

INSTITUTIONAL INTEGRITY

THE INTER-AMERICAN DEVELOPMENT BANK

Established in 1959, the Inter-American Development Bank (IDB) supports efforts by Latin American and Caribbean countries to reduce poverty and inequality. We aim to bring about development in a sustainable, climate-friendly way.

We are the largest source of development financing for Latin America and the Caribbean, with a strong commitment to achieve measurable results, increased integrity, transparency and accountability. We have an evolving reform agenda that seeks to increase our development impact in the region.

As a development bank, we provide loans, grants, technical assistance, and conduct research. Our shareholders are 48 member countries, including 26 Latin American and Caribbean borrowing members, who have a majority ownership of the IDB. Our Fund for Special Operations provides concessional financing to our most vulnerable member countries.

Given our shareholder base and prudent management, we have a strong financial position. As a result, the IDB is able to borrow in international markets at competitive rates that benefit our clients.

The IDB Group is composed of the Inter-American Development Bank, the Inter-American Investment Corporation (IIC) and the Multilateral Investment Fund (MIF). The IIC focuses on support for small and medium-sized businesses, while the MIF promotes private sector growth through grants and investments, with an emphasis on microenterprise.

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

www.iadb.org

www.iic.int

www.iadb.org/mif

FROM THE PRESIDENT

In July 2010, the Board of Governors of the IDB approved the *Report on the Ninth General Increase in the Resources of the Inter-American Development Bank*, establishing the IDB's strategic priorities, institutional reforms and accountability for results which will pave the way for a \$70 billion increase of the IDB's ordinary capital, the largest expansion of resources in the IDB's history. The Ninth Replenishment will allow the IDB to increase its efforts to reduce poverty and inequality in the region, provide a higher level of support for small and vulnerable countries, and deliver an unprecedented level of support for Haiti.



The extensive reforms that have led up to this capital increase will not only make the IDB bigger, but, above all, better. The new Institutional Strategy and the agenda to improve efficiency, transparency and governance at the IDB will raise accountability to unprecedented levels, positioning the IDB to help promote growth and economic opportunity more effectively across the hemisphere.

Recognizing that the IDB Group can only succeed in its mission if it is grounded in integrity, we have implemented a series of modifications that have focused on the functions of the various bodies charged with oversight, sanctions and investigation to improve our capacity to ensure that IDB-financed activities are free of fraud and corruption.

As one of these mechanisms, the Office of Institutional Integrity continues to play a critical part in ensuring integrity in the activities the IDB Group finances. The investigation of fraud and corruption in IDB Group-financed activities ensures that the IDB Group's projects achieve the expected results for which they were designed in an environment free of corruption.

The Office of Institutional Integrity's investigative work is supplemented by prevention activities supporting both sovereign-guaranteed operations and those involving the private sector. This year, the Office devoted more resources to help the countries in our hemisphere promote their own corruption prevention and investigation mechanisms. In addition, the Office continued its efforts to harmonize anti-corruption policies with our peer organizations, thus ensuring that we work together as international agencies in the investigation and prevention of Prohibited Practices.

I extend my heartfelt gratitude to those who partner with us and assist us in our efforts to advance and promote integrity.

—Luis Alberto Moreno

OFFICE OF INSTITUTIONAL INTEGRITY

This was a year of change for the Office of Institutional Integrity. It marked my first year as head of the Office. My vision was to rebuild and restructure the Office to improve its quality, efficiency and effectiveness. The Office faced a number of challenges during this transition. Despite this challenging environment, the Office had a very productive year.

As an important first step, the Office OF Institutional Integrity increased the diversity of its staff and hired professionals with backgrounds and experience in public policy and the legal and investigative profession. For example, the Office hired six individuals all having advanced degrees. In addition, all investigators are or will be Certified Fraud Examiners, a credential that denotes expertise in fraud prevention, detection and deterrence.

The newly reorganized staff sharpened its focus on three key areas: investigation, prevention and outreach. We gave high priority to the implementation of the recommendations of the *Report Concerning the Anti-Corruption Framework of the Inter-American Development Bank*, an external review of the IDB's anti-corruption policies. The Office tackled a backlog of cases, reduced its pending caseload, and worked on improving internal processes to increase the efficiency of investigations. We intensified our efforts in the prevention area and worked with countries to assist them in identifying and addressing integrity risks. The Office continued its work in the private sector arena and worked with others in the IDB Group, including IIC and MIF, to complete the new *Guidelines on Integrity Due Diligence for Non-Sovereign Guaranteed Operations*.

Along with the IDB's Legal Department, the Office was a key player in the negotiations leading to the signing of a historic cross-debarment agreement between the IDB and four other multilateral development banks in 2010, wherein entities debarred by one bank will be debarred for the same misconduct by the other signatories. This agreement marks a milestone in the global fight against corruption and will make the IDB Group's sanctions overall more effective and impactful.

Our work in this upcoming year will focus on developing greater and stronger partnerships with our Country Offices, taking every opportunity to communicate with them, visit them, and ensure that we are responsive to their needs and concerns. In parallel, we will also forge stronger bonds with countries to partner in the fight against corruption more effectively. The Office will further its work in developing and implementing effective measures to detect and prevent fraud and corruption.

The Office of Institutional Integrity will continue to improve its efficiency and effectiveness in handling investigations. With a staff of able investigators and a new case triage system that is expected to be implemented in 2011, we will continue using our resources to process and complete investigations in a timely manner.

In sum, we plan to continue to expand the ways in which the Office serves as a resource to the IDB Group and to further its integrity mission. In so doing, the Office of Institutional Integrity will hold itself to the highest standards of integrity, professionalism and excellence.

We are grateful to those who support the IDB Group's integrity efforts.

—Brigida Benitez

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“Corruption weakens
democratic institutions,
and discourages
investment and job
creation.

Ultimately, it hits
hardest the poor and
those without access to
proper legal recourse.”

—Luis Alberto Moreno, IDB President

Introduction

Integrity is fundamental to the IDB Group's core purpose to promote development throughout Latin America and the Caribbean. Corruption undermines the central mission of the IDB Group. The Office of Institutional Integrity is a cornerstone in the IDB Group's efforts to detect and prevent corruption.

The Office of Institutional Integrity is a resource to the IDB Group and a partner in fulfilling its development mission. In the context of increased lending by the IDB Group, the relevance and importance of the Office's work remains paramount. The Office is an integral part in the fight against fraud and corruption on behalf of the IDB Group, for, in the absence of integrity, development efforts are hindered.

WHY
INTEGRITY?

SAFEGUARDING
DEVELOPMENT
WITH
INTEGRITY

THE OFFICE OF INSTITUTIONAL INTEGRITY'S PERFORMANCE IN 2010 AT A GLANCE

INVESTIGATION

- ➡ **Review** of 139 allegations and 105 consultations.
- ➡ **Completion** of 154 cases.
- ➡ **Sanctions** against six firms and 13 individuals, as well as 17 letters of reprimand, resulting from investigations conducted by the Office of Institutional Integrity.
- ➡ **Declaration**, for the first time, of misprocurement by the IDB based on the Office of Institutional Integrity's recommendation and its findings in an investigation into acts of fraud and collusion.

PREVENTION

- ➡ **Partnership** with four countries to conduct Integrity Risk Reviews.
- ➡ **Completion** of the new *Guidelines on Integrity Due Diligence for Non-Sovereign Guaranteed Operations*.

OUTREACH

- ➡ **Convened** the first meeting on Integrity and Due Diligence in Private Sector Activities, attended by 14 comparator institutions.
- ➡ **Participation** in discussions about anti-corruption alongside national law enforcement, international financial institutions, and control agencies in Latin America and globally.

THE OFFICE OF INSTITUTIONAL INTEGRITY MANDATE

The Office of Institutional Integrity, an independent office of the IDB Group, plays a key role in leading the IDB Group's integrity efforts. The Office **investigates** information in connection with Prohibited Practices in IDB Group-financed activities, conducts **prevention** activities designed to detect and prevent Prohibited Practices, and engages in **outreach** by developing training programs on integrity-related issues and providing support to the operational divisions within the IDB Group.

The IDB Group's integrity framework is based on three pillars (*See Fig. 1*). The work of the Office of Institutional Integrity touches on all three core concepts, although its key focus relates to the second pillar.

Figure 1: The Pillars of Institutional Integrity



OFFICE OF INSTITUTIONAL INTEGRITY'S TEAM WORKING TOWARDS INTEGRITY

Over the past year, the Office of Institutional Integrity has pursued a focused recruitment strategy to enhance staffing and build up internal knowledge. The Office has hired professionals who have distinguished themselves in the legal and investigative profession. The Office now has a total staff of professionals with extensive experience in investigations, auditing, public policy and related fields. This diverse team, which is almost 60% female, spans 11 different nationalities from member countries—representing Latin America, Europe and the United States.

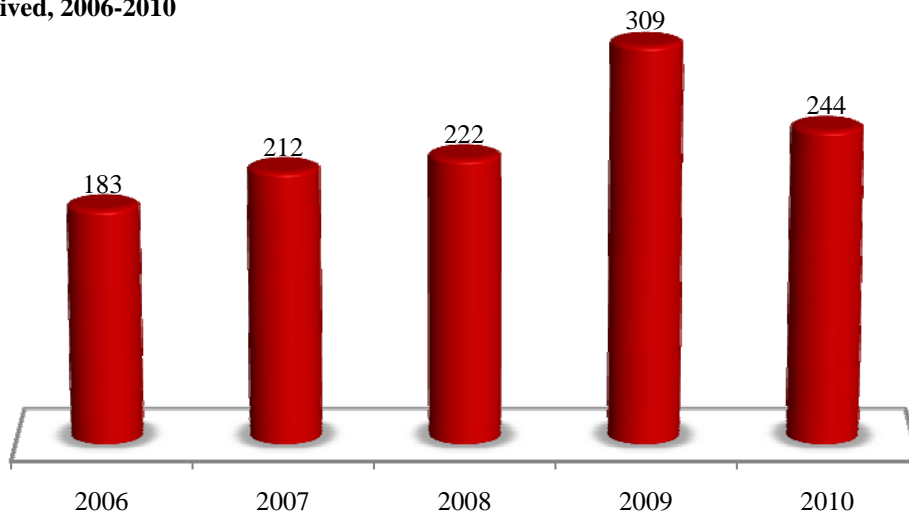
Investigation

In 2010, in terms of volume of resources, the IDB approved US\$12.7 billion, and the average annual level of approvals maintained its uptrend, moving from US\$6.2 billion (in the 2001–2005 period) to nearly US\$11 billion (for 2006–2010). Project disbursements were in the order of US\$10.9 billion. In terms of the number of operations, the IDB broke its historic 2009 record, approving 170 new projects, more than doubling the number of projects approved five years ago. The consultations and cases that the Office of Institutional Integrity receives arise in this context of a record number of operations and new projects.

CENTERED ON RESULTS

In 2010, the Office of Institutional Integrity received 244 inquiries (*See Fig. 2*), of which 139 were classified as allegations. The remaining 105 were consultations. The consultations came from IDB Group staff, clients, and the general public asking for advice on measures to prevent or mitigate risks of fraud or corruption, as well as requests for assistance with the interpretation of the IDB Group's anti-corruption policies. Of the 105 consultations, 41 concerned integrity issues in private sector/non-sovereign guaranteed operations.

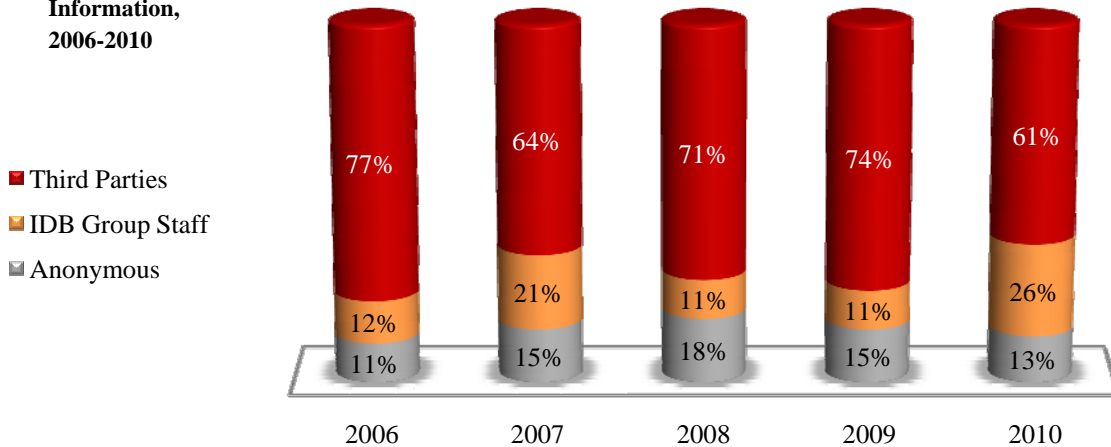
Figure 2
Total Inquiries
Received, 2006-2010



SOURCES OF INFORMATION

In 2010, as in past years, the sources of information continue to be mainly third parties, followed by IDB Group staff, and anonymous allegations (*See Fig. 3*).

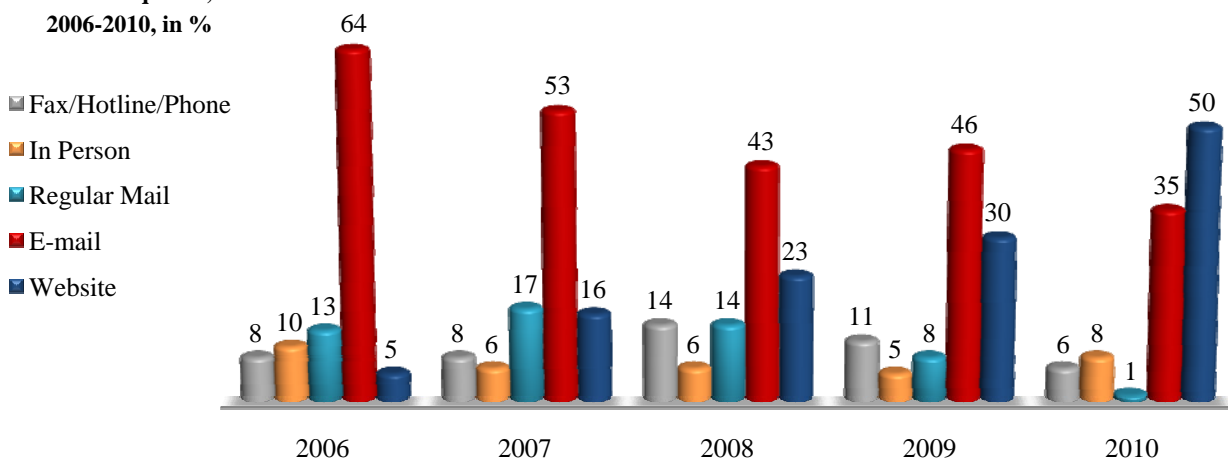
Figure 3
Sources of
Information,
2006-2010



REPORTING METHODS

The Office of Institutional Integrity offers several means to submit inquiries or allegations of Prohibited Practices. This includes e-mail, the website, postal mail, telephone, fax, hotline, and in person. Figure 4 provides a breakdown of the reporting mechanisms that have been utilized to submit inquiries over the past five years. In 2010, as in previous years, online (electronic) methods, and in particular the website, were the most commonly used methods to contact the Office: 85% of all allegations and consultations were submitted electronically.

Figure 4
Reporting Methods
of Inquiries,
2006-2010, in %



INVESTIGATIVE PROCESS

The Office of Institutional Integrity first reviews all new allegations and related information to determine whether it has jurisdiction to investigate the matter. Investigators determine what to do based on the following three criteria:

- 1) The allegation concerns an activity financed by the IDB Group.
- 2) The allegation concerns a potential violation of the IDB Group's Prohibited Practices (*See* Box 1).
- 3) The allegation provides sufficient credible information to warrant investigation.

If the allegation does not fulfill the three criteria listed above, the Office recommends to the Oversight Committee on Fraud and Corruption that the case be closed. Thirty-eight percent of all new allegations received in 2010 were closed at this initial stage. Of the new allegations that were closed, 15% did not involve an activity of the IDB Group, 36% did not concern a potential violation of the IDB's Prohibited Practices, and 13% did not provide sufficient information to investigate further.

Box 1 The IDB Group's Prohibited Practices¹

- (1) A ***corrupt practice*** is the offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence improperly the actions of another party.
- (2) A ***fraudulent practice*** is any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a party to obtain a financial or other benefit or to avoid an obligation.
- (3) A ***coercive practice*** is impairing or harming, or threatening to impair or harm, directly or indirectly, any party or the property of the party to improperly influence the actions of a party.
- (4) A ***collusive practice*** is an arrangement between two or more parties designed to achieve an improper purpose, including influencing improperly the actions of another party.

The remaining 36% were referrals to other units of the IDB Group or to other organizations. (*See* Table 1). For example, if an allegation involved staff misconduct, the matter was referred to and handled by the Ethics Office, pursuant to the Code of Ethics and Professional Conduct.

¹ In October 2009, the IDB's Board of Executive Directors endorsed ***obstructive practice*** as a fifth prohibited practice. This practice, along with the existing four others stated in the box above, may be reflected in upcoming proposed amendments to the IDB's procurement policies and would be implemented upon approval of those amendments by the Board.

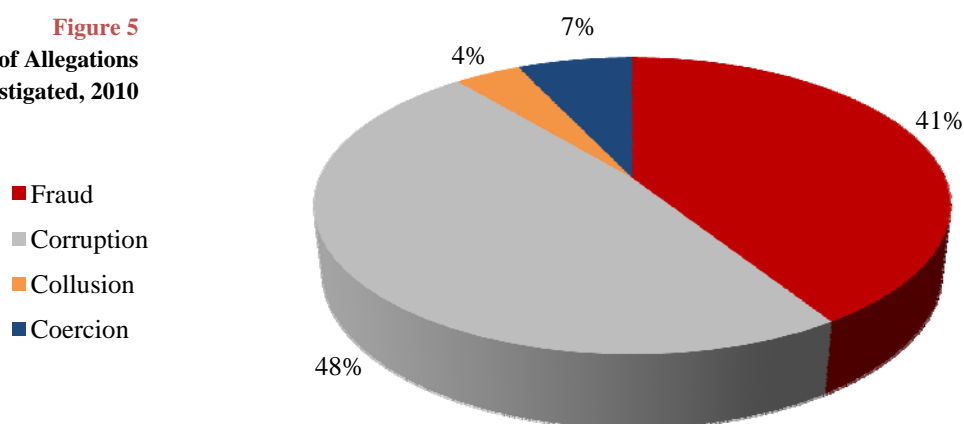
Table 1
Referrals

Total Referrals	19
Ethics Office	11
Operations Procurement Office	2
Information Technology Dept.	1
Human Resources Dept.	1
Legal Department	2
Other International Financial Institutions	1
National Authorities	1

If the three criteria discussed above are met, the Office of Institutional Integrity conducts an investigation. A closer look at the distribution of the new allegations according to violation type reveals that fraud and corruption are the most common cases, representing 89% of all new allegations. It is important to note that the Office bases its initial classification on the information contained in the allegation. Over the course of an investigation, and as more information about the case is gathered, the Office may modify its initial classification. Additional violations of Prohibited Practices may be uncovered during an investigation.

Figure 5 shows the types of allegations investigated in 2010.

Figure 5
Types of Allegations Investigated, 2010



COMPLETED INVESTIGATIONS AND OUTCOMES

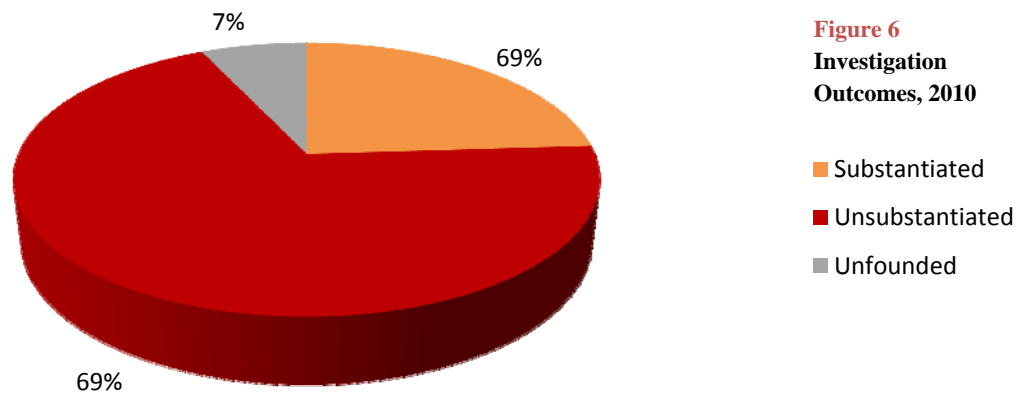
The Office of Institutional Integrity began 2010 with 80 pending cases, and opened 139 new cases over the year. At the same time, the Office completed 154 investigations (*See Table 2*).

Table 2
Case Flow, 2006-2010

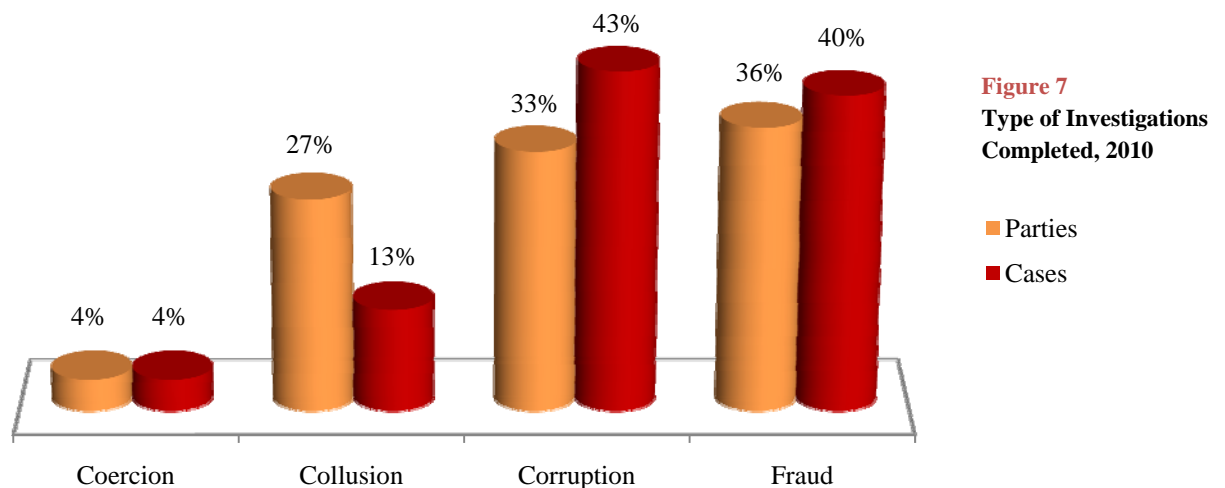
	2006	2007	2008	2009	2010
Cases pending from previous year	111	123	97	69	80
New cases	149	136	122	163	139
Total active cases	260	259	219	232	219
Cases completed	(137)	(162)	(150)	(152)	(154)
Cases pending at year's end	123	97	69	80	65

In 2010, the average age of the total active cases and of cases completed was approximately six months. The Office completed 70% of the total active cases. The oldest active case, which was closed during the year, had been open for approximately 3.2 years.

When the Office of Institutional Integrity substantiates an allegation against a firm or individual, it typically recommends to the Oversight Committee on Fraud and Corruption in a Notice of Administrative Action that the case be referred to the IDB Group's Sanctions Committee to initiate the sanctions process. In 2010, the Office submitted 95 investigations to the Oversight Committee on Fraud and Corruption. Of the investigations the Office completed during that period, it determined that 24% of the cases were substantiated (*See Fig. 6*). A case is substantiated when the evidence is sufficient to support a finding that the alleged Prohibited Practice occurred. A case is unsubstantiated when the evidence is insufficient either to confirm or deny that the alleged Prohibited Practice occurred. Cases are classified as unfounded when the evidence is sufficient to support a finding that the alleged Prohibited Practice is untrue.

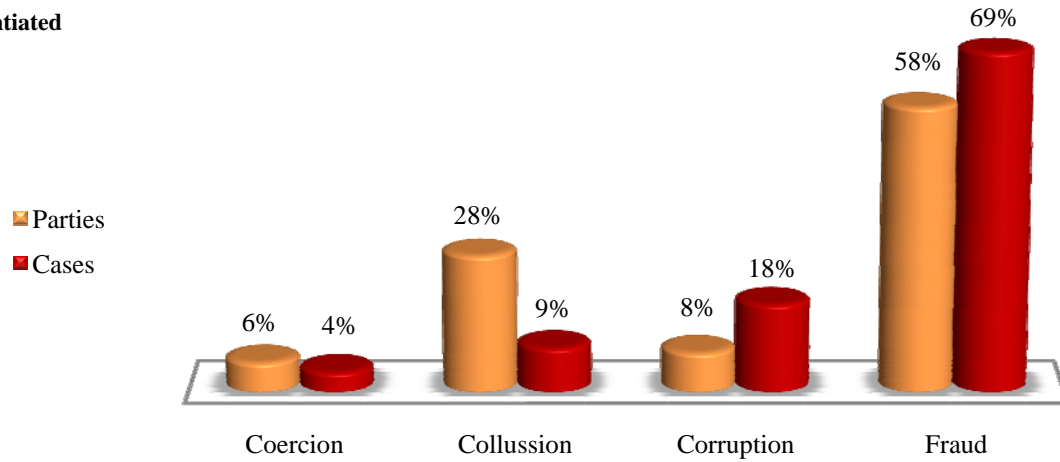


The majority of the completed cases involved investigations of fraud and corruption (*See Fig. 7*). This is consistent with the type of allegations received.



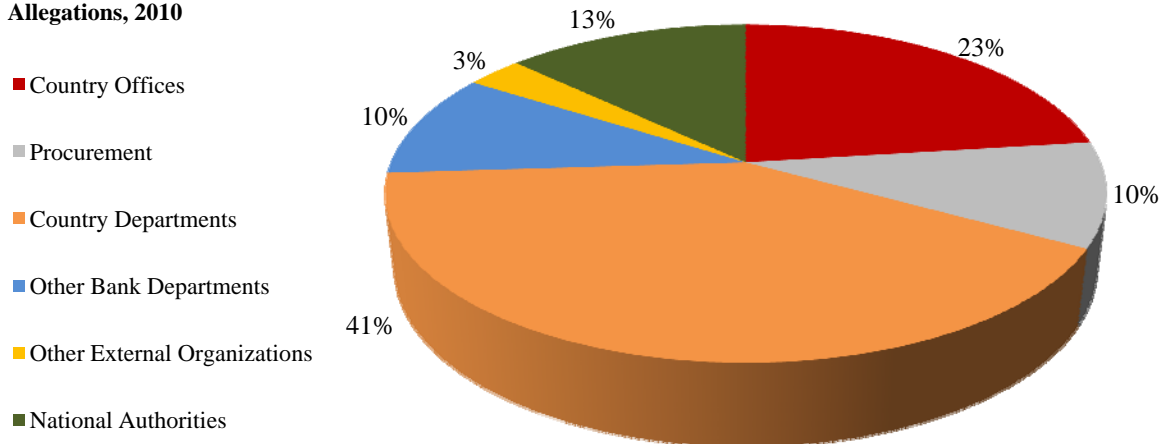
In 2010, 69% of the cases that were substantiated by the Office of Institutional Integrity involved investigations into acts of fraud, 18% can be classified as investigations of corruption, and 13% are cases related to collusion or coercion. Figure 8 shows the percentage of cases that the Office substantiated according to type of allegation and number of parties involved.

Figure 8
Type of Substantiated
Cases, 2010



In 2010, the Office referred 28% of the unfounded or unsubstantiated cases. Figure 9 shows to which IDB Group units or outside agencies the cases were referred.

Figure 9
Referrals for Unfounded
and Unsubstantiated
Allegations, 2010



SANCTIONS PROCESS

Pursuant to the IDB Group's Sanctions Procedures, after the Office of Institutional Integrity recommends to the Oversight Committee on Fraud and Corruption that a case be referred to the Sanctions Committee, an administrative process starts when the Notice of Administrative Action is delivered to the particular firm and/or individual allegedly involved in a Prohibited Practice. Respondents have two separate opportunities to reply to the Notice and the Office also has an opportunity to respond. Thereafter, the Sanctions Committee determines whether a sanctionable action has occurred, and, if so, what the appropriate sanction should be (*See Fig. 10*).



Figure 10
Sanctions Process

In 2010, the Sanctions Committee imposed a sanction or issued a letter of reprimand in 17 cases that the Office investigated. The Committee issued debarments against six firms and 13 individuals. Five firms and 12 individuals received letters of reprimand (*See Table 3*).

Type of Sanction	Length of sanction	Individuals	Firms
Letter of reprimand		12	5
Debarment	Permanent	2	2
	5 years	2	0
	4 years	0	0
	3 years	6	2
	2 years	0	0
	1 year	0	0
	6 months	3	2
Total		25	11

Table 3
Imposed Sanctions, 2010

The Office of Institutional Integrity investigations into allegations of Prohibited Practices that are not substantiated under the prevailing regulations may be documented in a Report of Investigation if the findings reveal important integrity risks or wrongdoing that should be shared with other units of the IDB Group and/or with national authorities. The Report of Investigation summarizes the findings of the investigation and typically contains recommendations on ways to mitigate integrity risks.

Reports of Investigation share lessons about important integrity risks.

EXTERNAL REVIEW OF THE IDB'S ANTI-CORRUPTION POLICIES

To ensure that the IDB maintained its leadership position on the issue of combating fraud and corruption, an independent external review of the IDB's capacity and mechanisms to detect fraud and corruption was conducted in 2008. This External Review (*Report Concerning the Anti-Corruption Framework of the Inter-American Development Bank*) was spearheaded by Richard Thornburgh and Jorge Santistevan de Noriega. The IDB's Board of Executive Directors approved an action plan proposed by Management to implement certain recommendations in the External Review. The Office of Institutional Integrity has focused its efforts on helping to implement the recommendations relevant to its work.

New Sanctions Process

Following the recommendations of the External Review, the IDB Group restructured its sanctions process and the new system is expected to be launched in 2011. To that end, the IDB Group created the position of a Case Officer to replace the Oversight Committee on Fraud and Corruption, which will become the new Anti-Corruption Policy Committee. The Case Officer will review the Office of Institutional Integrity's investigative findings and recommendations and may impose sanctions for wrongdoing, including a temporary suspension from participation in IDB Group-financed activities. The Case Officer's recommendations may be appealed to a new Sanctions Committee, which for the first time will include external members, as well as IDB Group staff. All seven Committee members will be appointed by the President. Individual cases will be adjudicated by three-member panels appointed by the Chairperson of the Sanctions Committee.

The Office of Institutional Integrity as an Independent Office

In 2010, upon the Board's approval, the Office was elevated to be an independent office within the IDB, with its Chief reporting to the IDB President. The Office has been tasked to lead the efforts to investigate fraud and corruption in IDB Group-financed activities and to assure the highest levels of integrity in the IDB Group's operations. The establishment of an independent office to perform these responsibilities reflects a recognition that this work is a priority of the IDB Group.

Voluntary Cooperation Program

The External Review identified the need to implement a voluntary self-reporting program. The voluntary cooperation program is a system that promotes the disclosure of wrongdoing and cooperation in investigating matters by employing means to encourage senior officials of an errant agency or corporation to reveal promptly their deviations from authorized practices, and to participate in stopping, or at least stemming, the potential for losses. The Office of Institutional Integrity

hired a firm to assist with the creation and implementation of a program for voluntary self-reporting of suspected fraud and corruption related to activities financed by the IDB Group. The Office will present its recommendation to the IDB President and to the Audit Committee of the Board of Executive Directors.

Case Selection Protocol

The External Review also identified the need for a case selection protocol, or triage mechanism, to facilitate the allocation of appropriate resources to investigate allegations. This would further assist the Office in its efforts to streamline its investigative process and handle allegations with greater efficiency and effectiveness. The Office contracted a firm that is assisting with the study, development, and implementation of a triage mechanism. The Office plans to present its recommendation to the IDB President and to the Audit Committee of the Board of Executive Directors.

ILLUSTRATIVE INVESTIGATIONS

In 2010, the Office of Institutional Integrity opened 139 cases for investigation. These cases varied in complexity, ranging from allegations of one-time fraud to complex and multi-jurisdictional matters in which several companies organized schemes that showed sophisticated forms of collusion.

The following section contains examples of investigations completed in 2010. These cases exemplify the Office's investigative process, experience, and commitment to investigating allegations of prohibited practices in IDB Group-financed activities.

CASE 1

Bid manipulation leads to declaration of misprocurement

The Office of Institutional Integrity investigated allegations of collusion and fraud during a procurement process for goods in a natural resource management project.

The Office found that the procurement process for several contracts had been manipulated in favor of one particular company. The analysis of the corresponding bidding documentation, witness interviews, and due diligence of the companies involved revealed several fabricated bids, bribes, fictitious companies, and simulated bid-reception and bid-invitation proceedings. Although the Office

found relevant evidence that the procurement processes had been manipulated, the evidence was not sufficient to determine which individuals were responsible for the fraudulent and collusive scheme. Therefore, the Office could not issue a Notice of Administrative Action and the IDB was unable to impose sanctions. Instead, the Office prepared a Report of Investigation identifying several risk factors that may have facilitated the occurrence of fraudulent practices. The Office recommended the IDB not to finance expenditures for goods and works which had not been procured in compliance with the agreed provisions in the loan contract and to declare misprocurement.

In 2010, the IDB followed the Office's recommendation to declare misprocurement and formally requested a reimbursement from the

Executing Agency. The Office worked closely with the IDB Operations Procurement Office and the project specialists in this matter.

IMPACT

Although the IDB's procurement guidelines specifically reserve the right to declare misprocurement if the IDB's "no objection" to the contract was based on incomplete, inaccurate, and misleading information furnished by the borrower, the decision to declare misprocurement on the grounds of an investigation marked a milestone in the IDB's efforts to enforce its integrity framework and promote accountability in its operations.

CASE 2

Conflict of interest highlights lessons for future due diligence

The Office of Institutional Integrity received an anonymous complaint relating to a significant multimillion dollar project being co-financed by several lenders. The complaint echoed press reports that a conflict of interest existed between the head of the Executing Agency and a winning bidder. Additionally, the complainant made other observations about deficiencies in the bidding process for the works in question.

The Office coordinated with other international financial institutions to examine the alleged conflict of interest and other components of the bid that had become the focus of public complaints surrounding this project.

The Office was able to obtain documents showing that the alleged conflict of interest had been properly neutralized prior to the tendering of the bid. It was observed, however, that several measures could have

been taken to avoid many of the integrity risks that accompanied this tender. For example, the Office obtained essential documentation of the relationship between members of the Executing Agency and the winning bidder, as well as important reports and communications surrounding the other alleged deficiencies in this bidding process. The Office also observed weaknesses in the anti-fraud and corruption provisions of this contract.

Accordingly, the Office of Institutional Integrity is using this case as an example of the due diligence procedures that could be employed to neutralize concerns over conflicts of interest. Also, because this matter highlighted typical conflicts of interest that can occur throughout the IDB's lending programs, the Office is recommending changes to procurement rules designed to minimize such conflicts. The Office is also coordinating with the other international financial institutions involved to support their efforts to potentially make similar

recommendations to their respective institutions.

CASE 3

Company fraudulently overbilled Executing Agency

When the IDB Group's funds are not used for the legitimate purposes for which they were designated, the project's beneficiaries suffer and the IDB Group's mission is thwarted. The misappropriation of IDB funds is a frequent fraud scheme and tends to occur during the execution phase of a project. A common practice is overbilling by submitting fraudulent invoices to the Executing Agency. Indeed, some companies cut corners to reduce their expenses at the cost of the project and the quality of the procured goods and services, yet they continue billing the Executing Agency for higher costs as if they were complying with their bid tender.

The Office of Institutional Integrity recently investigated such a case. The matter relates to a consultancy contract to supervise road works related to a program aimed at reducing transportation costs, time of travel for passengers and freight costs. The contract was worth over

US\$ 1 million. The allegation stated that a company was paying its workers lower salaries and providing them with fewer or none of the social benefits that it had committed to pay in the bid proposal.

At the same time, the company was billing the Executing Agency as if it had been paying the salaries and benefits stated in its proposal. The company also billed the Executing Agency for upward salary "adjustments" intended to compensate for cost-of-living increases; however, the professionals and technicians never received any salary adjustments.

After an investigation that included an analysis of a random sample of payment certificates the company submitted to the Executing Agency and a corroboration of the information contained in the company's original bid, the workers' receipts, and the company's payroll records, the Office prepared Notices of Administrative Action against two companies and two individuals, and recommended to the Oversight Committee on Fraud and Corruption that they be sanctioned for engaging in Prohibited Practices.

Prevention

PUBLIC SECTOR

The Office of Institutional Integrity uses lessons learned from investigations and draws from external sources to design and implement prevention tools. The Office developed the Integrity Risk Reviews and the Red Flags Matrix, two tools that assist operational and fiduciary units with strategic information to improve operation design and fiduciary activities.

Integrity Risk Reviews

An Integrity Risk Review (IRR) is a sector or country-specific risk analysis intended to reduce the likelihood of Prohibited Practices in IDB Group-financed activities. IRRs are typically requested by national authorities or by IDB's Country Departments, Sectors, and Country Offices.

The IRR is designed to provide strategic information and lessons learned that specialists may apply to IDB Group operations and fiduciary activities. They may be applied at the sector, country and/or regional level. The IRR draws from cases that the Office has investigated and matches this with state of the art research.

IDB Group internal sources include audit reports and interviews with IDB Group staff. External sources include reports from government oversight agencies, technical documents from other multilateral development banks, academic research papers, and interviews with key stakeholders.

This information forms the basis for the IRR, which results in two deliverables:

- 1) Training delivered to IDB Group staff, Executing Agencies, and representatives of the private sector, auditing firms and civil society. These trainings also serve as validation processes for the data collected, the lessons learned, and proposed recommendations.

The Office of Institutional Integrity's Prevention work uses information to deter prohibited practices and mitigate integrity and reputational risks in IDB Group-financed activities, and to improve IDB Group policies, procedures and mechanisms related to integrity and reputational risks.

2) A report that compiles all of the collected information, feedback from the trainings, and an action plan with recommendations to prevent the risks identified.

The Office of Institutional Integrity hopes to work with all of the Country Offices to conduct IRRs. At their request, the Office has thus far partnered with four countries:

Bolivia

The Office of Institutional Integrity continued working on an IRR for Bolivia that started in the fall of 2008. In April 2010, the Office delivered to the Bolivia Country Office a follow-up report based on the findings of the last mission. This report included detailed recommendations to mitigate the integrity risk identified. Based on this report, and at the request of the Country Office, the Office of Institutional Integrity conducted a mission to Bolivia in July 2010 to implement some of the recommendations. The mission included separate presentations for IDB Group staff, Executing Agencies, auditors, civil society organizations, and private sector firms. These presentations provided participants with information on the IDB Group's integrity policies, the investigative and adjudicatory mechanisms, and the available recourses to consult or present an allegation. The Office provided IDB Group staff with a special training session on falsification of documents, a practice observed in cases analyzed in Bolivia, and a training on the use of the Red Flags Matrix. The Office will conduct additional preventive activities with the Country Office in 2011.

Nicaragua

In 2009, the Office of Institutional Integrity started an IRR process for Nicaragua, at the request of the Governor for Nicaragua, the Ministry of Finance and Public Credit, the Comptroller General of the Republic, and the Nicaragua Country Office. In May 2010, the Office completed the IRR report, which included findings from the cases the Office had investigated in Nicaragua, feedback from the Office's previous mission to Managua, as well as integrity information from other sources. Based on this report, the Office worked with the Country Office to plan a new set of activities aimed at implementing the report's recommendations. To that end, the Office conducted a follow-up mission to Managua in December 2010 that included meetings with IDB Group staff, Executing Agencies, auditors, prosecutors, civil society, and private firms.

Paraguay

At the request of the Paraguayan Government, the Country Department for the Southern Cone and the Paraguay Country Office, the Office of Institutional Integrity prepared an IRR for Paraguay, which included a report and two training missions. Following up on these activities, in April 2010, the Office prepared a report based on the findings of the last training mission. The Country Office provided detailed comments and feedback on the report and the Office is working

with them on the agenda for the next mission, planned for early 2011, which will include specific training activities on the use of the Red Flags Matrix.

Peru

The Peru Country Office asked the Office of Institutional Integrity to conduct an IRR. In 2010, the Office began the analytical work by gathering and analyzing all relevant documentation. In addition to collecting and analyzing information, the IRR process includes conducting interviews with IDB Group staff and members of Executing Agencies, private sector firms, non-governmental organizations and public officials, among others.

In October 2010, the Office conducted a mission to Lima to present the preliminary results of the IRR. The presentations focused on the IDB Group's integrity framework, the context in Peru and case studies. The Office delivered a special training for project specialists on lessons learned from the most typical fraud matters that had been investigated in Peru. In addition, the Office made presentations to a wide range of audiences, including Executing Agencies, auditing firms, non-governmental organizations, civil society, and audit and investigative agencies.

Red Flags Matrix

The Red Flags Matrix is an interactive checklist jointly developed by the Office of Institutional Integrity and the Operations Procurement Office to assist fiduciary specialists in detecting and managing risks of fraud and corruption in project procurement. The Matrix, which is based on red flags identified in the Office's investigations and similar indicators used by peer institutions, is another preventive tool in the fight against fraud and corruption in IDB Group-financed activities.

The Matrix has been developed in the Procurement Plans Execution System (SEPA) and as a Stand Alone Program. Working with the Operations Procurement Office, the Office selected the countries and staff to participate in the pilot phase. The pilot successfully started in Argentina, Paraguay and Uruguay in SEPA, and as a Stand Alone in Bolivia. It is estimated that the pilot phase will last one year, with more countries gradually joining. The IDB's Knowledge and Learning Sector is supporting the preparation of case studies and other knowledge products related to this program.

In October and November 2010, the Office conducted a series of refresher training sessions with fiduciary specialists in Argentina, Paraguay and Uruguay. The Office of Institutional Integrity and the Operations Procurement Office are working with the specialists on consultations resulting from the use of the Red Flags Matrix.

PRIVATE SECTOR/ NON-SOVEREIGN GUARANTEED OPERATIONS

The Office of Institutional Integrity supports the IDB Group's private sector and non-sovereign guaranteed windows (NSG Windows)² with regard to integrity due diligence and related matters. Through this support, the Office seeks to minimize integrity and reputational risks in NSG operations. The support provided includes:

- Advising the NSG Windows how to conduct integrity due diligence.
- Providing guidance regarding the identification, assessment and mitigation of integrity and related reputational risks in specific operations.
- Working with NSG Windows and other internal stakeholders to improve the IDB Group policies and procedures that apply to integrity due diligence.
- Providing training to the staff of NSG Windows on integrity and related issues.
- Communicating with other multilateral development banks to maintain a harmonized approach and a level playing field for NSG Windows with regard to integrity and reputational risks.
- Advising IDB Group management on integrity and related issues.

Consultations and Advice

The Office of Institutional Integrity receives consultations from NSG Windows on a variety of integrity issues, ranging from questions about potential risk indicators in specific projects, to general inquiries regarding the application of IDB Group guidelines. The Office classifies such requests as “informal” and “formal” consultations. The Office responds to informal consultations by providing advice based on the facts as presented by the requesting NSG Window. If a Window requests a formal consultation, however, the Office requests a more thorough briefing on the underlying facts of an integrity issue, conducts additional due diligence, and prepares a detailed written analysis of the integrity and reputational risks related to the proposed operation. Such analysis usually recommends measures that could be taken to mitigate the risks encountered.

In 2010, the Office received 11 requests for formal consultations. During the same period, the Office regularly responded to informal consultations, which ranged from questions concerning particular operations to general inquiries about the conduct of integrity due diligence.

² The NSG Windows are the Inter-American Development Bank's Structured and Corporate Finance Department and Opportunities for the Majority Sector, as well as the Multilateral Investment Fund and the Inter-American Investment Corporation.

Participation in SCF and OMJ Project Approval Process

In January 2010, the Office of Institutional Integrity began participating in the eligibility and credit approval processes of two NSG Windows – Structured and Corporate Finance Department (SCF) and Opportunities for the Majority Sector (OMJ). Specifically, the Office participated in the eligibility review meetings and the quality and risk review meetings. By participating in these meetings, the Office has the opportunity to identify and resolve potential integrity issues in all SCF and OMJ projects prior to approval. In 2010, the Office provided comments in 82 such meetings. This constitutes a significant advance in the proactive treatment of integrity risk in SCF and OMJ projects.

The Office of Institutional Integrity uses its investigative, private sector, and other expertise to develop preventive tools to ensure integrity in all IDB Group-financed activities.

New Guidelines and Procedures Approved

In October, 2010, the IDB approved new *Guidelines on Integrity Due Diligence for Non-Sovereign Guaranteed Operations*, which became effective on December 1, 2010. These Guidelines replace the previous integrity guidelines and clarify the integrity due diligence requirements applicable to private sector and non-sovereign guaranteed operations. They also clarify the role of the Office of Institutional Integrity in supporting the integrity due diligence process. The Guidelines are the result of a working group process that was chaired by the Vice Presidency for Private Sector and Non-Sovereign Guaranteed Operations and included the participation of all NSG Windows, the Office of Institutional Integrity, and the Legal Department. The Guidelines were drafted primarily by the Office, following a plan agreed by the working group.

Pursuant to that plan, the Office also drafted Model Integrity Due Diligence Procedures to assist NSG Windows to change their procedures as required by the new Guidelines. These Procedures are intended to evolve, and the Office is working with NSG Windows to tailor the Model Procedures to each NSG Window's circumstances. The Office is also working to streamline integrity due diligence processes, including contracting with a service to provide continuous updating of electronic due diligence searches.

Outreach

TRAINING

A sound prevention strategy requires that staff members, borrowers and third parties receiving IDB Group funding are aware of the prevailing integrity standards and that they have the option to request advice and support to fulfill these standards. The Office of Institutional Integrity's outreach activities are key to gain the support of, and work in partnership with, key stakeholders to fulfill the mission of the IDB Group.

The Office of Institutional Integrity, in conjunction with the IDB's Knowledge and Learning Sector, is designing two knowledge tools, one instructor-led and the other interactive, for the Training Program on Integrity Risk and the Red Flags Matrix. The objective of these tools is to educate IDB Group staff on integrity risk in IDB Group-financed projects and reduce the likelihood of Prohibited Practices. The Integrity Risk training is approaching completion and its pilot phase is expected to begin shortly. These interactive tools will be developed in both Spanish and English and will include evaluation tests.

Throughout the year, the Office also provided training and presentations to a number of groups within the IDB Group, including Country Representatives, new hires and members of the Independent Consultation and Investigation Mechanism.

SUPPORT TO OPERATIONAL DIVISIONS

Upon request of operational divisions, the Office of Institutional Integrity provides assistance to enhance their ability to prevent, identify and mitigate integrity risks. The Office also provides general advice to operations with anti-corruption and integrity components.

At the request of the IDB's Social Protection and Health Division, for example, the Office wrote a report identifying integrity risks in a health project in Guatemala. This report served the project team as input during the preparation phase while elaborating the risk matrix for the project.

At the request of the IDB's Institutional Capacity of State Sector, the Office provided advice to the project team responsible for "Strengthening Civil Society Capacity to Monitor Compliance with Anticorruption Conventions."

The Office also provided advice to the IIC on the development of integrity components for FINPYME, a mechanism to diagnose small and medium-sized enterprises (SMEs) and help them gain access to

medium and long-term financing. More recently, the Office provided advice to IIC's program to foster and promote integrity and transparency within SMEs in the region. This commitment is the result of Memoranda of Understanding between the IDB and the World Economic Forum on spreading Partnering Against Corruption Initiative principles.

In conjunction with the new *Guidelines on Integrity Due Diligence for Non-Sovereign Guaranteed Operations*, the Office will expand its existing training program and outreach to the NSG Windows. In 2010, the Office provided four trainings on integrity due diligence and related topics, in response to requests from NSG Windows. In 2011, the Office will provide more frequent and varied training to NSG Windows. These trainings and other communications intend to ensure that investment officers have a clear understanding of the new due diligence requirements, and to assist the different NSG Windows in taking a consistent approach on matters of integrity and reputational risk.

ADVISING MANAGEMENT

Throughout the year, the Office of Institutional Integrity worked with the NSG Windows and the Legal Department to advise management on various matters, including offshore financial centers and anti-money laundering issues. The Office is taking the lead in developing a revised approach to the use of offshore financial centers in non-sovereign guaranteed operations.

IMPROVEMENT OF FIDUCIARY MECHANISMS

The Office of Institutional Integrity is part of the working group led by the Vice Presidency for Finance and Administration, which is working to implement a Centralized Ineligible List System. The system will prevent the IDB Group from hiring firms and individuals ineligible to receive IDB Group financing. It is expected that the system will become active in the first quarter of 2011.

COLLABORATION WITH OTHER MULTILATERAL DEVELOPMENT BANKS

The Office of Institutional Integrity continued to work closely and collaborate with the heads of integrity offices in other multilateral development banks (MDBs) and international financial institutions. The Office participated in regular meetings with these entities to discuss best practices and to harmonize our procedures.

In January 2010, the Office hosted a meeting of compliance and legal officials from 14 multilateral investment banks. The focus of this first annual meeting was to discuss opportunities to harmonize approaches in the management of integrity risk in private sector and non-sovereign guaranteed operations. Such efforts support the

“Cross-sanctioning combined with greater information sharing and coordinated investigations, should allow our institutions to more robustly prevent, detect, and deter corruption.”

**-Luis Alberto Moreno,
IDB President**

operations of the IDB Group by working to ensure a level playing field among MDBs with regard to integrity and reputational risk. The Office is currently working to organize the 2011 meeting.

On April 9, 2010, five leading MDBs, including the IDB, signed a landmark agreement to cross-debar firms and individuals found to have engaged in wrongdoing in MDB-financed activities. The agreement, which applies to debarments that exceed one year, was entered into by the IDB, along with the African Development Bank Group, the Asian Development Bank, the European Bank for Reconstruction and Development, and the World Bank Group. The IDB is currently in the process of implementing procedures so that cross-debarment becomes operational.

In September 2010, the Office hosted a delegation from the African Development Bank, which recently established an independent Integrity and Anti-Corruption Department. The African Development Bank visited the IDB Group to learn about the Office’s investigative procedures and the IDB Group’s sanctions process.

Glossary

Allegation: Inquiry related to misconduct.

Case: Processing of the information related to Prohibited Practices in IDB Group-financed activities, from allegation stage through its conclusion.

Consultation: Inquiry pertaining to integrity issues.

Inquiry: Information received by the Office of Institutional Integrity, which upon analysis may be classified as a consultation or an allegation.

Investigation: Examination of misconduct to determine whether the information known satisfies the threshold jurisdictional criteria, and if so, whether upon further investigation, it is substantiated, unsubstantiated or unfounded. Upon completion of an investigation, the Office of Institutional Integrity makes recommendations to the Oversight Committee on Fraud and Corruption. The Office of Institutional Integrity can recommend that a case be: (1) closed or (2) referred to the Sanctions Committee.

Substantiated: Case in which the evidence is sufficient to support a finding that the alleged Prohibited Practice occurred.

Unfounded: Case in which the evidence is sufficient to support a finding that the alleged Prohibited Practice is untrue.

Unsubstantiated: Case in which the evidence is insufficient either to confirm or deny that the alleged Prohibited Practice occurred.

Reporting Fraud and Corruption

Our investigations are primarily based on the allegations we receive; therefore, it is important that you take the initiative to report suspected acts of fraud or corruption. Fraud or corruption can be reported confidentially and securely through any of these options:

Phone:

Free International Phone Line
(877) 223-4551

Fax:

+ 1 (202) 312-4029

E-mail:

Allegations@idbfc.org
OII-Consult@iadb.org

Online:

<https://www.idbfc.org>

Mail or in person:

Inter-American Development Bank
Office of Institutional Integrity
Stop # B0680
1300 New York Avenue, N.W.
Washington, D.C. 20577, USA

**See
Something?
Say
Something!**

**What information should
I provide when reporting?**

We will be able to better follow up on your allegation if you give us as many details as possible, including the name of the project, the nature of the alleged wrongdoing, and documents that may be available to corroborate the allegation.

Remember to let us know how you can be reached for additional information or clarification.

The IDB Group's **Prohibited Practices** are listed on page 6.