PROCEEDS OF CORRUPTION: FRAMEWORKS FOR THE MANAGEMENT OF RETURNED ASSETS

DRAFT CONCEPT NOTE

February 11, 2009
A. **Context, Relevance, and Demand**

1. From a financial management perspective, international asset recovery cases present important challenges, one of which is find ways to ensure, or at least maximize, the social welfare that can be gained from the disposition and application of recovered assets. Responding to this specific challenge requires a good understanding and a careful consideration of both, the technical and the political economy elements that influence the management of returned assets. The main objective of this Concept Note (PCN), and ultimately of its final product, is to inform and assist policy makers in the selection of appropriate institutional arrangements that could help countries manage their recovered assets.

2. The UN Convention against Corruption (UNCAC) is the first legally binding international agreement to set an anti-corruption framework. The recovery of stolen assets is an important component and fundamental principle of the Convention, which dedicates an entire chapter to this issue. The Convention includes provisions that touch on the various elements of the asset recovery process, from the investigative stage to the actual return and disposition of forfeited assets, including provisions for international cooperation regarding the seizure, restrain and forfeiture of the proceeds of corruption.

3. Although there is considerable literature and experience regarding financial management frameworks, limited use and customization of such frameworks and principles has been done to fit the particular nature of the proceeds of corruption, so in some way this work is ground breaking and therefore extremely relevant for StAR.

4. There are at least two technical characteristics that suggest that the handling of the proceeds of corruption should be treated differently from other traditional sources of funds, including tax revenue, donor transfers, and even the forfeiture of the proceeds of other organized crime activities. First, proceeds of corruption have hitherto been less frequent and of significantly lower amounts than other traditional sources of revenue. In other words, asset recovery is likely to be a one-off event. Second, proceeds of corruption usually imply some damage made to the state through the diversion of public funds requiring some form of restitution to the state or the individual agency that was victim, while other sources of funds tend to be incremental. This last point has distributive implications. For example, should recovered funds stolen from a poorly run school text program within the department of education be allocated to the general budget or should they be restituted to the Ministry of Education?

5. There are also political economy considerations that suggest that proceeds of corruption might be treated differently from more traditional sources of revenue. For example, the returned of funds to a country where high government officials in the incumbent administration are believed to be involved in corrupt activities, presents some challenges that usually do not exist in other cases. For example, donors might refuse to lend or provide grants to a country if they think they will likely be stolen; however, the enforcement of a final sentence ordering the forfeiture of corrupt proceeds in the requested country might leave no other choice to authorities other than returned the assets in questions as ownership by the requesting state has been established in court. This is a sensitive area as often times countries have strong views for and against the use of
additional measures to ensure that assets restituted to victim countries are used for development purpose and for the benefit of their people.

6. Restituting countries argue that low levels of public accountability; weak public financial management systems (PFM); poor governance and endemic corruption are the main reasons why victim countries should adopt additional measures to ensure that repatriated funds are not stolen again. On the other hand, victim countries defend their right to freely and discretionally decide the final destination and use of their resources, and they often see the requests and concerns of foreign countries as a violation of their sovereignty, or as outright neo-colonialism. Authorities in victim countries also think these foreign demands pass judgment on their own integrity, and fail to draw a distinction between the former corrupt regime that stole the assets and the new administration in office. These tensions came up front-and-center during the negotiating rounds of the UNCAC. The issue was resolved and dealt in article 57 of the Convention, which provides for the return and disposition of assets between State Parties.

7. On this issue, the Action Plan included in the report released at the launch of the Stolen Asset Recovery (StAR) Initiative mentions that “the World Bank Group would offer its services to help monitor the use of the funds... Such involvement in monitoring would be purely voluntary, in keeping with the fundamental principle of the returned of stolen assets as embodied in the UNCAC.” In approaching this sensitive issue, the StAR Initiative is mindful and respectful of the views held by each individual country; however, StAR will not take sides on this debate, and will remain committed to its mandate and the provisions set forth by the Convention. The ultimate intention of this policy note is not to advocate for, nor suggest the use of special arrangements in the disposition of returned assets, but to present the stock of knowledge around this issue so policymakers can understand the menu of alternatives at their disposal, as well as their advantages and disadvantages, and help inform their decision. This objective should be understood in the context of what the Convention suggests in paragraph 5 of Article 57: “Where appropriate, States Parties may also give special consideration to concluding agreements or mutually acceptable arrangements, on a case-by-case basis, for the final disposal of confiscated property.” The World Bank has provided advisory services and technical assistance to countries that have voluntarily requested assistance in managing the use of returned assets. In 2005, the World Bank was jointly requested by the Governments of Nigeria and Switzerland to provide assistance in managing the use of more than $500 million repatriated Abacha funds. More recently, in 2008, the World Bank agreed to provide technical assistance and other services to the BOTA Foundation, a non-profit organization, created for the administration of approximately $84 million that were recovered as part of a settlement reached between the Governments of Kazakhstan, Switzerland and the United States. The lessons learnt in these two cases, plus the Bank’s experience in implementing expenditure tracking systems constitute a useful source of knowledge and country experience for this policy note.

B. OBJECTIVES, SCOPE AND DESCRIPTION OF THE TASK

8. As briefly mentioned above, the objective of this policy note will be to provide analytical elements that can inform decisions made by policy makers about available options and best-fit models that can be use in the management of returned assets. The
Final Product will review all phases within the public financial management process, from governance arrangements to external auditing mechanisms—including the internal controls, reporting requirements and others—and identify the available options that policy makers can select and use in the management of returned assets. In addition to this stock taking exercise, the note will provide policy makers with an account of the advantages and disadvantages in using each alternative. Also, the paper will discuss how country circumstances (i.e. quality of PFM system, legitimacy, and governance) and characteristics of the asset recovery case(s) (i.e. amounts and individuals involved) will affect the use of one alternative vis-à-vis others. In order to effectively assist and inform policy makers, this framework needs to be consistent with sound and accepted principles of public financial management, must be flexible enough to adapt to heterogeneous environments, and mindful of the technical and political economy factors that influence the decision making process of authorities.

9. The following list provides a non-exhaustive overview of challenges that should be considered when drafting the final product. These challenges should be weigh-in when assessing the pros and cons of the various management frameworks.

- **Fungible money.** A fundamental challenge in tracking public expenditures is the fact that money is fungible. This fact implies that any additional spending coming from one source (i.e. restituted assets) can be off-set one-to-one by reducing the contribution coming from another source (i.e. regular budget), including tax cuts. This makes the tracking of incremental spending an important challenge for any management framework.

- **Uncertainty about likelihood, amount and timing of restituted assets.** Asset recovery proceedings usually involve multiple jurisdictions and cases. Uncertainty about case outcome and timing of the eventual restitution of funds is an important factor in deciding about the individual elements in a management framework. For example, in terms of restituted amounts, when these represent a significant proportion of GDP, it will be important to ensure that the transfer is factored into the macroeconomic framework and projections of the country concerned to smooth out any adverse fiscal shocks. Conversely, when the amounts are small, preference should be given to “lighter” management structures so recovered assets are not wasted on administrative costs.

- **Inter-temporal consistency between stream of revenues and expenditures.** The one-off nature of recovered assets makes it an inappropriate source for financing long run government programs. Careful thought must be given to the idea of financing permanent programs with temporary resources.

- **Earmarking versus General Budget Allocation.** What are the benefits of earmarking returned assets to one, or a narrowly define list of sectors and agencies? In the Philippines, the Marcos assets were used to finance the land reform while in Nigeria resources were incorporated in the regular budget and allocation was decided following a process more similar to that of the regular budget. There is some risk in tying funds to specific sectors or agencies.

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1 This stocktaking exercise has partly been done and a good summary can be found in Annex A of the *Stolen Asset Recovery (StAR) Initiative: Challenges, Opportunities and Action Plan.*
Incentives in a particular agency may significantly change when the institution is allowed to keep and decide the purpose of forfeited assets.\(^2\)

- **Political Economy Factors.** The political nature of the asset recovery process can significantly affect the allocation decision. Should incremental resources coming from recovered assets be used to fight corruption? Should they be used as restoration to victims of human rights abuses—an issue that unfortunately is usually tied to grand corruption? Institutional arrangements and other political economy factors can certainly influence these decisions. Taking the argument a step further, if anticorruption efforts and law enforcement activities are identified as a cornerstone against organized crime and grand corruption, why are these agencies so under-funded that they need earmarked resources or extra-budgetary funds to supplement their operations?

- **Role of third parties in the management of returned assets.** Can private firms and civil society organizations (CSO) engaged as a third party in the management of public expenditures improve the effectiveness of government programs? If so, under what circumstances? Participation of third parties can enhance the domestic and international legitimacy of restituted countries; however, what is the precise role that third parties should have in this process, in which stages of the process can these entities add significant value? Is there a role for CSOs and the media in disseminating the information that corruption does not pay and funds are being recovered for the benefit of the public?

10. The Final Product will examine whether existing country case experience has follow the recommend practice. The idea is to determine whether countries have followed theoretically sound PFM principles and procedures, and if not, try to identify plausible reasons explaining those deviations. For example, there is anecdotal evidence suggesting that restituting countries are more inclined to err on the side of cautious, and therefore try to persuade victim countries to adopt additional measures that are not always consistent with sound PFM principles and practice. The reasons for this behavior are uncertain; however, hypotheses include political and domestic pressures from constituencies in restituting countries, and asymmetric negotiating balance between restituting and victim countries.

C. **Expected Outputs, Results and Results Indicators**

11. The Final Report will address the challenges outlined in the section B above. It will also rely on PFM principles, good practices and try to identify available alternatives within each of the components of the PFM process. Rather than providing clear-cut policy prescriptions, the report should inform the debate about the pros and cons of using different arrangements in managing repatriated assets, and through the revision of country case studies, it will exemplify what approaches have worked under specific

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\(^2\) Evidence in the US suggests that when law enforcement agencies are able to supplement their regular budgets with resources from a forfeiture fund, incentives are set so that tasks and human resources are allocated with the overall goal to maximize the agency’s own revenues, and not necessarily based on other social objectives, such as the prevention and control of crime. Even though this reward-based scheme may be optimal for the agency, it may lead to sub-optimal welfare gains for society as a whole.
institutional arrangements. The information should be presented in such a way that the reader can easily identify:

a) The available alternatives within each component of the PFM process;

b) The pros and cons of each alternative, and;

c) How well does each alternative fit a particular country context and the circumstances of the asset recovery efforts/cases?

12. The following paragraphs in this section illustrate some of the main points that must be considered to facilitate the reader with the elements necessary to identify the policy options that best fit his country’s needs.

Public Financial Management Principles

13. The broad objectives of public financial management are to achieve overall fiscal discipline, allocation of resources to priority needs, and efficient and effective allocation of public services. To achieve these objectives, especial attention should be given to all phases of the public financial management process, including the preparation of the budget, internal control and audit, procurement, monitoring and reporting arrangements, and external audit. A decade of intensive work has generated an unparalleled body of information and knowledge on the operation of public financial management (PFM) systems throughout the world. As a result of this work, five principles have emerged that reflect good practice in PFM work:

- A shared agenda - A country-led PFM reform strategy and action plan. The starting point for public financial management reform is a country-owned program of reform and a country-owned structure for managing the reform process.
- A shared work-program - A coordinated IFI-donor multi-year program of PFM work that supports and is aligned with the government’s strategy and budget processes. Country-led reform programs should form the basis for IFI-donor support. Ideally, a yearly program of support would be defined based upon a dialogue between the government and donors in a government-led forum.
- Commitment to a coordinated program of PFM work in support of a country strategy is complemented by making use of a country’s financial systems to the greatest extent feasible in all forms of aid delivery.
- A shared information pool that provides objective and consistent information on public financial management performance over time.
- Different arrangements may exist for PFM performance measurement and monitoring depending on country circumstances and accountability requirements of donors.

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4 Towards a Strengthened Approach to Supporting PFM Reform, Public Expenditure Working Group, October 30, 2004
14. Although the above principles are a result of the experience in implementing PFM reforms linked to the management of both national funds and donor aid, it should be made clear to the reader that recovered assets should not be treated as aid, particularly those restituted in the context of embezzlement cases. Notwithstanding this important distinction, a number of interesting propositions emerge from this experience and the principles listed above. In order to strengthen PFM systems: (i) Developing countries need to be in the driving seat; (ii) A long term horizon is paramount; (iii) Preference should be given to existing country systems; (iv) Frameworks should avoid silver-bullet approaches, be flexible and remain responsive to country circumstances; (v) Country-Donor dialogue should be fluid and constructive. These principles and the propositions that emerge from them can provide helpful guidance when evaluating best-fit alternatives for the management of returned assets.

Components in the Public Financial Management Process

15. The principles outlined above offer guidance when seeking to identify best-fit alternatives in each of the essential elements or components in the PFM process. The Final Product should follow this process that goes from the receipt of the funds to the auditing stage, and provide guidance and advice for policy makers. The following bullets provide a non-exhaustive list of PFM components that the note should address.

- **Location of Recipient Account.** Should funds be deposited on the Treasury’s Single Account usually located in Central Bank or, on the other extreme, be retained in escrow in a commercial bank outside the country? What are the available alternatives in-between these two extremes?

- **Type of Corporate Governance Structure and Arrangements** (if any). If funds are to follow existing country systems then no additional governance structure should be put in place; however, if a special fund is created then the issue of corporate governance becomes essential to ensure that recovered assets are not used to serve private interest. A balanced representation of stakeholders in the governance structure in off-budget funds will be a fundamental issue to consider.

- **Mechanism for Disbursement.** Again, if funds follow standard process, allocation and disbursement will rely on regular budgetary process with participation of all relevant ministries and the Legislature. On the other hand, if decision will be made by a separate entity, how should decisions be made (consensus, plurality, otherwise)? How should conflict of interest be prevented and managed? What accountability mechanism will be put in place to ensure effective and efficient allocation?

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5 More specific to the issue of managing returned assets, the G8 countries produced a short paper titled “Principles and Options for Disposition and Transfer of Confiscated Proceeds of Grand Corruption”. Annex 1 presents the seven principles outlined in the G8 document.

6 Just like a customer can purchase a suit at a tailor shop where it will be made to fit a specific size and style or get at a retail store, a policy maker can choose a management framework tailored to specific needs and circumstances, or select from a family of pre-established alternatives. Annex 2 presents a list of categories or “families” of management frameworks.
• **Internal Control Mechanisms.** Should special manuals or guidebooks be developed to ensure proper procedures will be followed, or should funds rely on existing procedures? Again, what are the in-between alternatives?

• **Accounting Standards.** What appropriate accounting standards should be followed? For example, should expenditures be “tagged” to facilitate tracking and reporting? Should expenditures be registered on cash or accrual basis?

• **Financial Reporting Requirements.** What formats should be employed for reporting financial information? Should country reports co-exist with other formats used in donors or World Bank projects?

• **Internal Auditing Mechanism.** Should auditing be left to Supreme Audit Institutions or the Comptroller General Office, or on the other hand, should enhance mechanism be put in place to ensure internal and administrative controls are followed.

• **Independent Auditing Arrangements.** Should independent/external audits be undertaken? What should be the precise terms of such auditing agreement?

• **Access and Dissemination of Information.** What means should be employed to share and disseminate information amongst stakeholders? Should that information be available to the public? If so, in what form and through what channels?

16. The Final Report should take into account the heterogeneous characteristics of the enabling environment, the particularities of each asset recovery case, and most important, be consistent with the framework provided by the UNCAC. The main result that this effort seeks to accomplish is improving the policy decisions related to the management of the proceeds of corruption by increasing the stock of knowledge around this issue. As mentioned in the introduction, little research has been conducted on managing the proceeds of corruption. By undertaking this effort, StAR seeks to spark the interest of countries in ensuring that the people in these countries benefits from the use of recovered assets. Furthermore, StAR hopes that this research will contribute to the adoption of measures that are consistent with sound PFM principles. Finally, it is also expected that the study will increase our understanding of the political economy factors that influence the decision regarding the management, allocation and disposition of repatriated funds.

D. **Methodology and Data**

17. In order to fulfill the objective stated in this PCN, and to cover the issues outlined in Section B, the researchers conducting this study should be able to draw on the existing literature and country case studies to illustrate the governance and financial management issues relevant for the discussion. The PFM literature offers a rich source of information, particularly in each of the components of the PFM process. Although some of the existing literature may not be specific to the proceeds of corruption, it can provide useful lessons that can be extrapolated to this particular context (i.e. the literature on, road funds, poverty funds and other sectors). The literature regarding the political economy elements of the fiscal and budgetary process can also be very informative.

18. Based on the review of the available literature, the Final Report described in Section C could very well have a “Decision-Tree” format. The Report should draw from existing country case studies. A list of potentially good cases that have been relatively
well documented includes Kazakhstan, Peru, Philippines, Nigeria, and a few other less documented cases (Mexico and Zambia). The following bullet points provide a short overview of the most interesting case studies:

- **Kazakhstan:** As mentioned earlier, the governments of Kazakhstan, Switzerland, and the US agreed to establish a NGO, the BOTA Foundation, to ensure that $84 million frozen in Switzerland be returned to Kazakhstan for the benefit of its people. The approach followed in this case relied on “ring-fencing” the resources to be spent in Educational Projects.

- **Peru:** Prior to the restitution of some $20 million from the US, Peru agreed to the creation of a special fund (the “FEDADOI”) for the administration and disposition of assets repatriated in the context of the Montesinos case. The FEDADOI was governed by a Board comprised by representatives from 5 ministries. As consequence of poorly defined expenditure categories, funds were mainly used to supplement the budget of the 5 ministries represented in the Board, for example, the Interior Ministry received over $9 million in 2004 that were used for the payment of vacations for both active and retired police personnel outstanding from fiscal years 1995 and 1996.

- **Philippines:** Over $600 million from looted Marcos funds were returned to the Philippines Treasury. All recovered assets followed an off-budget process and were allocated to the “Agrarian Reform Fund” to finance agrarian reform programs. In October 2006, the Commission on Audit discovered that a significant portion of the recovered assets were used to finance excessive and unnecessary expenses, unlikely to benefit low-income rural farmers and their families. Given that this is one of the first successful asset recovery cases, it is a well documented experience.

- **Nigeria:** In 2005, Nigeria received some $500 million of Abacha funds from Switzerland. The funds went to incremental funding of MDG-related activities (such as health, education, and rural infrastructure programs). Nigeria treated these resources as general revenues, and spent them through its usual public financial processes. However, weaknesses in the Nigerian public financial management system made it difficult to track spending. Nevertheless, a World Bank Public Expenditure Review found that the funds had generally been used in accordance with stated policy. Nigeria has since adopted a "virtual poverty fund" framework for the management of funds resulting from debt relief, which enables the tracking of spending of activities receiving funding from various sources. The Nigeria case study offers the experience of a less "intrusive" framework in the context of low capacity institutions and weak PFM systems.

- Additional studies for which there is less available information include: Mexico ($160 millions returned in the context of the Salinas Case) and Zambia ($60 million returned in the context of the Chiluba case).\(^7\)

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\(^7\) A case study that does not involved the proceeds of corruption but might an interesting experience to review is the use of a Virtual Poverty Fund in Ghana to manage aid and debt relief. Other interesting sources of experience might be found in sector funds like Road or Infrastructure Funds.
E. **Quality Assurance and Client Consultation**

19. The first measure to ensure the quality of this project is the inclusion of experts from the IMF, UNDOC, and World Bank, as well as external practitioners and researchers during the Peer Review process. A second measure includes consultations with the working group on asset recovery that is part of the Conference of State Parties to UNCAC. Once the final draft of the Final Report is completed, its approval and release will follow the standard World Bank procedures with a Decision Meeting chaired by PRMPS Director and the StAR Coordinator. A small number of civil society organizations may be invited to participate in the Decision Meeting of this product. The Final Report and the minutes of the decision meeting will be sent for approval to the StAR Management Committee.

F. **Audience & Dissemination Strategy**

20. This product is primarily aimed at an external audience that includes policy makers and advisors working in asset recovery related issues, public financial management specialist in Ministries of Finance and Central Banks. A secondary audience includes members and staff of the donor community, including bilateral agencies, IFIs working on governance and anti-corruption, and in financial management issues.

21. In order to ensure that product reaches its intended audience, the Final Report will be presented at the 3rd Conference of State Parties (CoSP) to UNCAC to be held in Doha, Qatar in December 2009. Additional efforts will be undertaken to present the findings of this research in other venues that would include the World Bank/IMF annual or spring meetings, and the DAC GOVNET Committee within the OECD. Depending on the interest generated by the paper, additional means for internal dissemination could be undertaken, i.e. organization of a “webinar”, BBLs and the repackaging of the Final Report in the form of a PREM Note.

G. **Team and Implementation Arrangements**

22. The study will be task managed by Victor Dumas (TTL). In order to conduct the research, the first task will be to identify an individual who will work with the TTL in undertaking this study. The TTL and selected candidate (internal or external) will be responsible for: (i) gathering all relevant information in the public domain, including that on particular country experiences, as well as in the broader literature in asset recovery related issues; (ii) conducting the necessary interviews with experts and consulting with relevant stakeholders, and; (iii) drafting the sections for the Final Report. If an internal candidate is selected, his or her time will be treated as cross-support given to PRMPS as the responsible unit. If an external candidate is selected, then he or she will be hired as a consultant.

H. **Process, Budget and Timetable**

23. The preparation of this report will be carried out in accordance with the following process and milestones:
• **Peer Review Meeting and Minutes of the meeting:** This task will be undertaken by the TTL who will be accountable for it.

• **Clearance by StAR Management Committee:** StAR coordinator will submit the PCN with the Minutes from the Review Meeting for the approval of the StAR MC.

• **Creation of Child Trust Fund and submission of GFR:** the TTL will coordinate these with the resource management staff.

• **Drafting of ToRs and hiring of consultant:** the TTL will draft the ToRs for the consultant. Hiring decision will follow Bank procurement rules and will be made by the PRMPS Sector Manager.

• **Draft Reports.** The TTL/Consultant will responsible for drafting and circulating the report for comments to Bank and UNODC staff, consolidating such comments, and incorporating them in the revised text.

• **Consultations:** the TTL will be responsible for coordinating consultations and complying with the quality assurance process established in this PCN.

• **Final Draft and Decision Meeting:** the TTL/Consultant will be responsible for producing the final draft of the Report and circulate it for comments prior to the Decision Meeting. This meeting will be chaired by PRMPS Director and the StAR Coordinator, and the TTL will be responsible for taking minutes of the meeting. If necessary, the consultant will need do final edits to the text.

• **Final Report:** the final report will be cleared by PRMPS Director and sent to the Management Committee for approval and dissemination. The StAR coordinator will coordinate approval by the MC.

• **Dissemination:** the TTL/Consultant will take part in any dissemination events. They will be responsible for the delivery of the main findings of the study.

• **Completion Report:** the TTL will draft the completion report after the dissemination efforts have been finalized.

24. The overall budget is presented in Table 1. Expenditures from StAR Multi-Donor Trust Fund will cover variable cost including: (i) consultant/cross-support time, (ii) cost of layout, design and printing of the Final Report, and; (iii) travel cost for dissemination at 3rd Conference of State Parties. It is envisioned that consultations will be held with the working group on asset recovery prior to the drafting of the Final Report. The date and modality is yet to be decided but options include a VC connection (preferred) or a trip to the location of the meeting (Vienna, Austria). Administrative support will be provided by PRMPS and TTL administrative staff time will be charged to the World Bank budget as required by the administration agreements of the StAR MDTF. The budget includes dissemination activities, as it is anticipated that Final Report will be presented at the 3rd Conference of State Parties (CoSP) to UNCAC. The MDTF will cover the travelling expenses to this event.

25. The schedule of disbursements and estimated expenditures covered by the StAR Multi-Donor Trust Fund is presented in Table 2. The timeline for deliverables is presented in Table 3. The Final Report is expected to be completed by August 1st, 2009.

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8 If the services of an expert are contracted via cross support it is possible that resources will come from regular Bank budget (BB) and not from the MDTF.
Table 1: Budget

<table>
<thead>
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<th>Cost Description</th>
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<th>UNODC</th>
<th>StAR MDTF</th>
<th>Other</th>
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<td>USD</td>
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<tr>
<td>Equipment Costs</td>
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Table 2: Disbursement Schedule for MDTF Resources

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<td>Short-Term Consultants (weeks)</td>
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<td>Staff Costs (weeks)</td>
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<td>Contractual Services/Cross-support</td>
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<td>Travel Expenses (trips)</td>
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<td>Equipment Costs</td>
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<td>Publication Costs</td>
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<td>Workshop Costs (participants)</td>
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Table 3: Timetable

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<td>Identification of Expert Group and Contracting of Consultant</td>
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<td>Final Report</td>
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<td>ACS Impact Assessment</td>
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Annex 1:
G8 ASSET RECOVERY INITIATIVE
Principles and Options for Disposition and Transfer of Confiscated Proceeds of Grand Corruption

**Principle 1:** Transparency. States must ensure transparency and accountability in the transfer and administration of confiscated assets.

**Principle 2:** Presumption of Transfer. Wherever possible and appropriate, without prejudice to other victims, assets recovered in grand corruption cases should benefit the people of the nations harmed by the underlying corrupt conduct.

**Principle 3:** Case-Specific Treatment. Disposition of confiscated assets must be considered in a case-specific manner.

**Principle 4:** Remedial Objectives. Serious consideration should be given to encouraging actions which fulfill UNCAC principles of combating corruption and repairing the damage done by corruption.

**Principle 5:** Consistency and Coordination. Wherever possible and appropriate, relevant development agencies should be consulted to ensure awareness of the transfers, avoid duplication of services, and encourage consistency with the identified needs of the people of the country receiving confiscated assets.

**Principle 6:** Encourage Use of an Agreement. An agreement or arrangement should be considered in a case-specific manner detailing the terms of the transfer and, where appropriate, ensuring the transparent and effective use and administration of transferred assets.

**Principle 7:** Preclusion of Benefit to Offenders. The disposition of confiscated assets should not benefit persons involved in the commission of the offence.
Annex 2:

Categories or “families” of management frameworks

The following list provides a non-exhaustive compendium of alternatives that range from reliance on existing country systems to a framework that creates a completely parallel alternative (Ring-fencing). The purpose of the list is to illustrate the wide range of available options.

- **Pure Country System (No Additional Measures):** It is of fundamental importance to understand that additional measures should only take place if countries voluntarily agree to them. The UN Convention against Corruption (UNCAC) explicitly embraces this principle. Furthermore, even when involved countries are not Parties to UNCAC and, therefore are not bind by its provisions, additional measures should not be imposed on a country. Experience has shown that interest and commitment of countries receiving the funds is paramount for a successful experience.

- **General Budget Approach:** assess the quality of expenditure and the soundness of budget processes and institutions as a whole. This alternative is the preferred approach of public financial management specialists given the drawbacks associated with managing a dedicated fund. The advantages of this approach are its low cost and the benefits from an overall review of the budgetary process, namely the identification of specific weakness that can lead to a useful policy prescription and reducing concerns about fungible resources. The main disadvantage is that if country PFM systems are weak, fiduciary assessment and results may be inaccurate and/or misleading. This would generate doubts about the appropriate use of recovered funds.

- **Earmarking or Tagging of Expenditures Approach:** the intention here is to allocate additional resources to specific sectors or programs, in which overall spending levels would be monitored to ensure the desired shift in budget composition (i.e. achievement of MDG goals as was the case in Nigeria). The advantage of this approach is the low cost of ensuring the resources reach specific areas of development. The main disadvantage is the lack of a detailed audit trail from beginning to end, so precise flow and destiny of recovered assets remains unknown.

- **Virtual Fund Approach:** uses the existing budget system to tag and track spending items without setting up a separate institutional arrangement. This intermediate solution between relying on country and parallel system is a good alternative when countries PFM systems are weak. This approach was successfully used in the enhanced HPIC Debt Relief Initiative and has its origins in Uganda. The fund is financed with resources that would come from various sources, i.e. government revenues, donor funds and restituted assets. Expenditures can be both earmarked or allocated to general expenditures. Civil Society Organizations could potentially participate at different stages of the process, i.e. allocation, expending and ex-post monitoring. The advantages of this approach are its reliance in country systems despite its weaknesses which enhance the
likelihood that a “learning-by-doing” process takes place, and it also brings in other actors in civil society which raises government accountability and public awareness. The disadvantage is it can be costly.

• **Extra-budgetary funds (EBFs) and Forfeiture Funds.** The term EBFs refers to all government transactions that are not included in the budget. According to the IMF, this kind of off-budget arrangement represents more than 40 percent of central government expenditures in the world, and may serve different purposes, for instance, social security, health, infrastructure and macroeconomic stability. Donors generally have relied on EBFs as their preferred channel to provide aid, although the Paris declaration calls for increased use of country systems through time; however, public finance practitioners have argued that EBFs can actually undermine the creation of a sound and strong public financial management system in recipient countries. EBFs might also distort the allocation of resources, making the evaluation of the overall macroeconomic or fiscal situation in the country significantly more difficult. Finally, EBFs might lead to less transparency and control of public funds, as well as an increase in rent-seeking activities and corruption. Despite this evidence, countries have decided to adopt EBFs. In some contexts, they have emerged as a result of low confidence about the effectiveness and reliability of the public financial management system. In others, they are used to ensure funding for a particular agency or sector, as is the case of Forfeiture Funds used in the US and managed by the Department of Treasury and the Department of Justice.

• **Ring-Fencing Approach:** relies on completely parallel system by which resources are allocated to specific projects following a completely off-budget procedure. In principle, the government is completely by-passed and a NGO is set up and made responsible for managing, allocating and managing the restituted resources. However, a less radical implementation of this approach could allow for a more participatory role of the government in the process. The advantage of this approach is the almost assurance that restituted funds are used for development. The disadvantages are its high cost, the failure to improve countries PFM systems and achieve an overall incremental shift in specific expenditures. The disadvantages in using this approach suggest that its use should be very limited and countries should forego the use of these special arrangements.