock Exchange Socially Responsible Investment Index. Barclays pointed Global Witness towards its sustainability report, which mentions its work with the UN Environment Programme Finance Initiative, an alliance of 160 financial institutions, to develop an online resource for banks on the human rights issues associated with lending.<sup>388</sup>

However, neither the Equator Principles, the UN Global Compact, nor the UNEP Finance Initiative explicitly apply to resource-backed loans such as these. The Wolfsberg Group, meanwhile, mentions 'project finance/export credits' among the services that present a money laundering risk, and briefly addresses due diligence for syndicated loans in its FAQs on anti-money laundering issues for investment and commercial banking. But it too does not explicitly tackle resource-backed loans.<sup>389</sup> And while these voluntary initiatives present useful emerging standards, they are not underpinned by rigorous monitoring and there is no real sanction for non-compliance (see Box

7: Regulation rather than voluntary initiatives, on page 114). By signing up to them, though, banks are rightly acknowledging the potential consequences of their loans on the ground and the resulting reputational risk for themselves.

Fortis explicitly said that it applies the Equator Principles 'beyond project finance', for example 'corporate/hybrid transactions that are related to a single asset as far as this is possible.' However, it added that 'For trade finance, including structured commodity finance, we consistently find that the extensive information required to assess compliance with the Equator Principles is not available. In these types of transactions, where we have concerns about environmental, social or governance issues, we instead assess the client based on its capacity, commitment and track record on these issues.'<sup>390</sup> So what Fortis seems to be saying here is that when it comes to transactions of the category that includes oil backed loans, it cannot perform the due diligence it would apply under the voluntary Equator Principles, but instead assesses the record of the client on these issues. This chapter has outlined the many governance issues associated with doing business with Sonangol.

Finally, as with each of the cases in this report, there is the regulatory issue. As with the Deutsche Bank and Turkmenistan case, the regulators are not required to look at the issue of resource-backed lending. Once again this is despite the fact that public lending institutions were not prepared to keep lending into such a corrupt situation. All the noise on the issue has been created by NGOs and subsequently the media.

Just as it is no longer acceptable for a bank that takes its responsibilities seriously to finance a project that harms human rights or pollutes, it should no longer be acceptable to hide behind the secrecy of commercial confidentiality to make untransparent resource-backed loans to governments or state-owned companies that fail to provide full, independently audited disclosure of their receipt and disbursement of oil revenues. The money that is released to Sonangol (and thus, due to fungibility of funds between the two, also potentially to the Angolan government) from these loans is repaid from future oil revenues, and thus consists of the patrimony of the Angolan people, which according to the Angolan constitution should be exploited and used 'for the benefit of the community as a whole'.<sup>391</sup>

Yet the Angolan parliament has no opportunity to scrutinise these loans. As a result of the culture of secrecy surrounding these deals, with select details released to the trade press only when banks feel like doing so, it is impossible for the Angolan people to see where the country's wealth is going. In fact, ironically, it appears that banks have been publicising even fewer details of their oil-backed loans to Angola since Global Witness criticised 2005's loan.<sup>392</sup>

It is very difficult under the current regime for Angolan citizens to hold their government to account. Parliament is weak, and civil society is put under pressure. There is thus a greater responsibility on the part of the international community to ensure transparency over the provision and use of funds.

It is time for banks to be required to verify the use of loans they make, and this should involve transparency over the verification of use of loans. Lending into such environments should also be an issue of concern for banks' shareholders. Where a state-owned company does not have independently audited and published accounts available to ensure that proper risk assessment is carried out, banks should be required to report publicly to their shareholders on what basis their risk assessments have been made. Crucially, banks should also be required to publish

details of loans made to any governments or state owned companies. Otherwise, claiming that they are lending to a state oil company and that this is good business, banks will continue to be able to support a regime that suppresses dissent, still does not fully and publicly account for its oil money, and allows children to die in unconscionable numbers despite its growing wealth.

### Action needed:

- Banks should be required to publish details of loans to governments or state-owned companies, including fees and charges.
- Banks should be required to transparently verify use of the loans they make to governments and state-owned companies.
- Where a state-owned enterprise receiving a loan does not have independently audited and published accounts available to ensure proper risk assessment is carried out, or some other independent oversight mechanism, banks should be required to report publicly to their shareholders on what basis their risk assessments have been made.

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Shamefaced?  
Governance and  
transparency in  
Angola under  
**President dos**  
**Santos** are still dire.  
Credit: Mikhail  
Metzel/AP



# THE PROBLEM WITH THE FINANCIAL ACTION TASK FORCE



The face of the Financial Action Task Force: FATF is failing to use its powers to name and shame countries that are not stopping flows of dirty money.  
Credit: Reuters/Corbis

The Financial Action Task Force performs a crucial role. There are two layers to the anti-money laundering regulatory system. Banks are monitored by their regulators to ensure that they are compliant with the law of that jurisdiction. Each jurisdiction is then monitored by FATF or one of its regional bodies, to ensure that its laws are compliant with the global standard set by FATF, and that these laws are being enforced in practice.

FATF's 40+9 Recommendations, backed by the threat of sanctions for jurisdictions that insufficiently put them into place,

have had a dramatic impact in getting anti-money laundering laws onto the books of countries that previously had none. But since 2002, FATF has largely withdrawn from the practice of 'naming and shaming' non-compliant jurisdictions which occurred under its previous Non-Compliant Countries and Territories (NCCT) Process.

Moreover, it has yet to move from evaluating whether a jurisdiction has put into place anti-money laundering laws that meet FATF's standards, to taking action against countries for failure effectively to implement those laws.

These decisions have led to a gap between FATF's professed standards, and their actual implementation at national level in many states. While this problem has begun to be addressed during 2008 through warnings issued to a few states, much of FATF's process has remained confidential and most of its activities are carried out by financial regulatory and enforcement officials with minimal public participation. There has been too limited focus in practice on combating the laundering of corrupt funds, compared with the focus on combating terrorist finance. There are also important gaps in FATF's recommendations themselves, especially in connection with ensuring sufficient transparency over beneficial ownership of assets.

*If you know there's no landing space to land your plane, you don't take off in the first place. It's the same with money: if there's nowhere to land it once you've stolen it, you can't steal it.*

Nigerian anti-corruption investigator, 2008<sup>393</sup>

None of these limitations is inherent to FATF's structure. All of them could be addressed if FATF chose to address these four principal current weaknesses:

### 1. Increasing the impact of FATF recommendations.

One weakness is that FATF is not using the powers at its disposal effectively. FATF has no legal enforcement powers of its own. This is an inevitable consequence of its status as an intergovernmental body. FATF is a creature of its member states; it is the vehicle through which they can take action against corrupt funds. This is why Global Witness's recommendations are targeted at the governments of the world's key economies, rather than directly at FATF.

However, in Global Witness's view FATF could use some of the non-legal powers that are at its disposal to put more effective pressure on countries to tighten up their AML standards and, crucially, to make sure that their rules are enforced. These powers are simple but potentially effective: naming and shaming, and public pressure.

Between 1999 and 2002 FATF ran a Non-Compliant Countries and Territories (NCCT) list which effectively blacklisted

those jurisdictions whose AML regimes were insufficient. The countries on the blacklist were forced by being named on the list to rewrite their legislation in order to avoid the impact of potential sanctions. The list dwindled as they did this. However, since the IMF and World Bank became involved in the anti-money laundering system in 2002, the blacklist approach has been dropped, leaving little risk in practice to jurisdictions who have failed to enforce FATF guidelines.

In recognition of this gap, the FATF initiated a new process in 2006, the 'International Cooperation Review Group,' which, FATF says, aims to 'identify, examine and engage with vulnerable jurisdictions that are failing to implement AML/CFT systems. The FATF has said that it: 'will continue to use this process to reach out to those countries and, where appropriate, will take firm action when a country chooses not to engage with the appropriate FSRB [FATF-style Regional Body] or the FATF to reform its systems.'<sup>394</sup>

It is not clear how the FATF determines when it will move beyond this confidential, non-public process, to a more public stigmatisation. In February 2008 FATF issued an advisory warning that Uzbekistan, Iran, Pakistan, Turkmenistan, São Tomé and Príncipe and Northern Cyprus had serious deficiencies in their anti-money laundering and counter terrorist financing regimes.<sup>395</sup> As a consequence, the majority of FATF members issued advisories to their financial institutions warning them to take this into account in their analysis of country risk. The purpose of this was threefold: punishment (by making it harder for banks to do business in these countries); prevention of contagion (by making it less likely that criminal or terrorist money from these countries would move into the financial system), and remedy (pressing these countries to change their anti-money laundering regimes; there is no sign of this happening in Iran or Uzbekistan).

This process is for the serious cases. But it is generally for non-members. While there is nothing theoretically preventing a FATF member from receiving this treatment, (just as there was nothing theoretically preventing a FATF member ending up on the old NCCT list) it hasn't happened yet.

The fact is, though, that a number of FATF members themselves have yet effectively

to implement FATF's recommendations. Within the past three years, for example, both the US and the UK were found still to have failed to make it a legal requirement to identify beneficial owners.<sup>396</sup>

One of the recurring complaints about FATF from the small island nations who are frequently its target has been that it focuses on their deficiencies at the expense of those closer to home, in the regulatory centres of power in the major economies. This means that the major financial centres are without a leg to stand on when lecturing the more typically perceived secrecy jurisdictions. Of 24 FATF member states evaluated in the last three years, none have legislation in compliance with FATF's Recommendation

6 which says countries must require their banks to perform enhanced due diligence on politically exposed persons. Only four countries were 'largely compliant', two were 'partially compliant' and eighteen of them were non-compliant.<sup>397</sup> See table below.

So what happens to the FATF members whose regulations are less than fully compliant with FATF standards? According to FATF's website, the current procedure is an escalating package of peer-pressure type measures, beginning by requiring the country to deliver a progress report at FATF plenary meetings, then a letter to the country's president from the FATF president or a high-level mission to the offending country. While somewhat humiliating for the civil servants responsible

### *Analysis of FATF member states' compliance with key FATF Recommendations*

Country	Date of mutual evaluation	Rec. 1. Money laundering must be made illegal	Rec. 5. Banks should be required to undertake customer due diligence to identify the beneficial owner	Rec. 6. Banks should be required to do enhanced due diligence for Politically Exposed Persons (PEPS)	Rec. 33. Countries must prevent the unlawful use of legal persons [eg companies] by money launderers	Rec. 34. Countries must prevent the unlawful use of legal arrangements, especially trusts, by money launderers	Non-compliant; NC
Australia	October 2005	LC	NC	NC	LC	PC	
Belgium	June 2005	C	LC	LC	PC	N/A	
Canada	February 2008	LC	NC	NC	NC	PC	
China	June 2007	PC	PC	NC	NC	PC	
Denmark	June 2006	LC	PC	NC	PC	PC	
Finland	October 2007	PC	PC	NC	PC	N/A	
Greece	June 2007	PC	PC	NC	NC	N/A	
Hong Kong	June 2008	LC	PC	PC	PC	PC	
Iceland	October 2006	PC	PC	NC	PC	N/A	
Ireland	February 2006	LC	PC	NC	PC	PC	
Italy	October 2005	C	PC	NC	C	PC	
Japan	October 2008	LC	NC	NC	NC	NC	
Norway	June 2005	LC	PC	NC	LC	N/A	
Portugal	October 2006	LC	PC	NC	PC	PC	
Qatar	April 2008	PC	NC	NC	LC	PC	
Russia	June 2008	LC	PC	PC	PC	N/A	
Singapore	February 2008	PC	LC	LC	PC	PC	
Spain	June 2006	LC	PC	NC	PC	N/A	
Sweden	February 2006	LC	PC	NC	PC	N/A	
Switzerland	October 2005	LC	PC	LC	NC	N/A	
Turkey	February 2007	PC	NC	NC	PC	N/A	
UAE	April 2008	PC	NC	NC	PC	C	
UK	June 2007	C	PC	NC	PC	PC	
US	June 2006	LC	PC	LC	NC	NC	

- Non-compliant;  
NC
- Partially compliant;  
PC
- Largely compliant;  
LC
- Compliant  
C

for anti-money laundering regulation, these are hardly a terrifying prospect overall. There are no publicly available statistics on how many times these measures have been invoked.

The penultimate option is application of FATF Recommendation 21, in which FATF calls on financial institutions to conduct extra due diligence on transactions involving people, companies or banks domiciled in the non-complying country.<sup>398</sup> As far as Global Witness understands, Recommendation 21 has never been activated. As a final resort, FATF can suspend its members, but this has not happened either.

What this means is that there is not a great deal of pressure on members that are non-compliant with the FATF standards. This is why Global Witness is recommending that FATF publish a clear list of the compliance status of each country with each recommendation, and the date by which it has to comply, to make it easier for the media and public to exert pressure for improvement. This would have the added advantage of making customer due diligence easier. FATF Recommendation 9, for example, allows financial institutions to rely on intermediaries to perform customer due diligence functions, as long as various criteria are fulfilled – including that the intermediaries are in a jurisdiction that adequately applies the FATF Recommendations. Such a list would help to make it clear which jurisdictions these are.

It is also why Global Witness is recommending that FATF begins a new name and shame process. This time it should identify those FATF members who, despite being compliant with the recommendation to have laws in place, are failing to enforce those laws. To strengthen this focus on implementation, FATF should develop the capacity to investigate referrals from regulators, law enforcement, parliamentarians or NGOs, as well as those cases that are revealed by its own mutual evaluations to identify jurisdictions that may have laws in place, but are not properly enforcing them.

## **2. Making FATF's activities more accountable and accessible to the public**

The second weakness is that FATF appears to operate in isolation from many of the other actors who are working on anti-corruption efforts, and is not sufficiently publicly accountable.

Participation in FATF is led by each member state's ministry of finance. However, there are many other actors, both in government and outside, who are working on anti-corruption efforts and who could lend support and new perspectives to FATF's work. Ministries of development deal with the impacts of corruption every day in their work; other government departments may lead on participation in the UN Convention Against Corruption or the OECD Anti-Bribery Convention. Anti-corruption commissions, the law enforcement officials who are dealing with corruption and money laundering on the front line, and a recent proliferation of asset recovery organisations, both private and inter-governmental, would all have useful contributions to make. But Global Witness has heard many of them bemoan the fact that FATF operates in isolation. Meanwhile, a growing civil society movement, both in the developing and developed worlds, is mobilising against corruption and the role played by the financial sector.

Moreover, despite the huge importance of FATF's work, and the potential it has to make much greater inroads into corruption and therefore poverty, there is little accountability, whether to other parts of government, parliaments, or the public. Parliaments rarely discuss FATF, and the public has not heard of it, despite the power it has to reduce poverty and therefore reduce the need for tax-payer funded aid donations.

This all means there is little pressure to up its game. FATF meetings continue to be a technical gathering of finance ministry civil servants, which are observed only by prospective country members, inter-governmental bodies such as the OECD and UN, financial intelligence units (which process the suspicious activity reports from banks) and the international financial institutions such as the IMF and World Bank. Whilst of course, anti-money laundering being a technical subject, FATF must retain its technical experts, it should also open its doors to other participants, both governmental and non-governmental, and conduct some of its deliberations and all of its votes in open session.

## **3. Strengthening FATF's capacities to combat the laundering of the proceeds of corruption**

The third weakness is that FATF's focus on terrorist financing has not been

matched by equal attention to the fight against corrupt funds.

FATF was originally set up in 1989 to counter the proceeds of the drug trade, and its remit later expanded to all organised crime and, after September 2001, to terrorist financing. The imperative to stop terrorist funds gave it a shot in the arm of political will, and for the last few years the IMF and World Bank have also been on board helping to carry out the evaluations – although they only joined in on the condition that the naming and shaming of particular jurisdictions stopped. But the effort put into fighting terrorist funding has not been matched with equal political will to fight the proceeds of corruption, and their pernicious effects on poverty.

The latest revised mandate, agreed under the UK's FATF presidency in April 2008 to take FATF forward to 2012, is full of laudable aims on tackling terrorist finance and 'proliferation finance', as well as 'criminal' proceeds, but fails to make even one mention of corruption or its effect on poverty.<sup>399</sup> 'Corruption' is intended to be implicit within use of the word 'criminal', and Global Witness has been given to understand that one of the reasons for not being explicit about corruption is that it could generate political opposition to FATF's work in some countries. But the message that this communicates to financial institutions, who may not be aware of the politics behind FATF's choice of words, is that corruption is a much lower priority. Global Witness is concerned that many financial institutions, and also many non-financial institutions that are regulated for anti-money laundering purposes, such as trust and company service providers, are still too likely to regard corruption as a petty offence rather than the major economic and social threat that it presents to many poor countries.

The result of this is most dramatically illustrated by the instruction to Bank of East Asia to pay Denis Christel Sassou Nguesso's credit card bill, which has been stamped 'record of terrorists checked' (see Chapter 5). What will it take to make sure that such an instruction has been stamped 'record of PEPs checked'? And when Riggs wrote to HSBC in Luxembourg and Banco Santander in Spain, wanting to know who was behind the Kalunga and Apexside accounts: would there have been a different response

if there was a potential terrorist involved, rather than potentially looted oil money?

This is why Global Witness is recommending that FATF convene a task force to focus on the prevention of corrupt money flows, and is calling for countries to be required to publish PEP lists and asset disclosure lists as a condition of FATF membership. Both of these requirements would make it much easier for banks to identify customers at higher risk of presenting corruptly acquired funds.

#### **4. Providing sufficient transparency about ownership of assets**

The fourth weakness is that there are loopholes in FATF's standards themselves, which means that the AML framework it promotes is not sufficient to curtail the flows of corrupt money.

The key loophole concerns transparency over beneficial ownership of companies and other



arrangements such as trusts that people use to hide their identity and thus their funds. Identification of beneficial ownership, as some of the case studies in this report have shown, is at the heart of identifying corrupt funds, or for that matter, terrorist funds. If you don't know who is in control of the entity that is opening the account, you have not yet identified your customer. FATF itself has identified corporate vehicles as a key money laundering risk.<sup>400</sup>

FATF Recommendations 33 and 34 require countries to take measures to prevent the unlawful use of legal persons (eg companies) or legal arrangements (eg trusts) respectively. For companies, Recommendation 33 says 'Countries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities.' For trusts, Recommendation 34 says countries should 'ensure that there is adequate, accurate and timely information on express trusts, including information on the settler, trustee and beneficiaries.' Both say that 'Countries could consider measures to facilitate access to beneficial ownership and control information to financial institutions.'

What might these measures be? FATF's Methodology for Assessing Compliance suggests a variety of mechanisms that countries 'could' use in 'seeking to ensure that there is adequate transparency.'

These range from:

1. 'A system of central registration where a national registry records the required ownership and control details for all companies and other legal persons [for Rec 33].. / details on trusts (ie settlors, trustees, beneficiaries and protectors) and other legal arrangements [for rec 34] registered in that country. The relevant information **could be either publicly available or only available to competent authorities.**' [emphasis added]
2. 'Requiring company service provider/ trust providers to obtain, verify and retain records of the beneficial ownership and control of legal persons/ details of the trust or other similar legal arrangements'.
3. 'Relying on the investigative and other powers of law enforcement, regulatory, supervisory, or other competent

authorities in a jurisdiction to obtain or have access to the information.'

So a crucial element of an effective anti-money laundering regime, ie a publicly available national registry providing transparency over who owns what, is not a mandatory criterion when FATF measures countries' compliance with its recommendations.

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*It is ironic that the international community would fail to produce a single, unified set of rules to take on a criminal activity that thrives precisely on exploiting differences in laws and regulations.*

Nigel Morris-Cotterill, anti-money laundering expert, 2001<sup>401</sup>

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This is an extraordinary issue to leave to the discretion of individual jurisdictions. The question of whether company ownership or trust information is publicly available is at the heart of what permits the offshore financial centres to survive and to peddle their noxious trade of secrecy. What is particularly extraordinary is that deep in its published methodology for assessing compliance, FATF itself is suggesting the solution to the problem: public registries of information on companies and trusts. But it does not make this a mandatory requirement, merely an option. Those financial centres that wish to make a living by providing secrecy to their clients simply take the easier option of ensuring that law enforcement and regulatory authorities have access to the information, rather than making it public.

This issue goes way beyond enabling banks to fulfil their customer due diligence requirements. Public registries would also mean that those wishing to hide illicit gains (whether from corruption or, indeed, tax fraud) would have nowhere to hide. A number of secrecy jurisdictions keep their noses clean and get relatively good marks for providing cross-border legal assistance by responding promptly when asked for details on a particular case under investigation. But they have to be formally asked by national authorities, who need to know what they are looking for and not just be on a 'fishing expedition'. What is the likelihood that a state currently in the hands of a kleptocrat is going to put in a

formal request relating to his assets overseas? The only time this happens is when regimes change and the successor government tries to chase the assets stolen by their predecessor – sometimes as convenient cover for their own corrupt activities.

Even if an official request is put in, it is one thing for a law enforcement official, in the middle of an investigation, to put in a specific request when he knows the name of the company that he is looking for. It is quite another – let's be straight, it is completely impossible – for citizens of impoverished but resource-rich countries to be able to see in which jurisdictions their rulers are stashing their looted assets, when they have no idea of the company names and no weight of the law behind them. Information exchange on request, the current system, is the lowest common denominator of disclosure. Expensive, time consuming and cumbersome, for ten years this system has failed to produce sufficient results. Requests for information are frequently

not fulfilled, and the bar is set too high to produce information. Even if it is provided, the public does not know whether real live ownership information is being disclosed, or straw men. Nor is information provided about how many requests have been fulfilled.

FATF would argue that it has set out the requirement in Recommendations 33 and 34: to prevent the unlawful use of companies and trusts by money launderers and ensure that beneficial ownership information is available, and that beyond that, in the spirit of the risk-based approach, it is up to individual jurisdictions to decide exactly how they should do this. Global Witness believes, however, that this is such a crucial point that complete published transparent records should be part of the explicit mandatory standard, and that the governments which constitute FATF are fundamentally shirking their responsibilities – and undermining their laudable efforts elsewhere – until they require and enforce this.<sup>402</sup>



FATF is not helping ordinary citizens in developing countries.  
Credit: Peter Turnley/Corbis

# 10

# CONCLUSION AND RECOMMENDATIONS

## What went wrong

The banks that feature in this report are hiding behind a series of convenient excuses – of being prevented by bank secrecy laws from disclosing the name of a customer (HSBC and Banco Santander, with the Equatorial Guinea oil funds transfers from Riggs); of dealing with a commercial entity, when in fact it was a state owned company in a corrupt state (the many banks that have provided oil-backed loans to Angola's state oil company, Sonangol); of dealing with state funds, when actually the state has been captured by a human rights-abusing dictator (Deutsche Bank and Turkmenistan); of dealing with a correspondent bank, when the customers behind it were pillaging the state to pay for conflict (Citibank and Liberia).

Crucially, these banks are able to hide behind customer confidentiality, and in some cases bank secrecy laws as well, in declining to respond to any of Global Witness's questions about these cases. The banks cannot tell us what they have done, and nor can the regulators. All we can see is the end result: that the banks ended up doing business with these dubious customers.

If all countries were getting full marks from FATF for their anti-money laundering laws, if FATF was investigating enforcement of laws as well as just their mere existence on the books, and if the standards pushed by FATF were not full of loopholes, then perhaps it would be enough to rely on the regulators doing their job properly. But as this report has shown, this is not the case. Global Witness therefore

Testimony by bankers about the credit crunch has revealed an arrogant culture that took unacceptable risks.  
Credit: Matthew Cavanaugh/Corbis



## Box 6: Natural resources: the common link

There is a common thread running through all of the stories in this report, despite the different types of banking activity. Each time, the customer was involved in a situation where, at the very least, natural resource revenues were not being transparently accounted for.

- **natural resource revenues were unaccounted for in a country with huge oil income and clear concerns over corruption** (Angola, where commercial banks, on the basis of providing trade finance to a state oil company, were actually going to a government that couldn't access other forms of credit and had huge holes in the budget)
- **natural resource revenues had been apparently diverted for private use by politically exposed persons** (Equatorial Guinea, where Riggs' violations were flagrant; and Republic of Congo, where Bank of East Asia accepted an account for a shell company whose beneficial owner was the son of the President of Congo and responsible for marketing the country's oil)
- **natural resource revenues were kept offshore, off budget and away from scrutiny** (Turkmenistan's gas funds, where Deutsche Bank, on the basis of holding central bank accounts, was actually doing business with a repressive dictator who had sole effective control of the money)
- **natural resource revenues were funding conflict** (Liberian timber payments through Fortis and Citibank; in the latter case, through correspondent accounts.)

believes it is in the public interest, both for citizens of resource-rich but poor countries and citizens of countries whose governments are responsible for regulating banks, to highlight the concerns raised by these cases.

Each story has been examined from three perspectives: the bank's ethics, the bank's compliance with due diligence processes, and regulatory action.

• **Ethical failure?** There seems to be a yawning gulf between the statements that banks make about their commitment to sustainable development and human rights, and the business they are doing with countries that cannot account transparently for their natural resource revenues.

• **Compliance failure?** From the compliance perspective, these banks were required to do due diligence to know their customer. Global Witness does not know from the available evidence exactly what due diligence they did, and the banks do not have to tell us. So we do not know if they fulfilled their regulatory obligations to know their customer. What we can see very clearly from the available evidence, though, is that in each case, the bank ended up doing business with customers about whom there was information available in the public domain that should have raised significant concerns.

• **Regulatory failure?** In some of these cases Global Witness has not been able to find out from regulators if they have taken any action. In others, regulators were not on the case because they themselves are not required to be; these are the emerging, unregulated issues on which attention now needs to be focused.

Behind all this, though, is a systemic failure: that of the governments who control the commanding heights of the world's economy to tackle seriously and holistically the problem of dirty money. They are happy to pass anti-money laundering laws that look good on paper, and use the Financial Action Task Force to ensure that other nations adopt similar laws, but have not made a joined up effort to ensure that these laws are being implemented in a way that actually reduces corrupt money flows. The G8 nations make strong statements about wanting to end poverty and corruption, but allow gigantic loopholes to remain in the rules.

### The consequences

The consequences of these failings cannot be understated. Financial flows are not a by product of the corrupt shadow state, but are integral to its survival.

• Large-scale corruption cannot take place without financial intermediaries to help move the money so that it can be enjoyed far from where it was looted, such as Bank of East Asia (and the trust and company service providers) for Denis Christel Sassou Nguesso and the Congolese oil funds.

## Box 7: Regulation rather than voluntary initiatives?

Readers will note that while this report has examined each case from the perspective of the bank's ethics, the bank's due diligence obligations, and the duties of the regulators, the majority of the recommendations tackle the identified problems from the perspective of regulatory obligations. The first recommendation does call on banks to improve their culture of due diligence, but then it is followed by a recommendation calling for this effective due diligence to be a legal obligation that is rigorously enforced. While there is a role for the kind of voluntary initiatives that allow banks to display their ethical wares, particularly in building norms, such initiatives do not fare particularly well in these stories.

The Wolfsberg Principles, an initiative by eleven of the world's largest international private banks to develop principles and policies for anti-money laundering, know your customer and counter terrorist finance, was set up in 2000 after Citibank suffered the huge embarrassment of the US Senate Permanent Subcommittee on Investigations probing its private banking arrangements for politically exposed figures. Six of the banks that feature in this report – Banco Santander, Barclays, Citigroup, Deutsche Bank, HSBC and Société Générale are among the eleven members of the Wolfsberg Group. HSBC cited its co-chairing of the Wolfsberg Group in its response to Global Witness's enquiries. Yet these banks have either held accounts for prominent PEPs, or taken part in transactions that raise questions, yet whose nature is not addressed by the Wolfsberg Group.

Crucially, it only has eleven members; what are the rest of the world's banks doing? Insiders who have been involved in Wolfsberg meetings have told Global Witness that it is not achieving anything beyond a statement of intent. Meanwhile it can potentially serve as a block on substantive change to

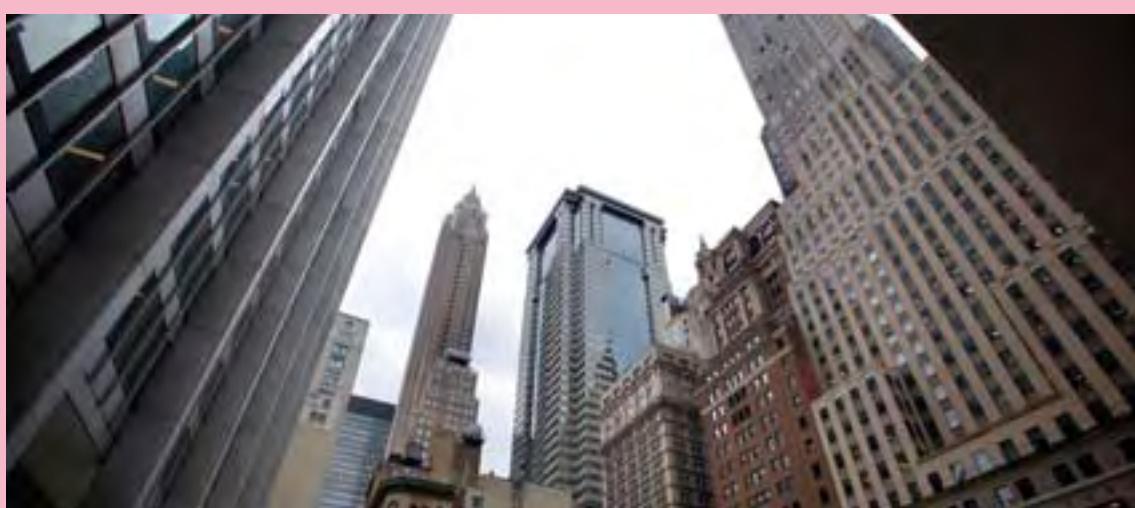
the regulatory framework, because it allows a few of the biggest banks to say 'we're already doing something.'

Then there is the Global Compact, membership of which has been repeatedly cited by Deutsche Bank in its replies to Global Witness about both the Turkmen central bank accounts and its participation in oil backed lending to Sonangol in Angola. The Global Compact describes itself as the 'world's largest corporate citizenship' initiative, with 4,700 businesses among its members in 130 countries, all of whom have signed up to its 10 principles on human rights, labour, the environment and anti-corruption. While it is willing to de-list members if they do not provide regular progress updates, and its 'Integrity Measures' provide an opportunity for dialogue between complainants and companies, the Compact is explicit that it does not provide any monitoring or policing functions.

Global Witness has repeatedly asked Deutsche Bank to explain how its human rights commitments under the Global Compact are compatible with having done business with the late President Niyazov's regime in Turkmenistan. It has repeatedly refused to answer this question. Yet it continues to cite its membership of the Global Compact whenever Global Witness asks any questions about its policies.

The problem here is that voluntary initiatives largely depend on companies or banks being able to show the public what they have done, since very few of these initiatives have effective monitoring mechanisms. Many of the other voluntary corporate initiatives deal with social and environmental impacts where it is rather more apparent whether companies or banks have complied or not. With the Equator Principles, for example, the environmental and social impact of new infrastructure funded by project finance deals can be evident to anyone who cares to visit the affected area with a camera and notebook.

But when it comes to banks providing services to customers that may be corrupt, whether they are individuals, institutions



Regulators of Wall Street and of other financial centres must do more to tackle the proceeds of foreign corruption.  
Credit: Steve Forrest/  
Panos

or states, it is far less evident to the public eye what is happening. In fact, this information is strictly protected by customer confidentiality and, in some jurisdictions, banking secrecy rules.

In each of these stories, Global Witness has written to the relevant bank to ask about its relationship with the customer, about the due diligence that it did, about the SARs it might have filed. They all cited customer confidentiality for their refusal to respond, and many also pointed out that they are prohibited by law from providing any information about their customer relationships (although Global Witness maintains that banking secrecy laws should not have prevented some of them being rather more forthcoming about their more general policies). In addition, the SARs regulatory regime explicitly prevents disclosure – ‘tipping off’ – by either a bank or a regulator that a SAR has been filed.

So how can the public know, on such huge questions of public interest for the countries in question, whether the banks are doing what they should do? The answer from the banking industry is that their regulators will ensure this. So in each story, Global Witness has also written to the relevant regulator. Again, of course, the regulators are prevented from sharing this information with us. (Ironically, the only case in which Global Witness has had any substantive communication from a regulator is the

one case in which the situation we have identified is not yet subject to the same regulations, because they are classified as central bank accounts: that of the Turkmen accounts at Deutsche Bank.)

So on an issue where banks are not able to tell the public what they are doing, and where regulators are not able to talk either, and the voluntary initiatives have no effective monitoring mechanisms, how can the public have any faith that such voluntary mechanisms are meaningful? In a field that operates on the basis of secrecy and confidentiality, a voluntary mechanism such as the Wolfsberg Standards may be welcome in its dissemination of best practice and advice to banks, but it cannot be taken as any more than that, and no voluntary mechanism can be seen as a substitute for a regulatory regime that rigorously enforces a set of rules that promote transparency.

Global Witness does recommend that banks start to take a more holistic view of their sustainability responsibilities, and include their anti-corruption work among the things that they do to prevent social and economic abuse, since corruption causes precisely these problems. But ultimately, the link between the fight against corruption and promotion of sustainability is too important for this issue to be left in the ethical corner, where it can be ignored whenever convenient or whenever profit margins are looking uncomfortably tight.

- Repressive dictatorships cannot flourish if they cannot find a way to keep funds away from the budget and away from rivals, as Niyazov did with Deutsche Bank.
- Those who sell natural resources to fund conflict, such as Charles Taylor and his regime, cannot receive payments for their goods, or payments into their personal accounts, without access to the global financial system and the willingness of banks such as Citibank and Fortis to open accounts and correspondent relationships with banks in war-torn countries.
- Oil-rich but corrupt governments such as Angola's, unable to gain a credit rating and unwilling to do business with the public financial institutions that would require a light to be shone into the opaque corners of their budgets, cannot find a way to raise money unless commercial banks are prepared to lend against the oil revenues despite concerns about where the money may be going.

While corruption survives, so will poverty. The goals that the international community has set itself to tackle poverty are clear: the Millennium Development Goals need to be achieved by 2015, which is fast approaching.<sup>403</sup> Even with falling commodity prices, natural resources offer a huge opportunity for many developing countries to lift their populations out of poverty, in a way that could be far more sustainable – and involving far greater amounts of money – than the provision of aid from the developed world.

But by failing to ensure that their banks do not contribute to corruption, the governments of the rich world are ensuring that this opportunity cannot be taken. With one hand they continue to give aid, but with the other they are holding open the floodgates to allow much greater amounts to flow back through their own financial systems. This is not something their taxpayers, who fund the aid, should be comfortable with.

The governments of the rich world need to tackle the facilitators of corruption proactively, rather than waiting to respond half-heartedly to the next scandal that is uncovered by a journalist, NGO or parliamentary investigation. All promises by the developed world to reduce poverty will be meaningless unless the will to do this is found.

## **The Recommendations**

In Section A, we set out three key principles: banks must change their culture of due diligence; banks must be regulated to force them to do due diligence effectively to weed out corrupt funds; and there needs to be vastly improved international cooperation through FATF to ensure that this happens.

In Section B, we propose specific actions to implement the three key principles. These new rules would help to close loopholes in the system and help banks identify and avoid corrupt funds.

In Section C, we offer some specific recommendations arising from the case studies in the report.

### **The coming reassessment of the regulatory system for banks offers an opportunity to overhaul the way we fight corrupt funds, an opportunity which must be taken.**

Some of the same factors which caused the banking crisis – bankers doing the minimum they can get away with when it comes to sticking to the rules, lack of disclosure of key information and lack of joined-up regulation – are also those which allow corrupt, criminal and terrorist funds to enter the financial system. The entire banking regulatory system is now up for re-evaluation. If PEPs from corrupt countries are able to move their money around without questions, then that means the system may also be open to other forms of crime, as well as terrorist funds. It means that the regulators do not know enough about their system. Vulnerability to one kind of destabilising money is vulnerability to another.

## **A. Three key principles**

### **1. Banks must change their culture of know-your-customer due diligence, and not treat it solely as a box-ticking exercise of finding the minimum information necessary to comply with the law.**

Banks should adopt policies so that if they cannot identify the ultimate beneficial owner of the funds, or the settlor and beneficiary if the customer is a trust, and if they cannot identify a natural person (not a legal entity) who does not pose a corruption risk, they must not accept the customer as a client. They

## What banks can do right now to change their culture and curtail illicit financial flows



**By Raymond Baker,**  
author of  
*Capitalism's Achilles Heel: Dirty Money and How to Renew the Free-Market System*

Suppose, just suppose, that a bank decides that it no longer wants to receive illicitly generated money of any type, whether the proceeds of corruption or criminal activity or commercial tax evasion. What could it do? Consider the following five steps.

1. Announce that this is the bank's policy.  
 'We welcome funds that have been legally earned and transferred and will be legally utilized. We do not wish to handle funds that have broken laws in their origin, movement, or use.' I've known lots of corrupt government officials and serial tax evaders and a few criminals who would respond to an inhospitable environment by keeping their money close at hand or taking it elsewhere, which is exactly what I want them to do.

2. Inform account holders in writing of this policy in a communication from the highest level of the bank's executive staff.

3. Ask account holders to respond in writing that they have received the communication and will abide by the bank's directive.

4. Close 'Hold All Mail' accounts. Foreign account holders are often offered arrangements whereby no bank statements or other correspondence is sent to the account holder's foreign address. These are almost invariably accounts dealing in suspect or tax evading funds. With proper notice to clients, end such account services.

5. Allow exceptions in situations where the health or safety of an individual is at stake. If a long-term depositor needs to handle an emergency, such as a medical crisis or ransom demand, bank executives should be permitted to respond, duly noting the exception to bank policy.

Of course a tighter regulatory regime is needed – the financial crisis has demonstrated that. However, notice that all of the above steps simply underline bank policy. The goal of such steps is to curtail – not stop but substantially curtail – illicit financial flows passing into or through the bank.

Any bank implementing such measures can make its new policy a positive contribution toward its desire to be as responsible a member of the global financial community as possible. Such a bank will get my business immediately and I hope yours as well.

should adopt this standard even if they are not legally required by their jurisdiction to do so.

International discussions on corruption have expended endless hot air on defining a PEP, and varying definitions are still in use. But this debate is a diversion from the more important matter at hand, which is that regulations requiring banks to identify PEPs are meaningless if banks cannot identify their customer in the first place. Global Witness has attended some of the most high-profile international anti-money laundering conferences, at which the conversation rarely moves beyond defining PEPs to the real point: if you don't know who your customer is because he's at the top of complicated ownership structure in an

opaque jurisdiction, how can you know if he's a PEP? Or, for that matter, a terrorist?

Many of the cases in this report do not involve people on the uncertain borderline of those who might or might not be considered to be a PEP; they are heads of state or their immediate family members from countries with disturbing evidence of corruption. Yet they were able to open accounts anyway, whether in their names or those of companies behind which they are hiding.

**2. Banks must be properly regulated to force them to do their know your customer due diligence properly, so that if they cannot identify the ultimate beneficial owner of the funds, or the**

**settlor and beneficiary if the customer is a trust, and if they cannot identify a natural person (not a legal entity) who does not pose a corruption risk, they must not accept the customer as a client.**

Anti-money laundering laws must be absolutely explicit, and consistent across different jurisdictions, that banks must identify the natural person behind the funds, investigate the source of funds, and refuse the customer if they present a corruption risk. Regulators are in the front line of ensuring that this is enforced, and should treat the prevention of corrupt money flows as a priority.

This is the scandal at the heart of the system, because customer identification has been the crucial element of money laundering laws since their inception in the 1980s. Yet inconsistencies and a failure by many jurisdictions to be sufficiently explicit about what is required from banks in practice mean that there are still too many loopholes that can be exploited. Of 24 FATF members evaluated in the recent round of FATF evaluations, none were fully compliant with Recommendation 5, which

requires countries to have laws in place obliging banks to identify their customer.

Many secrecy jurisdictions have thousands of companies registered in each office building, none of which consists of more than legal documents in a lawyer or company service provider's office. The onus should be put on banks to demonstrate that they have established that the company opening an account is carrying out genuine business, rather than just being set up for the purpose of moving money around.

As Chapter 2 showed, the culture of compliance is too often solely about avoiding reputational risk, rather than a concern not to take corrupt business. The UK's regulator, the FSA, noted this in 2006 with a survey of banks' systems to deal with PEPs. It found that banks were not so interested in the likelihood that their customer was corrupt, but only in the likelihood that there might be a public scandal which might affect the bank's reputation (see page 22). Regulators need to take responsibility for ensuring that banks change this culture of compliance so that its

The oil is offshore...  
all too often so is  
the money.  
*Credit: Paul Velasco/  
Gallo Images/Corbis*



main focus is avoiding taking the corrupt funds rather than just avoiding scandal.

While it is important that banks develop their own effective know-your-customer policies, as per the previous recommendation, leaving banks to do it on their own without regulatory oversight will not work, because the avoidance of corrupt funds inevitably involves turning down potential business, and not all banks are willing to do this. The subprime crisis and ensuing credit crunch have shown, among other things, that allowing banks to self-regulate does not work. They consistently claim that they employ the cleverest people in the world and can be allowed to manage their own risk. But if, as they have shown, they cannot safely manage the task that is of greatest importance to them – making a profit – then it seems clear that they cannot be expected to self-regulate when it comes to ethical issues.

### **3. International coordination on anti-money laundering must be improved by strengthening the workings of the Financial Action Task Force (FATF). The governments that participate in FATF should:**

- a) Set up a taskforce specifically to tackle the proceeds of corruption, including the prominent role played by natural resources in corrupt money flows. External experts including law enforcement officials who are at the coalface of fighting corruption and money laundering should be invited to take part.
- b) Undertake a new FATF name and shame list focusing on countries – including its own members – that are not implementing their regulations, rather than on the existence of a legal framework. The first version, the Non-Cooperative Countries and Territories List, was instrumental in getting anti-money laundering regulations onto the laws of many jurisdictions that had not previously had them. The problem now is ensuring that they are implemented.
- c) Publish a clearly accessible roster of each country's compliance status with each of the FATF recommendations, and the date by which that country has to comply, in order to increase the public pressure for compliance.
- d) Change FATF's culture to include acknowledgment of the wider development

impacts of its work, inviting representatives of development as well as finance ministries, and forging stronger links with other actors and organisations working on anti-corruption issues including government officials dealing with UNCAC and the OECD anti-bribery convention, anti-corruption commissions, law enforcement, and civil society.

- e) Make its workings more transparent, including by voting in open sessions, and allowing external stakeholders to take part in some of its meetings.
- f) Ensure that FATF's mutual evaluation reports (and those of its regional bodies) are published promptly. If the original findings are altered after discussion in plenary, the original finding, the objection, and the final text should all be provided.<sup>404</sup>
- g) In order to strengthen its capacity to assess the effectiveness of implementation, FATF should develop the capacity to investigate referrals from regulators, law enforcement, parliamentarians or NGOs, as well as those cases that are revealed by its own mutual evaluations to identify jurisdictions that may have laws in place, but are not properly enforcing them.

See Chapter 9 for an analysis of Global Witness's concerns about FATF.

## **B. New rules to implement these principles**

These are specific actions to implement the three principles above, close loopholes in the system, and help banks identify and avoid corrupt funds. These should be undertaken by the governments of the world's major economies, which should then incorporate them in a revised set of FATF Recommendations to ensure that they are required and enforced globally.

These changes should also be supported by the IMF, which is closely involved in monitoring country's compliance with the FATF Recommendations, and the World Bank. (The World Bank is itself a big user of banking services, both by issuing bonds and placing its own funds within the financial system. Given that it already has a blacklist of contractors who are debarred from receiving its contracts because they have broken its rules against corruption and fraud, it should also consider doing the same to banks).

Ordinary citizens in the US and elsewhere are now being harmed by the same opacity and lack of due diligence that have devastated the developing world for years.

Credit:  
David J. Phillip/AP



**4. Every jurisdiction should publish an online registry of beneficial ownership of companies and trusts. Such transparency should become a mandatory criterion for jurisdictions to be in compliance with FATF Recommendations 33 and 34, which require countries to prevent misuse of corporate vehicles and legal arrangements such as trusts.**

This would help banks to fulfil their know-your-customer requirements. Risks are highly concentrated in these vehicles, and because of this, they create huge risk for the financial system. Risks would be dramatically reduced with more transparency.

**5. National regulators should be required by FATF to assess the effectiveness of the commercial PEP databases on which the banks they regulate rely to carry out their customer due diligence. FATF should specify the minimum standards of information that should be provided and ensure that effective regulation is taking place, and should consider accrediting independent evaluators**

who can assess the quality of PEP information for particular countries.

There is currently no definitive list of PEPs. Instead, banks must rely on an ever-increasing array of commercial services that research and provide lists of PEPs and their associates, along with information about business dealings, court cases, corruption allegations, appearances in the press. They then check their potential and existing customers against these databases. A survey by KPMG into banks' anti-money laundering procedures found that banks in Europe and North America were most likely to rely entirely on commercial lists they had purchased.<sup>405</sup>

This makes nice money for the companies providing the databases, and allows the banks to claim that they have done their due diligence. Whether they have enough appropriate information in them is open to question; some money laundering experts claim that no database will have sufficient information on its own. Each of the database providers that Global Witness has spoken to claims that theirs is the only one which provides usable intelligence rather than raw data. But there is no real incentive for the

private database providers to ensure that they have sufficient data. Meanwhile preliminary as-yet unpublished research seen by Global Witness into some of the most widely used databases of information about PEPs has shown that large numbers of politically exposed figures are not represented.

**6. Each jurisdiction should be required to maintain a public income and asset declaration database for its Head of State and senior public officials (those who would qualify as politically exposed persons), to assist banks in identifying the proceeds of corruption.**

The United Nations Convention on Corruption calls on States Parties to 'consider' doing this, as part of its chapter on Asset Recovery. It envisages that this would be useful when investigating, claiming and recovering the proceeds of corruption. However, if FATF required each jurisdiction to implement income and asset disclosure for its Head of State and senior public officials, and required banks to refer to this when assessing PEP accounts, it would help to prevent any funds misappropriated by PEPs making their way into the financial system in the first place. This would be far easier than trying to use asset recovery procedures to get them back afterwards, as the Nigerians who have had such trouble trying to get Sani Abacha's loot back from British banks know all too well. A survey of the 148 countries eligible to receive World Bank support found that in 104 countries, senior officials must disclose their income and assets in some form. Of these, 71 nations require their officials to declare assets only to an anticorruption body or other government entity; the other 33 also require that they be published.<sup>406</sup>

**7. Banks should be required by regulation to respond to requests for information from other banks or their own overseas branches that are subject to supervision by any regulator from a country that is broadly in compliance with FATF standards without falling foul of banking secrecy laws, whether the request is being made in connection with an inquiry relating to money laundering, terrorist finance, or tax fraud risk.**

Banks can currently shelter behind secrecy laws in order to remain deliberately blind

to information about customers using their branches in other jurisdictions, or to the owners of accounts into which they might be asked to make transfers. Both of these situations prevent banks from properly fulfilling their customer due diligence requirements. In the first: a bank effectively has a correspondent relationship with its branches in other jurisdictions, so ought to be able to ask its correspondent bank about its customers if necessary, in order to fulfil its obligation to understand if its correspondent bank has sufficient due diligence procedures in place.

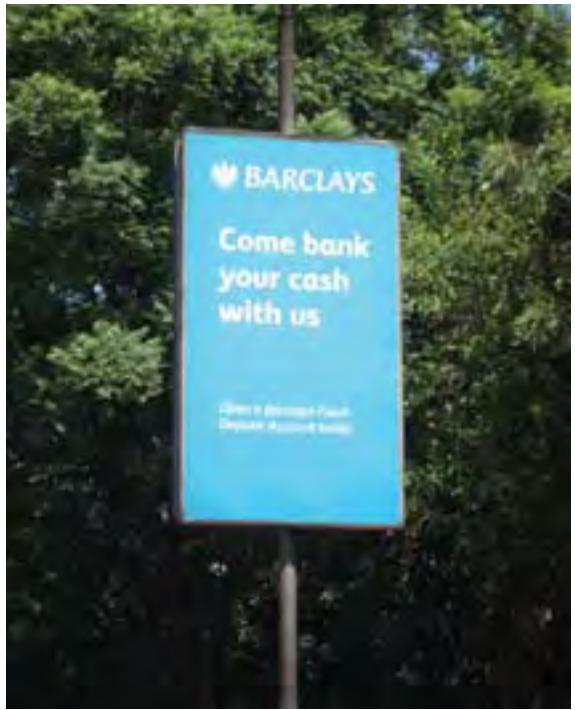
In the second situation, a bank needs to be able to perform ongoing due diligence into transactions performed through its accounts, and in some cases this might mean enquiring about the beneficial ownership of an account at a bank in another jurisdiction into which it is transferring funds. If banking secrecy laws prevent it gathering this information, then they are impeding the due diligence process.

**8. Each jurisdiction should, as a condition of membership of FATF or one of its regional bodies, publish information annually detailing the number of requests for cross-border legal assistance in financial investigations that it has received, specified by the country of origin, the type of offence to which the investigation relates, the total amount of funds involved for each country making a request, and the proportion of these requests that it has been able to fulfil.**

While jurisdictions are currently able to claim publicly that they are responsive to requests for assistance in assembling evidence or tracing assets that have entered the financial system, a significant volume of anecdotal evidence suggests there are many obstacles in the way of those states that wish to prosecute cases or recover assets. A significant step towards encouraging countries to respond more effectively to requests would be mandatory transparency over the number of requests that they receive and the number that they fulfil.

**9. Banks wishing to handle transactions involving natural resource revenues should be required to have adequate information to ensure that the funds are not being diverted from government purposes. In cases where no such**

Barclays sign, Kenya.  
Banks need to be  
careful who they  
take money from.  
*Credit: Global Witness*



### **information exists, they should not be permitted to perform the transaction.**

The ability to account transparently for natural resource revenues provides a very clear indication of governance standards and the level of corruption in a country. This recognition needs to be incorporated into the way banks make their own decisions about where to do business. The IMF's *Guide to Resource Revenue Transparency* is a useful – albeit voluntary – benchmarking of standards for transparency of revenues from natural resources as well as transparency of bidding, licensing and contract procedures , which the IMF should consider incorporating as a mandatory standard for assessment into its Article IV Consultations and Reports on Observance of Standards and Codes.<sup>407</sup> Where international financial institutions have expressed concerns about a country's failure to account for its natural resource revenues, FATF should issue clear guidance and warnings to banks.

**10. Banks should be required to publish details of loans they make to sovereign governments or state owned companies (including fees and charges), as well as central bank accounts that they hold for other countries so that the populations of those countries know how much money their government is borrowing in their name, and where their nation's wealth is being held. Proposed loans should be**

**published in a timely fashion so that the parliament of the recipient country has an opportunity to scrutinise the deal. Banks should also be required to transparently verify use of the loans they make to governments and state-owned companies, and when they loan to state-owned companies that do not publish independently audited accounts, should be required to report publicly to their shareholders on how they have made their risk assessments.**

The general principle of transparency has been accepted, if by no means uniformly adopted in the natural resource sector with the Extractive Industries Transparency Initiative (EITI), and international financial institutions in some instances refusing to lend unless there is transparency over natural resource payments and budgets. Commercial banks should increase their transparency, and this should take the form of providing information about loans made to sovereign governments or state owned companies, as well as information about central bank accounts they hold for other countries.

Because many loan contracts currently include legally enforceable confidentiality clauses, the only way for transparency over loans to happen would be for governments to require banks to do it, with the details published in an open registry held by the IMF. (The IMF, World Bank and other multilateral lenders should also be subject to the same reporting requirements.) The same registry should also hold details of all official country lending.

**11. Banks should be required to develop procedures to recognise and avoid the proceeds of natural resources that are fuelling conflict, regardless of whether official sanctions have yet been applied.** There are certain commodities which are inherently at risk of being used to fund conflict, such as timber, diamonds, coltan, and oil. However, there are currently no rules in place covering transactions of this type treating them as high risk in the way that PEP transactions are treated as high risk. Too often sanctions are not applied for political reasons, so it entirely ineffective for banks to wait to act until sanctions have been imposed.

Such procedures would not only help banks to implement their existing anti-money laundering obligations, but would also enable

them to get ahead of the game with their human rights commitments, an arena in which voluntary standards are currently being developed and expanded by John Ruggie, the UN Special Representative on business and human rights, and which may ultimately result in hard regulation. FATF should assist this process by undertaking a ‘typologies’ exercise (its name for the studies into particular money laundering vulnerabilities that it produces) for conflict resources, with a view to issuing guidance and, if necessary, a new recommendation.

### C. Recommendations relating to particular cases

12. The IMF should find out and disclose the names of the commercial banks that are holding Equatorial Guinea's oil revenues and ensure that there is proper oversight of the funds held in them.
13. The French government should reopen the investigation into the French assets of foreign rulers that could not have been purchased with their official salaries.

14. Hong Kong should regulate trust and company service providers to ensure that they comply with the anti-money laundering regulations, and should make it a legal requirement to perform customer due diligence.

15. The Anguillan authorities should investigate the role of Orient Investments and Pacific Investments in setting up a corporate structure for Denis Christel Sassou Nguesso, if they have not done so already, and ensure that their officers pass an appropriate fit and proper person test to hold a corporate service provider licence.

16. The UK should take responsibility for ensuring that its Overseas Territories do not provide services that facilitate corruption.

17. Deutsche Bank should explain how its membership of the Global Compact was consistent with a relationship with Niyazov's Turkmenistan.



If banks cannot be sure they really know their customer, they should not take the money.  
Credit: Roy McMahon/Corbis

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# GLOSSARY

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**AML**

Anti-money laundering: a term usually used in the context of the regulatory regime designed to prevent and detect money laundering.

**Article IV consultation**

Annual review of a country's economy and governance performed by the IMF on all of its members.

**Arbitrage**

Arbitrage is the practice of taking advantage of different regulatory regimes to reduce costs and legal responsibilities.

**Compliance**

The functions and mechanisms in a financial institution that are responsible of ensuring that the institution meets its legal and regulatory obligations.

**Correspondent banking**

A correspondent bank is one which holds an account for another bank, allowing the second bank to provide services to its customers in a country in which it does not itself has a presence.

**Corruption Perceptions Index**

An annual ranking of the world's most corrupt countries published by the NGO Transparency International. It measures perceptions of corruption by 'expert and business surveys.' While a useful indication of the amount of corruption in its traditionally perceived form, ie bribery, it does not systematically measure countries' contributions to corruption through lack of transparency and insufficient anti-money laundering

provisions in their financial sectors.

**CFT**

Combating the financing of terrorism: a term usually used in the context of the regulatory regime designed to prevent and detect the transmission of funds intended to be used for terrorist activities.

**Due diligence**

In the context of the anti-money laundering regulations, the research a financial institution is required to do into the identity of their customer and their source of funds.

**EBRD**

European Bank for Reconstruction and Development.

**EITI**

Extractive Industries Transparency Initiative, a multi-stakeholder coalition of governments, companies, civil society, investors and international institutions that sets a standard for governments to publish resource revenues and companies to publish resource payments.

**Equator Principles**

A voluntary initiative setting environmental and social standards for project financing, to which more than 60 banks have signed up.

**FATF**

Financial Action Task Force: an intergovernmental organisation that sets and monitors implementation of global anti-money laundering standards. The standard is embodied in the 40+9 Recommendations, which were last updated in 2003.

**FSRB**

FATF-style Regional Body. There are 9 of these regional organisations working towards implementation of the FATF 40+9 Recommendations among their members.

**IMF**

International Monetary Fund.

**Kleptocracy**

Literally, ‘rule by thieves’; a style of governance characterised by high level corruption and looting of state funds.

**KYC**

Know your customer: one of the cornerstones of the anti-money regulations is the requirement to ‘know your customer’ by verifying their identify and source of funds.

**LIBOR**

The London Inter-Bank Offered Rate is the most widely used benchmark for the rate at which banks lend money to each other.

**Legal arrangement**

In the context of the anti money laundering regulations, a legal structure such as a trust.

**Legal person**

An entity which is seen by the law as having a legal personality separate from the natural individuals who make it up, such as a company or association.

**Money laundering**

The process by which the proceeds of crime are disguised so that they can be used by the criminal without detection. There are usually three stages: placement, where the money is moved into the financial system; layering, where it is moved around through a series of financial transactions to break associations with its origins and make it harder to trace, and integration, where it is used again by the criminal once its origins and form have been disguised.

**Natural person**

The legal term for a real person, as opposed to an entity (such as an organisation or company) which in the eyes of the law could be treated separately from the real person or people behind it.

**OECD**

Organisation for Economic Cooperation and Development: a grouping of the world’s 30 richest economies.

**Offshore financial centre**

A community of bankers, accountants, lawyers and trust companies based in a secrecy jurisdiction that sell financial services to those non-residents wishing to take advantage of the regulatory structure and secrecy offered by that jurisdiction (see secrecy jurisdiction).

**PEP**

Politically Exposed Person: a public official, who by dint of their position could potentially have opportunities to appropriate public funds or take bribes; or their family members of close associates. The anti-money laundering regulations require that bank accounts belonging to PEPs or companies controlled by them should be subjected to extra scrutiny.

**Predicate offence**

The criminal offence which created the proceeds of crime which are being laundered.

**Private banking**

The provision of banking services to wealthy individuals and families.

**Project finance**

A form of financing in which the loan is repaid from the cash flow of the project that is being financed and is secured against the project’s assets; often used for infrastructure development.

**PWYP**

Publish What You Pay: a civil society coalition of over 300 NGOs worldwide, of which Global Witness was a founder member, calling for the mandatory disclosure of payments made by oil, gas and mining companies to all governments for the extraction of natural resources. The coalition also calls on resource-rich developing country governments to publish full details on resource revenues.

**Resource curse**

The phenomenon by which natural resource wealth results in poor standards of human development, bad governance, increased corruption and sometimes conflict.

**ROSC**

Report on Observance of Standards and Codes: detailed assessments carried out by the IMF and World Bank into a jurisdiction’s compliance with various standards for financial supervision, including fiscal transparency, banking supervision and anti-money laundering policies. ROSCs are voluntary. The ROSCs on anti-money

laundering, if they take place, can substitute for a FATF mutual evaluation and vice versa.

### **SAR**

Suspicious activity report: one of the cornerstones of the anti-money laundering regime, whereby financial institutions are required to submit reports detailing suspicious behaviour to their country's Financial Intelligence Unit (FIU) – the body mandated to gather them and pass on relevant intelligence to law enforcement.

### **Secrecy jurisdiction**

A jurisdiction that creates legislation that assists persons – real or legal – to avoid the regulatory obligations imposed on them in the place where they undertake the substance of their economic transactions (this is the definition put forward by the Tax Justice Network). The activities of those non-residents (different laws usually apply to residents) undertaking transactions in these jurisdictions are protected by secrecy provisions, often in law. These are not just banking secrecy, but also include allowing nominee directors and shareholders of companies, not requiring accounts to be published, or not cooperating with requests from other states, either by not holding information on trusts or by not having information exchange agreements. They usually offer low or negligible rates of tax.

### **Settlor**

A settlor is the individual who establishes a trust by transferring assets into it.

### **Shell company**

A company that does not perform any substantive business, but is used as a name for paper transactions in order to move money around.

### **Signature bonus**

An upfront payment made by an oil company to a government in return for rights to explore or exploit oil.

### **Trade finance**

Financing that enables companies to bridge the gap between the purchase and sale of a product; methods range from letters of credit through to complex loans syndicated by a large group of banks.

### **Ultimate beneficial owner**

The natural person who has a controlling interest over the funds in a bank account,

or over a company or legal entity. It is not necessarily the same person as the legal owner.

### **UNCAC**

United Nations Convention Against Corruption: the first global anti-corruption treaty, signed in 2003, came into force in 2005.

### **Vulture fund**

A pejorative term for debt traders who buy distressed debt from poor countries and then litigate to gain creditor judgments forcing repayment.

### **Wolfsberg Group**

A group of 11 global banks that have developed a voluntary set of standards on anti-money laundering, know your customer and counter terrorist financing.



# ENDNOTES

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- <sup>87</sup> FATF, *Summary of the Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: Spain*, 23 June 2006, pp10-11
- <sup>88</sup> IMF, *Luxembourg: Detailed Assessment of Observance of Standards and Codes – FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism*, December 2004, p41
- <sup>89</sup> Section 314 of the Patriot Act allows US banks to share information on suspected money laundering or terrorist financing. The banks are immune from prosecution for any information shared under this provision.
- <sup>90</sup> Minority staff of the permanent subcommittee on investigations of the US Senate, *Money Laundering and Foreign Corruption: Enforcement and Effectiveness of the Patriot Act Case Study Involving Riggs Bank*. 15 July 2004, pp55-56
- <sup>91</sup> 'Testimony of Jack Blum before the Committee on Finance, US Senate', 24 July 2008
- <sup>92</sup> Ibid, p56
- <sup>93</sup> A US-based bank has a correspondent relationship with any foreign bank for which it provides banking services. The preamble to the American secondary legislation implementing the Patriot Act states that: 'for purposes of this rule, foreign branches of U.S. banks will be treated as foreign banks.' Therefore any branch located outside the US of an American bank is considered to have a correspondent relationship with its parent US-based bank. Under US banking

- regulations, US-based branches of foreign banks, for example HSBC USA, are treated as US banks, and are therefore subject to the same regulation. Therefore HSBC USA has a correspondent relationship with its branch in Luxembourg. Federal Register, 71, Jan 4 2006, p 498; US. 31 CFR 103.11; 31 CFR 103.176
- <sup>94</sup> See the FATF website for the full recommendation, [www.fatf-gafi.org](http://www.fatf-gafi.org)
- <sup>95</sup> 31 USC 103.176
- <sup>96</sup> HSBC letter to Global Witness, 7 August 2008
- <sup>97</sup> Banco Santander did respond to a later letter that posed related questions, see page 35
- <sup>98</sup> IMF, *Luxembourg: Detailed Assessment of Observance of Standards and Codes – FATF Recommendations for Anti-Money Laundering and Combating the Financing of Terrorism*, October 2004, p35
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- <sup>100</sup> FATF, *Methodology for Assessing Compliance with the FATF 40 Recommendations and the FATF 9 Special Recommendations*, February 2008 version, para 4, p5
- <sup>101</sup> Article 9 (3) of OECD Convention, Article 46 (8) of UNCAC
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- <sup>103</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>104</sup> Sherpa, Survie, Fédération des Congolais de la Diaspora, *Plainte À Monsieur le Procureur de la République près le Tribunal de Grande Instance de Paris*, 27 March 2007
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- <sup>108</sup> Affidavit by Teodoro Nguema Obiang in the ex-parte application between Maseve Investments 7 (PTY) Ltd and the Government of the Republic of Equatorial Guinea, Teodoro Nguema Obiang, The Registrar of Deeds, Western Cape, and the Director-General of Foreign Affairs, Case no 1407/2006 in the High Court of South Africa (Cape Provincial Division), 8 August 2006
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- <sup>110</sup> Joseph Stiglitz, *Testimony to the House Financial Services Committee*, 22 May 2007, pp8-9
- <sup>111</sup> Letter from Barclays to Global Witness, 22 August 2008
- <sup>112</sup> See Wolfsberg Group website, [www.wolfsberg-principles.com](http://www.wolfsberg-principles.com)
- <sup>113</sup> This and the other euro equivalents in this chapter are the values cited in the police file
- <sup>114</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>115</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>116</sup> HSBC *Annual Report and Accounts*, 2000, p9
- <sup>117</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>118</sup> Letter from HSBC to Global Witness, 7 August 2008; letter from BNP Paribas to Global Witness, 29 August 2008
- <sup>119</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>120</sup> Shelby Super Cars press release, 'It's Official: SSC's Ultimate Aero Speed Record is Validated by Guinness World Records', 10 September 2007
- <sup>121</sup> One long-lasting insecticide-treated net costs \$5 or €3.53. These nets can reduce the number of children dying of malaria by 44 per cent. (Source: WHO major study in Kenya, <http://www.who.int/mediacentre/news/releases/2007/pr43/en/index.html>. Last accessed 22 September 2008). There are 241 000 under 18s in EG (Source: UNICEF fact sheets, [http://www.unicef.org/infobycountry/equatorialguinea\\_statistics.html](http://www.unicef.org/infobycountry/equatorialguinea_statistics.html). Last accessed 22 September 2008)
- <sup>122</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>123</sup> French police documents reviewed by Sherpa and Global Witness
- <sup>124</sup> Henri Astier, 'Sarkozy's Africa policy shift,' *BBC News*, 26 September 2007
- <sup>125</sup> Sherpa, Transparency International France, *Legal Complaint against African Heads of State for misappropriation of public assets (MPA): How can NGOs play a role in recovering stolen assets?*, December 2008
- <sup>126</sup> French police documents reviewed by Sherpa and Global Witness
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- <sup>136</sup> Letter from BNP Paribas to Global Witness, 29 August 2008
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- <sup>144</sup> International Monetary Fund, *Republic of Congo: Staff-Monitored Program*, 28 March 2008, Table 2, p20, dollar figure calculated from average CFA/\$ exchange rate for 2006
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- <sup>146</sup> High Court Approved Judgment, Mr Justice Stanley Burnton, between Long Beach Limited and Denis Christel Sassou Ngueso and Global Witness Limited, 15 August 2007, Case no HQ07X02371, paras 49-52
- <sup>147</sup> Company Information Sheet for Long Beach Ltd states that the company was incorporated on 3 March 2003, with ICS Secretaries Ltd listed as the company secretary. The address for Long Beach Ltd is stated as ICS Trust (Asia) Ltd's address at 8th Floor, Henley Building, 5 Queen's Road, Central, Hong Kong. ICS Trust (Asia) Ltd address confirmed in its listing in Hong Kong Companies House: Integrated Companies Registry Information System, accessed 11/10/2007. This also shows that ICS Trust (Asia) Ltd was itself incorporated in St Kitts and Nevis.
- <sup>148</sup> Company Information Sheet for Long Beach Ltd. According to evidence submitted to Hong Kong court proceedings, Orient and Pacific are both companies in the ICS group, and provide nominee services to clients. Paragraph 3 of 'Cotrade Asia' section of Annex to Mr Justice Carlson's judgment of 31 May 2007 in the High Court of the Hong Kong Special Administrative Region, between Kensington International Ltd and ICS Secretaries Limited, p24
- <sup>149</sup> Company information sheet for Long Beach Ltd
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