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CORRUPTION: VIOLENT EXTREMISM, KLEPTOCRACY, AND THE DANGERS OF FAILING GOVERNANCE

UNITED STATES SENATE COMMITTEE ON FOREIGN RELATIONS

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Testimony of Gayle E. Smith
Administrator, U.S. Agency for International Development
Senate Foreign Relations Committee
Corruption: Violent Extremism, Kleptocracy, and the Dangers of Failing Governance
June 30, 2016

Chairman Corker, Ranking Member Cardin, and distinguished members of the Committee: thank you for inviting me here to discuss the United States Agency for International Development's work to combat corruption across the globe. I want to thank you for shining a light on this important topic, and for your continued leadership and ongoing commitment to root out corruption and advance accountability and transparency.

Corruption takes on many forms, from the bribery of public officials to collusion in public procurement to the wholesale theft of government assets. Although its different forms may cause varying degrees of harm, corruption as a whole tears at the fabric of society and hinders inclusive economic growth and democratic governance. Additionally, corruption poses major security risks to the United States, often enabling radicalization and violent extremism and fueling political instability and conflict. That is why President Obama views corruption as a fundamental obstacle to peace, prosperity, and human rights, and our Administration has sought to elevate anti-corruption efforts across our foreign policy and development agendas.

As the United States' lead development agency, USAID plays a critical role in the U.S. Government's strategy to stem the tide of corruption and hold to account all those who exploit the public trust for private gain. Our work takes us to every corner of the world, where we have seen firsthand the devastating impacts corruption can have on people, communities, and countries. But, encouragingly, we are also seeing new and promising trends on which to build.

Bolstered by the strong model of transparency and accountability the United States has constructed here at home, the fight against corruption has become increasingly central to our international development policy and strategy. As we continue to work with our partners to foster sustained and inclusive economic growth and promote open, effective, and democratic governance around the world, we are integrating anti-corruption efforts into the way the Agency does business – across borders and across sectors.

THE MANY COSTS OF CORRUPTION

For the countries where USAID works, the costs of corruption are significant and lasting. In some severe cases of systemic corruption, we have seen substantial portions of country budgets lost to waste, fraud, and abuse, stalling and in some cases halting development progress altogether. In total, according to the United Nations, corruption, bribery, theft, and tax evasion cost developing countries approximately \$1.26 trillion each year.

But the losses caused by corruption are not measured in dollars alone. We can also see the effects of corruption in missed opportunities for economic growth and development. Corruption lowers the confidence of the private sector in developing economies, hampering prospects for investment that can catalyze growth. Corruption siphons away scarce resources from public investments in much-needed social services and the productive sectors which fuel economic growth. It is worth noting that these opportunity costs are felt most acutely by the world's poor, who depend on those services and

stand to benefit the most from economic empowerment. Women, too, disproportionately suffer the impacts of corruption.

The costs of corruption are also evident in the eroding public confidence in government. Poor governance and corruption alienates publics in democracies and entrenched authoritarian regimes alike, as they see that a few people benefit from their connections while larger numbers of people are left out.

Additionally, systemic corruption fuels rising insecurity and enables dangerous transnational threats. The more corrupt an environment is, the easier it is for violent extremists to establish themselves as an alternative to ruling elites perceived to be immoral and unaccountable. Endemic corruption can also provide extremist groups with the enabling environment they need to access financial systems and align with criminal and other illicit networks.

EMERGING OPPORTUNITIES TO TACKLE CORRUPTION

Even as risks and threats posed by corruption continue to increase, we are seeing new windows of opportunity emerge. First, all across the world, there is growing popular demand for increased accountability and transparency from governments. It was a call to end corruption that helped spur the Tunisian revolution in 2010, and that same call drove hundreds of thousands of Ukrainians to the Maidan three years later. More recently the release of the Panama Papers turned the world's attention to illicit financial activity by the wealthy and well-connected on every continent, spurring massive protests and the Prime Minister's resignation in Iceland and sparking outrage and debate from North America to Asia.

In Guatemala last year, where impunity once reigned, people took to the streets and spurred the legal and orderly removal of the sitting President and Vice President. All over the world, civil society has intensified its demands for honest government and seeks to remove corrupt leaders from office through elections, impeachment, prosecutions, or civil protest. Second, we are seeing more – though still insufficient – top-down interest in reform, as leaders are increasingly demonstrating a willingness to put political capital in the fight against corruption. Some governments have shown they have the political will to build the institutions required to reduce and prevent corruption, increase transparency of public revenues and finances, and enhance accountability for budgeting and delivery of services. For example, Senegal passed a sweeping transparency law in 2012, and the Tunisian Minister of Finance is working directly with USAID to root out corruption in tax and customs collections. The leaders of Nigeria and Afghanistan – two countries historically plagued by severe corruption – have each made significant commitments to combat corruption and have followed up with concrete actions. In Nigeria, where corruption in the oil sector is especially pervasive, President Buhari's administration has undertaken a series of reforms aimed at reducing graft and improving transparency, including a restructuring of the state-owned Nigerian National Petroleum Corporation.

And in Afghanistan, President Ghani is personally invested in the fight against corruption. Along with Chief Executive Officer Abdullah and senior ministers, he established and chairs the National Procurement Commission, which meets weekly. His government has created a new High Council on Good Governance, Corruption, and Justice to coordinate anti-corruption efforts throughout the government and is also working to implement recommendations made by the Afghanistan Independent Joint Anti-Corruption Monitoring and Evaluation Committee (MEC). At the invitation

of the Afghan Ministry of Public Health, the MEC recently completed a comprehensive anti-corruption assessment, and the recommendations of that public report are under review for implementation. Other ministries have volunteered for similar corruption assessments.

In recent months, I have met with the leaders of Ukraine, Albania, Georgia, and Guatemala. In each of these meetings, these leaders raised corruption as a major concern, and asked for support in dealing with specific aspects of the challenge, ranging from technical assistance on customs reform to experts on transparent financial management. This kind of engagement is a necessary first step on the long road to ending corruption.

Finally, a global consensus is now emerging that transparency and accountability are pre-requisites for achieving sustained and inclusive development progress. It was not long ago that the United States was one of few governments consistently championing transparency and accountability, but that is no longer the case. This new global consensus is embodied in the Sustainable Development Goals (SDGs), which world leaders from 193 countries endorsed in September 2015. In part due to the hard work and engagement of the U.S. Government, the goals explicitly recognize – through Goal 16 – that corruption and related challenges hinder growth and progress. Importantly, the SDGs are more than just aspirational; they include targets against which governments – and their citizens – can measure progress. And growing multilateral partnerships like the Open Government Partnership are helping countries meet Goal 16 targets and pursue other governance reforms.

This global recognition has already translated into concrete commitments. In the Common African Position on the Post-2015 Development Agenda, African leaders affirmed their support for anti-corruption efforts and committed to adopting new measures to fight corruption and strengthen good governance. As another example of the global consensus at work, in May 2016 leaders of more than 40 governments gathered in London to commit to deepen and widen the fight against corruption through better coordination of government action, including efforts to advance beneficial ownership transparency, to increase revenue transparency in key sectors including energy, and to share know-how and data required to enforce laws against corruption and money laundering and to recover stolen assets

There is no question that the development, democratic governance, and security challenges posed by corruption have become more urgent and complex. But with increased citizen demand, growing commitment from leaders, and a shared global agenda, there is new and significant momentum behind U.S. efforts to attack corruption from all angles.

U.S. LEADERSHIP IN THE GLOBAL FIGHT AGAINST CORRUPTION

That is why – building on decades of U.S. leadership – President Obama has made fighting corruption a national security priority. The United States has been a leader in anti-corruption efforts since the *Foreign Corrupt Practices Act* (FCPA) – the first ever law prohibiting bribery of foreign officials – was enacted in 1977. Since then, U.S. Government agencies have developed a comprehensive, whole-of-government approach both to enforce the FCPA and other laws prohibiting corruption and to initiate policies and programs to institute good governance across the globe. In addition to USAID, those agencies include the Department of State, the Department of Justice, the Securities and Exchange Commission, the Department of the Treasury, the Department of Commerce, the Millennium Challenge Corporation, the Overseas Private Investment Corporation, the Trade and Development Agency, the United States Trade Representative, and others.

Each agency makes up a vital component of a comprehensive agenda that has helped make the United States the global standard-bearer in countering corruption both at home and across the globe. For example, the Treasury Department works to protect the U.S. financial system from abuse by illicit actors, including corrupt individuals. And the Department of Justice (DOJ) pursues corrupt foreign officials who plunder state coffers for personal gain and then try to place those funds within the U.S. financial system, while DOJ, the SEC, and their law enforcement partners pursue bribe paying individuals and companies over which the United States has jurisdiction.

The Overseas Private Investment Corporation and Trade and Development Agency seek to provide financial and technical support to countries that have consistently demonstrated progress in strengthening good governance. The Millennium Challenge Corporation incentivizes countries to demonstrate a positive track record and concrete plan to reduce corruption in order to achieve eligibility. The Department of Commerce, through commercial diplomacy and other initiatives abroad and in numerous international fora, promotes transparency and anti-corruption efforts in our trading partners in order to create a level playing field for U.S. businesses.

By engaging such a diverse array of agencies in anti-corruption work – each with different missions, authorities, and tools – the United States is able to attack corruption from every angle, including through building and enforcing the rule of law; enhancing the disclosure, detection, and prevention of corrupt practices; and engaging civil society, foreign governments, and multilateral institutions as partners. For USAID, U.S. global anti-corruption efforts also include the promotion of human rights, participatory democracy, accountable and transparent governance, and economic empowerment.

HOW USAID TACKLES CORRUPTION

USAID’s primary role within the U.S. strategy is to empower citizens, embed norms and standards, and build accountable and transparent institutions. With programs in more than 100 countries worldwide, we are uniquely positioned on the front lines of the fight against global corruption. By leveraging this position – as well as our existing relationships with governments and civil society – we work to address corruption at its roots. And, where we can enlist governments and their citizens as able and willing partners, we are increasing the scale and impact of anti-corruption efforts in the countries, regions, and sectors in which we operate.

This is essential. Unless people, communities, and countries take ownership of their challenges and their progress, development cannot be sustainable or inclusive. The same is true for efforts to combat corruption. Guided by this principle, USAID works to be a strategic and effective partner of civil society and governments. We do this by: (1) advancing accountability, (2) improving open, effective, and democratic governance, (3) strengthening adherence to international norms and standards, and (4) promoting multilateral efforts to tackle corruption.

Advancing accountability

The United States should hold governments, corporations, organizations, and individuals to account through enforcement measures and by other means. But from a development perspective, accountability is most effectively sustained when a vibrant civil society has the rights, capacity, and tools to hold governments, businesses, and citizens to account. Through our support for civil society,

USAID and our partners enhance the capacity of citizen watchdogs to oversee local public spending, promote community development and reconstruction, and monitor the delivery of services. The civil society groups we support also educate the public on their rights, and on the many different tools available to them.

For example, in Pakistan, USAID's Citizens' Voice Project (CVP) is supporting provincial governments to inform people about the Right to Information Act, a new law that grants citizens access to information previously withheld from the public. CVP has supported nearly 200 civil society groups to amplify citizen voices and facilitate productive engagement with the government. And in Paraguay, web-based programs developed to improve citizen oversight of government data helped unearth multiple cases of corruption. This exposure led to the firing of 1,000 ghost employees in the Ministry of Education who had been receiving salaries without actually working, and placed two members of Congress and the Chancellor of the National University under criminal investigation.

But the continuing backlash against civil society and closing of political space in countries across the globe compromises the ability of citizen groups to demand transparency and accountability. That's why we have joined our partners in the U.S. Government, governments around the world, the philanthropic community, and multilateral partners to push back against these emerging restrictions and dangerous trends. Through the President's *Stand With Civil Society* agenda, we work to improve the policy environment for civil society organizations, increase multilateral and diplomatic pressure against restrictive laws, and develop innovative ways to support civil society where it is under duress.

In some contexts, advancing accountability requires us to first help expose the nature and scope of corruption. This has the dual benefit of raising awareness among citizens and drawing the attention of prosecutorial and investigative bodies. One way we do this is through training investigative journalists and supporting high profile and high-impact reporting on corruption. In Fiscal Year 2015, USAID contributed approximately \$30 million to support media development in more than 25 countries. This relatively small amount of funding can eventually pay significant dividends in terms of transparency, asset recovery, and other law enforcement actions.

For example, USAID, along with the State Department, supported the Organized Crime and Corruption Reporting Project (OCCRP), a network of investigative journalists working across Europe and Eurasia. OCCRP's reporting has resulted in the recovery of at least \$600 million in hidden assets by tax authorities, as well as more than \$2.8 billion in fines, seizures, and asset freezes. Additionally, 1,300 companies were closed and 80 people arrested because of illegal activity exposed by the group.

USAID also works to enhance accountability by improving the auditing capacity within governments. In April 2016, we signed a Memorandum of Understanding with the Government Accountability Office's Center for Audit Excellence to collaborate on training and technical assistance efforts to strengthen auditing organizations in developing countries.

Going forward, USAID will continue to support citizens as they expose corruption and hold their leaders accountable.

Improving open, effective, and democratic governance

Fighting corruption is also central to our core strategic goal of supporting democracy, human rights, and governance. As we support citizens who are demanding change, and help build their capacity to

hold their governments accountable, we must also support governments as they work to strengthen their institutions and develop more efficient and effective systems – with built-in transparency. Our work to strengthen justice sectors offers a great example of this work. USAID is a global leader in the promotion of the rule of law, with a long history of joining with our interagency partners in supporting justice system reforms in every region of the world. This support includes a whole of government approach in developing training and professional development opportunities for judges and prosecutors, empowering them to take on corrupt officials and elites.

New technologies and innovations are accelerating our efforts. For example, we are installing computer automation to track cases in all 74 of Jordan’s courts to improve judicial efficiency, and in Honduras we supported the establishment of the country’s first Legal Assistance and Anti-Corruption Complaint Center. In Fiscal Year 2015, the Center tracked 65 formal corruption complaints, ultimately leading to 12 investigations.

Innovations and modernized systems are changing the way governments operate in other sectors as well. In vulnerable environments, we are leveraging programming in sectors like health and education to combat corruption. In countries with high vulnerability to corruption, we apply these innovative management systems in specific sectors like health and education, both to counter corruption and improve the delivery of services. To help governments collect revenues and budget more cost-effectively, we have helped implement standards of transparency and accountability for public financial management. And to help governments save costs, we have made great strides helping reform public procurement systems and institutionalize e-governance. These systems reduce opportunity for corrupt activity by limiting face-to-face interactions with public officials and automatically tracking all transactions.

For example, in Albania, we are supporting efforts to develop One-Stop Service Centers for all municipal transactions. These centers will help local governments be more responsive, while limiting room for corrupt practices. In some places, we are quickly seeing a sizable impact from these new systems. Less than five months after Ukraine introduced new electronic procurement software to cut down on opportunities for corruption, an estimated \$65 million has already been saved.

In 2002, Georgia had one of the worst reputations in the former Soviet Union for bribe-taking and corruption, with more than 4 out of 5 businesses reporting that they were expected to give gifts in meetings with tax officials. After the Rose Revolution and subsequent 2004 elections, USAID partnered with the new government in support of a major reorganization and other reforms of the tax and customs departments. By 2008, only 8.4 percent of businesses continued to complain about expectations of corruption by tax officials – an astounding drop of more than 80 percent. And from 2002 to 2011, Georgia increased tax revenue by about 12.6 percent of GDP.

Not only do improved systems save money and increase revenue, they also offer an opportunity for governments to reinvest those savings in the growth of their economies and in the well-being of their people. This can occur in any sector. After USAID supported an analysis of the central and individual hospital payroll systems in the Dominican Republic, the Ministry of Public Health took action to clean the payroll. In total, the Ministry eliminated more than 4,000 ghost workers, leading to a savings of \$9.5 million. And now, those savings are being used to hire health care workers and increase access to primary care across the country. The investments, along with the elimination of user fees and increased membership in national health insurance, are already paying off. One impoverished region witnessed a 500 percent increase in patient consultations over a one-year period.

As these kinds of successes continue to occur, more countries are likely to replicate the results, which will be necessary to achieve the scale we need. USAID will continue to build the evidence base for smart governance reforms across all of the sectors in which we work, just as we will continue to encourage the adoption of innovative systems and technologies.

Strengthening adherence to international norms and standards

USAID also has an important role to play in developing and embedding the international norms and standards that incentivize anti-corruption action. U.S. leadership has been essential in establishing and implementing the international legal frameworks that guide corruption enforcement today, such as the UN Convention Against Corruption (UNCAC) and the Organization for Economic Cooperation and Development Anti-Bribery Convention.

USAID has helped to establish a powerful and visible platform to strengthen international norms in the natural resources sector, a sector ripe for corrupt activity in many countries. The Extractive Industries Transparency Initiative (EITI) is a multi-stakeholder initiative to increase revenue transparency and create a new standard of accountability. With strong support from Congress, USAID has contributed more than \$26 million between Fiscal Year 2008 and Fiscal Year 2015 to support country-led efforts to join or implement EITI.

By lifting up governments that are publishing key financial information or audit results, we showcase how these actions foster growth and make countries more attractive to foreign investment. In Peru, for example, we helped bring together oil and mining companies, government officials, and prominent civil society organizations to foster a dialogue on the benefits of EITI membership. And in 2012, Peru became the first country in Latin America to become EITI compliant.

USAID has helped emerging democracies meet their obligations under a number of other international standards for transparency and accountability, including UNCAC. Additionally, it is important that jurisdictions effectively implement the Financial Action Task Force global standards on anti-money laundering and countering the financing of terrorism, which include standards for the disclosure of true beneficial ownership of companies. Moving forward, every USAID mission will outline plans to support country-level SDG implementation in its five-year strategy, which includes support for meeting good governance and anti-corruption targets like the significant reduction of illicit finance by 2030.

We will continue to promote the adoption and adherence to the international norms and standards that provide a guide for global cooperation on combating corruption.

Promoting multilateral efforts to tackle corruption

Similarly, we will continue to bring the global community together in the fight against corruption. In many of the countries where we work, multilateral support and engagement is essential to help build the capacity and incentivize the steps required to achieve scale in our anti-corruption work. USAID forges partnerships with other donors, multilateral agencies, and civil society organizations to help leverage and sustain local initiatives and to help enable the sharing of best practices and replication.

The Open Government Partnership (OGP) – a multilateral initiative launched by the United States and seven other governments in 2011 – is the most prominent example of this approach. With 70 countries now participating, OGP helps reform-minded officials and citizens promote transparency, engage, and harness new technologies to fight corruption and improve governance.

As a multilateral public platform, OGP has been effective in engaging the interest of governments in greater transparency, but that alone is not enough. That is why USAID supports efforts to help countries become eligible for the OGP, and assists member countries with the implementation of their National Action Plans. Once again, our efforts here are bolstered by U.S. leadership at home. The United States is also meeting its obligations under the OGP, including by submitting our own National Action Plan for civil society scrutiny. In addition to being good practice, this kind of leadership by example also gives us more credibility on the international stage. More than a dozen USAID missions plan to provide \$14 million to support OGP in Fiscal Year 2015 and \$10 million in Fiscal Year 2016.

OGP is a dynamic example of the preventive, positive and scalable USAID approach. Since its launch in 2011, it has grown quickly to include 70 countries and more than 2,000 commitments to undertake reforms jointly developed by government and citizens. Brazil, Croatia, and Sierra Leone all passed Access to Information Laws—some of which were stalled for years—in order to join the Partnership. Following the UK Anti-Corruption Summit in May, Nigeria became the latest country to join OGP and commit to fighting corruption at every level.

We have also supported multilateral engagement at the regional level. This approach has shown promise in strengthening the capabilities of internal government watchdogs, like inspectors general and other auditors. For example, the U.S.-Africa Partnership on Illicit Finance is designed to promote action to combat illicit finance in Africa.

Senegal has joined the United States in developing a national action plan, and six other nations are writing their own.

And in the Middle East and North Africa, which has the least transparent and open budget process in the world according to the 2015 Open Budget Survey, we are supporting several countries – including Algeria, Egypt, Iraq, Morocco, and Tunisia – to implement international standards and best practices for government audit and oversight. And through the Effective Institutions Platform, we are helping support a learning alliance of Latin American Supreme Audit Institutions, and highlighting ways these institutions can strengthen their work to target government corruption and financial mismanagement.

PROTECTING TAXPAYER RESOURCES FROM CORRUPTION

The last thing I want to touch on is how we are working to safeguard USAID investments from corruption. This is absolutely essential.

We continually look for new opportunities to improve our monitoring approach and attack the challenges from every angle. For example, in Afghanistan, one of the most difficult places we work, USAID developed a multi-tiered monitoring approach. The approach allows project managers to gather and analyze data from multiple sources, triangulate information to increase our confidence in the reporting, and use the results to make programmatic decisions. In Syria, innovative tracking mechanisms are used to ensure targeted beneficiaries receive assistance; these include biometrics

such as ID cards, finger prints, or iris scans; electronic distribution of transfers; distinct marking of paper vouchers; regular in-person and unannounced visits to beneficiary households, distribution sites, or vendor shops. And in some places plagued by corruption, terrorism, violent extremism, and conflict – where our investments face the greatest risks – we conduct vetting programs to keep American funds out of the hands of bad actors.

We have also developed new tools to assess the capabilities of partner governments and other recipients to properly administer funds. One such tool is the Public Financial Management Risk Assessment Framework, which has led to several decisions not to utilize host government systems because of insufficient controls. Other practices like fixed obligation grants can ensure that disbursements are only made against agreed-upon results. Additionally, since 2012 Congress has required the publication of annual reports on fiscal transparency of governments that receive aid from the United States, ensuring that U.S. taxpayer money is used appropriately. These reviews also serve to sustain a dialogue with governments focused on improving their fiscal performance.

Of course, USAID’s Inspector General is also essential to protecting taxpayer dollars and preventing fraud, waste, and abuse, and I want to thank the Committee for confirming Ann Calveresi-Barr to serve in this important role. USAID missions around the world greatly appreciate oversight from the Office of the Inspector General, often proactively requesting investigations.

The hard truth is that, even with the smart steps we have taken and careful measures we have put in place, we are sometimes vulnerable. USAID is called to serve in some of the most difficult environments imaginable, where access constraints often hinder our ability to ensure proper oversight of projects. Despite these constraints, we are committed to working closely with Congress to prevent corruption and other misuses of taxpayer dollars. And we are equally committed to taking swift action upon learning of any such abuse.

CONCLUSION

I want to thank you again for the opportunity to share with you the important work USAID is doing, as part of a larger U.S. whole-of-government strategy, to invest in the prevention and elimination of corruption worldwide. Our experience demonstrates that the most effective pathway to reaching scale is to help create compacts between citizens and governments that enable countries to institutionalize good governance, deliver social services efficiently and fairly and provide wide access to economic opportunity. Our leaders, staff and implementing partners will continue to prioritize and practice anti-corruption no matter which sector they work in.

Going forward, we will continue to make progress in infusing anti-corruption work into the bloodstream of the Agency, including through mission-led country strategies, our broader democracy and governance work, and through our sector-based programming in fields like global health and education. Further integration into the way we do business will be instrumental to implementing a comprehensive and successful long-term anti-corruption strategy. USAID shares this Committee’s deep commitment to the values of transparency and accountability, and we will continue to promote them through our work to advance human rights and dignity around the world.

Thank you.

**Testimony of
Assistant Secretary Tom Malinowski
Democracy, Human Rights and Labor Bureau**

**Senate Foreign Relations Committee
“Corruption: Violent Extremism, Kleptocracy, and the Dangers
of Failing Governance”
June 30, 2016**

Chairman Corker, Ranking Member Cardin and members of the Committee, thank you for this opportunity to testify on the corrosive effects of corruption and kleptocracy and our efforts to combat them. We are grateful to the Committee for bringing increased attention to this challenge.

During one of my first visits to Africa in this job, I met a group of refugees who had fled a terror-ridden country on account of insecurity. They were trained professionals who had found work in their host country and were grateful for refuge, but when I asked what their new life was like, they noted treatment at the hands of the local police as one of the key challenges they continued to face. They each noted that they had been arrested at some point and held at the police station until a relative or friend could pay a bribe to get them out. One joked that they called the police station the “people market.” Seeing as how they had fled terrorism, I asked whether they would call the police if someone they suspected of having terrorist links moved into their neighborhood. The group laughed, and one man replied: “Of course not. If we did that, either the police would arrest us again to get a bribe, or, if they arrested the terrorist, someone would bribe him out, and then he’d come to kill us.”

Mr. Chairman, I have heard some version of this story again and again in every corner of the world. I think it illustrates well the connection on which you have asked us to focus today—between corruption and violent extremism.

Success in the fight against violent extremism depends in part on maintaining trust between governments and the communities where violent extremists hide and seek recruits. It can come down to whether people in those communities will call the police when they suspect trouble—to offer information or to ask for help. Corruption destroys that trust. When the authorities are as likely to shake people down as they are to protect them, people sometimes end up fearing the authorities more than the violent extremists. And some will be susceptible to terrorist propaganda that promises to purify their societies of this scourge.

As Secretary Kerry has said, there is no greater cause of disillusionment or surer way to alienate citizens from the state than the “sense that the system is rigged against them and that people in positions of power are crooks who steal the future of their own people.” Terrorist groups from Nigeria to Iraq to Afghanistan have exploited such grievances to build support through promises of well-resourced, uncorrupt schools, hospitals, justice, security, and public services. And when these groups threaten the people and state, corruption inhibits the ability of the state to fight back. Where military and police promotions, equipment, and loyalties are sold to the highest bidder, security forces cannot fight effectively. When procurement systems are

exploited, weapons end up on the black market. And when border guards can be bribed, terrorists travel freely along with illicit arms flows and human trafficking.

Fighting corruption is thus critical to our security. It's equally important to our shared prosperity. U.S. companies are disadvantaged by corrupt markets abroad, where they lose contracts to competitors that are willing to pay bribes. The World Bank estimates that approximately \$1 trillion is paid every year in bribes by the private sector alone, enriching elites to the detriment of desperately needed public investments, from education to healthcare to food security.

Fighting corruption is also central to our promotion of human rights and democracy. I've long thought that corruption is the main organizing principle of the authoritarian states responsible for most human rights abuses, and most instability, in the world. The opportunity to profit from graft is the reason why many dictators seek and cling to power. Corruption gives them a means of purchasing loyalty—and a means of enforcing it, since everyone addicted to these ill-gotten gains has a stake in the regime's survival and anyone who breaks ranks can be selectively prosecuted.

At the same time—and here is where the opportunity lies—corruption can be an authoritarian government's greatest political vulnerability. Such governments can sometimes manufacture excuses for shooting demonstrators, arresting a critic, or censoring a newspaper but no cultural, patriotic, or national security argument can justify stealing. Anger over corruption helped inspire the uprisings of the Arab Spring. It is one of the central grievances of the movement to restore good governance to Venezuela. It is one reason why so many Africans don't want their leaders to stay in power for life. It is the cause around which the most effective opponents of Putinism in Russia rally. Dictators see this, and they are becoming increasingly ruthless in silencing those who tell the truth about corruption; some of the human rights activists we work hardest to protect are those threatened for reporting on bribery, kickbacks, and the movement of illicit funds across borders. But it is becoming harder and harder to hide corruption, and that is a ray of hope for those struggling for more democratic governance around the world, at a moment when such hope is greatly needed.

For all these reasons, the 2015 National Security Strategy included corruption as a global concern and likewise through the QDDR and other policies, Secretary Kerry has insisted that we treat corruption as a first order national security priority. With our colleagues at the White House, Treasury, Justice, and USAID, the State Department has made a concerted push to combat corruption. Our comprehensive, whole-of-government approach is committed to supporting government reformers and civil society actors who hold leaders and institutions accountable and to strengthening international norms against corruption. For example by promoting Goal 16 of the Sustainable Development Goals; and leading by example to further strengthen our own anti-corruption efforts by putting forward wide-ranging commitments at the UK Anti-Corruption Summit last month.

A Three-Pronged Approach:

Over the last several years, independent civil society-led investigations supported by the State Department's Bureau for Democracy, Rights, and Labor (DRL) and USAID have steadily worked to reveal instances of massive corruption involving foreign companies and foreign

officials in their communities, and to report on law enforcement actions taken abroad against such officials and those who would corrupt them. By exposing corrupt conduct at home, civil society has provided important leads to domestic and foreign law enforcement and increased the impact of successful criminal investigations. The Justice Department – and, increasingly, other law enforcement authorities around the world – have launched their own probes that have resulted in billions of dollars in fines being levied against bribe payers and millions of dollars in recoveries from foreign kleptocrats for the benefit of the people harmed by the abuse of public office.

For just a few million dollars in U.S. support for civil society, this approach represents a good return on investment and an important element of a broader, effective strategy to combat grand corruption.

That strategy begins by promoting greater transparency globally and domestically and supporting multilateral anti-corruption initiatives. Law enforcement investigations like those I described have become more successful in part because of reforms the United States has promoted through the G-20, the United Nations Convention Against Corruption, the Financial Action Task Force (FATF), the Extractive Industries Transparency Initiative, and other institutions to increase the transparency of banking transactions, company records, extractive industry payments to governments, and the assets of public officials. The Bureau for International Law and Narcotics' Anti-Corruption team is at negotiating tables around the world to ensure these standards are continuously strengthened. Greater transparency and accountability also empowers civil society to expose corruption affecting their own communities. In 2011, President Obama launched the Open Government Partnership with seven world leaders to encourage governments in partnership with civil society to advance transparency and accountability through national action plans for reform. Seventy countries now participate in the Partnership and are subject to independent review every two years. In addition to implementing our own action plan at home, the United States supports efforts to help other countries join OGP and assists with the implementation of their action plans. We are working to improve transparency in the extractive sectors by supporting the Extractive Industries Transparency Initiative globally and, under the leadership of the Department of the Interior, within the United States through a multi-stakeholder group that brings together companies, state and tribal governments, and civil society. The SEC's issuance this week of a final rule implementing Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act strengthens our credibility on corruption and transparency internationally.

Second, we need to support civil society-led investigations. Greater transparency leaves evidence of corruption hiding in plain sight, but someone still has to sort through the gigabytes of information that governments, companies, and financial institutions disclose each day to find it. Transnational networks of journalists and non-governmental organizations like those that have recently reported on notorious examples of kleptocracy can effectively advance this work through a combination of local knowledge and relationships with counterparts in other countries. Journalists and NGO networks are often the first to uncover illicit activity because they can deploy researchers in multiple countries at once, and because they tend to have anonymous sources who provide them with information, key documents, or road maps for how to obtain them. By exposing suspect conduct, journalists and NGOs have sparked further investigation by

law enforcement authorities or enabled financial institutions to better scrutinize the accounts of their clients.

Third, we need to support effective law enforcement. Ultimately, corruption is a crime committed by powerful people accustomed to impunity. While non-governmental networks can expose suspect activity, only governments can prosecute it. Furthermore, civil society often lacks the access to financial and other protected information available to law enforcement.

Wherever possible, we should invest in the capacity of governments with the will to be part of the solution, and this is a role that the State Department in particular, working in coordination and in conjunction with USAID and the Justice Department, can play. It is especially important that we coordinate and provide such support quickly to countries where reformers have come to power and have asked our help to strengthen institutions or to bring corrupt actors to justice and to recover their assets. A good example is Burma, where the success of a historic democratic transition will depend in part on whether the new government can get control of natural resource revenues that in the past have disappeared from public accounts. We are ramping up our support to the government and civil society to help. Kenya is another: a key outcome of President Obama's visit there was a joint commitment on good governance and anti-corruption in which our two countries promised to work together on everything from ethics training to procurement reform to police accountability. A third is Nigeria, where we are providing a variety of assistance to the government's Economic and Financial Crimes Commission and working to deepen our collaboration on asset recovery. We have many other opportunities to engage such governments in 2016—for example in Sri Lanka, Tunisia, Guatemala, Mozambique, and Burkina Faso.

And where governments lack the will to act, and funds connected to illicit activities touch the U.S. financial system, our own law enforcement institutions can play a key role. The Justice Department established a Kleptocracy Unit in 2010, which has taken on cases including the recovery of assets stolen by the late Nigerian Head of State Sani Abacha and his associates, to funds misappropriated by the Second Vice President of Equatorial Guinea Teodoro Nguema Obiang, and corrupt monies tied to the former head of the Department of Health and Social Security in Honduras. The Justice Department Fraud Section's Foreign Corrupt Practices Act Unit criminally prosecutes those individuals and companies over which the United States has jurisdiction who pay bribes to foreign corrupt officials. And the FBI recently established three International Corruption Squads to investigate and prosecute such foreign corruption. They could do even more with greater capacity and by strengthening legal authorities to combat kleptocracy.

Current Efforts

Across this range of efforts, there is more to be done.

For example, while we have done a great deal to promote financial transparency around the world, we still have work to do at home. When I ask human rights activists around the world how the United States can best help them, they often say something like: "We know you don't control what happens in Russia or the Congo, but you do control what happens in America. So please, at the very least, don't let those who profit from abuse of power in our country to hide their money in yours."

And yet, as you know Mr. Chairman, it is still possible for kleptocrats and those who seek to hide their wealth from around the world, and criminals of every other sort, to establish anonymously owned shell companies in the United States, and to use them to stash their illicitly acquired wealth in banks all over the world. That's why the Obama administration is proposing legislation to require all companies formed in the United States to identify their "beneficial ownership"—the actual human beings who own or control them—to the Department of the Treasury and make that information more readily available to law enforcement. There are few pieces of legislation that Congress can pass this year that will do more to advance the cause of global human rights and anti-corruption, and I hope Congress will act.

The successes of the Department of Justice's Kleptocracy Asset Recovery Initiative are mostly achieved through civil forfeiture actions. Preserving and strengthening that authority will be instrumental to the success of U.S. efforts to combat kleptocracy going forward. U.S. law enforcement could be strengthened through additional legislative steps to enhance the Department of Justice's ability to prevent bad actors from concealing and laundering illegal proceeds of transnational corruption and allow U.S. prosecutors to more effectively pursue such cases.

We can also do more to support the civil society groups that uncover evidence of corruption as more information about kleptocrats' finances becomes available. Efforts supported by DRL at the State Department have demonstrated the potential of this work. When a DRL-USAID funded investigative media organization uncovered a \$20 billion money laundering operation that funneled money from Russia through Moldovan courts to Latvia and the UK, a local investigation revealed that a Latvian bank was the destination for many of these funds. Latvian regulators asked the European Central Bank to revoke the bank's license, and it did. In Central America, two journalists we supported revealed the embezzlement of millions of dollars by the mayor of a Guatemalan town. The story was quickly picked up by several media organizations, eventually prompting an investigation that resulted in the now former mayor's disqualification from the 2015 elections. In Kyrgyzstan, when an investigative media story developed as part of a DRL grant revealed \$200,000 in funding embezzled by a local official, the resulting outcry prompted local law enforcement to launch an official investigation.

To build on this work, we announced at the UK Anti-Corruption Summit that State would establish a Global Consortium with USAID support to support the work of civil society and investigative journalists to uncover corruption. We will be making an initial investment in the Consortium, and hope that other governments as well as private foundations will contribute as well.

Asset recovery, essential to our international commitment to return stolen assets for the benefit of the people harmed by corruption, will be strengthened by the United States commitment to co-host in 2017 the first meeting of a Global Forum on Asset Recovery, a new mechanism to work collaboratively on major asset recovery cases where there is emergent need, modeled after the successful Ukraine and Arab Forums on Asset Recovery. With an initial focus on Nigeria, Sri Lanka, Tunisia, and Ukraine, this Forum will support law enforcement and civil society efforts in these countries while also providing a key way to reinforce the capacity of reform-minded governments with political will.

At the State Department, we can reinforce these efforts through responsible, effective implementation of the visa restriction for kleptocrats and by ensuring that U.S. foreign assistance discourages rather than inadvertently fuels corruption. In London, the United States committed to integrate anti-corruption into training for foreign security forces, ensure that our security assistance works to improve governance, and better assesses risk of corruption throughout our cooperation with foreign security forces. We are encouraged by the strong support of allies at the Department of Defense on these efforts and know there is more we can do.

CONCLUSION

Across all of these efforts, Congressional support will be vital to strong and effective follow through. None of this will be easy. Recent headlines have revealed the pervasiveness of global corruption and the deep web of laws, practice, and systems that will need to change—much bigger than any one law firm—to root it out. But this effort also reflects the growing capacity and will of those who demand accountability and expose the truth. We will not rid the world of dishonesty and greed, but we can realistically hope to empower willing reformers to set their countries on a new path, and to increase the likelihood that kleptocracy is exposed and punished—not just years after the fact but when the officials involved are still in power. And if we can make powerful leaders think twice before accepting a bribe or demanding a kickback or hiding their wealth in a shell company, if we can enforce the law at the highest levels and disrupt illicit supply chains, we strengthen our efforts to tackle the lower level corruption of police officers and petty civil servants that bedevils ordinary people, makes them more susceptible to violent extremism, and undermines democratic governance and security in so many countries.

Just as, over the last half century, the human rights movement took human rights from the periphery of international relations to a core policy concern—to ensure global security and the protection of universal values—our goal is to make anti-corruption a similar international priority today.

Thank you for the opportunity to testify today and for your partnership in the hard work ahead. I look forward to any questions.

Corruption: Violent Extremism, Kleptocracy, and the Dangers of Failing Governance

**Testimony of Carl Gershman
President, National Endowment for Democracy
Senate Foreign Relations Committee
June 30, 2016**

Mr. Chairman, thank you for the opportunity to testify before the Committee on the topic of corruption and kleptocracy. The Committee's strong voice on the corrosive impact of corruption is exceptionally important. I also want to thank you for your critical efforts to draw attention to the pervasive problem of government corruption and its implications for democratic governance and political stability.

Senator Cardin, I also would like to commend you for your leadership on the Sergei Magnitsky Act and the Global Magnitsky bill. The impact of the Sergei Magnitsky Act in spotlighting human rights abuses in Russia is visible in the tenacious - and brazen - efforts the Russian government has put into discrediting Sergei Magnitsky posthumously. A controversial film that was shown earlier this month in Washington – one that that a *Washington Post* editorial referred to as “agitprop” – offers a manipulated and evidently dishonest depiction of Sergei Magnitsky. This cynical effort, and others like it, aim to remove Magnitsky's name from your pending legislation. Why? Because the Magnitsky case and the sanctions that have been imposed on key human rights abusers as a result of the act passed in his name put a sorely-needed spotlight on Russia's dangerous kleptocratic regime. The Magnitsky Act holds such abusers to account in ways that beleaguered Russian institutions cannot, given the thorough removal of checks on power by the Putin regime.

It is important to stress at the outset that corruption is a pervasive problem in many societies and has the effect of undermining public confidence government institutions. The scourge of corruption is typically viewed as a symptom of a larger institutional problem. All countries, to one degree or another, suffer from corruption. Systems in which independent media, civil society, courts, and political opposition are weak or marginalized are particularly vulnerable because they do not possess the needed accountability and transparency to prevent corrupt practices from taking root. In kleptocracies, however, the challenge is much more acute.

In kleptocratic settings, corruption is at the heart of the problem and not chiefly a symptom of it. Karen Dawisha, the author of *Putin's Kleptocracy* and one of the foremost experts on this issue, makes the observation that “in kleptocracies risk is nationalized and rewards are privatized.” Participation in the spoils of kleptocracies is organized and controlled by top political elites, who raid state resources with immunity and impunity.

In kleptocracies, the instruments of the state are directed to shielding and enabling the corrupt activities of dominant power holders. Corruption is the lifeblood of these systems, like the one in present day Russia, and the glue for regime survival. Therefore, in kleptocratic systems where the stakes for power are all or nothing, whistleblowers who seek to expose corrupt practices themselves routinely become targets of law enforcement; investigative journalists and

oppositionists become enemies of the state; and independent businesses are brought to heel in order to preserve the kleptocratic order.

It needs to be emphasized that in the era of globalization, kleptocracy represents an exceedingly dangerous threat to democracy internationally. Corruption has generally been considered a problem that corrodes developing democracies from within. Well-resourced kleptocracies differ in that they project their sophisticated corrupt practices beyond national borders with an ever-increasing impact felt in new and established democracies alike. Kleptocracy has emerged a serious global threat. Parasitic at home, abroad kleptocratic regimes by their nature seek to exploit the vulnerabilities in the institutions of individual democratic states, as well as regional and global rules-based institutions. They use global financial institutions to invest and protect their money, and with their stolen resources, they buy influence in the democracies and neutralize political opposition. Kleptocracy has become a crucial pillar of the international resurgence of authoritarian countries.

For these reasons, and with support from the Congress, the National Endowment for Democracy is devoting special attention to the issue of kleptocracy as part of a dedicated, strategic response to a number of fundamental and inter-related challenges that characterize different aspects of the present crisis of democracy.

In addition to kleptocracy, NED will be focusing strategic attention on five key problems: the systematic assault by authoritarian regimes on international democratic norms and values; the failure of transition and effective governance in many countries where autocrats have fallen; the rise of Islamist and other forms of religious and sectarian extremism; the closing of civic space in scores of countries; and an information offensive by Russia and other authoritarian regimes that is influencing opinion and undermining the integrity of the information space in many regions.

While aspects of these problems have long been common to systems of absolute power, together they represent a more formidable and integrated threat to democracy than anything the world has experienced since the end of the Cold War. NED will continue to fund programs that support democracy efforts in specific countries, but it is also fashioning a new approach that consists of effective transnational responses to key strategic challenges. In doing so, it will be able to build on its record over more than three decades of addressing critical challenges to democracy, and to leverage the experience and expertise of its core institutes and many dedicated partners around the world.

COMBATING MODERN KLEPTOCRACY

Returning to the principal subject of today's hearing, I would like to reemphasize the serious threat posed by modern kleptocracy.

Until now, NED has supported anti-corruption, transparency, and accountability projects, but has not focused on the transnational impact and phenomenon of modern kleptocracies and their negative impact on democratic, norms, values, and institutions in democratic and democratizing countries.

I will stress several key points relating to the challenge posed by kleptocracy:

Kleptocracy is a global threat. The taking of money out of corrupt countries by kleptocrats is a long-standing practice – think of Mobutu Sese Seko’s Zaire and Ferdinand Marcos’ Philippines – but in the present hyper-globalized era the scale and sophistication of this activity presents new and serious challenges to democracy. In this sense, and as the Panama Papers so vividly reveal, modern kleptocracy thrives by crossing borders, in the process projecting a wider, corrosive threat to democracy and its institutions.

Kleptocracy is a key pillar of the global authoritarian resurgence that is visible in so many critical spheres. This includes in regional and international organizations, activities such as election monitoring and the autocrats’ treatment of civil society, as well as the projection of propaganda through lavishly funded international media enterprises, such as the Russian government’s RT. Simply put, these regimes are reshaping the rules of the game.

The challenge presented by regimes in Moscow, Beijing, and elsewhere is being taken to an entirely new level by virtue of their projection of illiberal values and standards beyond their own national borders. Just a decade ago, few political observers could even have imagined such a development. It’s especially troubling that this growth in authoritarian ambition is taking place at a time when malaise seems to grip the world’s leading democracies.

Kleptocracy Subverts Democracy. Kleptocrats exploit the benefits of globalization to enrich themselves, hollow out their own countries’ institutions, and subvert the democracies. Given these particular features, kleptocracy should be understood as an especially acute subset of corrupt systems. The issue of kleptocracy is an important one for activists who are working for democracy in countries ruled by hybrid and autocratic governments. Such activists are on the frontlines in the struggle against resurgent authoritarianism where regimes are tightening political controls and closing civic space. The activists who took to the Maidan in Ukraine sought to extract their country from the kleptocratic grip of former President Viktor Yanukovich.

Deeply entrenched corruption has been an extraordinary challenge since Ukraine achieved its independence a quarter century ago. But in the four years that he was in power, Yanukovich took the country’s corruption to new heights, enabling the theft of a vast amount of Ukraine’s public wealth. As the analyst Anders Aslund notes, nearly \$40 billion was estimated to have been stolen from the state while Yanukovich was in power. This massive corruption funneled wealth primarily to the president, his relatives, and a limited circle of businessmen around the president. This systematic corruption has ravaged Ukraine and has been central to its population’s determination to chart a more democratically accountable course.

As journalist Oliver Bullough observes: “In 1991, Ukraine’s GDP was about two-thirds of Poland’s GDP; now it is less than one quarter.” He notes that state corruption on such a scale has ruined Ukraine, “dooming a generation of Ukrainians to poor education, unsafe streets and blighted careers.” The responsibility for such massive theft does not lie with unscrupulous Ukrainians alone, however. There would not be corruption on such a vast and sophisticated scale without offshore centers like Panama. “If you steal money, you need somewhere to launder it;

otherwise it is useless.” This raises the important issue of Western enablers, a subject which I will return to shortly.

Azerbaijan has descended into an ever more repressive and kleptocratic form of governance. Journalists who seek to report on the extraordinary corruption of the country’s ruling elite end up in jail, or worse. Courageous Khadija Ismailiyova, who produced detailed investigative reporting linking the family of Azerbaijani President Ilham Aliyev to massive corrupt enterprises, was sent to prison on patently trumped up charges. She was released last month. As Gerald Knaus points out in a July 2015 *Journal of Democracy* issue titled “Europe and Azerbaijan: The End of Shame,” Azerbaijan’s kleptocracy has a profound and corrosive effect within but also beyond the country’s borders. Knaus explains in painful detail the ways in which the authorities in Azerbaijan “captured” the Council of Europe and in the process managed to neuter its human rights work.

In Angola, as journalists such as Rafael Marques de Morais have observed, the country’s political elite has taken control of virtually all of the country’s public wealth. Here, too, the Angolan kleptocrats do not simply deprive their own country of critically needed resources for improving health, education, and infrastructure, but use this wealth beyond national borders to acquire an influential hand in media and financial institutions inside EU member state Portugal. Russia’s kleptocracy has managed similar feats in Latvia, also an EU member state.

The fact that these authoritarian regimes are also kleptocratic makes the challenge facing democracy activists in such countries even more difficult. This is because the kleptocrats have been able to establish an objective alliance with banks and other institutions that make up the global financial system. These institutions readily receive the stolen funds after they have been laundered through various offshore structures. With these assets safely invested and protected within the global system, the kleptocrats can then use the stolen funds to increase their domination at home and to purchase influence abroad, all the while expanding their holdings and leverage in the West and buying extravagantly priced properties in London, New York, Miami, and other global capitals.

The problem of Western enablers. The purchase of multimillion dollar properties, the arrangement of opaque offshore financial instruments, and the laundering of a kleptocrat’s public image, do not happen by accident or on its own. Professional intermediaries in the established democracies are critical links for venal kleptocrats who seek to move ill-gotten gains from authoritarian systems into the democracies, where they can enjoy the rule of law. As journalist Bullough observes, “only with the help of Western enablers can a foreign kleptocrat transform the ownership of a questionable fortune, earned in an unstable country where jail is often one court decision away, into a respected philanthropist” who can be photographed alongside celebrated international figures and media stars.

Anne Applebaum has noted the irony that while the rule of law prevails in Britain, “over the past couple of decades, London’s accountants and lawyers have helped launder billions of dollars of stolen money through the British Virgin Islands, among other British overseas territories.” Their complicity in kleptocracy has corroded the legal integrity of the British system. As Bullough notes, “what Western enablers do is in a sense more egregious than what foreign kleptocrats do,

because in the West we have a genuine, institutionalized rule of law, while kleptocrats operate in systems where no real rules exist. The result is that Western enablers effectively undermine democracy in foreign countries, even as Western governments lecture those same countries about civil society and the rule of law.” A crucial element necessary for combating modern kleptocracy will be bringing the professional intermediaries in the West – the enablers – out of the shadows and into the sunlight.

Kleptocracy is an engine for extremism. Kleptocratic governments by their nature extinguish or prevent the emergence of institutions that can hold them accountable, leading to governance arrangements that feature unchecked power and impunity. This is the modus operandi of “rule by thieves.” Critically, kleptocratic regimes deny space for moderate political voices that could offer possible alternatives to existing policies and leaders. In the kleptocracies of Eurasia and the Middle East, for instance, this kind of harsh political marginalization, where virtually all moderate voices are targeted, opens the way for extremists. Azerbaijani scholar Altay Goyushov observes that by repressing peaceful activists and reformers in Azerbaijan, the kleptocratic regime in Baku “argues that it is taking steps to ensure stability. They have this exactly wrong. By eliminating moderate voices in society, Azerbaijan’s leaders set the stage for anti-Western environment that will serve as a breeding ground for extremists, who pose a grave security threat to both the region and the West.”

RESPONDING TO THE CHALLENGE

Because kleptocracy is a global challenge it requires a response that takes the transnational nature of this problem into account. To this end, NED is at the beginning stages of an effort to analyze the scope and key elements of this problem, while deepening linkages among existing country-level anti-kleptocracy initiatives and those working at the regional or international level. We will look to expand and strengthen existing anti-corruption efforts that address key components of kleptocratic systems and support efforts by civil society and journalists to challenge regimes, leaders and institutions that are perpetuating kleptocracy.

Ending the symbiotic relationship between kleptocrats and the international financial system will be a critical dimension of our efforts. In this regard, it will be important to support activists and investigative journalists who are working within kleptocratic countries to fight state theft and to help them connect with international actors who are trying to monitor the flow of illicit capital and block its investment in the international financial system. We must identify how grassroots activists and such international actors can find more effective ways of working with and supporting each other. Through such cooperation, we hope that the activists will find new allies and outlets for their investigative reports, while the international actors will gain useful contact with indigenous groups whose knowledge of the way funds are stolen might contribute to the development of laws and strategies to block the receipt of these funds by the global banking system.

Greater cooperation among people fighting kleptocracy at different levels might also help efforts to alert the publics in democratic countries to the serious security risks they face by allowing hostile autocracies to exploit their institutions and legal protections to aggrandize their own power. Just as it is urgently important to end the corrupting collaboration between the

kleptocrats and their enablers, it is equally important to build a new partnership between the activists fighting for the rule of law in kleptocratic countries and potential allies in the established democracies who are committed to the defense of democratic values. Building such a partnership will help protect our own interests and security and advance the cause of democracy at a moment when it is in peril around the world.

Thank you, again, for the opportunity to contribute this testimony.



CARNEGIE
ENDOWMENT FOR
INTERNATIONAL PEACE

Congressional Testimony

**CORRUPTION: VIOLENT EXTREMISM,
KLEPTOCRACY, AND THE DANGERS
OF FAILING GOVERNANCE**

Testimony by **Sarah Chayes**
Senior Associate,
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Testimony before the Senate Foreign Relations
Committee

June 30, 2016

I'd like to thank Chairman Corker for holding this important hearing. Just calling it has already had the salutary impact of challenging officials in the foreign policy and assistance communities to think through the implications of corruption for their operations. And my thanks also to Ranking Member Cardin for extending this invitation for me to testify today.

There is a growing recognition of the impact of corruption on the U.S. national interest. Signs of the rising awareness can be found in recent official statements. “From the Arab Spring to Latin America,” wrote U.S. Secretary of State John Kerry in May, “political turbulence has made clear that governments are unwise to shrug off their citizens’ growing concerns about corruption....It is long past time for the international community to treat corruption with the seriousness and attention it deserves.”¹

And yet, given the consequences of the type of sophisticated and systemic corruption that has taken widespread hold in the past quarter-century, especially its impact on global stability and the legitimacy of governments—and therefore on the U.S. national interest—the policy approaches to the problem remain disproportionately weak.

The issue of corruption should be central to foreign and international trade policy development and should inform the way U.S. assistance—military as well as civilian—is shaped. Members of Congress can provide important guidance to the executive branch to help make that happen.

The scope of global corruption:

Given the mesmerizing capacity of numbers to focus our imaginations these big-data days, it is tempting to seek a dollar figure to quantify the scale of corruption worldwide. By its nature, of course, that is a fraught proposition, given the incentives for the corrupt to conceal their deeds and the facilities the current globalized economy offers them for doing so.

The non-profit organization Global Financial Integrity, for example, uses strict methodologies to derive an estimate as to the quantity of money illicitly departing developing countries annually.² That number, however, leaves out cash transfers, whereas millions certainly³ and doubtless billions of physical dollars are shipped around by the criminal and the corrupt each year. It also mixes the proceeds of corruption with the proceeds of other sorts of criminality in its reckoning. And it misses all corruptly obtained money that is spent within the countries where it was looted.⁴

But even if it were possible to arrive at a fair estimate of the sum siphoned into the pockets of the corrupt each year, that would not constitute an adequate measure of the scope of the problem. At least as important as the monetary losses corruption inflicts on countries and their populations is the damage of a less material order.

When a policeman or a doctor or a registrar of deeds demands a pay-off, he or she doesn't do it politely. The shakedown is typically accompanied by arrogant contempt. The victims—like that young Tunisian who lit himself on fire in 2011, setting off the Arab Spring revolutions—suffer scalding humiliation alongside the theft of their scarce resources.

The injustice of the way the whole system functions compounds the injury. It's not as though everyone is poor side-by-side. When people have to walk past huge mansions with strings of electric lights burning day and night while the power is cut off to their part of town, or when they keep being forced to jump aside when a swish SUV splashes past them on a pitted street, and when they know the money to buy these things has been skimmed off of public works or development contracts—or has been extorted from people like them—the sense of personal injury grows. And with the expanding availability of information through the electronic media, such juxtapositions are on increasing display.

Especially galling to many victims of corruption is that the very officials to whom they might turn to report the abuses are the primary abusers themselves. As an indignant young Afghan man put it to me in 2009, referring to the police, “They’re supposed to be defending the law, and they’re the ones breaking it!”

Far from representing an accepted “part of the culture,” in other words, as so many Westerners surmise, corruption is experienced as a bitter betrayal by people I have interviewed in nearly a dozen countries on three continents, corroding their respect for their public institutions. They see their governments as a hostile force—against which, of course, there is no recourse. They and other victims are left either to suffer or rebel.

All too frequently, and contrary to conventional wisdom, corrupt practices can't be summed up as the venal behavior of a certain number of individuals. They represent a sophisticated set of operating procedures employed by a successful, if sometimes loosely structured or contentious, network. This is a final point to bear in mind when considering the “scope” of the problem. The street-level foot soldiers in these corruption syndicates—the cops or the clerks or the customs officials who shake down ordinary people—are passing part of their take up the line, just like rank-and-file members of the Mafia.

At the top, the syndicates typically bend parts of the government apparatus to serve their purposes, be it the tax authority, the justice sector, the legislature, or the ministry of energy and industry. Other agencies may pose a threat, or command a fat budget that can be pillaged. Such was the fate of the Iraqi and Nigerian militaries, both of which collapsed when challenged in 2014. Their platoons were filled with ghost soldiers who existed on paper only, their officers collecting their pay. Officers had been selling materiel, leaving those troops who did take the field disarmed before the enemy.⁵

Another way these networks pursue their self-enrichment goals is to integrate across to the private sector. The principal companies in industries most likely to benefit from government contracting or concessions, such as construction or mining or energy, are owned by the president's daughter or son-in-law or by retired generals. Network members dominate regulated sectors, such as telecoms and banking. In Azerbaijan, for example, the family of President Ilham Aliyev owns no fewer than eleven banks.⁶

The structured nature of so many of these systems poses an added problem of scope for policymakers. It means that remedies aimed at individual corrupt actors and their facilitators are important but insufficient. The challenge is one of policy alignment, for at least minimal consistency across the disparate agencies of the U.S. government, so as to send a legible message to corrupt networks and truly affect their incentive structures.

Based on research I have been conducting over the past five years, I estimate the number of countries that fall into this category of widespread and systemic corruption at just over 60.⁷

How corruption impacts national and international security:

It's hard to miss the rising level of indignation at the kind of systemic and often ostentatious corruption described above. In just the past year, popular protests have broken out in Azerbaijan, Brazil, Guatemala, Honduras, Iraq, Lebanon, Malaysia, Moldova, and Venezuela. Two chiefs of state have fallen.

But not all the victims have been able to express their frustration in such relatively civil ways. The revolutions of the Arab Spring and Ukraine represent, at least in part, more determined variations on such anti-corruption protests. In every country that erupted in 2011, demonstrators denounced the corruption of detested ruling cliques, and demanded legal accounting for corrupt officials and a return of looted assets.

Those revolutions have degenerated into some of the chief security challenges Washington is currently confronting: a lingering East-West stand-off on the redrawn Ukrainian frontier, slaughter in Syria, the implosion of Libya, Yemen and part of Iraq, and an expanding insurgency in Egypt.

For, corruption fuels the scourge of terrorism too: it gives credence to the arguments of militant religious extremists such as the self-proclaimed Islamic State, and has helped them gain recruits or submissiveness from Afghanistan and Iraq to Pakistan, Central Asia, the Sahel, and West Africa. The pitch is a simple one, rooted in the manifest moral deviance of the corrupt: "They were saying the truth about the violations committed by government agencies," residents of Maiduguri, Nigeria told me during an outdoor conversation on November 21, 2015, explaining the early preaching of the extremist group Boko Haram. "They said, if our constitution were based on the Islamic system, all these things wouldn't be happening; it would be a just and fair society."

It may seem a spurious argument, especially in light of the behavior of extremist organizations when they gain power (including the government of Iran). But it can be awfully persuasive to a young Nigerian man whose sister has just been fondled by a professor as the cost of matriculation. Indeed, a glance at Western history, including our own, indicates that militant puritanical religion is a frequent reaction to abusively corrupt governance.⁸

The anger is not just directed against host-country governments, either. When the United States is seen as intimately associated with the corrupt practices, victims not unreasonably assume our country explicitly approves them. "The Afghan government is your face," a member of my manufacturing cooperative in downtown Kandahar, Afghanistan told me one day. "If it's pretty or it's ugly, it's your face."

In light of this reality, counterterrorism partnerships that reinforce abusively corrupt governments may be doing more harm than good. They may lead to the radicalization of a dozen people for every one that is killed, and excite anger against the U.S. patron as well as the venal local client.

Other security challenges that are inflamed by corruption include chronic outbreaks of violence due to rivalry among competing kleptocratic networks (as in Somalia or the Democratic Republic of Congo, for example)⁹ and the reinforcement of transnational organized crime structures through their interpenetration with corrupt governments in their home bases (as in Central America or the Balkans). It would not be unreasonable to ascribe even some of the adventurism of China and Russia to corruption, and an effort to distract a restive population from its grievances via an appeal to nationalist feeling.

The effectiveness of current anti-corruption efforts:

There is no question that corruption has attracted measurably increased policy attention over the past year, not just in words but in deed. Some 30 investigators have been added to the U.S. Department of Justice's anti-kleptocracy unit; the State Department's regional bureaus now feature an anti-corruption assignment; and the United States is participating in several multinational law enforcement initiatives aimed at information sharing and asset recovery.

Still, given the dimensions of the problem, the approaches adopted to date have been sadly inadequate.

Corruption, first of all, is typically viewed as a functional specialization, and a poorly rewarded one at that. It is subcontracted to often marginal units within the State Department or USAID: the Bureau of International Narcotics and Law Enforcement Affairs, for example, where it counts, presumably, as a subset of law enforcement. According to two young officials reflecting on the atmosphere within the State Department over the past several months, the mention of corruption is met with "rolled eyes," in one bureau; elsewhere interest in the topic is seen as a career-killer.

At USAID, an organization whose business model entails investing millions of dollars per year into severely corrupt environments, a comparison between the number of personnel assigned to LGBT rights, clearly a vital issue touching fundamental human dignity, and the number of people assigned to corruption might be instructive.

Where steps are being taken, moreover, they are scattershot. Decisions to pursue kleptocracy investigations are made by front-line investigators, on the sole basis of the quality of evidence that has come to hand, not any deliberate strategy. The focus on beneficial ownership or transparency initiatives carries with it the implication that corruption is the work of disconnected individuals, who can be taken on individually. Transparency becomes an end in itself, when too often it fails to result in ultimate accountability. Support to civil society groups is provided in blissful isolation from the countervailing incentives that other aspects of U.S. engagement may be providing to a corrupt leadership. Sometimes the contradiction puts beleaguered activists or reformist government officials in impossible, even life-threatening, situations.

Indeed, it is this disconnect that likely precludes current U.S. anti-corruption programming from having any noticeable impact. When Washington is providing millions of dollars in military and development assistance, or when the CIA station chief is handing over a similar sum per month to a corrupt leader in private meetings, as has been the case in Afghanistan,¹⁰ a few hundred thousand dollars spent on capacity building for the inspector general of police, for example, or to support a civic group agitating for budget transparency, is almost laughable. Indeed, viewed from the

perspective of the corrupt leader, U.S. policy is hardly even contradictory; it's clear: the United States approves of his venal practices, and the occasional public scolding or paltry anti-corruption programming must surely just be designed to check a box or mollify Congress, rather than to convey any meaningful message as to U.S. policy.

It is in this light that the U.S. Congress should frame its questions to the military and civilian assistance communities. It is not so important to ask what is being spent on what programs designed to curb corruption, but rather what steps are being taken to shape flagship projects, such as Power Africa, or our military partnership with Ethiopia, in such a way that their implementation and outcomes don't inadvertently benefit the kleptocratic network.

Recommendations:

The Foreign Relations Committee can push Congress to help remedy some of these deficiencies in approach by taking the following steps.

- For every assistance package (USAID, INL, and State Department-overseen military programming) of significant size, require that a systemic political economy analysis, depicting the structure of corrupt networks, the main revenue streams they capture, and their key external enablers and facilitators be completed and submitted to Congress alongside the funding request.¹¹
- Require that such a request include a strategy for mitigating any reinforcement the programming might provide to the corrupt governing system.
- Require that budgets for projects that, due to some other security or diplomatic imperative, are knowingly launched in severely corrupt environments devote a greater than normal proportion of the funds to monitoring and evaluation; require that the RFP or project design include provisions for citizens' oversight of project delivery, and suspension or cancellation where misuse of funds is discovered. Improvement of governance should be considered as an equally important goal of such projects as their stated objectives.
- Redirect some appropriations away from the already well-resourced U.S. Department of Defense counterterrorism or countering-violent-extremism programming toward civilian-led activities that can help curb partner governments' corruption and dissociate the United States from it.
- Direct the U.S. Department of State and USAID to increase the number of billets, including intelligence billets, for personnel deeply versed in corruption and its implications for the broad range of programming and diplomatic relations. (And direct USAID to spend its allocated anti-corruption budget to this effect, instead of passing it along to State.)
- Direct the U.S. Department of State to develop mandatory training on the implications of corruption, its structure and functioning, and ways in which diplomatic relations, trade promotion, and civilian and military assistance interact with it, for all political, economy, and political-military officers.

There are a variety of other actions Congress could take that lie outside the purview of this Committee. I would be happy to elaborate as appropriate.

Please accept my gratitude for the opportunity to contribute to this deliberation.

¹ John Kerry, “Time to Treat Corruption With the Seriousness It Deserves,” U.S. Department of State, May 12, 2016, accessed June 28, 2016 at <http://www.state.gov/secretary/remarks/2016/05/257175.htm>. See also his remarks delivered at “Against Corruption,” a summit hosted by British Prime Minister David Cameron on May 12, 2016, accessed June 28, 2016 at <http://www.state.gov/secretary/remarks/2016/05/257130.htm>

² Global Financial Integrity (GFI), “Data by Country,” accessed June 27, 2016 at <http://www.gfintegrity.org/issues/data-by-country/>.

³ According to reporting by the *Wall Street Journal* in 2010, as much as \$10 million per day was leaving Afghanistan at that time, much but hardly all of it declared. Matthew Rosenberg, “Corruption Suspected in Airlift of Billions in Cash from Kabul,” *Wall Street Journal* June 25, 2010. A U.S. intelligence professional told me that millions of dollars in cash had been flown out of Nigeria in the wake of the March 2015 election of Muhammadu Buhari as president.

⁴ See GFI’s methodological note here: <http://www.gfintegrity.org/issues/illicit-financial-flows-analytical-methodologies-utilized-global-financial-integrity/>

⁵ See, for example, David Kirkpatrick, “Graft Hobbles Iraq’s Military in Fighting ISIS,” *New York Times* November 23, 2014, or Aryn Baker, “Nigeria’s Military Quails When Faced with Boko Haram,” *Time Magazine*, February 10, 2015.

⁶ Organized Crime and Corruption Reporting Project, “Azerbaijani First Family Big on Banking” June 11, 2015, accessed June 28, 2016 at <https://www.occrp.org/en/corruptistan/azerbaijan/2015/06/11/azerbaijani-first-family-big-on-banking.html>. For a full discussion of the way kleptocratic elites structure their networks, see Sarah Chayes, “The Structure of Corruption: A Systemic Analysis,” Carnegie Endowment for International Peace, expected July 1, 2016.

⁷ The countries are: Afghanistan, Algeria, Angola, Armenia, Azerbaijan, Bahrain, Bangladesh, Brazil, Bulgaria, Burkina Faso, Burundi, Cameroon, Chad, China, Colombia, Cote d’Ivoire, Egypt, Equatorial Guinea, Eritrea, Ethiopia, Guatemala Guinea, Guinea-Bissau, Guyana, Honduras, Iceland, India, Indonesia, Kazakhstan, Kenya, Kyrgyzstan, Lebanon, Libya, Mali, Mexico, Moldova, Morocco, Nepal, Niger, Nigeria, Pakistan, Paraguay, Philippines, Romania, Sierra Leone, Slovenia, Somalia, South Africa, South Sudan, Sudan, Syria, Tajikistan, Thailand, Tunisia, Turkey, Turkmenistan, Uganda, Ukraine, Uzbekistan, Venezuela, Yemen, and Zimbabwe. This list was derived by Carnegie Junior Fellow Julu Katticaran by aggregating the following indices: The African Development Bank Country Policy and Institutional Assessments, Afrobarometer, Asian Development Bank Country Policy and Institutional Assessments, European Bank for Reconstruction and Development Transition Report, Economist Intelligence Unit Riskwire and Democracy Index, Freedom House, Global Integrity Index, Gallup World Poll, International Budget Project Open Budget Index, Latinobarometro Sustainability Index, Political Economic Risk Consultancy Corruption in Asia Survey, Political Risk Services International Country Risk Guide, Transparency International Corruption Perceptions Index and Global Corruption Barometer Survey, U.S. State Department Trafficking in People report, World Justice Project Rule of Law Index, plus my own qualitative corroboration as to degree of structure.

⁸ For a complete discussion of how puritanical religion is often a reaction to severe corruption, see Sarah Chayes, *Thieves of State: Why Corruption Threatens Global Security* (New York: W.W. Norton, 2015).

⁹ See Alex de Waal, *The Real Politics of the Horn of Africa: Money, Politics, and the Business of Power* (New York: Polity, 2015). Note de Waal uses the terminology of the marketplace, rather than corruption, but the his description applies.

¹⁰ Matthew Rosenberg, “With Bags of Cash, CIA Seeks Influence in Afghanistan,” *New York Times*, April 28, 2013.

¹¹ For a template for such an analysis, see Chayes “Structure.”