

# U4 Expert Answer



## Overview of corruption in the telecommunications sector

### Query

**Could you provide an overview of corruption-related issues in the telecommunications sector, with a focus on SADC countries?**

### Content

1. Why does corruption in the telecommunications sector matter?
2. Overview of corruption in the telecommunications sector
3. Overview of current anti-corruption efforts in the telecommunications sector
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regulations very difficult to achieve. This also means that policies and regulatory actions that have been corrupted by special interests are often difficult to identify.

Given the social and economic significance of telecommunications, corruption in the sector has significant negative effects from macro-level development to individual citizens. It ranges from petty bribery on the side of consumers to capture of regulatory authorities by special businesses or political interests.

### Summary

With its high revenue generation potential, its complex technical and governance structure and its deep interrelations between public and private sector components, the recently liberalised telecommunications industry is particularly vulnerable to corruption. From an economic perspective many segments of the telecommunications sector are prone to network and scale effects and continuous technological disruption, all of which makes the establishment of competitive markets, the determination of fair prices and the setting of public interest-oriented

The licensing process is particularly prone to corruption and undue influence because of its strategic importance and complexity. Corruption is however also a problem seen in regulation, price-setting, in the supply chain as well as customer services.

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historically had a strong influence on the shaping of industry policy, managing to maintain a dominant position after liberalisation and restrict new market entries (OECD 2014).

With the emergence of the digital age, telecommunications operators have become extremely powerful actors as the new gatekeepers of information and communication (Blackman, Srivastava 2011). The capture of the telecommunications authorities and operators for political purposes is thus an extremely important issue with regard to corruption and abuse of power in the sector, be it for patronage steering jobs to supporters (see section on nepotism) or services directed at geographical areas with political supporters. In Ethiopia for example, experts argue that state capture might be one of the most significant issues linked to network design, with the risk of favouring certain companies and geographical areas that are sympathetic to the government and party interests (Plummer 2012). Policy capture can also be used for information control and censorship. It is virtually impossible to adopt a single measure to control communication networks and information flows, the internet and phone calls without the cooperation of telecommunications operators. In many cases this is done outside of any due process. In Uganda, during the riots in 2009 and 2011, the regulatory authority forced all telecommunications operators to block all communications that had any political content or else they would risk losing their operation licence (Sekyewa 2013).

### **Cronyism and nepotism**

Nepotism and cronyism are such widespread issues in the telecommunications sector that Ewan Sutherland uses the term “crony-capitalism” to talk about the telecommunications industry (Sutherland 2012). It refers to situations in which public officials and decision-makers place their cronies and relatives in strategic positions in oversight and regulatory bodies, or favours telecommunications companies owned by their allies and families (Sutherland 2011a).

In South Africa, former member of parliament and minister of communications Dina Pule was found guilty by the Parliament’s Ethics Committee of nepotism and of “causing improper benefits to be afforded to Mr Phosane Mngqibisa on the basis of his relationship with her” (TechCentral 2013). Similarly, investigations into the assets of Ben Ali’s extended family has found that relatives of the former Tunisian president owned many of the companies operating in the telecommunications

sector, which was protected by barriers to market entry (Washington Post 2014).

### **Conflict of interest**

In the telecommunications sector, many decisions regarding the structure of the market and industry are made by the public sector (number of licences, regulation of prices etc.). A public official working in telecommunications might hold shares in a particular company, which he could have acquired as a bribe (Sutherland 2011a), or have a relative owning shares in a telecommunications company, or have been offered a post-employment job in a company from the sector etc. – all of which might influence his judgement.

The example of Thailand’s former prime minister Thaksin Shinawatra is illustrative of a failure to separate official and business interests in telecommunications. (Sutherland 2011a). In 2010, Thailand’s Supreme Court’s Criminal Division for Political Office Holders found Thaksin Shinawatra guilty of conflict of interest, related to the US\$2.2 billion tax-free sale of his telecommunications company, Shin Corp, to Singapore’s Temasek Holdings. US\$1.4 billion of his assets were consequently seized (StAR 2012). Similarly, Lonestar Communications, the only operator allowed on the Liberian market in the early 2000s was proven to be owned to a substantial degree by Charles Taylor and other members of the government (Sutherland 2012b).

For more information about conflict of interest in public procurement more generally, please refer to a previous answer entitled [Conflict of interest in public procurement](#).

### *Private corruption*

#### **Money laundering**

The recent scandal involving the Swedish telecommunications company TeliaSonera in its operations in Uzbekistan provides a good example of money laundering in the sector. Swedish and Swiss prosecutors are currently investigating Gulnara Karimova, the daughter of Uzbekistan’s president, on suspicion of bribery and money laundering to allow Nordic telecom company TeliaSonera enter the Uzbek market. In 2007, US\$358 million was paid by TeliaSonera to Takilant, a Gibraltar-registered firm and front for Gulnara Karimova. Prosecutors “suspect that Gulnara Karimova, who also served as a public official during the time period relevant for the case, was the one who orchestrated, controlled, and also was the one

who primarily benefited from the procedure” (Chicago Tribune 2014).

### **Corporate misconduct and lack of integrity**

Numerous cases of business, accounting and tax fraud within the telecommunications industry, such as transfer pricing or insider trading, have demonstrated the complexity of intra- and inter-company structures and the possibility for telecommunications firms to disguise actual revenues, costs and operations from the relevant authorities (Sutherland 2011a, KPMG 2004). Though not necessarily directly linked to corruption, such accounting fraud schemes – including fraudulent consulting, sham contracts, and fictitious invoices and contracts – demonstrate the lack of transparency of certain telecommunications firms (Shah 2012).

The 2002 Worldcom scandal, surfing the wave of the burst of the “dotcom bubble”, is one of the biggest accounting frauds that was staged in the telecommunications industry. The company had rapidly accumulated debt and used fraudulent accounting methods to disguise losses and keep their stock prices high. The scandal led to Worldcom filing for bankruptcy in 2003. The SEC estimated that the company’s assets were inflated by approximately US\$11 billion (SEC 2003).

Misallocation, theft and embezzlement of company resources is another risk to be considered in the telecommunications industry, as demonstrated by the recent arrest of Chey Tae-won, the head of one of the largest South Korean conglomerates and owner of the country’s biggest mobile carrier. Chey Tae-won was convicted of embezzling US\$45.6 million from the mobile phone company SK Telecom and an SK subsidiary, SK C&C, in 2008 (The New York Times 2013).

## **3 Overview of current anti-corruption efforts**

### **Tools to reduce corruption in the awarding of concessions and licences**

All stakeholders operating in and around the telecommunications industry have a role to play in building and maintaining a clean licensing system. This includes civil society and the media, who are important

players in terms of ensuring the laws, rules and licence conditions are properly and truthfully implemented.

To promote good governance within and proper administration of the telecommunications sector, both the supply and demand elements of corruption should be tackled. Open bidding and contracting, enhanced transparency, integrity and monitoring mechanisms and training of regulatory officials, as well as corporate integrity and incentives and deterrents for the private sector should be combined to reduce grand corruption (Transparency International 2010).

The role of the regulatory authority is absolutely crucial to ensuring good governance and integrity in the telecommunications market, particularly because public interest and a competitive market structure are difficult to determine and safeguard in a market environment that is characterised by strong network and scale effects. As described above, the regulatory authority needs to operate with sufficient levels of structural autonomy and financial independence and have integrity and accountability measures in place (Blackman, Srivastava 2011). Moreover, regulatory authorities need to have skilled and trained staff as well as deep knowledge of the market (Sutherland 2013).

For additional information about tools used to reduce corruption in public procurement more broadly, please refer to the previous answer entitled [Tools to reduce private sector engagement in grand corruption during the award of public contracts, concessions and licenses](#).

### **The importance of corporate transparency and integrity**

#### *Transparency of ownership structure*

Many examples of corruption in the telecommunications industry point to the issue of companies’ ownership and structural opacity. An important measure to improve integrity in the sector is transparency of the ownership of telecommunications operators. A large number of operators use shell companies registered in tax havens, or use nominee companies, to conceal the names of their owners (Sutherland 2013).

Experts advocate the disclosure of beneficial ownership and details of operators’ corporate architectures, as well as for of a public registry of beneficial ownership. Regulatory authorities could play a significant role by requiring bidding companies to disclose their ownership



and corporate architecture, like the Danish regulators did for TeliaSonera (Sutherland 2013).

### *Integrity measures and training*

Beside transparency measures, telecommunications companies should put in place solid anti-corruption, integrity and accountability policies. The telecommunications sector obtains quite a poor result with regard to the transparency of anti-corruption programmes in Transparency International's TRAC report (Transparency International 2012). Moreover, according to business people working in the telecommunications sector, only a very limited number of telecommunications companies have adopted measures to protect whistleblowers and prohibit facilitation payments (Transparency International 2011a).

In addition, it is important (as in all complex and corruption-prone industries) that firms invest in skilled human resources employees and training for their staff to make them aware of relevant laws and regulations as well as corruption risks and vulnerabilities.

## Investigation and prosecution

### *International and national legal framework*

The telecommunications sector has important economic and social implications and involves a significant number of state bodies. It is therefore important to ensure that states have ratified international and regional anti-corruption conventions (such as the UNCAC, the OECD convention, the African Union Convention on Preventing and Combating Corruption or the SADC Protocol against Corruption), and that they properly implement them. A solid national integrity system with strong and well-managed institutions can help prevent corruption risks, such as conflicts of interest, undue influence on political officials and civil servants etc. (Sutherland 2011a).

A strong and independent judiciary is an important tool for preventing and fighting corruption. Some of the biggest foreign bribery cases have been directed at companies with sizable interests in telecommunications (Siemens, Alcatel-Lucent, Magyar-Deutsche Telekom etc.). There have also been a number of major domestic corruption cases, such as India's 2G spectrum scandal, as well as administrative sanctions within companies (TeliaSonera's CEO had to resign after the disclosure of the alleged bribery scandal in Uzbekistan). This is a crucial aspect of reducing

corruption in a region like Southern Africa, where the independence of the judiciary is not systematically guaranteed, as indicated by the poor scores of many of the region's countries on the WJP Rule of Law Index 2014 (World Justice Project 2014).

## Potential of an EITI for telecommunications

There are a number of international multi-stakeholder initiatives (such as CoST and EITI) promoting open contracting, that is, enhanced transparency and equal access to information and opportunity for participation, as a means to reduce opportunities for corrupt behaviour in the awarding of government contracts, leases and licenses (Wickberg 2013a). Experts suggest that this kind of multi-stakeholder forum and the development of common integrity standards could also benefit the telecommunications sector, as the problems related to the constant interaction between public and private actors are similar to those of other public utilities sectors (Sutherland 2012).

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