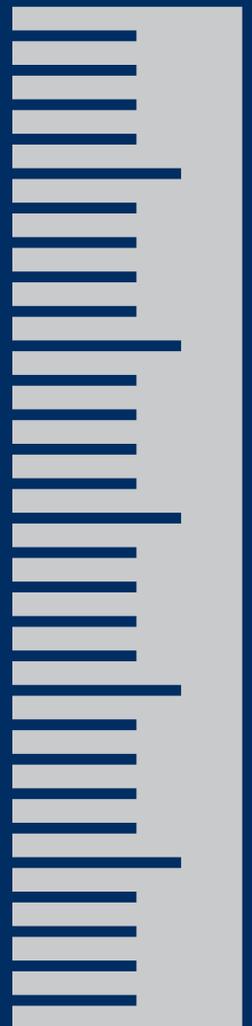


DEFENCE
COMPANIES
ANTI-
CORRUPTION
INDEX 2012



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Foreword



Corruption threatens all nations and companies. The issue increasingly dominates daily headlines and public debate around the world. Companies are often well aware of the financial, legal, and reputational consequences of corruption – fines, loss of public trust, reduction in stock price, blacklisting, and even prison. Yet, to the despair of many trustworthy people working in the sector, defence has maintained a reputation for dishonesty and corruption.

But there is also a major opportunity. Those defence companies that do take the subject seriously have the chance to be seen by their government clients as better companies with which to do business. As governments toughen their attitudes towards corruption, having a reputation for zero tolerance of corruption will be a distinguishing asset for a defence company. Ignoring both the risk and the opportunity is poor business strategy.

Collaborating with Transparency International UK's Defence and Security Programme since 2006, I launched the Common Industry Standards – an initiative that led to the first Europe-wide set of standards to tackle the practice of bribery among defence companies. This same initiative led to the creation in 2010 of IFBEC, a global defence industry forum for raising business conduct standards among defence companies. It is clear that there is an appetite for change in the industry.

With this ground-breaking study, Transparency International UK is encouraging companies to move a step further. This comprehensive analysis of the major defence companies from all over the world examines what systems and processes they have in place to prevent corruption, based on the information available. Its purpose is to raise standards globally, promote good practice in preventing corruption, and increase transparency in the sector. I very much hope that the industry responds to the challenge.

A handwritten signature in blue ink, which appears to read 'Lord Robertson'.

The Rt Hon Lord Robertson
of Port Ellen KT GCMG honFRSE PC,
Former Secretary General of NATO

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Executive Summary

The purpose of this study is to assist industry-wide improvement in reducing corruption in international defence sales.

www.defenceindex.org
www.ti-defence.org

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Corruption in defence is dangerous, divisive and wasteful.

The defence sector is crucial to a country's security, and yet has a reputation for secrecy and corruption. News stories about corruption in defence deals appear regularly in the news in many countries. This must change.

Corruption in defence is dangerous, divisive and wasteful. It puts international security at risk; it can lead to regional arms races to satisfy the greed of intermediaries; and billions can be wasted in dishonest arms deals. This reputation has a detrimental effect for companies and governments alike, much to the frustration of the many honest people working in it.

What the news stories often don't tell is what defence companies are – and are not – doing to combat corruption. At a time of increased scrutiny by governments and citizens alike, it is very much in a company's interest to prevent corruption, and how it does this will increasingly become a competitive advantage. This report looks into what defence companies currently do and fail to do to prevent corruption. The purpose is to assist in raising anti-corruption standards across a major sector that is global in nature yet whose business has historically been hidden from public view.

The 129 companies analysed in this study are those with the greatest defence revenue from the six largest arms exporting nations, plus the largest defence companies from a further twenty-five countries. Together, these companies account for over USD 500 billion of global defence revenue, and USD 11 trillion of total revenue.¹ The defence sector by nature is complex and diverse – companies in this index include traditional arms manufacturers as well as consultants, technology providers, logistics specialists and construction firms.

The companies are scored on 34 questions that inquire into the specifics of the ethics and anti-corruption systems they have in place. The information used to compile the Index is drawn from what companies disclose publicly on their websites about their anti-corruption systems.

Transparency International UK also invited all the companies to present evidence about their anti-corruption practices to supplement what could be found publicly. Thirty-four of the companies provided such information, sharing material from internal company sources. The report presents the results for these companies on the basis of both publicly available information and how they would have scored if they made public the additional internal evidence.

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Two thirds of defence companies do not provide adequate levels of transparency.

RESULTS BASED ON PUBLIC INFORMATION ONLY

Ten companies score in the top two bands. Fluor Corporation is the only company to score in Band A. In Band B are Accenture, BAE Systems, Fujitsu, Hewlett-Packard Company, Meggitt, Northrop Grumman Corporation, Serco Group, Thales, and United Technologies Corporation.

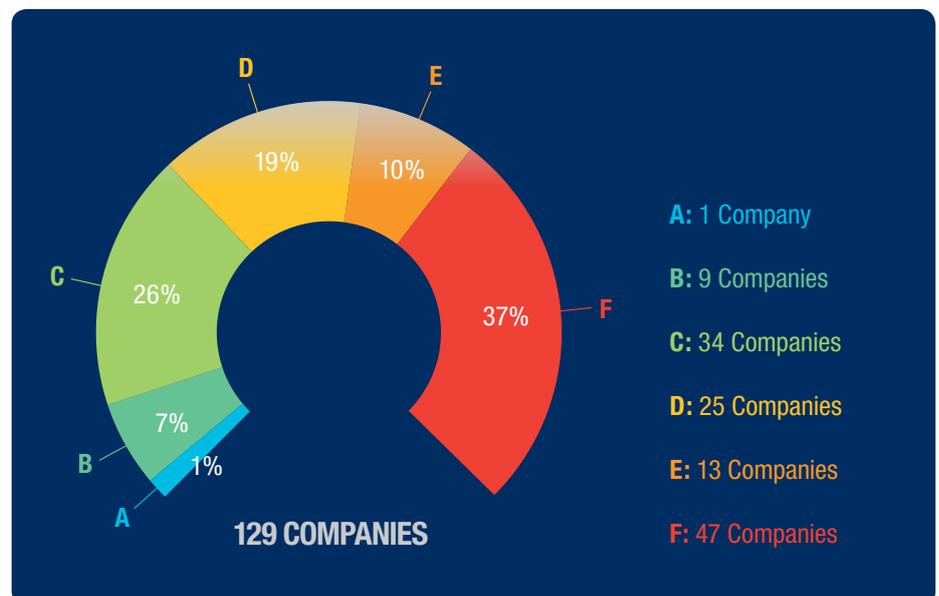
These companies publicly demonstrate in considerable detail the systems and procedures that they have in place to prevent corruption. This is to their credit, and demonstrates clearly that there is no confidentiality or secrecy barrier to good public disclosure about anti-corruption in the defence industry.

However, this group represents less than ten per cent of the companies studied. Two thirds of defence companies do not provide adequate levels of transparency. Almost half of the total – 60 out of 129 – provide very little evidence of having basic systems in place to prevent corruption and instil strong ethical values, scoring in Bands E and F. This includes companies from all the major arms exporting nations: USA, Russia, Germany, France, the UK and China.

RESULTS BASED ON BOTH INTERNAL AND PUBLIC INFORMATION

The thirty-four companies that provided internal information on their anti-corruption systems are predominantly companies that rank reasonably well on the basis of their public disclosure only: 28 of the 34 are in Bands A to C in the public-information ranking, with just six in Bands D and E.

The inclusion of company-internal information would have improved the company results on average by one to two bands, with almost half of the 34 moving up to Band A. The improvement is mostly due to additional disclosure in two specific areas: in how they assess the risk of corruption (e.g. in business decisions, in geographical scope, in particular product sectors), and in how they train staff on ethics and anti-corruption measures. There is little impact of internal information in respect of the three other areas – Leadership practices, Codes and policies, or Personnel practices.



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GOOD AND BAD PRACTICE

The detail of this study provides numerous examples of good practice from which all companies can learn. Several of them can serve as best practice across the defence sector as a whole. Perhaps the best practice of all, and the most convincing to us as a civil society organisation, is that there are defence companies who have instituted a practice of regular assessment of their total ethics and compliance programme by an independent organisation (such as a law or accountancy firm) and who have committed to publishing the assessment in full. ThyssenKrupp AG and BAE Systems are the only two defence companies in the survey that we are aware of who commission such external assessments and make them publicly available.

It is also striking how bad practice is increasingly obvious when compared with the good examples. There are three main culprits.

- **Legal jargon:** There are many Codes of Conduct that focus on legal compliance and use legal jargon that may make them difficult for employees to find useful, or even intelligible. This could be a product of lawyers having drafted most of the anti-corruption programme.

- **“Box-ticking”:** The tone of the whole ethics and compliance programme – all the way from the CEO statement in the Annual Report through to detailed policies – is written in a style that lacks any conviction. This “box-ticking” style is immediately obvious to the interested reader, and it is likely this is also obvious to the company’s employees.

- **Lack of transparency:** The fact that 90 per cent of the companies have little on their websites about ethics and anti-corruption speaks for itself. That this number should include so many companies who are major global players is an extremely disappointing result.

ACTIONS

The Chief Executives of defence companies worldwide are the principal audience for this report. The following are four immediate actions they can undertake to implement good ethics and anti-corruption systems:

1. Review your company’s ethics and anti-corruption systems, comparing them with the results of this study. Require that an improvement plan be put in place and review progress at main Board level. Review the information disclosed publicly by your company so that your commitment is clear to all. We suggest you aim to provide ‘Band A’ level disclosure.

For the 85 companies in Bands D to F, analyse why your company demonstrates such limited evidence of ethics and compliance systems, and insist that substantive improvement plans be put in place.

2. Commission an independent external organisation to assess annually your company’s total ethics and compliance systems, and commit to publishing the report.

3. Speak up for industry-wide improvements in ethics and compliance standards in the defence sector. There is much scope for more visible external leadership and for multi-country collaboration. Actively support IFBEC, the new global defence forum for good business and ethical conduct, and make it the leading sector example of pro-active corporate behaviour.

4. Commit your company to engage with stakeholders who promote transparency and accountability of the defence sector. Be active in the next phase of this study. Ensure that your Heads of Ethics and Compliance participate fully, and that progress is regularly presented to your Board.

This report also makes recommendations for **Government Defence Procurement Chiefs**, who can constructively use this information to demand higher anti-corruption standards from bidders; and for **institutional investors and civil society**, who both for too long have hesitated to engage with corruption issues in the defence sector.

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The Study

Our intention is to provide solid data through which all defence companies can embed zero tolerance of corruption.

Transparency International UK (TI-UK) has been working to improve anti-corruption standards in the global defence industry since 2004. Part of our mission is to facilitate new industry initiatives and advocate action on key defence corruption risks. Governments and companies repeatedly ask what constitutes good practice. This study is part of answering that question. For a comprehensive explanation of the methodology and questionnaire, please visit the Defence Companies Anti-Corruption Index website at <http://www.defenceindex.org>

THE QUESTIONNAIRE:

The questionnaire comprises 34 questions. These are organised into five pillars: 1) Leadership, governance, and organisation; 2) Risk assessment; 3) Company codes and policies; 4) Training; and 5) Personnel and helplines. The questions cover what TI-UK regards as the basic capabilities that a global defence company should have in place. Each question is assessed against a 'model answer', which represents a full response. The model answers were reviewed and clarified during the study to ensure consistency across companies.

SOURCES OF INFORMATION:

The information to answer these questions should be, in TI-UK's view, available on the company's website as a matter of good practice and public accountability. TI-UK collected all data by desk research between January and July 2012. The sources included company websites and the relevant links and documents directly accessible through them. Typical documents included annual reports, social responsibility reports and corporate governance sections of the website.

Thirty-four companies also provided additional internal information about their anti-corruption systems and practices. Companies were under no obligation to do so, but TI-UK had hoped that – in the spirit of raising standards across the industry – more would participate. The reasons that some companies did not choose to provide further information varied: some did not want to share confidential information with

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TI-UK; some said they did not have the time to respond; and some had concerns about TI-UK's work quality or methodology.

THE PROCESS:

TI-UK used readily available public information to assess companies against the 34 questions. The draft analysis was then sent to the company for comment: this was the company's opportunity to guide TI-UK towards other publicly available information that may have been missed, and/or to provide additional internal information. The results of the assessments for companies based on public information are presented in our index and discussed on pages 8-13.

Where companies provided internal information, TI-UK reviewed and discussed the documents with the company. The results of this exercise, showing the impact of this information, are presented separately on pages 14-19.

Once all assessments were completed, they went through internal and external peer reviews, after which the companies received a copy of the finalised assessment. They were also given an opportunity to make any further statements should they wish to, and these are available on the Index website. All companies that did not respond were contacted multiple times, by letter, email and telephone. The findings are based on information gathered between January and July 20, 2012, and therefore do not take account of any changes made by individual companies thereafter.

THE COMPANIES:

Most of the companies included in this study lie within the group of top 100 global defence companies, as measured by defence revenue in 2010. In addition, in order to have a truly global range of companies, we added companies that were of an arms-exporting nationality that were not within the top 100, but which nonetheless had either actual or estimated revenue of at least USD100 million. This resulted in a final population of 129 companies from 31 countries.

Of these, 34 provided additional company-internal information and engaged in detail with TI-UK. The companies were: BAE Systems, Bechtel Corporation, Boeing, Chemring Group, CSC, Cubic Corporation, Daewoo Shipbuilding & Marine Engineering, Day & Zimmerman, Diehl Stiftung, DynCorp International, FLIR Systems, Fluor Corporation, Fujitsu, General Electric Aviation, Harris Corporation, Hewlett-Packard Company, Honeywell International, Indra, Jacobs Engineering, KBR Inc., Kongsberg Gruppen ASA, Lockheed Martin, Meggitt, Mitsubishi Heavy Industries, MTU Aero Engines GmbH, NEC Corporation, QinetiQ Group, Raytheon Company, Rockwell Collins, Saab AB, SAIC, Serco Group, ThyssenKrupp AG and Tognum. Four further companies wished to provide internal information but were too late to be able to be included. These were Accenture, Aselsan, Rafael Advanced Defense Systems and Rheinmetall.

THE SCORING:

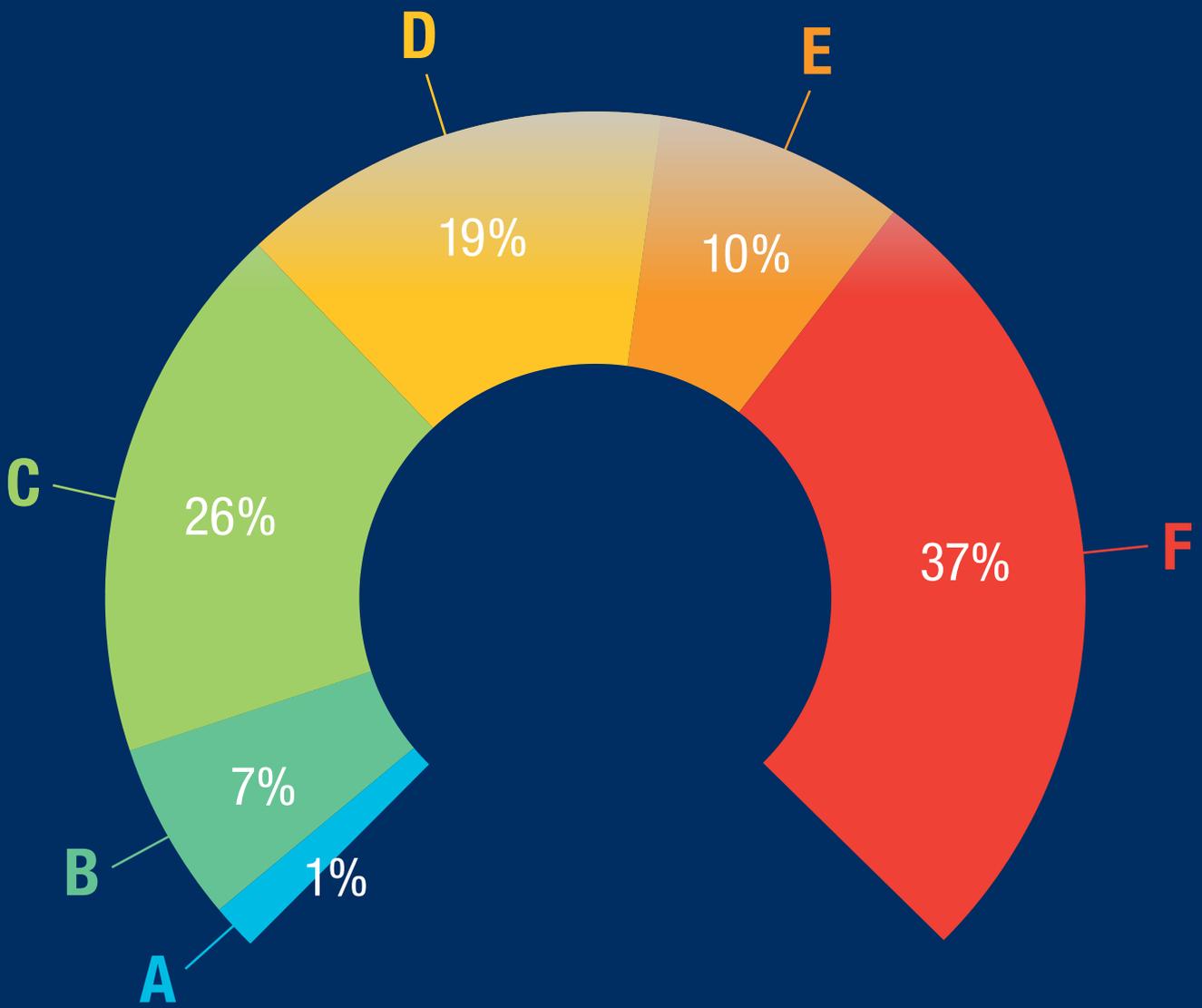
The companies are scored on the 34 questions, and then placed into one of six bands, from A to F, based on their scores.

Band A or B mean that we have seen plentiful or good evidence that basic ethics and compliance systems and processes exist. Bands E and F represent scores from 33 per cent down to 0 per cent, indicating there is only poor or no evidence of anti-corruption processes. Bands C and D are intermediate results – either because of a mix of good and poor evidence across the index questions, or because of more uniformly average evidence.

Band	Lower % Score	Upper % Score	Evidence of at least basic ethics and compliance systems
A	83.3	100	Extensive evidence
B	66.7	83.2	Good evidence
C	50.0	66.6	Moderate evidence
D	33.3	49.9	Limited evidence
E	16.7	33.2	Very limited evidence
F	0	16.6	Almost no evidence

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Banding based on public information



129 COMPANIES

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A 1 Company

FLUOR CORPORATION *

B 9 Companies

ACCENTURE, BAE SYSTEMS*, FUJITSU*, HEWLETT PACKARD COMPANY*, MEGGITT*, NORTHROP GRUMMAN CORPORATION, SERCO GROUP*, THALES S.A., UNITED TECHNOLOGIES CORPORATION

C 34 Companies

BECHTEL CORPORATION*, BOEING*, CHEMRING GROUP*, COBHAM, CSC*, DAY & ZIMMERMAN*, DYNACORP INTERNATIONAL*, EADS, FINMECCANICA S.P.A., GENERAL DYNAMICS CORPORATION, GENERAL ELECTRIC AVIATION*, GKN, GOODRICH CORPORATION, HARRIS CORPORATION*, HONEYWELL INTERNATIONAL*, INDRA SISTEMAS, S.A.*, ITT EXELIS, JACOBS ENGINEERING*, KBR INC.*, KONGSBERG GRUPPEN ASA*, L3 COMMUNICATIONS HOLDINGS, LOCKHEED MARTIN*, OSHKOSH CORPORATION, QINETIQ GROUP*, RAYTHEON COMPANY*, ROCKWELL COLLINS*, ROLLS ROYCE, SAAB AB*, SAIC*, TELEDYNE TECHNOLOGIES, TEXTRON, THYSSENKRUPP AG*, URS CORPORATION, VSE CORPORATION

D 25 Companies

AAR CORPORATION, ALION SCIENCE & TECHNOLOGY CORPORATION, ALLIANT TECHSYSTEMS (ATK), AVIO S.P.A., BABCOCK INTERNATIONAL GROUP, BOOZ ALLEN HAMILTON, CACI INTERNATIONAL, CAE, CUBIC CORPORATION*, CURTISS-WRIGHT CORPORATION, DAEWOO SHIPBUILDING & MARINE ENGINEERING*, DIEHL STIFTUNG & CO. KG*, ELBIT SYSTEMS, EMBRAER S.A., FLIR SYSTEMS*, HINDUSTAN AERONAUTICS, MANTECH INTERNATIONAL, MBDA MISSILE SYSTEMS, MTU AERO ENGINES GMBH*, NAMMO AS, NAVISTAR INTERNATIONAL CORPORATION, NEC CORPORATION*, RAFAEL ADVANCED DEFENSE SYSTEMS, SAFRAN S.A., TOGNUM*

E 13 Companies

ASELSAN, DASSAULT AVIATION, DCNS S.A., FINCANTIERI, GORKY AUTOMOBILE PLANT, IHI MARINE, MITSUBISHI ELECTRIC CORPORATION, MITSUBISHI HEAVY INDUSTRIES*, RHEINMETALL AG, RTI SYSTEMS, RUAG, SAMSUNG TECHWIN, ULTRA ELECTRONICS HOLDINGS

F 47 Companies

ABU DHABI SHIPBUILDING, ALMAZ-ANTEY, ANTONOV ASTC, ARAB ORGANISATION FOR INDUSTRIALISATION, ARINC, ARSENAL AD, AVIATION INDUSTRY CORPORATION OF CHINA, AVIBRAS INDÚSTRIA AEROSPACIAL, BATTELLE, BHARAT EARTH MOVERS LIMITED (BEML), BHARAT ELECTRONICS, BOUSTEAD NAVAL SHIPYARD, BUMAR GROUP, CHINA SHIPBUILDING INDUSTRY CORPORATION, DAMEN SCHELDE NAVAL SHIPBUILDING, DENELSOC, DOOSAN DST, GENERAL ATOMICS, HEAVY INDUSTRIES TAXILA, IRKUT CORPORATION, ISRAEL AEROSPACE INDUSTRIES, ISRAEL MILITARY INDUSTRIES, KAWASAKI HEAVY INDUSTRIES, KHARKOV STATE AIRCRAFT MANUFACTURING COMPANY, KRAUSS-MAFFEI WEGMANN, LIG NEX1, MC DEAN, NAVANTIA, NEXTER, NORINCO, OTOKAR, PAKISTAN ORDNANCE FACTORIES, PATRIA OYJ, POONGSAN, RUSSIAN HELICOPTERS, SAPURA GROUP, SATUMA, SRA INTERNATIONAL, SRC INC., ST ENGINEERING, SUKHOI, TATRA A.S., TRV CORPORATION, TULA KB PRIBOROSTROYENIYA, UNITED ENGINE CORPORATION, WYLE LABORATORIES, ZODIAC SA HOLDING

BANDING DEFINITIONS

Based on level of evidence for basic anti-corruption systems in place:

Band A: Extensive

Band B: Good

Band C: Moderate

Band D: Limited

Band E: Very limited

Band F: Little or none

NOTE

An asterisk by the company name means that they are one of the companies that shared internal company information with TI. These companies are scored again based on this data found on page 15.

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Analysis

Companies can use the evidence from this study to develop a plan for improvements in their ethics and anti-corruption systems.

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BANDS A AND B

Of the 129 companies, ten score in Band A or B, which means they have good, publicly available evidence of having at least basic ethics and anti-corruption compliance systems in place. The group includes four American companies (Fluor Corporation in Band A, Hewlett-Packard Company, Northrop Grumman Corporation and United Technologies Corporation), five European companies (Accenture, BAE Systems, Meggitt, Serco Group, Thales) and one Japanese company (Fujitsu). Both publicly owned and privately owned companies are represented.

Half of them are not 'pure' defence companies – for example, Fluor (9% defence), Accenture (3% defence), Fujitsu (1% defence) and Hewlett Packard (0.8% defence). These companies have valuable good practices of anti-corruption procedures that may be useful for the defence community.

Within Band B there is nonetheless significant variation. Six companies publish good information on three of the five pillar areas – leadership, policies, and personnel – but provide little to no information on the other two areas: assessing corruption risk and training. Few of the companies show public evidence of sustained leadership engagement promoting anti-corruption and ethics.

The companies in Bands A and B demonstrate a number of good practices and a strong dedication to ethics and anti-corruption. Almost all combine a values-based approach and a legal-based approach. They focus on building strong values – such as integrity, honesty, accountability, and openness – across the organisation. Additionally, they provide clear rules, grounded in compliance with anti-corruption laws.

It is clear from Fluor and the nine companies in Band B that there is no secrecy or confidentiality bar to defence companies publishing good information about their anti-corruption systems on their websites. Not disclosing, or hiding behind supposed confidentiality of information, is clearly not justified. As the key customers of defence companies, taxpayers, investors and governments have a legitimate expectation to learn what mechanisms companies apply to prevent corruption so that they can monitor the company's adherence to these commitments.

We recommend that companies in Band B upgrade their website disclosure to Band A levels. Such clarity sends a clear message to clients, to governments and to the public about the company's commitment not to tolerate corruption.

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BANDS C AND D

There is a large block of companies in the intermediate Bands C (34 companies) and D (25 companies). Those in Band C score just above 50 per cent – not poor, but definitely not a good level of public disclosure; and those in Band D score above 33 per cent, signifying only limited disclosure. To understand them better, we have analysed these groups according to the five pillars of 1) Leadership, governance, and organisation; 2) Risk assessment; 3) Company codes and policies; 4) Training; and 5) Personnel and helplines. The average results across these companies are shown below:

Overall Results	Band C	Band D
Leadership	C	D
Risk Management	D	E
Company Policies and Codes	C	C
Training	D	E
Personnel and Helplines	A	B

The analysis shows that both groups of companies provide a good level of detail on personnel and helplines, provide moderate levels of disclosure on their company policies and codes, disclose equally little on risk management, and differ in what they disclose about leadership and training.

The other distinguishing feature, which may also reflect the difference noted above on leadership, is that more than half of the companies in Band C chose to participate in our study by providing internal information (20 of 34), whilst only 7 of 25 from Band D participated.

BANDS E AND F

Almost half of the defence companies are not able to publicly demonstrate that they have basic anti-corruption systems in place. This includes companies from all the major arms exporting nations: USA, Russia, Germany, France, the UK and China. Sixty of the 129 the defence companies score less than 33 per cent on the basis of their public information, which means they are ranked in Bands E or F. Forty-seven of the 130 companies score in the lowest of the six bands, Band F. This means that they disclose little or no information on the company's basic anti-corruption measures.

Some of the largest global exporters are in Bands E and F. These include all nine Russian companies and the three Chinese companies included in the study. Additionally, it includes two of the six French companies, Dassault Aviation and DCNS (Band E); two German companies, Rheinmetall (Band E) and Krauss-Maffei Wegmann of Germany (Band F); Ultra Electronics of the United Kingdom (Band E); and several US companies. Others included Navantia of Spain (Band E), Fincantieri of Italy (Band E), Damen Schelde of The Netherlands (Band F), Israel Aerospace Industries and Israel Military Industries (Band F), Patria of Finland (Band E) and RUAG of Switzerland (Band E).

We recommend that the CEOs of the 119 companies in Bands C to F use the evidence from this study to inform and develop a plan to improve their anti-corruption systems, and upgrade the disclosure of these on their websites.

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It is important that defence companies from rapidly growing arms exporting countries meet global standards of anti-corruption.

SMALLER ARMS EXPORTERS

The defence industry has an unusual global structure. The major arms exporting companies are concentrated in just a small number of countries. According to SIPRI, exports from the top six countries – USA, Russia, Germany, France, UK and China – account for 79 per cent of international defence sales, and the top twelve countries – including Spain, Netherlands, Italy, Israel, Sweden and Ukraine – account for 94 per cent of international defence sales.²

At the same time, because of the strategic nature of the defence sector, many other countries have significant national arms industries, and an increasing number of them are seeking to expand domestic arms production into international arms markets. In order to capture this growing branch of the defence industry, our survey includes companies from 31 countries. These included countries such as Brazil, Bulgaria, Czech Republic, Egypt, India, Malaysia, Pakistan, Poland, South Korea, Turkey and United Arab Emirates.³

Some of these additional companies are clearly aware of the subject of ethics and compliance – for example they publish annual reports that state their stance against corruption or how they regulate gifts and hospitality. However, the majority either publish very limited information on their anti-corruption programmes, or do not demonstrate any public evidence of such programmes. Most of these companies score relatively poorly: of the 27 companies in this group, 23 are in Bands E to F.

Companies from these nations are playing a major and increasing role in selling arms around the world. They also often act as partners or suppliers to the largest arms exporters. It is therefore crucial that they meet global anti-corruption standards. Both the national governments and defence company joint-venture partners should insist that these companies strengthen their anti-corruption standards.

Many of these smaller companies in our survey are participants of the UN Global Compact or are headquartered in countries that have ratified the OECD Anti-Bribery Convention: memberships that carry obligations for reporting on anti-corruption practices. Therefore there is no discernible barrier preventing all these companies from publishing more information to demonstrate their commitment against corruption.

It is important that defence companies from rapidly growing arms exporting countries meet global standards of anti-corruption. We recommend they implement improvement plans to upgrade their anti-corruption practices and commit to higher levels of transparency. Their government customers (and sometimes owners) should demand higher anti-corruption standards from these companies to ensure they are getting the best value for money.

SPECIALISATION ON DEFENCE PRODUCTS

The 129 companies range from those that are highly focused on the defence sector, with more than 80 per cent of sales originating from defence (e.g. General Dynamics, BAE Systems and Patria), through to companies with less than 5 per cent defence sales (e.g. Accenture, Fujitsu and ThyssenKrupp). **Analysis of the results by defence specialisation shows that disclosure is generally better in those companies that are not focused on defence products.**

COMPANY OWNERSHIP

Publicly owned companies have better disclosure than private companies, who in turn have better disclosure than state companies (54 per cent, 10 per cent and 0 per cent respectively in Bands A to C).

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Bandings for 34 companies which provided internal information

A principal purpose of this study is to understand the actual anti-corruption systems that companies have in place.

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For each company that provided internal information, we show their band based on public information only (the same data as already shown), together with what their score would be if the company-internal information reviewed by TI-UK were made public.

Company	Public Information	Internal & public Information
BAE SYSTEMS	B	B
BECHTEL CORPORATION	C	A
BOEING	C	A
CHEMRING GROUP	C	B
CSC	C	B
CUBIC CORPORATION	D	C
DAEWOO SHIPBUILDING & MARINE ENGINEERING	D	C
DAY & ZIMMERMAN	C	A
DIEHL STIFTUNG & CO. KG	D	C
DYNCORP INTERNATIONAL	C	A
FLIR SYSTEMS	D	C
FLUOR CORPORATION	A	A
FUJITSU	B	A
GENERAL ELECTRIC AVIATION	C	B
HARRIS CORPORATION	C	A
HEWLETT-PACKARD COMPANY	B	A
HONEYWELL INTERNATIONAL	C	A
INDRA SISTEMAS, S.A.	C	B
JACOBS ENGINEERING	C	B
KBR INC.	C	A
KONGSBERG GRUPPEN ASA	C	B
LOCKHEED MARTIN	C	A
MEGGITT	B	A
MITSUBISHI HEAVY INDUSTRIES	E	C
MTU AERO ENGINES	D	B
NEC CORPORATION	D	B
QINETIQ GROUP	C	B
RAYTHEON COMPANY	C	A
ROCKWELL COLLINS	C	A
SAAB AB	C	B
SAIC	C	B
SERCO GROUP	B	A
THYSSEN KRUPP AG	C	A
TOGNUM	D	C

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The opportunity to review company-internal or confidential information helps to understand how commitment against corruption is embedded inside the company.

A 16 Companies

BECHTEL CORPORATION (C)
 BOEING (C)
 DAY & ZIMMERMAN (C)
 DYNCORP INTERNATIONAL (C)
 FLUOR CORPORATION (A)
 FUJITSU (B)
 HARRIS CORPORATION (C)
 HEWLETT-PACKARD COMPANY (B)
 HONEYWELL INTERNATIONAL (C)
 KBR INC. (C)
 LOCKHEED MARTIN (C)
 MEGGITT (B)
 RAYTHEON COMPANY (C)
 ROCKWELL COLLINS (C)
 SERCO GROUP (B)
 THYSSEN KRUPP AG (C)

B 12 Companies

BAE SYSTEMS (B)
 CHEMRING GROUP (C)
 CSC (C)
 GENERAL ELECTRIC AVIATION (C)
 INDRA (C)
 JACOBS ENGINEERING (C)
 KONGSBERG GRUPPEN ASA (C)
 MTU AERO ENGINES (D)
 NEC CORPORATION (D)
 QINETIQ GROUP (C)
 SAAB AB (C)
 SAIC (C)

C 6 Companies

CUBIC (D)
 DAEWOO SHIPBUILDING
 & MARINE ENGINEERING (D)
 DIEHL STIFTUNG & CO. KG (D)
 MITSUBISHI HEAVY INDUSTRIES (E)
 FLIR SYSTEMS (D)
 TOGNUM (D)

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The depth of engagement by defence companies varied and was self-selected. Some companies were committed to being fully open about their systems; others produced documents only on specific information requests; and a few promised additional materials but did not provide it.

The company-internal information that we reviewed includes documents such as the following: training logs, training materials and videos, compliance handbooks and accompanying guidance notes, risk assessment methodologies and results, codes of conduct for suppliers, terms and conditions for agents, due diligence questionnaires for agents, internal compliance

auditing procedures and plans, board minutes, submissions to the Board, CEO and leadership speeches, internal videos, newsletters and emails.

What characterises the companies providing company-internal information? They are, of course, not a random sample. They are mostly companies that already have the better disclosure practices. They will be seeking recognition of their actual systems.

Nevertheless, they all demonstrate openness, and this is to their credit. Working with an external civil society organisation, without any control over the results, also demonstrates leadership. Such leadership on ethics and anti-corruption

will be one of the features that distinguishes successful defence companies from the others. We encourage all other defence company CEOs also to make known both internally and externally their anti-corruption commitment.

Reviewing company-internal information of this nature has a major limitation because it is not available for public scrutiny. It is for this reason that the main index produced for this report is based on public information only. TI-UK believes that transparency is a fundamental component for citizens, governments, investors, and activists to hold companies accountable for their actions and commitments.

D 0 Companies

E 0 Companies

F 0 Companies

This table shows the band for each company that provided internal information. It is based on what their score would be if the company-internal information were made public. The letter in parenthesis represents the company's band based on public information only.

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Defence leaders are not speaking out on the importance of ethics and anti-corruption in their industry, even among good-practice companies.

The results show that including company-internal information makes a significant difference to the results: with the inclusion of internal information, the companies on average would have improved their score by between one and two bands. Thus, most companies that are in Band C, based on public information only, would move up to Bands A or B, whilst most of those in Band B would move up to Band A.

To understand this better, we have analysed the effect of internal information across the five pillars of ethics and anti-corruption systems. The results are shown in the table to the right, ordered by how much the results changed in each category.

Leadership, organisation and monitoring improve by only one band on average from an already low starting point. This is a big surprise and a disappointment. The two most critical questions in this pillar are whether there is evidence of strong CEO leadership on the importance of ethics and anti-corruption, both internally within the organisation and externally. These questions do not shift greatly in score upon review of internal information. The answer, mostly, is that there is little more internal evidence from these companies than what is already publicly available.

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Band	Average band based on public information (%)	Average band based on internal & public information (%)	Band Change
Personnel & Helplines	A	A	0
Company Policies & Codes	C	B	+1
Leadership, Organisation & Monitoring	C	B	+1
Training	D	B	+2
Risk Management	D	A	+3
Overall Band	C	B	+1

Personnel policies and helplines do not change at all with the provision of internal information. Almost all companies already have substantive information about personnel policies related to ethics and corruption on their websites, and there is not much internally that adds to that. The only area where companies score poorly is the question on whether companies formally declare their conflicts of interest. Whilst many companies publish information on how they define conflicts of interest, very few then document how an employee should report this information and how senior management should use this information to determine if a conflict exists.

Codes and Policies change by one band. The impact of participation on the average scores is relatively modest, companies on average change by one band though significantly this does not improve to Band A. This is disappointing as reporting on anti-corruption codes and policies is hardly a new practice. This indicates that overall, most companies have a relatively good public disclosure on only some anti-corruption policies and codes. But there are still many policy areas, such as facilitation payments and lobbying, that companies have a significant scope to improve.

Training improves by two bands. This is uniform across most of the companies – they apparently disclose much less on training in ethics and anti-corruption than they are actually doing. In particular, companies do not disclose very much information on how they target or customise their training for those employees most at-risk of corruption, such as those in procurement or sales.

Risk management shows the greatest improvement from internal information, moving a massive three bands from a Band D to a Band A score. Most companies who participated achieve Band A. This looks in part like a simple disclosure gap – companies have the procedures but do not make them public. Companies with better practices were explicit in their belief that risk management constitutes a competitive advantage.

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Good Practice

Repeatedly emphasising to employees that corruption will not be tolerated across the company is a central ingredient in preventing corruption before it happens, and much more convincing than apologising if or when it does.

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TI-UK detailed a few examples of good practice on anti-corruption systems in both public disclosure and company-internal information. This section presents a few examples drawn from both of these data sources. More are available on the website at: www.defenceindex.org

LEADERSHIP

Leadership plays a central part of setting the expectations of acceptable behaviour across the company and of how the industry is viewed by society. Speaking out demonstrates conviction, it can move a whole industry, and it is more powerful in motivating employees than the easier internal messaging. Whilst CEOs may feel exposed talking so publicly about corruption, this should not be an excuse not to speak out. Such external engagement—for example, at industry conferences and to the media – demonstrates to governments, the public and other companies that corruption will not be tolerated.

However, very few defence companies show significant evidence of external leadership. A surprisingly low 13 out of 129 CEOs demonstrate strong external engagement outside the company against corruption. This is a very small number.

EXAMPLE OF GOOD PRACTICE:

Good examples of external leadership include Accenture's CEO upholding the principles of the UN Global Compact; Fluor's CEO addressing corruption at the 2012 World Economic Forum Meeting in Davos; and a Thales interview with its CEO discussing Thales's involvement on anti-corruption platforms such as the G20 in its 2011 Corporate Responsibility Report. Such examples, however, are too few and far between.

ORGANISATION AND GOVERNANCE

A key element of any good ethics and compliance systems is a monitoring and updating process to ensure the continued effectiveness of the system. Good practice is where the company both periodically reviews the whole programme in detail and does frequent monitoring of specific parts of it.

EXAMPLE OF GOOD PRACTICE:

ThyssenKrupp AG and BAE Systems are the only companies companies we are aware of in the survey that commissions an annual assessment from an outside organisation of the strengths and weaknesses of its full compliance and ethics programme and go so far as to publish this documentation. In the case of ThyssenKrupp AG, the outside assessment organisation is rotated each year, for example between an accounting firm and a legal firm.

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POLICIES AND CODES

Making anti-corruption policies clear:

Some companies make their anti-corruption policies very clear. The policies are written in straightforward, accessible language that defines what corruption is, applies them to both government and non-government officials, and are not solely couched in legal jargon.

Some companies do not make their Code of Conduct and their associated policies public. TI-UK believes that this is unacceptable practice – companies must publish their Codes of Conduct in keeping with the spirit of a serious approach to good business conduct.

Codes of Conduct vary widely in terms of length, ease of reading and CEO engagement. Many are written in legal language, seemingly written by and for lawyers. These codes tend to focus on compliance with the law. Legal language, however, does not always provide clear and straightforward policies for employees to follow. Dense legal language can often be confusing or inaccessible to employees who are not familiar with the law. This can make it very difficult for employees who are looking for clear and practical guidance to navigate complex grey areas, such as conflicts of interest.

On the other hand, some of the best performers use clear language and appropriate detail to allow employee and advisers to see clearly what was and was not acceptable, even if they also have legal language in their policies.

EXAMPLE OF GOOD PRACTICE:

Fujitsu's Code of Conduct has a clear list of red flags or "warning signs" that may indicate a payment is corrupt, such as when an agent "asks for an unusually large fee or an increase in a previously agreed fee to close the deal."

RISK MANAGEMENT

Assessing corruption risk is an important part of any proper ethics and compliance system. There are multiple risks that are associated with conducting defence deals. Risks differ with each business deal, in different countries, in different product areas and with different joint venture partners. Understanding where the risk lies also enables companies to develop and put in place sufficient contractual and monitoring terms to apply high anti-corruption standards to third parties, such as agents and suppliers.

This is an area where there is almost no publicly available information from companies. One reason for this gap could be that publicly disclosing risk management procedures is a relatively new practice. At the same time, it is one of the key reporting elements that UN Global Compact guides companies to report on.⁴ In its guidance on the 2010 UK Bribery Act, Transparency International UK is emphatic that reporting on risk assessment process is essential, because it "will enable stakeholders to judge material issues, form a view on whether the company is managing the issues adequately and if need be, enter into discussion with the company if concerns arise."⁵

TI-UK received much more detailed information and good practice examples from the internal information provided by companies. With the inclusion of internal information, 27 companies have quite sophisticated systems that review all ethics and compliance risks on a regular basis, up to six times per year. They have templates and methodologies for analysing the relative severity of the risks so these can be prioritised against one another. The risks are prioritised and discussed at Board level each year. Each risk is assigned to a senior person, who is then responsible for taking whatever action is needed to mitigate the risk, and a timeline by which they need to complete these actions (e.g. to update a policy or provide a targeted training to an at-risk employee group).

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Agents: Many companies recognise that agents pose a significant corruption risk to companies. In these cases, good practice includes conducting extensive due diligence on potential agents. They then require formal justification of the agent's role and the proportionality of the commission. Finally, they require senior management sign-off at headquarter level for all agent contracts worldwide.

EXAMPLE OF GOOD PRACTICE:

Some companies have particularly comprehensive corruption risk assessment methodologies, including BAE Systems, Boeing, General Electric Aviation, Jacobs Engineering, Meggitt and Daewoo Shipbuilding & Marine Systems. Fluor Corporation summarises its risk assessment process in its 2010 Corporate Sustainability Report as the following: "We utilize a formalized and systematic process for assessing and monitoring the company's business risks, including the potential for corruption associated with execution of capital projects around the world. Our approach is designed to identify what can go wrong and develop mitigation strategies for eliminating such risks."

TRAINING

Training is a key component of mitigating the company's exposure to corruption risk. Good practice companies keep training "fresh" and relevant to employees so as to derive the maximum possible benefit from what is a time and resource intensive exercise. Companies make use of real past examples and create hypothetical scenarios to bring to life real issues that employees have or could face in the field.

Companies have to find a suitable balance between face-to-face and online anti-corruption training. Face-to-face training is more effective at imparting knowledge as it allows employees to discuss questions and issues in-depth, but it is costly. One way that companies have chosen to prioritise the use of face-to-face training is to provide customised anti-corruption training to employees in the most sensitive and risky situations (e.g. staff working in sales and procurement or in countries that are perceived to have a high level of corruption).

EXAMPLE OF GOOD PRACTICE:

Raytheon provides an example of good practice for anti-corruption training programmes. Some of Raytheon's training is provided to all employees through video vignettes based on actual cases, which Raytheon argues is "powerful and relevant for employees" (DII Best Practice Forum: Tailoring Training to Address Trends 2011). The "EthicSpace" series provide short video clips that tell stories about ethical concerns faced by our employees. Episodes are delivered to employees via email each quarter and cover topics such as use of social media, labour charging, competitive intelligence, and reporting concerns" (Corporate Responsibility Report 2011). Raytheon conducts follow-up surveys and small focus groups to improve the effectiveness of the training.

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Actions

CEOS AND CORPORATE LEADERS

CEOs and corporate leaders have a fiduciary duty to protect their companies, their employees and their shareholders from the financial and reputational repercussions of a potential corruption case. They also have an ethical duty to other stakeholders, to ensure that corruption does not distort markets or enable public funds to be squandered.

1. Review your company's ethics and anti-corruption systems, comparing them with the results of this study. Require that an improvement plan be put in place and review progress at Main Board level. Review the information disclosed publicly by your company so that your commitment is clear to all. We suggest you aim to provide 'Band A' level disclosure.

For the 85 companies in Bands D to F, analyse why your company demonstrates such limited evidence of ethics and compliance systems, and insist that substantive improvement plans be put in place.

2. Commission an independent external organisation to assess annually your company's total ethics and compliance systems, and commit to publishing the report.

3. Speak up for industry-wide improvements in ethics and compliance standards in the defence sector. There is much scope for more visible external leadership and for multi-country collaboration. Actively support IFBEC, the new global defence forum for good business and ethical conduct, and make it the leading sector example of pro-active corporate behaviour.

4. Commit your company to engage with stakeholders who promote transparency and accountability of the defence sector. Be active in the next phase of this study. Ensure that your Heads of Ethics and Compliance participate fully, and that progress is regularly presented to your Board.

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DEFENCE MINISTERS & GOVERNMENT DEFENCE PROCUREMENT CHIEFS

This study provides vital information for governments, showing how and where defence contractors may be able to improve individually and in driving industry-wide improvement.

- 1.** We suggest that all Defence Ministries and Governments review this study and consider how they can be more stringent in specifying minimum anti-corruption standards for all bidding companies.
- 2.** Governments owning stakes in state or military-owned defence companies should insist on major improvements in ethics and compliance practices from these companies.

INSTITUTIONAL INVESTORS

Investors desire to protect their investment. It is in their interest to assess the companies in which they invest.

- 1.** Encourage all the defence companies in whom they invest to be public about their anti-corruption measures, and to sign up for public reporting vehicles such as the Global Reporting Initiative.
- 2.** Insist that the companies adopt independent external review of their anti-corruption programmes, and to publish the results of the findings.
- 3.** Ask the CEO and the Chair of the Board to explain personally what their ethics and compliance systems are, and why they do not rank higher in this assessment.

CIVIL SOCIETY

Civil society has the opportunity to use this study to drive change and improvement across the industry.

- 1.** Campaign for better public disclosure by all defence companies in your country. Use this study as the evidence base for what should be expected of all defence companies.
- 2.** Meet the CEOs of the defence companies active in your country and discuss this report with him/her; suggest a collaborative campaign to make this sector the most transparent industry sector in the country.

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Endnotes

1. As compiled from Defense News 2010 Top 100, SIPRI Top 100 Arms-Producing and Military Services Companies 2010, and defence companies' own financial reporting.

2. According to SIPRI 2007-2011 data, global arms exports come predominantly from six nations: the USA (30%), Russia (24%), Germany (9%), France (8%), the United Kingdom (4%) and China (4%). These six companies comprise 79% of global arms exports. The next six (Spain, Netherlands, Italy, Israel, Sweden and Ukraine) represent a further 15%.

3. This data was compiled using SIPRI Top 100 <http://www.sipri.org/research/armaments/production/Top100> and company financial listings. For complete list see Methodology document online at www.defenceindex.org

4. For more information on the UN Global Compact's guidance on reporting procedures for risk management and other anti-corruption areas, see the 2009 report "Reporting Guidance on the 10th Principle Against Corruption." Reporting element D-3 contains specific recommendations on disclosing risk management procedures.

5. For more information see Transparency International UK, Adequate Procedures – Guidance to the UK Bribery Act 2010 <http://www.transparency.org.uk/our-work/bribery-act/adequate-procedures>: "It is good practice for the company to disclose publicly its risk assessment process, including the results of any stakeholder consultations, to describe the significant risks identified as well as the actions being taken to mitigate the risks. Disclosure will act as an impetus to risk assessment. It will enable stakeholders to judge material issues, form a view on whether the company is managing the issues adequately and if need be, enter into discussion with the company if concerns arise. Finally, the process of regular disclosure in itself will encourage the company to strive for improvement and to live up to its previous commitments and targets."

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Follow Up Thanks

We welcome contact from defence companies that want to improve their ethics and compliance systems, and from companies that have updated their processes and/or their website since this study was finalised. Please contact TI-UK for any further information or comments at **ci@transparency.org.uk**.

More information, analysis and follow-up from this study will be placed on our Index website in the coming months.

TI-UK has commenced a second phase of this study, using fifty-five more detailed questions. This phase is aimed at further identifying and spreading good practice across the industry. TI-UK encourages all the companies in this study, and other defence companies who are interested, to participate in this exercise. The questions are available on the report's website:

www.defenceindex.org

This Defence Companies Anti-Corruption Index will be updated in two years time to measure progress in the industry.

TI-UK would like to thank all the companies and individuals who have encouraged us to do this study. We would particularly like to thank those companies that participated in providing internal information. We appreciate that it has involved a 'leap of faith' on their part and we hope that the result will have the commonly desired effect of a significant improvement across the whole defence industry.

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Study authors: Mark Pyman, Tiffany Clarke, Saad Mustafa and Gareth Somerset

Supporting contributors: Anne-Christine Wegener, Maria Gili, Dessi Hristova, Joseph Plant and Cormac Seachoy

External peer reviewers: John Bray, Simon Webley, John Howe, and two others who wish to remain anonymous.

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Transparency International UK
32-36 Loman Street
London SE10 9EW
United Kingdom

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“This comprehensive analysis of the major defence companies from all over the world examines what systems and processes they have in place to prevent corruption. Its purpose is to raise standards globally, promote good practice in preventing corruption, and increase transparency in the sector. I very much hope that the industry responds to the challenge.” Lord Robertson, Former Secretary General of NATO

“Corruption’s potential to damage the effectiveness and legitimacy of defence companies and armed forces cannot be overstated. This deep analysis of company practices will be invaluable. It will drive company improvement and will enable governments to better see behind the veil of corporate PR.” John Githongo, Inuka Kenya, and former Permanent Secretary for Governance and Ethics in the Office of the President, Kenya.

