Anticorruption Policy: Enhancing the Role of the Asian Development Bank in Relation to Tax Integrity

This document is being disclosed to the public prior to its consideration by ADB’s Board of Directors in accordance with ADB’s Public Communications Policy 2011.
# ABBREVIATIONS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
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<tr>
<td>AEOI</td>
<td>automatic exchange of information</td>
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<td>BEPS</td>
<td>base erosion and profit shifting</td>
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<td>DMC</td>
<td>developing member country</td>
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<td>EOIR</td>
<td>exchange of information on request</td>
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<td>FATF</td>
<td>Financial Action Task Force</td>
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<td>IDD</td>
<td>integrity due diligence</td>
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<td>IFI</td>
<td>international financial institution</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>OAG</td>
<td>Office of the Auditor General</td>
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<td>OAGA</td>
<td>Office of the Auditor General, Anticorruption Unit</td>
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<td>OAGI</td>
<td>Office of the Auditor General, Integrity Division</td>
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<td>OAI</td>
<td>Office of Anticorruption and Integrity</td>
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<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>RRP</td>
<td>report and recommendation of the President</td>
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<td>PSOD</td>
<td>Private Sector Operations Department</td>
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<td>PSTS</td>
<td>Private Sector Transaction Support Division</td>
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<tr>
<td>TA</td>
<td>technical assistance</td>
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<td>UN</td>
<td>United Nations</td>
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In preparing any country program or strategy, financing any project, or by making any designation of or reference to a particular territory or geographic area in this document, the Asian Development Bank does not intend to make any judgments as to the legal or other status of any territory or area.
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I. INTRODUCTION

1. This paper sets out the proposed response of the Asian Development Bank (ADB) to global developments in relation to addressing tax secrecy, tax evasion, and legal forms of aggressive tax planning at both the country and project levels. These tax integrity issues are present and pressing global concerns. While these issues adversely affect both developed and developing countries, the effect of lost tax revenues on developing countries in Asia is comparatively more severe.\(^1\)

2. In ADB's nonsovereign operations,\(^2\) tax integrity issues may arise whether the shareholding structure is onshore (where the project is located) or offshore (in another jurisdiction). Tax integrity issues arise primarily, but not exclusively, through the use of offshore jurisdictions and cross-border structures. ADB acknowledges that there are numerous legitimate reasons for the use of structures involving offshore jurisdictions,\(^3\) including tax optimization to eliminate double taxation on income and profits, as well as other operational, management, and administrative efficiencies and flexibility, especially where structures involve multiple international investors in numerous jurisdictions. However, ADB also recognizes that offshore structures may pose higher risks because they have greater potential to obscure beneficial ownership and sources of funds. Therefore, offshore structures can more easily facilitate corruption, tax evasion, money laundering, financing of terrorism, and other illicit purposes.

3. The post-2015 development agenda\(^4\) has recognized that domestic resource mobilization is essential to provide governments with sustainable revenue resources to finance

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\(^2\) Nonsovereign operations comprise the provision of any loan, guarantee, equity investment, or other financing arrangement to privately held, state-owned, or subsovereign entities, in each case, (i) without a government guarantee; or (ii) with a government guarantee, under terms that do not allow ADB, upon default by the guarantor, to accelerate, suspend, or cancel any other loan or guarantee between ADB and the related sovereign entity.

\(^3\) Offshore jurisdictions may be referred to as “offshore financial centers,” which refers to jurisdictions that have certain characteristics such as (i) financial centers where a large number of banking activities are performed with nonresident counterparts, (ii) assets and liabilities of the financial system exceeding the needs of the domestic markets, and (iii) specific advantages in relation to taxation or banking secrecy provided. (IMF. 2000. Offshore Financial Centers: *IMF Background Paper*. http://www.imf.org/external/np/mae/oshore/2000/eng/back.htm.)

\(^4\) The Post-2015 Development Agenda is an ambitious global vision that seeks to tackle extreme poverty, curb climate change, and put the world on a more prosperous and sustainable path by 2030. It includes the following four key components: (i) The Declaration - a vision statement of what we want to achieve in the next development agenda; (ii) Goals and Targets – a new set of goals and targets to build on and succeed the MDGs; (iii) Financing and the Means of Implementation – the “how” of delivering the Post-2015 Development Agenda; and (iv) Monitoring and Review – defining a process to track progress on commitments made by all stakeholders. http://www.unfoundation.org/what-we-do/working-with-the-un/post-2015-development-agenda/?referrer=https://www.google.com.ph/
the Sustainable Development Goals.\(^5\) It calls for developing countries to strengthen their tax systems, reduce illicit financial flows, and tackle corruption as pressing development priorities.\(^6\) These measures are crucial to meet the financial needs of the post-2015 Development Agenda. ADB recognizes that capacity constraints impede improvements in domestic revenue systems. ADB is well-placed to help its developing member countries (DMCs) address capacity constraints in tax integrity as part of wider support for domestic revenue mobilization. Such assistance will need to take into account the rapidly developing international tax landscape.

### II. GLOBAL DEVELOPMENTS

4. The global landscape has changed significantly since 2009 as tax secrecy has given way to increasingly strong tax transparency to combat tax evasion. Tremendous progress has been achieved by the widespread implementation of the international tax standard for exchange of information on request (EOIR),\(^7\) as well as the strong momentum toward universal acceptance of the standard for automatic exchange of information (AEOI).\(^8\) Together, these two complementary tax standards\(^9\) will substantially improve the ability of tax authorities to detect tax evasion and ensure that their tax laws are being properly applied. The Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum),\(^10\) through its assessments and peer review process, is promoting both standards.\(^11\) For many jurisdictions (unless they have a sufficiently large treaty network), the Organisation for Economic Co-operation and Development (OECD) considers joining the Multilateral Convention on Mutual Administrative Assistance in Tax Matters the only practical route to implementing the international standards, especially for AEOI.\(^12\)

5. Jurisdictions, particularly developing ones, face significant resource and capacity challenges in implementing AEOI. All jurisdictions must (i) enact legislation to facilitate AEOI in


\(^8\) EOIR is found in Article 26 of the OECD Model Tax Convention on Income and on Capital as well as the United Nations Model Double Taxation Convention between Developed and Developing Countries. It requires a tax authority to provide, on request, “foreseeably relevant information” for the administration or enforcement of the domestic tax laws of another tax authority.

\(^9\) AEOI requires tax authorities to disclose financial account information of nonresidents with the tax authorities of the account holders’ country of residence automatically under the globally agreed common reporting standard. Thus, tax authorities will send and receive pre-agreed information each year without having to send a specific request.

\(^10\) The fundamental limitation of EOIR is that the tax authority requesting the information must know enough to make the request and approach the appropriate counterpart jurisdiction. This may not always be the case. However, when AEOI is globally implemented, information brought to light by AEOI may give tax authorities the information they need to enable them to make targeted information requests under EOIR.

\(^11\) The Global Forum is the largest tax body in the world. Its mandate is to counter tax evasion by increasing (i) global tax transparency; (ii) international cooperation; and (iii) the transparency of corporate bodies, arrangements, and financial information.

\(^12\) Currently, 106 jurisdictions participate in the convention, including 15 jurisdictions covered by territorial extension.
accordance with the agreed timetable, and (ii) satisfy confidentiality and data safeguard requirements before another jurisdiction is obliged to disclose to any such jurisdiction any information under AEOI. Once implemented, developing jurisdictions will require more capacity and resources to enable them to fully use the information they receive under AEOI, as well as to make requests of other jurisdictions under EOIR. In short, developing jurisdictions require assistance both to implement and benefit from AEOI.

6. In light of these challenges, questions remain on the continued progress of the global tax transparency agenda, including whether jurisdictions will be able to enact the required legislation and satisfy confidentiality and data safeguard requirements within the required timescale and, if they are able to do so, how effectively such jurisdictions will implement AEOI.

7. Initiatives to reduce opportunities for legal forms of aggressive tax planning by multinational corporations are also transforming the global tax landscape. Such tax planning exploits gaps and mismatches in tax rules to make profits “disappear” for tax purposes, or shifts profits to locations where there is little or no real activity but taxes are low, resulting in little or no overall corporate tax being paid. This form of planning is referred to as base erosion and profit shifting (BEPS), which depletes the tax resources of governments, distorts competition, and (together with tax evasion) undermines the authority and effectiveness of domestic revenue systems and governments. Thus, countering BEPS is not simply a question of raising revenue. It is also about designing a tax system that promotes inclusiveness, encourages good governance, supports investments and job creation, matches society’s views on reducing inequality, and advances social justice. This is particularly relevant in developing Asia where many economies have low tax collection rates, usually 20% gross domestic product or lower.

8. The OECD spearheaded an internationally coordinated and comprehensive reform of international tax rules to counter BEPS in the form of an action plan. The plan requires and/or encourages governments to introduce substantive measures into domestic law to increase tax transparency and curtail the ability of multinational corporations to implement BEPS. Developing jurisdictions struggling to fight against the erosion of their domestic tax base can benefit from the BEPS action plan with the support of international and regional organizations. Many developing jurisdictions are seeking technical assistance (TA) in this area.

13 As of July 2016, 101 jurisdictions had committed to implement the AEOI standard in 2017 or 2018.
14 The Group of Eight (G8) has stated that “developing countries should have the information and capacity to collect the taxes owed to them—and other countries have a duty to help them.” G8 Lough Erne Declaration, 18 June 2013.
15 The OECD recognizes that low or non-taxation is not itself of concern but becomes a concern when it is achieved by practices that artificially separate taxable income from the activities that generate it.
16 The OECD estimates that 4%-10% of global corporate income tax (totaling $100–$240 billion annually) is lost through BEPS.
18 OECD. 2013. Action Plan on Base Erosion and Profit Shifting. https://www.oecd.orgctp/BEPSActionPlan.pdf. The BEPS action plan equips governments with the domestic and international instruments needed to tackle BEPS. It provides countries with tools to ensure that profits are taxed where economic activities generating the profits are performed and where value is created. These tools also give businesses greater certainty by reducing disputes over the application of international tax rules and standardizing compliance requirements. http://www.oecd.orgctp/beps-about.htm
19 According to the Addis Tax Initiative (footnote 29), developing countries are seeking TA to boost their tax collection, improve their domestic tax compliance, and strengthen tools and procedures to stem both cross-border and domestic tax evasion and avoidance.
9. In 2016, the OECD established a new inclusive framework to (i) monitor and support implementation of the BEPS action plan; (ii) review progress on the implementation of the BEPS measures, particularly the minimum standards in the BEPS action plan; and (iii) complete remaining technical work related to BEPS. The United Nations (UN), the International Monetary Fund (IMF), and the World Bank Group are involved in promoting BEPS measures and, together with the OECD, have established the Platform for Collaboration on Tax to better support governments in addressing tax challenges, including BEPS. The platform will develop tool kits to (i) translate certain complex BEPS measures into user-friendly guidance for low-capacity countries, and (ii) address international tax issues not included in the BEPS action plan that may be more relevant for developing countries.

10. Concerted efforts are being made to achieve the global implementation of the BEPS action plan. While certain BEPS measures (such as transparency initiatives and the model treaty-based agreements) are likely to be implemented globally in a short time, questions remain on how other BEPS measures will be enacted and whether such rules will produce a largely consistent international regime—or will be fragmented along national lines.

11. The challenges for ADB’s DMCs in responding to these global developments are evident:

   (i) As of October 2016, 25 DMCs are not members of the Global Forum. Such DMCs have not committed to promote international tax transparency and cooperation or agreed to adopt and be assessed by EOIR.

   (ii) DMCs assessed by the Global Forum may find it challenging to comply with EOIR because

      (a) a huge increase in the number of requests for information was received and is forecast to continue, which may impact the ability of tax authorities (particularly those in smaller, under-resourced, developing jurisdictions) to respond in a timely manner; and

      (b) the Global Forum’s next round of reviews (commencing late 2016) will require jurisdictions to implement legislation requiring the disclosure of beneficial ownership information, which even large and well-resourced members may find challenging to implement effectively within the required timescale.

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20 In July 2015, the UN Third International Conference on Financing for Development issued the Addis Ababa Action Agenda, which commits countries to substantially reduce illicit financial flows by 2030 by combating tax evasion and corruption, reducing opportunities for aggressive tax avoidance, and scaling up international tax cooperation. The Addis Tax Initiative was issued by 36 conference participants (footnote 29).

21 BEPS tax transparency measures comprise country-by-country reporting and mandatory disclosure of private tax rulings. Country-by-country reporting is intended to give tax administrations a picture of where multinational corporation profits are reported and where real activity takes place. Mandatory disclosure of private tax rulings is intended to ensure that low or no tax jurisdictions do not provide arrangements that approach non-taxation to multinational corporations without other jurisdictions being aware of these arrangements.

22 Model treaty-based agreements apply to treaty abuse, permanent establishment rules, and certain aspects of hybrid mismatch arrangements.

23 For example, national implementation is likely to vary widely in relation to transfer pricing and the controlled foreign company rule.

24 Participating jurisdictions will be entitled to make requests of other jurisdictions under EOIR. Membership of the Global Forum also entitles jurisdictions to benefit from assistance provided by the Global Forum to enable such jurisdictions to implement EOIR.
12. As an international financial institution (IFI) with a mandate to foster the economic growth, cooperation, and development of its DMCs, ADB recognizes the need to strengthen its assistance to DMCs in stemming tax evasion and the erosion of their domestic tax bases. ADB will fulfill this role primarily by increasing TA to enhance the capacity and regional cooperation of tax authorities in order to enable DMCs to meet these challenges. ADB is committed to increasing its support for tax integrity initiatives in DMCs and adopting a multiyear effort for this work to implement the areas of TA operations (Appendix 2).

13. Among other things, with this policy update, ADB will increase its support for tax integrity initiatives in DMCs, with the aim of helping them (i) broaden and protect their domestic tax base, (ii) enhance the capacity of their tax administrations, (iii) improve domestic tax compliance, and (iv) improve tools and procedures to stem both cross-border and domestic tax evasion and avoidance. Thus, ADB’s objective is to build upon and develop the TA program it has already undertaken (Appendix 2).

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25 Jurisdictions that have committed to implement AEOI are expected to join the convention (if they have not already done so), because this is the most practical way to implement AEOI (para. 4).
27 Jurisdictions are required to commit to implement certain standards in specified key areas, which must be implemented in totality (such as country-by-country reporting and treaty abuse), but have discretion as to the extent to which they wish to implement other measures (such as the guidance for the application of transfer pricing rules and provisions to eliminate the “mismatch” effect of hybrid arrangements). Developing jurisdictions may consider that, while they face the same challenges as developed jurisdictions, their priorities and requirements differ.
28 As noted in para. 9, the platform (established by the UN, IMF, World Bank Group, and OECD) recognizes the particular challenges faced by developing countries when addressing BEPS issues.
14. ADB supports leading organizations working in this area and participates as an observer in the Global Forum. ADB welcomes the Addis Tax Initiative and collaborates with development partners to achieve the objectives of the initiative.  

Pursuant to ADB’s policy on combating money laundering and the financing of terrorism (AML Policy), ADB also commits to strengthen its cooperation with the Financial Action Task Force (FATF). ADB’s Sustainable Development and Climate Change Department is in coordination with the platform leaders, who coordinate their activities and share information with regional tax organizations and IFIs.

15. At the project level, ADB is committed to conduct due diligence to obtain reasonable assurance that the projects it finances do not facilitate tax evasion. While ADB recognizes that its role in relation to BEPS issues is primarily at the country level, since taxation issues are within the sovereignty of its DMCs, ADB will take steps to ensure that the projects in which it invests do not involve material related-party contracts that inappropriately transfer income to a group company or related persons and entities in an offshore jurisdiction (para. 28 v).

16. In addressing tax integrity issues as described in this paper, ADB seeks to demonstrate in a practical and effective way its support for and promotion of global tax integrity.

IV. ADB’S EXISTING APPROACH TO TAX INTEGRITY

17. ADB’s provision of recent TA to its DMCs is detailed in Appendix 1.

18. ADB adopts a risk-based approach to assessing integrity risks, including tax evasion. This approach, which is in line with international best practices, means that project teams are required to focus their efforts on projects where integrity and reputational risks to ADB are significant, while limiting their integrity checks where integrity and reputational risks are considered to be low. A risk-based approach means ADB will always assess risks and determine the extent to which they can be mitigated. If perceptions of risk change, a risk-based approach requires internal processes to be modified to take this into account. It is thus a dynamic and proportionate approach to addressing risk.

19. ADB’s existing risk-based approach means that project teams are required to (i) seek to identify the ultimate beneficial owners of ADB’s client; and (ii) satisfy themselves regarding the transparency of the clients’ shareholding structure, the business reasons for any complex ownership structure, and the use of offshore jurisdictions in the shareholding structure. Adopting a risk-based approach also requires ADB to (i) take into account the ratings of relevant jurisdictions provided by lead organizations (e.g., Global Forum, FATF, and the UN),

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29 The Addis Tax Initiative was launched at the 2015 Finance for Development Conference (footnote 19). It is designed to dramatically increase donor support for building tax capacity in poorer countries, step up domestic resource mobilization, and promote policy coherence.


31 The FATF recommendations include tax evasion as a predicate offense for money laundering and the FATF standard for disclosure of beneficial ownership information represents the international standard adopted by the Global Forum.

32 See for example the FATF recommendations, which adopt a risk-based approach.

33 ADB’s internal procedures for the conduct of integrity due diligence (IDD) have been regularly updated since 2012 to take account of lessons learned and IFI best practices.
international sanctions, and considerations of violations of law (including tax laws); and (ii) disclose relevant information to ADB’s Board of Directors.

20. ADB’s risk-based approach seeks to address the risks identified in each project, including secrecy risks associated with the use of offshore jurisdictions. It does not automatically prevent ADB from considering a project because a jurisdiction involved in the project was given a certain rating or classification by a lead organization. However, if ADB’s risk assessment identifies integrity concerns (which could relate to any of the issues mentioned in para. 19), ADB will only proceed once it is satisfied that the risks have been appropriately mitigated.  

21. ADB considers its risk-based approach to assessing integrity risks (including tax evasion) to be appropriate since, as an IFI, ADB seeks to manage its relationships with any members that are noncompliant with international standards. At the project level, ADB seeks to address and mitigate risk, rather than to “de-risk,” by conducting due diligence and being satisfied that the risks of proceeding with the project and sponsors in question are acceptable.

22. However, in light of global developments promoting tax transparency and addressing aggressive tax planning, ADB recognizes that its existing approach to addressing tax secrecy and tax evasion needs to be strengthened. ADB’s approach must evolve to reflect lessons learned and future global developments. As such, it is timely for ADB to set out the principles it will follow when addressing tax integrity issues (Tax Integrity Principles).

V. PROPOSED UPDATE

23. ADB proposes to update its Anticorruption Policy (1998, as amended to date) to take into account issues of tax integrity at the country and project levels.

24. The rationale for updating ADB’s Anticorruption Policy is as follows:
(i) ADB is mandated to support competitive markets and efficient, accountable, and transparent public administration as part of its broader work on good governance and capacity building.
(ii) A lack of tax integrity and a culture of low tax compliance increase the risk of corruption. Corruption, money laundering, and financing of terrorism damage financial sector institutions and—together with tax evasion and aggressive forms of tax planning—(a) distort competitive markets; (b) hinder efficient, accountable, and transparent public administration; and (c) adversely impact the domestic resources of DMCs.
(iii) ADB is mandated to seek to ensure that projects financed and administered by ADB comply with the highest ethical standards and are not used for the

34 For example, if a jurisdiction’s disclosure of beneficial ownership information raises concerns at a country level, ADB will satisfy itself in this regard at a project level (para. 19).
35 De-risking refers to the phenomenon of financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk. De-risking is contrary to the FATF’s risk-based approach.
36 See para. 28.
37 The Anticorruption Policy is implemented in accordance with ADB’s Integrity Principles and Guidelines 2015, as amended from time to time (Appendix 4). This update to the Anticorruption Policy is intended to address tax integrity issues and is not intended to be a comprehensive review of the implementation of the Anticorruption Policy.
38 Anticorruption Policy, para. 14 (i).
39 Anticorruption Policy, para. 14 (iii).
purposes of corruption, tax evasion, money laundering, financing of terrorism, or other illicit purposes. A lack of tax transparency at the project level increases the risk of tax evasion, corruption, money laundering, and financing of terrorism.

25. As with previous updates to the Anticorruption Policy, no changes will be made to the existing provisions of the Anticorruption Policy.

26. The update to ADB's Anticorruption Policy will complement AML Policy. A key element of ADB's AML Policy is to help DMCs implement effective systems to combat money laundering and the financing of terrorism. Under the AML Policy, ADB also adopts the FATF recommendations to guide ADB operations. Through the AML Policy, ADB recognizes its role in assisting international efforts to protect the international financial system against money laundering and the financing of terrorism at both country and operational levels. ADB reflects this mandate by (among other things) taking into account in its nonsovereign operations the risks posed by jurisdictions identified by FATF as having strategic money laundering or financing of terrorism deficiencies.

27. ADB recognizes that, while pursuing its vision of an Asia and Pacific region free of poverty, it has a role to play not only in global efforts to combat money laundering and the financing of terrorism, but also in promoting global tax integrity. Therefore, ADB proposes the following:

(i) ADB will adopt the Tax Integrity Principles, approach, and recommendations contained in this document as a policy paper and as a Management directive in the form of staff instructions.

(ii) ADB will support and promote international tax integrity, including the work of lead organizations such as the Global Forum, FATF, and the UN in this area.

(iii) ADB will support tax integrity initiatives in Asia and the Pacific by increasing TA operations that (a) assist DMCs in promoting their domestic resource mobilization by enhancing their ability to protect themselves against tax evasion and BEPS, (b) develop the capacity of DMCs to become members of and participate in the work of the Global Forum, and (c) support DMC participation in BEPS initiatives promoted by lead organizations.

(iv) ADB will encourage the inclusion of tax integrity issues in the policy dialogue with DMCs, where necessary and appropriate, particularly when DMCs request ADB's assistance in this area. In such cases, these issues should be explicitly

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41 ADB's response to tax evasion and BEPS issues will be addressed in an update to ADB's Anticorruption Policy for the reasons set out in para. 24. This does not imply that legal forms of tax planning by multinational corporations constitute illegal activity or corruption.

42 Footnote 30, para 63.

43 Footnote 30, para. 70.

44 For clarity, "document" includes the main text and the appendices.

45 In determining appropriate TA, ADB will consider (i) the DMC's request; (ii) ADB's relative strengths and focus areas; (iii) existing support provided by development partners, including lead organizations or other international financial institutions; and (iv) latest development in the international tax landscape. The Office of Anticorruption and Integrity (OAI) and the Sustainable Development and Climate Change Department (SDCC) will cooperate and coordinate with other ADB departments to ensure that there will be no duplication of TA assistance, and that ADB's TAs will be targeted to complement any TA provided by such development partners. ADB will advise DMCs of the availability of TA through policy dialogue, including during discussions on country partnership strategies.
incorporated into country partnership strategies and their updates, country operations business plans, regional cooperation strategies and programs, and relevant sector and aid agency consultations.

28. ADB’s Tax Integrity Principles, which reflect a risk-based as well as a prohibitive approach, are as follows:

(i) ADB seeks to obtain reasonable assurance that each transaction it finances does not facilitate tax secrecy, tax evasion, and tax fraud. If ADB cannot obtain such reasonable assurance, it will not finance the transaction.

(ii) ADB carries out enhanced vigilance where ADB’s client or its significant shareholders are established in an intermediate jurisdiction.\(^{46}\)

(iii) Where an intermediate jurisdiction is a jurisdiction of concern,\(^{47}\) ADB ascertains from its client the sound business reasons for the use of each intermediate jurisdiction. If ADB cannot obtain reasonable assurance of tax transparency, ADB will not finance the transaction.

(iv) If ADB’s client is either established in, or controlled by an entity established in, an intermediate jurisdiction classified as noncompliant by the Global Forum for EOI, additional safeguards will apply. ADB will not finance such a transaction unless (a) it has conducted enhanced tax integrity due diligence (IDD) to ascertain that the tax integrity risks are low and acceptable to ADB; and (b) ADB is satisfied that there is a sound business or policy objective for financing the transaction that should take priority over the rationale for not financing. If either of these two conditions is not fulfilled, ADB will not finance the transaction.\(^{48}\)

(v) Material related party contracts under which ADB’s client makes excessive payments to an offshore related party (typically in a no-tax or low-tax jurisdiction) may inappropriately transfer assets out of its DMCs. ADB seeks to obtain reasonable assurance that each transaction it finances does not facilitate such an unacceptable tax integrity practice.

(vi) ADB discloses tax integrity and other significant integrity risks to the Board of Directors in an integrity appendix to be attached to each report and recommendation of the President (RRP) for nonsovereign operations, cleared by the Office of Anticorruption and Integrity (OAI).\(^{49}\)

(vii) ADB addresses tax integrity issues during project approval.

(viii) ADB requires tax integrity provisions to be addressed, as appropriate, in legal documents.

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\(^{46}\) ADB will adopt a broad definition of an intermediate jurisdiction in its operational procedures. The definition will include the jurisdiction in which ADB’s client is established if this is not the project host country. When considering an ultimate beneficial owner of ADB’s client, an intermediate jurisdiction will comprise each jurisdiction where a shareholder of ADB’s client is established, excluding the project host country and the jurisdiction of the ultimate beneficial owner.

\(^{47}\) A jurisdiction of concern will be described in ADB’s operational procedures. It will cover an intermediate jurisdiction that (i) has not been assessed by the Global Forum in relation to EOI, (ii) is not rated as either compliant or largely compliant by the Global Forum for EOI, (iii) is listed as an uncooperative jurisdiction by the OECD (when its list of uncooperative jurisdictions is published), and (iv) has a poor rating for the implementation of AEOI (when such ratings are published).

\(^{48}\) A compelling business or policy objective alone cannot justify ADB financing the transaction, unless the tax integrity risks are also low and acceptable to ADB. ADB considers this deterrent necessary given the risks and lack of transparency associated with noncompliant jurisdictions. ADB would only conclude that a business or policy objective should take priority over the rationale for not financing in an exceptional case.

\(^{49}\) The integrity appendix will be a linked document to the RRP. References to an RRP also refer to a report to the President.
29. ADB will implement the Tax Integrity Principles by adopting new internal procedures, which are summarized in Appendix 3. Unlike the Tax Integrity Principles, ADB may revise or supplement the internal procedures at an operational level from time to time to reflect, among other things, changes in the global tax environment. Any changes made to the internal procedures described in Appendix 3 will be reported to the Board at each review of the implementation of this policy.  

30. With the objective of ensuring that ADB’s internal procedures in relation to tax integrity remain up to date, ADB proposes the following:
   (i) To ensure that tax integrity issues are addressed at each key project processing stage, ADB will update its internal procedures on IDD to incorporate the Tax Integrity Principles, its approach to implementing the Tax Integrity Principles (as summarized in Appendix 3), and any consequential revisions to ADB’s internal processes and templates.
   (ii) ADB will update its internal procedures on IDD to incorporate any revisions thereto that may be recommended upon the conclusion of the tax expert’s review (para. 31 iv).
   (iii) ADB will update its internal procedures on IDD, as required thereafter, to take into account global developments and lessons learned, and to adopt appropriate approaches and strengthen its ability to identify and mitigate tax integrity risks.
   (iv) ADB will allocate the resource needs as will be described in paras. 32–40.

31. ADB also proposes the following measures for departments and offices:
   (i) OAI will change ADB’s internal procedures for IDD as required to implement the Tax Integrity Principles (para. 28), including clearing the integrity appendix to be attached to each RRP for nonsovereign operations.
   (ii) OAI and the Budget, Personnel, and Management Systems Department will collaborate in providing training in tax integrity due diligence to staff involved in nonsovereign operations, financial analysts, and project implementation officers.
   (iii) OAI and staff involved in nonsovereign operations will keep up with the latest developments and maintain working contacts with multilateral and bilateral agencies engaged in tax integrity issues by participating in meetings and workshops of key organizations and agencies such as the Global Forum, OECD, and the UN.
   (iv) OAI, the Private Sector Operations Department (PSOD), and departments involved in nonsovereign operations will strengthen their understanding on the indicators of tax evasion and BEPS issues that are relevant for ADB’s nonsovereign operations (such as material related party contracts) by engaging (a) an international tax expert to assess ADB’s exposure to such issues in PSOD’s portfolio, recommend ways to mitigate such concerns, advise on best practices to obtain assurance of tax transparency in different project structures, and strengthen ADB’s IDD procedures where gaps are identified; and (b) an international tax expert to provide ongoing tax integrity advice to PSOD and other departments involved in nonsovereign operations, as required.

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50 Also para. 31(v).
51 Revisions will be required to (i) ADB’s procedures for the general conduct of IDD for nonsovereign operations; (ii) ADB’s staff instructions in relation to credit and other processes for nonsovereign operations; and (iii) ADB’s document templates, including the RRP.
(v) OAI will monitor the implementation of the policies contained in this paper, including the design and implementation of the TA operations described in Appendix 2, and will report to the Board of Directors 1 year after the policy becomes effective and thereafter after every 3 years or as appropriate, in light of international developments.

VI. RESOURCES

32. To properly implement the tax due diligence required under the proposed policy, ADB will need to supplement OAI and PSOD staff resources. The additional resource allocations anticipated in this paper take into account that ADB previously allocated considerable staff resources for IDD.

A. Office of Anticorruption and Integrity

33. In 2016, ADB allocated to OAI one additional national staff position for IDD. Upon approval of the policy, it is envisaged that resources to engage two tax experts (one international and one national consultant) will be required. OAI will ascertain the most cost effective ways to ensure that it has appropriate access to tax integrity research and information, and also anticipates that a modest increase in administrative resources will be required for these purposes.

34. For 2018, it is anticipated that two additional staff positions (one international and one national) will be required, as well as a modest increase in administrative and consulting resources.

B. Private Sector Operations Department

35. Since PSOD has taken significant steps to improve its IDD processes and procedures, it is well on its way to establishing an efficient and targeted IDD unit that conducts targeted reviews of key risks. PSOD currently has two international positions (one is under recruitment) and 0.8 administrative positions allocated to IDD. PSOD’s IDD staff members are supported by 14 national consultants.

36. Nevertheless, the IDD outputs currently expected from the Private Sector Transaction Support Division (PSTS) will require more than the existing staff resources. The proposed policy changes will further stretch limited resources and require PSTS to engage specialized assistance to address tax transparency.

37. In 2017, PSTS seeks to enhance its staff resources by adding two national staff members to meet current and new task requirements. A modest increase in administrative resources to cover tax expert and retainer fees is also envisaged.

38. For 2018, two additional staff positions (one international and one national) may be required as well as an increase in administrative and consulting resources.

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52 While preliminary IDD is conducted by PSOD project officers on their projects, the Private Sector Transaction Support Division (PSTS) conducts searches, completes required checklists, and advises and supports the PSOD project officers throughout project processing and administration. PSTS shares one associate project analyst (0.5%) and one operations assistant (0.3%) with other units in PSOD.
C. Technical Assistance

39. Where assistance through TA is appropriate, TA resources will also be required. The decision on whether assistance should be provided through loans, TA loans, or TA grants will be judged taking into account the overall context of the DMC. 53

40. To enable ADB to increase country and regional support to DMCs through TA, ADB will require an increase in its TA allocation. Whether assistance should be provided through loans or grants will be judged taking into account the overall context of the DMC.

VII. REQUEST FOR BOARD APPROVAL

41. It is recommended that the Board approve the Proposed Update (Section V) and Resources (Section VI) as described in paras. 23–40.

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53 For 2016, ADB already received one request for assistance from a DMC with regard to membership of the Global Forum. Another DMC that is a member of the Global Forum requested assistance in relation to the peer review process.
EXISTING TECHNICAL ASSISTANCE TO DEVELOPING MEMBER COUNTRIES

1. Asian Development Bank (ADB) has undertaken a program of technical assistance (TA) to assist developing member countries (DMCs) in (i) combating money laundering and the financing of terrorism; and (ii) improving their tax collection capacity fairly and effectively through broadening and protecting their domestic tax base, enhancing the capacity of tax administrations, improving domestic tax compliance, and improving tools and procedures to stem both cross-border and domestic tax evasion and avoidance.

2. To enhance the capacity and regional cooperation of tax authorities in DMCs, ADB conducted the following regional conferences and training seminars on tax issues to identify challenges these authorities face:
   (ii) Fundamentals of Effective Exchange of Information (Phnom Penh, August 2015).
   (iii) Enhancing Effective Exchange of Information (Manila, September 2015).
   (iv) Detecting Cross-Border Tax Evasion (Tokyo, November 2015).
   (v) Tax Evasion: Investigation and Compliance Strategies (Tokyo, March 2016).

3. ADB, Organisation for Economic Co-operation and Development, and the Global Forum on Transparency and Exchange of Information for Tax Purposes jointly organized the following regional conferences on implementing exchange of information for tax purposes:
   (i) A Regional Training Seminar on Exchange of Information for Tax Purposes (Manila, September 2013).

4. ADB supported the following diagnostic assessments of the capacity of tax administrations to protect and increase tax revenues in DMCs and to identify key areas where capacity building and reform measures will be most effective:
   (i) Capacity development needs assessment for Cambodia, People’s Republic of China, Indonesia, Malaysia, Mongolia, Papua New Guinea, Philippines, Thailand and Viet Nam.
   (iv) Workshop on Revenue Statistics in Asia jointly organized with OECD (Seoul, October 2015).
ADB’S PROPOSED COVERAGE FOR TECHNICAL ASSISTANCE TO DEVELOPING MEMBER COUNTRIES

To increase its support for tax integrity initiatives in its developing member countries (DMCs), the Asian Development Bank (ADB) envisages providing additional technical assistance (TA) in the following areas:¹

(i) Develop capacity of DMCs to become members of and participate in the work of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum).²

(a) The TA would assist DMCs that need to improve their legislation, policies, and administrative practice in relation to the Global Forum’s standard for the exchange of information on request (EOIR). The focus of ADB’s TA will be DMCs that demonstrate their commitment either to join the Global Forum, to implement EOIR, and/or to improve their current Global Forum ratings.

(b) The TA would assist DMCs that wish to commit to the emerging standard for the automatic exchange of information (AEOI), or that have committed to do so in or before 2018, and that need to implement the necessary changes to their legislation, policies, and administrative practice to achieve such a commitment.

(ii) Promote domestic resource mobilization (DRM) in DMCs.³

ADB recognizes that tax and nontax revenue are essential components of DRM; and without effective mobilization of domestic resources, the Sustainable Development Goals cannot be achieved.⁴ ADB’s objective will therefore be to target its TA to address the many challenges confronting its DMCs when raising tax revenue, such as a difficult external environment and weak administrative capacity.⁵

ADB will aim to provide TA to assist DMCs in

(a) enhancing government approaches on anticorruption,⁶ and

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¹ The Office of Anticorruption and Integrity and the Sustainable Development and Climate Change Department will cooperate and coordinate with other ADB departments to ensure that there will be no duplication of TA assistance, and that ADB’s TA will be targeted to complement any TA provided by other development partners.
² ADB recently approved the concept note for $2 million for this purpose.
³ This discussion on DRM does not describe broader ADB initiatives on DRM. It does not limit ADB from providing support and assistance in other areas of DRM (e.g., improvements to tax policy, efficient tax administration, and procurement and state-owned enterprise reform) under ADB’s work on governance and public management.
⁶ OAI has existing anticorruption TA operations that will be used for this purpose. As of 15 November 2016, $470,000 was available for this purpose.
(b) improving tools and procedures to stem cross-border and domestic tax evasion.

(iii) Protect DMCs against Base Erosion and Profit Shifting (BEPS) and supporting DMC participation in BEPS initiatives.\(^7\)

Countering BEPS is not simply a question of raising revenue (main text, para. 7); it is about designing a tax system that promotes inclusiveness and encourages good governance. The TA would focus on DMCs that wish to participate in the BEPS inclusive framework to tackle BEPS. The TA will assist such DMCs in

(a) considering their priorities for addressing BEPS issues; the extent to which they should implement BEPS measures; and whether such DMCs are facing more pressing tax issues than those set out in the BEPS action plan;\(^8\) and

(b) strengthening the capacity of tax authorities to collect taxes by implementing the legislative and other changes required by DMCs to adopt BEPS measures within their legal and regulatory tax frameworks.

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\(^7\) ADB has approved the concept note and $1 million for this purpose.

\(^8\) While jurisdictions are required to commit to implementing certain standards in specified key areas, which must be implemented in totality (such as country-by-country reporting and treaty abuse), they have discretion as to the extent to which they wish to implement other measures (such as the guidance for the application of transfer pricing rules and provisions to eliminate the “mismatch” effect of hybrid arrangements). Developing jurisdictions may consider that, while they face the same challenges as developed jurisdictions, their priorities and requirements differ.
ABD’S INTERNAL PROCEDURES FOR IMPLEMENTING
THE TAX INTEGRITY PRINCIPLES

The following illustrates how the Asian Development Bank (ADB) will implement the Tax Integrity Principles.¹

1. Reasonable assurance that ADB’s financing does not facilitate tax secrecy, tax evasion, and tax fraud

(i) At a project level and as part of ADB’s general integrity due diligence (IDD), ADB seeks to ascertain the ultimate beneficial owners (UBOs) of ADB’s client. For the purposes of this appendix, ADB’s client includes, in the case of an ADB investment in a private equity fund, the general partner and fund manager, as well as any carry vehicle.

(ii) ADB assesses public disclosures in relation to ADB’s client, its shareholders (including UBOs), and key persons and entities involved in the proposed transaction to ascertain whether tax integrity issues arise in relation to such entities and persons.

(iii) When assessing tax integrity risks, ADB considers the Exchange of Information on Request (EOIR) ratings of the project host country and intermediate jurisdictions issued by the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum), and considers whether such jurisdiction has committed to implement the Automatic Exchange of Information (AEOI) in (or before) 2018. ADB will consider the list of uncooperative jurisdictions to be published by the Organisation for Economic Co-operation and Development (OECD); and will also consider any ratings issued by the Global Forum in relation to AEOI (anticipated after 2018).

(iv) ADB recognizes the greater tax integrity risks posed by transactions involving intermediate jurisdictions.²

2. Where there are intermediate jurisdictions

(i) ADB carries out tax IDD on ADB’s client if it is established in an intermediate jurisdiction and/or on any significant shareholders of ADB’s client that are established in an intermediate jurisdiction.³

(ii) The objective of this tax IDD is to consider whether the ownership structure of ADB’s client is transparent.

(iii) Indicators of transparency are described in paragraph 1(iii).

3. Where there are intermediate jurisdictions of concern

(i) ADB requires enhanced tax IDD to be carried out if ADB’s client or any of its significant shareholders is established in an intermediate jurisdiction that (a) has not been assessed by the Global Forum in relation to EOIR, (b) is not rated as

¹ This is a summary and is not intended to be exhaustive.
² ADB acknowledges that, while there are numerous legitimate reasons for the use of intermediate jurisdictions, their use may pose higher risks because they provide greater potential to obscure beneficial ownership and sources of funds, and thereby facilitate corruption, tax evasion, money laundering, financing of terrorism, and other illicit purposes (main text, para. 2).
³ ADB recognizes that it is not always feasible to identify—and therefore to carry out tax or other IDD on—all shareholders. ADB discloses unidentified ownership to its Board of Directors in the report and recommendation of the President with an explanation of the reasons why ADB is comfortable proceeding in the absence of such information.
either compliant or largely compliant by the Global Forum for EOIR, (c) is listed as an uncooperative jurisdiction by the OECD (when its list of uncooperative jurisdictions is published), or (d) has a poor rating for the implementation of AEOI (when such ratings are published).

(ii) ADB will adjust the indicators of high tax risk that trigger enhanced IDD according to the changing global tax transparency environment. For example, when AEOI is implemented, some indicators of high risk may need to be revised to focus on instances where AEOI does not apply.

(iii) If a proposed transaction is within paragraph 3(i), ADB’s client will be required to explain to ADB the sound business reasons for the use of any entity in its shareholding structure in an intermediate jurisdiction (this assessment will not be limited to the intermediate jurisdiction/s of concern).

(iv) Sound business reasons will vary from transaction to transaction and may include the following:

(a) establishing a common investment vehicle in a stable, investor-friendly jurisdiction that (where investors are of different nationalities) also provides a neutral platform for the investment (thereby attracting capital from numerous sources);
(b) establishing a common investment vehicle in a jurisdiction with a robust legal system that recognizes and enforces investment agreements and the creation and enforcement of security; and
(c) the lawful avoidance of double taxation, but will not include aggressive means of tax planning referred to in para. 5.

4. Noncompliant intermediate jurisdictions

(i) If ADB’s client is either established in, or controlled by an entity established in, an intermediate jurisdiction classified as noncompliant for EOIR by the Global Forum, ADB will not finance such a transaction unless (a) ADB is satisfied that there is a sound business or policy objective for ADB to finance the transaction that should take priority over the rationale for not financing, and (b) ADB has conducted enhanced tax IDD to ascertain that the tax integrity risks are low and acceptable to ADB.

(ii) An example of a sound business or policy objective justifying ADB’s decision to finance the transaction might be that no other entity is operating in the relevant sector or jurisdiction, and if the transaction does not proceed, valuable developmental outcomes could not be achieved, thereby thwarting ADB’s development mandate.

5. Material related party contracts

ADB will review and assess material related-party contracts from an integrity perspective, to ensure they are entered into on an arm’s length basis, consistent with the current practice of the Private Sector Operations Department (PSOD) relating to material related-party contracts in its commercial due diligence.
6. **Reporting to the Board of Directors**
   (i) ADB discloses integrity issues to the Board of Directors in an appendix to the report and recommendation of the President (RRP) for nonsovereign operations; the Office of Anticorruption and Integrity must clear this appendix.
   (ii) The appendix shall explain, in relation to the transaction under approval, whether tax IDD has been conducted and, if so, the outcome of such tax IDD.
   (iii) If para. 4 applies, the RRP will set out in detail the sound business or policy objective for ADB to finance the transaction that should take priority over the rationale for not financing the transaction. The appendix will explain the basis upon which ADB (having carried out enhanced tax IDD) has reasonable assurance that the tax integrity risks of the transaction are low and acceptable to ADB.

7. **Tax integrity during project approval**
   (i) Integrity (including tax integrity) issues should be addressed at each key project processing stage.
   (ii) Changes in the ADB client’s shareholding structure should be monitored during project administration.

8. **Legal documentation**

   ADB includes in its financing documents integrity representations, warranties, and covenants addressing issues such as fraud, corruption, money laundering, and the financing of terrorism. ADB should also include provisions on identified tax integrity risks where appropriate. A breach of any of these provisions should give rise to appropriate remedies for ADB.

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4 The integrity appendix is a linked document to the RRP. References to an RRP also refer to a report to the President.
ADB’S ANTICORRUPTION POLICY AND THE INTEGRITY PRINCIPLES AND GUIDELINES

1. The Anticorruption Policy (1998, as amended to date) designated the then Office of the General Auditor¹ as the initial point of contact for alleged incidents of corruption among Asian Development Bank (ADB) projects and staff, and instructed Office of the General Auditor to work out appropriate procedures for performing this function. The Anticorruption Policy provided for changes in the Procurement Guidelines and the Guidelines on the Use of Consultants, establishing the principle of declaration of ineligibility (sanctions)² along the same lines as the World Bank,³ i.e., allowing ADB to declare a firm or an individual ineligible (either indefinitely or for a stated period of time) to participate in ADB-financed activities if ADB determines that the firm or individual has engaged in corrupt and fraudulent practices in executing or competing for an ADB-financed contract.

2. In September 1999, ADB established an Anticorruption Unit (OAGA) within the Office of the Auditor General (OAG) to focus on activities relating to the implementation of the Anticorruption Policy and to handle matters related to such allegations.⁴

3. OAG’s investigation procedures were then governed by ADB’s Guidelines on Operational Procedures, Section 55 (GP 55) issued in July 2000. In conjunction with ADB’s revision of its Operations Manual in 2003, OAG revised its audit manual and incorporated anticorruption procedures into chapter 800. The procedures applying to ADB’s handling of allegations of fraud and corruption (GP 55) became obsolete upon ADB’s issuance of its new Operations Manual in 2003. In December 2003, the ADB President approved OAG’s new audit manual.

4. In November 2004, ADB’s Board of Directors approved the clarification of certain aspects of the Anticorruption Policy (primarily terms and definitions related to corruption and fraud) to address critical issues that affect OAGA’s activities and ability to assure and promote the ethical standards required by the Anticorruption Policy.⁵

5. In view of the Board approved policy update, in September 2005 ADB approved revised anticorruption investigation guidelines and procedures⁶, which incorporated Anticorruption Policy clarifications and the scope of work of the Integrity Division (OAGI).⁷ This replaces ADB’s anticorruption procedures (formerly chapter 800 of the audit manual).

6. In February 2006, the presidents of ADB, African Development Bank, European Bank for Reconstruction and Development, European Investment Bank, Inter-American Development Bank, International Monetary Fund, and the World Bank, recognizing that a unified and coordinated approach is critical to the success of a shared effort to fight corruption, agreed to establish a joint international financial institution (IFI) anticorruption task force to work toward a

¹ Later renamed to Office of the Auditor General (OAG).
² Debarments are also referred to as sanctions.
³ Anticorruption Policy. para. 60.
⁴ In December 2004, OAGA was upgraded to an Integrity Division (OAGI) with expanded functions to cope with the growth in volume and complexity in investigations of fraud and corruption.
⁷ In October 2009, OAGI became the Office of Anticorruption and Integrity (OAI) when the Integrity Division was separated from OAG.
A consistent and harmonized approach to combat fraud and corruption, including developing common principles and guidelines for investigations.

7. Following a recommendation by the task force to their respective institutions, ADB’s Board of Directors approved the harmonized definitions on fraudulent and corrupt practices in late 2006. In line with the Board approval of the harmonized definitions, the President, on 7 November 2006, approved the revised Integrity Principles and Guidelines, which incorporated the common principles and guidelines for investigations endorsed by the IFI task force.

8. The endorsement by the IFIs of common guidelines and principles laid the groundwork for the potential harmonization of other aspects of each IFI’s anticorruption efforts. To enable a coordinated approach among the IFIs and strengthen the fight against corruption, the IFIs signed the Agreement for Mutual Enforcement of Debarment Decisions in 2010. Under the agreement, entities sanctioned by one IFI may be ineligible to do business with another IFI. ADB revised implementing documents including the Integrity Principles and Guidelines, the Procurement Guidelines, and the Guidelines on the Use of Consultants to reflect the agreement.

9. The current Integrity Principles and Guidelines, which is consistent with the harmonized framework, contain provisions relating to the investigation process, sanctions, remedial actions for violations of the Anticorruption Policy, procedures for appeal and reinstatement, disclosure of sanctions, and cross debarment.

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10 As approved by the Board, the ADB President signed the agreement. ADB. 2010. *Anticorruption Policy: Harmonization of Debarments*. Manila.
12 Sanctions and remedial actions that may be imposed include debarments, reprimands, restitution and remedies, as well as cautions.