



## Shadow Value Chains

Tracing the link between corruption, illicit activity and lootable natural resources from West Africa

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## Abstract

The illicit natural resource trade continues to benefit corrupt officials, criminal and terrorist networks and divert resources away from development, security and the common good in West Africa. How are Liberian timber, Sierra Leonean diamonds, Malian gold and Nigerian oil traded outside of, and intertwined with, legal value chains before ending up in what is often legal consumer markets? By collating recent knowledge of the 'shadow value chains' of these resources, this paper seeks to explore if and how illegally traded natural resources sponsor other types of illicit activity, such as organised crime and terrorism. Furthermore, how are these activities facilitated by corruption in the different cases? The paper gives a number of recommendations. Perhaps the most important one is that in order to improve interventions, in-depth understanding of local power relations and incentive structures in these individual shadow value chains is crucial. Such knowledge should be paired with increased attention to how international actors and networks facilitate and accommodate illegitimate private gains stemming from lootable West African natural resources.

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## 1. Introduction

Sierra Leone, Liberia, Mali and Nigeria all face grave challenges relating to security and deficient development despite having large deposits of natural resources that could potentially be used to address these challenges. West Africa has, at the same time, earned a reputation as a hotbed of criminal activity such as trafficking in drugs and humans, smuggling and piracy,<sup>1</sup> while recent upsurges in terrorism and separatism in Mali and Nigeria have led to increased attention to the funding of such activities. This paper asks whether natural resource revenues play any role in sponsoring these activities (transnational crime, terrorism and conflict) and, if so, whether corruption in the management of natural resource revenues plays a role.

This U4 Issue Paper examines four case studies: diamonds in Sierra Leone; timber in Liberia; gold in Mali and oil in Nigeria.<sup>2</sup> All of these resources have a history of being exploited for criminal and militant activity in the region, especially during the 1990s and early 2000s.<sup>3</sup> Despite a variety of hard and soft interventions to improve natural resource governing systems, West African natural resources<sup>4</sup> continue to be stolen and exploited (OECD 2012) and often find their way through illegal markets before ending up in legal consumer markets (FATF 2016). These commodities find their way to legal or illegal markets through what this paper has termed 'shadow value chains', meaning value chains that run, often parallel to or intertwined, with legal value chains. The paper argues that in order to limit the exploitation of natural resources for illicit and illegal purposes, more attention needs to be paid to the dynamics of the diverse value chains of these commodities. Such attention is required to avoid accepting unsupported assumptions at face value or relying on outdated evidence of links between natural resources and various forms of illicit and illegal activity. More importantly, and as this paper claims, in order to create better interventions, in-depth knowledge and understanding of local power relations and the incentive structures tied to these individual shadow value chains is crucial. Such knowledge should be paired with increased attention on how international actors and networks facilitate and accommodate illegitimate private gains stemming from West African natural resources.

This issue paper attempts to collate some of the more recent knowledge of whether and how illegally traded natural resources sponsor other types of illicit activity in West Africa, understood broadly to encompass crime, smuggling, terrorist activity, militancy and insurgency activity. This question is answered in a three-step approach: first, how are resources diverted from the legal value chain? Second, do illicitly extracted or traded resources finance illicit or illegal activity on their way to consumer markets? Third, how are these activities facilitated by corruption in the different cases? The findings show that in all four countries studied, deeply entrenched patterns of corruption serve as a facilitating factor for the diversion of natural resources from their legal value chains enabling shadow value chains to exist and flourish. The

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1 Two fresh reports by the OECD and FATF have, e.g. found West African smuggling of narcotics, contraband and humans are a source of funding for terrorist groups and criminal syndicates (Reitano & Diesing 2016, FATF-GIABA-GABAC 2016).

2 In each of the four countries, at least one of the resources is of particular significance, and the issue paper will therefore mainly focus on one commodity per country. While the paper has a country-specific focus, the supply chains of these resources are transnational and usually involve multiple sites of extraction and trade across borders. Since illicit activities tend to span across borders, the issue paper also draws on evidence from across the region.

3 Although oil has perhaps historically been subject to looting to a lesser degree than the other three resources, petroleum products are illegally exploited to a high degree in this particular area (see chapter on Nigeria for more detail).

4 According to the WTO (2010), natural resources are 'stocks of materials that exist in the natural environment that are both scarce and economically useful in production or consumption, either in their raw state or after minimal amount of processing'. This study will focus on natural resources that originate in West Africa.

paper also finds that while all of the resources sponsor illicit activity to some extent, some of the links that are commonly referred to remain insufficiently documented and should be further explored.

Most of this issue paper is dedicated to the four case studies. First, the paper engages in a short review of the relevant literature, then proceeds to the four cases studies and concludes by summarising the key findings. The subsequent section provides a list of recommendations for development cooperation partners to consider when designing new interventions aimed at limiting the risks of funding illicit activity through the natural resource trade. Lastly, the paper identifies some main knowledge gaps that should be addressed in order to facilitate improved interventions aimed at limiting corruption and circumventing the means through which these resources are used to sponsor illicit activity.

## 1.1 Methodology

In order to investigate the ways in which natural resources fund illicit activity, the paper investigates the value chains of lootable resources,<sup>5</sup> that is, their flow from the point of extraction, via intermediaries and onto consumer markets. By using this approach, the paper aims to identify the points, in the supply chain, at which a resource is stolen and if and where it re-enters the legal supply chain at a later stage. In order to do so, the paper surveys the main findings of recent literature on the link between violent conflict, terrorist activity and other illicit activities, and natural resources. Specific focus will be on corruption as an enabling/facilitating factor throughout the review. The focus on value chains stems from a 'follow the money' type of logic. It is also in accordance with the ongoing OECD Initiative for Policy Dialogue on Natural Resource-based Development, which recently produced a major typology of corruption risks in the extractive value chain (OECD 2017). The desk study will rely on, and combine, findings from empirically-related strands of literature that do not always speak to each other. These include the civil war literature, the terrorism literature, the poverty literature, the resource curse literature and studies within political economy, e.g. those on financial flows and corruption.

Researching illicit activity poses methodological challenges as most of the evidence is anecdotal. This often means that the evidence forms a poor basis for more general conclusions or, in the worst case, it might be unreliable. Accessing detailed data on how natural resources sponsor illicit activity may also be challenging due to the interest among law enforcement agencies *not* to publish detailed information on recent cases, e.g. of money laundering, as such information can be used by criminals to avoid detection. Therefore, the published case reports by, for example, the Financial Action Task Force (FATF) are often generic and possibly not up to date with the latest developments in the *modus operandi* of money launderers. To avoid weak inferences, this paper has strived to search for those patterns that have been identified by more than one case study and which are (preferably) based on field research. In addition, findings are sometimes supported by information stemming from criminal cases, which provide additional insights into illicit transactions. Another methodological issue affecting this paper is the shortage of accurate estimates of illicit trade, which are key to grasping the magnitude of the problem. The available estimates are usually built on aggregates of interception rates (OECD 2016a), which makes them inaccurate, and the numbers should hence be viewed with caution.

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5 The four resources are 'lootable', meaning that they can easily be extracted by unskilled labour, are easy to transport and do not need refinement before transport (Lujala 2003; Ross 2002). Alluvial diamonds and gold are, prime examples of lootable natural resources.

## 2. Background

### 2.1 What do we know from the existing literature?

Some of the literature that this study taps into overlap and ‘speak’ to each other (corruption is an area of interest to most of them); however, others appear to exist more in parallel. This desk review thus intends to combine and collate some of the key findings from different studies in order to determine whether they hold some answers to how lootable natural resources sponsor illicit activity or find their way to consumer markets. This section is not an exhaustive summary of all the works in this area.<sup>6</sup> Instead, it will focus on discussing the state of knowledge directly relating to the focus of the paper.

#### **Natural resources and the financing of armed conflict**

There is a rich body of research exploring the links between natural resources and armed conflicts. For some time, the academic debate was focused on ‘greed’ versus ‘grievance’, i.e. conflicts were driven by economic greed, social deprivation or grievance (Nielsen & Bulte 2014). The literature has come to no affirmative answer on this question, and depending on the conflict and context, both greed and grievance can be important factors (ibid). In light of this research, some important findings have emerged, for example, Lujala et al. (2005) found a positive correlation between lootable diamonds and conflict and that established states with lootable diamonds are more likely to be involved in civil conflict than countries with diamonds that require sophisticated technology. This is in accordance with Ross (2002), who actually introduced the concept of ‘lootable resources’. On a macro level, however, factors such as increasing or declining commodity prices (Bruckner & Ciccone 2010), ethnic fragmentation/marginalization (Caselli & Coleman 2013; Montalvo & Reynal-Querol 2005) and stagnant growth (Hoeffler et al. 2009) are all important factors in the resource-conflict nexus. For example, in Sierra Leone, the importance of diamonds as a motivation for engaging in fighting is somewhat mixed. Humphreys and Weinstein (2008) found that money and diamonds are important factors for engaging in conflict, and Miguel and Bellows (2009) found that war tends to be more intense in diamond-rich areas. However, Richards (2003) found that diamonds are not an important motivating factor on the individual level for engaging in conflict. Still, all of these studies on Sierra Leone agree that a mix of factors such as economic, social exclusion and social pressure bear significance in explaining armed conflict.

Rents generated from natural resources are also an important aspect in terms of explaining conflict or even the absence of conflict. Research shows that rents can in fact have a stabilising effect by serving as a means to paying off/silencing opposition (Bjorvatn & Naghavi 2011) or maintaining political patronage and thus making sure that powerful actors gain from the status quo (ibid). This is especially effective in cases where resources generate large rent flows (Torvik & Aslaksen 2006). Acemoglu et al. (2010) found that rent-seeking governments had a choice between 1) maintaining a strong army and increasing the risk of a coup or 2) maintaining a weak army, which increases the risk of violent conflict. Thus, there is a link between natural resources and conflict, although there is debate on how strong this link actually is and on the causal factors that determine the circumstances under which conflict materialises in resource-rich countries (Nielsen & Bulte 2014).

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<sup>6</sup> For some useful literature reviews, see, e.g. Williams and Dupuy’s (2016) Corruption in resource management; UNCRI’s (2015) illicit trafficking in precious metals; Cuvelier, Vlassenroot and Olin (2014); Mildner, Lauster & Wodni (2011) on the links between governance, natural resources and conflict.

## Natural resources and the financing of terrorism<sup>7</sup>

Much like criminal networks and rebel groups, terrorist organisations need access to revenue for their survival and to run their operations. Due to their illegal nature, they all usually need to resort to illegal revenues and methods (sometimes in combination with legal enterprises). The particular preoccupation with putting an end to terrorist activity around the world has propelled increasing political interest in terrorist revenue sources. Studies focusing on such revenue sources have thus become more common, often tracking the funding of terrorist networks to state sponsorship, criminal activities (such as looting and bank robberies), legal activities (such as investments and commercial activity) and fundraising (see, e.g. Freeman's 2011 typology).

In several recent reports, the FATF has found that there is a risk that terrorist funding may also be associated with all of the four natural resources examined in this paper (FATF 2015; FATF-GIABA-GABAC 2016; FATF 2013a). Oil, gas, timber, diamonds and gold represent profitable sources of revenue and may also be appealing to terrorist organisations because of weak regulation in these sectors, low levels of detection, weak institutions in the countries where these resources are located and political instability in West Africa in general. However, few studies explicitly connect these resources to terrorist groups in the region. Studies focusing on the revenue sources of Boko Haram, Ansar Eddine, the Movement for Unity and Jihad in West Africa (MUJAO), Al Qaida in the Maghreb (AQIM) and other associated groups in northern Mali have *not* pointed to natural resources as one of their important sources of revenue, sometimes in contrast with assumptions and speculations (e.g. FATF-GIABA-GABAC 2016). There are, however, reports from intelligence agencies and security forces indicating that gold, diamonds and coltan may be illegally trafficked by regional terrorist organisations (ibid). There is some anecdotal (and often dated) evidence establishing a connection between Al Qaida and diamonds (e.g. Raphaeli 2003) as well as Hezbollah and diamonds (Levitt 2005a). However, most recent studies on this topic have found that the trafficking of drugs, humans and weapons, kidnapping, extortion, illicit smuggling of migrants, robberies and looting, etc. are in fact more important revenue sources for West African terrorist organisations (FATF-GIABA-GABAC 2016; Reitano & Shaw 2015; Lacher 2012; Smith 2014).

Few studies address whether natural resources are used by terrorist groups as a money laundering tool. Still, the prevalence in all four countries in this study of variants of so-called 'Hawala banking', or underground banking, is well known (Look 2012). Some of these 'banks' accept not only cash and cheques but also diamonds and gold at one location and pay a corresponding sum in cash at another (Schneider & Caruso 2011). This makes the system particularly susceptible to money laundering (McCusker 2005). More attention should therefore be paid to natural resources as currency in money laundering schemes.

A string of research points out that contemporary organised crime and terrorists alike are organised in decentralised networks and that they tend to use similar strategies to access illicit markets as well as the lawful global economy to earn money. Not only do they thrive from the same (unlawful) contextual circumstances, but terrorists and criminal networks are also becoming harder to separate from each other (Miklaucic and Brewer 2013, Dishman 2016). Some studies thus suggest that the convergence of interests of these networks has led terrorists to cooperate with cartels and trafficking organisations and to collude

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7 Terrorism is here understood in accordance with the oft-cited definition proposed by the UN in 2005, but which failed to reach consensus in the General Assembly: 'any action intended to cause death or serious bodily harm to civilians or noncombatants, when the purpose of such an act, by its nature or context, is to intimidate a population or to compel a government or an international organization to carry out or to abstain from any act constitutes an act of terrorism' (UN general Assembly 2005, §8).

with insurgents, creating a reality where categorising them as “terrorists” and “criminals” is becoming decreasingly fruitful (Matfess and Miklaucic 2016, Dishman 2016).

## Natural resources and organised crime

Valuable natural resources have always attracted criminal syndicates and, as such, are linked to organised crime in two main ways. One is the structured and large-scale illegal extraction and trade in natural resources, which in itself, is an example of organised crime. Second, criminal organisations have used natural resources as a source of income or as a means to launder money (FATF and APG 2015; FATF 2013b). Still, natural resource-related crimes constitute an under-explored field within criminology. Green crimes are often regarded as more significant environmental issues than criminal issues, and traditionally NGOs have devoted more attention to illegal resource exploitation than criminologists and law enforcement agencies (Boekhout van Solinge 2014). This means that NGOs are often at the forefront of producing updated empirical descriptions of the relationship between organised crime and natural resources (examples include the Global Initiative against Transnational Organized Crime and Global Witness). Other types of organised crime, e.g. drug or human trafficking often coincide and coexist with organised natural resource-related crime due to weak governance structures that serve as enablers (Anig 2009; Reitano & Shaw 2015). Well-functioning networks developed for one type of illicit activity (e.g. in Nigeria and Mali) can often easily be adapted to new activities and new commodities (see, e.g. UNODC 2013). An example of such versatility is illustrated by the case of criminal groups in Peru and Colombia, which had long focused on drug trafficking, who moved into artisanal gold mining when crack-downs on drug syndicates reduced the profitability of trafficking drugs to the USA (Global Initiative against Organized Crime 2016). However, as with other criminal activity, most empirical reports contain limited detail of how criminal syndicates operate within the natural resource sector, especially at the level of international organised crime. This tendency is clearly illustrated in the case of oil theft in Nigeria, where there is a substantial body of literature discussing the networks complicit in (more primitive) illegal oil bunkering in the Niger Delta (Obi 2010; Obi & Rustad 2011; Watts 2004; Bøås 2011). At the same time, there is a considerable shortage of knowledge of sophisticated oil theft, which is necessarily connected to supply chains regionally and internationally and which often involves states agencies.<sup>8</sup>

## Corruption in natural resource management

Arguably, the links between natural resources, corruption and illicit activity are often difficult to establish due to the latter two activities being opaque by their very nature. Previous research has often identified that criminal, insurgent and terrorist groups use different forms of corruption in order to access and trade natural resources (Kolstad, Søreide, & Williams 2008; Reed 2009, 2016). Contexts in which corruption is a systemic issue, anti-money laundering controls are generally weak, making it easier for criminal groups to integrate the funds generated from the illicit trade into the formal system (Kyriakos-Saad et al. 2012; Goredema 2011). It is thus well established in the literature that corruption plays a role as an enabler/facilitator in the access and trade of natural resources and that it enables criminal groups to launder the proceeds of illicit trade. An OECD (2014) review of 427 processed transnational corruption legal cases showed that 19 percent of the cases took place in the extractive sector. This makes the extractive sector one of the most corruption prone sectors overall (OECD 2014). The OECD (2016b) also recognised that it

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8 There is also little knowledge of the illegal markets for oil and gas, especially those that buy and sell large amounts of stolen petroleum products and which diffuse illegal oil into legal international markets. This gap may in part be explained by the difficulty associated with collecting such data, but it may also be due to a relatively low interest in these issues from political circles in Nigeria as well as internationally (see Katsouris & Sayne 2013).

is not sufficient to focus solely on multinational companies and host governments to address issues within the extractive sector. The report called for an approach that tackles both supply and demand sides on a national, regional and international level in order to challenge corruption (ibid).

The discussion on illicit financial outflows or capital flight in relation to trade in natural resources has often primarily focused on the size and significance of the problem (Ajayi & Ndikumana 2014; Global Financial Integrity 2015). In order to move the agenda forward, there is currently a call for improved understanding of the local drivers and dynamics that enable the illicit financial flows relating to natural resource extraction and/or corrupt politicians (Forstater 2016). A similar trend is also emerging in the natural resource management literature, where there has previously been a focus on transparency and technical solutions aimed at improving resource governance (Corrigan 2014; Humphrey et al. 2007). Parts of this literature have recently pointed to the need for more in-depth knowledge of local contexts. A suggested means to that end is political ecology analysis, which focuses on the relationship between political, economic and social factors in relation to environmental issues and changes (Williams and Le Billion, 2017). In terms of oil-related corruption in Nigeria, a range of detailed studies exist, including some recent ones (see, e.g. Sayne, Gillies, & Katsouris 2015; Sayne & Gillies 2016).

In general, we can conclude that there is considerable knowledge about the drivers of corruption and how corruption facilitates illegal trade in natural resources in general. There is, however, less new knowledge of how this benefits other illicit or illegal actors or activities, such as criminals, terrorists, rebels etc. In all of the four case studies, there is a striking lack of detail on the international aspects of the networks that facilitate or engage in natural resource theft, corruption and/or money laundering. Very few studies, even though otherwise extremely well researched, manage to establish links to international criminal syndicates, large international markets, transnational companies, etc. that actually move beyond allegations or anecdotal evidence (although there are exceptions, including the Berne Declaration 2013).

## 2.2 Framing corruption and complicity in the four cases

Corruption, understood broadly as ‘the abuse of entrusted power for private benefit’ (Transparency International 2017), can take many forms. As mentioned above, the literature is rife with examples of petty corruption and more sophisticated or grand corruption in natural resource management (NRM) in both developing and developed states. Corruption can be *ad hoc* or delimited, but in many developing countries, it permeates the governance of public resources and diverts these resources from public purposes for private gain. In order to devise sensible interventions to curb corruption and the illicit exploitation of natural resources or their proceeds, we need to move beyond acquiring knowledge of particular corruption plots and work to acquire knowledge of how corruption forms part of NRM in each context in which interventions are intended. One of the most important conclusions of this report is that resource revenues emanating from diamonds, timber, gold and oil are critical to patronage networks and clientelistic structures in which state actors are deeply embedded. This has profound implications for the manner in which we study *how* these resources wind up funding illicit activities and *why* that is the case. It also has direct implications for how we understand corruption and the measures aimed at countering it.

The four countries studied in this report all ranked low in the Transparency International Corruption Perceptions Index, meaning there are perceptions of high levels of corruption in all four countries. Nigeria recorded the highest perceptions of corruption, followed by Sierra Leone, Mali and Liberia (Transparency International 2016). In the four country contexts, often referred to as ‘neo-patrimonial systems’, a system of real power and decision-making about natural resources tends to lie at least partially outside formal institutions (Cammack 2007). Instead, decisions are made by ‘big men’ and their cronies, most often a combination of state and non-state actors. These actors are connected and driven by a logic of personal

and particularistic interest rather than the greater good of a population or state (ibid). These networks reach from the upper echelons of society (militant leaders, community leaders, members of parliament, chiefs, party officials, national bureaucrats) and down the chain to local clerks and security officers as well as villagers and criminal gangs (ibid). They also frequently include tribal leaders and international business actors. As such, these networks exist both outside of and intertwined with the state. Some of these arrangements can be termed 'informal institutions' and function according to unwritten rules that are sufficiently systematic without being formalised (Kahn 2010). In order for these networks or institutions to work over time and become stable, the benefits must be consistent with the distribution of power among participants, which is where the role of natural resources comes in. Patrons maintain power due to the fact that they distribute resources (money, favours, valuable commodities, rents) and, consequently, have a constant need to access liquid resources such as cash or lootable commodities like diamonds, which can be easily passed between individuals and which patrons can distribute. Central to the understanding of neo-patrimonial systems is therefore an understanding of the distribution of power within these systems. Kahn (2010) refers to this as the relative 'holding power' of different groups and organisations contesting the distribution of resources; holding power is partly based on income and wealth and partly on the historically rooted capacities of different groups of organised crime.

The exact structure and workings of the patronage systems involved in the extraction and flow of lootable resources are not identical across contexts but, nevertheless, seem to have some central traits in common. As described above, they tend to be governed not by state institutions with the occasional corrupt feature but, rather, by political settlements encompassing a variety of actors with negotiated access to resources. The role of 'the state' within these structures may differ substantially, and state actors may play a variety of roles in such networks, often depending on their strength and interests in a geographical area or within a particular trade/industry. In states where state authority is patchy or weak, such as in the north of Mali, in the north of Nigeria or in the remote rural parts of Sierra Leone and Liberia, state actors may have only limited ability to project their influence onto peripheral areas, and other governing arrangements may thus dominate these areas. State control may therefore be a form of 'negotiated compromise' with local strong men (Reitano & Shaw 2015). In such instances, state actors may only control the main choke points of trade but may also play a significant role, especially by producing the relevant documentation or licences required to successfully export resources (ibid, 44). In other cases, such as in Nigeria, the state largely controls the oil sector, which in this case also means that the role of the state within these oil networks is even greater.<sup>9</sup> In fact, in Nigeria, state complicity may mean that larger parts of entire state sectors, such as parts of the security apparatus or government departments, are embedded in the larger political settlements that engage in resource extraction for private gain *at the same time* as they maintain their official functions and support legal extraction. In such a system, formal institutions may form part of *informal institutions*, which in turn are dependent on the formal economic structure working and absorbing illegal resources. This makes for a complex system that includes elements of both patrimonialism and legal-rational rule (Oarhe 2013; Hastings & Phillips 2015).

State actors and politicians at the higher levels of government are more likely to be involved in lucrative large-scale theft or corrupt endeavours that require greater levels of 'protection'. An OECD (2017) review of 131 concluded large-scale corruption, including the involvement of higher-level public officials, was more often observed in the award of concessions, procurement of goods and services commodity trading, revenue management through natural resource funds and public spending (OECD 2017). Local state representatives are more often involved in smaller-scale operations or in processes related to customs

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9 This need not always be the case. Some states control access to resources without participating as extracting actors.

clearance, immigration rule and tax collection (ibid). However, the benefits emanating from corrupt schemes are negotiated relative to their power and position within the network (Kahn 2010). As such, the role of state actors may range from facilitators and protectors to key players within such settlements.

This study thus builds on an understanding that corruption is the 'lifeblood' of these neo-patrimonial systems, which means that it is often baked into opaque NRM structures. However, the subsequent case studies will attempt to identify some of the more concrete ways that corruption along the value chains of diamonds, timber, gold and oil facilitates other illicit activities in the four countries. Some of these include bribery, embezzlement, extortion, conflict of interest, nepotism in licenses/permits and fraud. Stenberg Johnson (2015, 8) has defined some of the most central forms of corruption. In this study, the following will be of relevance:

**Bribery:** The act of dishonestly persuading someone to act in one's favour by means of payment or other inducement. Inducements can take the form of gifts, loans, fees, rewards, facilitation fees or other advantages (taxes, services, donations, etc.).

**Embezzlement/misappropriation:** Stealing or misdirecting funds or assets placed in one's trust or under one's control.

**Fraud:** The act of intentionally and dishonestly deceiving someone in order to gain an unfair or illegal advantage (financial, political or other).

**Patronage, nepotism and clientelism:** Patronage in government refers to the practice of appointing people directly based on personal or party considerations. Nepotism is a narrow type of patronage, whereby offices or benefits are granted to close friends or relatives rather than on the basis of merit. Clientelism was originally conceived as the exchange of votes for political support, but it has come to refer to long-term patron-client relationships in which various types of favours are exchanged. Clientelism may not be illegal in itself.

**Rent-seeking:** The socially costly pursuit of rents, for example, the high returns that might be gained from the monopoly control of a particular commodity or service. This is not necessarily an act of corruption, but it may be.

**Conflict of interest:** A conflict between the public duty and private interests of a public official. It arises when the public official's private interests have the potential to improperly influence his or her performance of official duties and responsibilities.

In most countries, bribery, embezzlement and fraud are considered to be criminal acts, whereas different forms of patronage, rent seeking and conflict of interest are concepts that are primarily used to describe corruption. Another related concept that is central to this issue paper is **organised crime**, defined according to the United Nations Convention against Transnational Organized Crime (UNTOC) Article 2(a) as: *'a group of three or more persons that was not randomly formed; existing for a period of time; acting in concert with the aim of at least one crime punishable by at least four years' incarceration, in order to obtain, directly or indirectly, a financial or other material benefit'* (UNTOC 2004).

### 3. Case studies: How are natural resources used as a financial source for illicit activity?

This section aims to provide insight into the value chains of diamonds, timber, gold and oil in order to shed light on how these resources may be exploited to fund illicit activities. The ambitions of this section are not to provide a complete empirical picture of these issues; nevertheless, the four different case studies serve to identify some of the *risks* of sponsoring illicit activity associated with trade in these commodities.

#### 3.1 Sierra Leone – Are diamonds forever a rebel’s best friend?

##### Context

Sierra Leone is a small country with a population of around 6.5 million and is rife with natural resources, including diamonds (World Bank 2015). It is portrayed as an example of a country in which vast natural resources are a source of conflict rather than development (Collier & Hoeffler 1998). Sierra Leone became famous in light of the 1991–2002 civil war, the story made famous by a variety of books and the Hollywood production *Blood Diamond*. The initial debate on the most significant factors of the civil war outbreak revolved around greed (Collier 2000) and grievance (Richard 2003; Rosser 2006). While the debate concerning the role of diamonds in the civil war has been nuanced over time,<sup>10</sup> the civil war itself can be explained by a variety of factors, such as Sierra Leone being a neo-patrimonial state which suffered from issues such as social exclusion resulting from longstanding patron–client relationships (Bøås 2001). The development of patron–client relationships began with the withdrawal of the colonial power, whereby ‘strongmen’ filled the vacuum left by colonialists (Bøås 2001). Leadership in Sierra Leone has historically revolved around ‘strongmen’ who provided for their network in order to maintain order, doing so with a mix of severe political violence and patronage (Christensen & Utas 2008). Historically in Sierra Leone, when the power of ‘strongmen’ diminished and leaders were no longer able to fend off competing factions, there was a high risk of political violence (Bøås 2001). This dynamic has been used to explain the outbreak of the civil war; as support for Sierra Leone dried up, so did resources for distribution in patronage networks, leading politicians to struggle to maintain both networks and stability (ibid). This tendency is also important for grasping the outbreak of the civil war as it brings a nuance to the previously popular and established picture of Sierra Leone and that the civil war was primarily about diamonds.

According to the United Nations (1993), Sierra Leone had the second lowest global living standard before the war, despite the country’s vast natural resources. Sierra Leone lacked a functioning governance structure and had a history of patronage systems stemming from the one-party state as well as from the Paramount Chieftaincy system (Maconachie & Binns 2007).<sup>11</sup>

Before the 1990s, authoritarian leaders, whose primary concern was self-enrichment, ruled Sierra Leone for over two decades (Reno 1995). The parties to the decade-long civil war were originally the Revolutionary United Front (RUF) and the Sierra Leone Army (SLA). As the civil war went on, other factions formed

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10 Diamonds are reportedly not considered an important incentive on the individual level for engaging in the conflict (Richards 2003). However, Humphreys and Weinstein (2008) found that fighters who were offered money or diamonds were much more likely to engage in the conflict. The paper also found that most of the low-level fighters were actually worse off after the end of the conflict (Ibid).

11 British colonial rule implemented the Paramount Chieftaincy system, giving power to local chiefs to collect taxes, control judicial systems and allocate land. The system still exists as a parallel governing logic in Sierra Leone, where the chiefs still have significant power in local politics (Acemoglu et al. 2014).

such as the Armed Forces Revolutionary Council (AFRC), which later became an ally of the RUF (Keen 2005). An illustrative notion from the civil war were *'sobels'*, soldiers who fought for the SLA in the daytime and the RUF at night – soldiers at day and rebels at night (Keen 2003). This is just one example of a very intricate situation in which loyalty became difficult to determine and conflict a way of life. The lack of resources within the SLA made it considerably more attractive to join the rebels (RUF), who often engaged in looting and raids.

The civil war had horrific impacts on the population, with over 50,000 Sierra Leoneans killed, half of the population displaced from their homes and thousands of victims of violence and sexual abuse (Human Rights Watch 1999). After a series of coups and failed peace agreements, the civil war was declared over in January 2002 by President Ahmad Tejan Kabbah from the Sierra Leone People's Party (SLPP) (Gberie 2002). President Ernest Bai Koroma, representing the All People's Congress (APC), has been serving as president since 2007.<sup>12</sup>

In 1999, the United Nations deployed military personnel to Sierra Leone under the United Nations Mission in Sierra Leone (UNAMSIL), and peacekeeping troops remained there until 2005. Beyond the military interventions, Sierra Leone saw an influx of development aid aimed at improving basic services and governance. Sierra Leone has, since the end of the civil war, been a relatively stable country, recording an improved Human Development Index as well as life expectancy from 2000–2014 (UNDP 2016). According to the Ibrahim Index of African Governance (IIAG), Sierra Leone has made substantial improvements in security and the rule of law since 2006 (IIAG 2016). Despite the improvements, however, Sierra Leone continues to struggle with governance and poverty issues (Bertelsmann Stiftung's Transformation Index 2016a).

## The importance of diamonds to Sierra Leone

A key factor in Sierra Leone's diamond mining sector is that most diamonds are found in river beds (alluvial diamonds) and not in kimberlites, which requires a more sophisticated extraction process (Gberie 2002). This makes Sierra Leone's diamonds 'lootable', as they are accessible through traditional mining techniques that do not require advanced machinery or technology. Alluvial diamonds thus provide better opportunities for illegal mining than kimberlite diamonds. Further, artisanal mining is more difficult to control than kimberlite mining (Levin & Gberie 2006).

Official figures from 2014 show that around 30 percent of exported diamonds stem from alluvial mining, however, a significant amount of the alluvial diamond trade is conducted outside the formal system (Kimberley Process 2014). The exported diamonds are 'rough diamonds' that are less valuable than cut diamonds used for jewellery and industrial purposes. Globally, Europe and the US are the two biggest markets for diamond jewellery, according to the consulting company Bain (2015). The net import of

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<sup>12</sup> The APC is a previous opposition party which established popularity by challenging the previously dominant SLPP party (Bertelsmann Stiftung's Transformation Index 2016a).

rough diamonds from Sierra Leone for the purpose of cutting and polishing are, according to the same report, dominated by India, followed by China.<sup>13</sup>

### Artisanal Mining

Artisanal mining (ASM) can be formal or informal, legal or illegal. Informal mining usually refers to mining that does not meet all legal requirements, but nonetheless takes place in permitted zones, while illegal mining implies an outright violation of the law (UNTOC 2016). Artisanal mining is labour intensive, which means that minerals are extracted from the soil with unsophisticated technology. In general, it is based predominantly on simplified forms of exploration, extraction, processing and transportation. ASM usually exploits marginal or small deposits. It is usually not capital intensive and is generally performed in groups or cooperatives, e.g. families or work groups of 4–10 persons (OECD 2013). It is thus often associated with poverty and the illegal economy, negative environmental and health impacts and negative social impacts, including child labour, forced labour, gender based violence, prostitution and crime in general (UNICRI 2015).

## A historic perspective on the Sierra Leone Diamond Trade

The history of diamond mining in Sierra Leone is important because it provides a glance into the establishment of the complex patronage system that still dominates diamond mining and trade today. Diamonds were first discovered in Sierra Leone in the 1930s. In the early days, the government granted exclusive extraction rights to an affiliate of DeBeers, the Sierra Leone Selection Trust (Maconachie & Binns 2007). The company held the exclusive rights until 1956 when the introduction of the alluvial mining scheme by President Siaka Stevens allowed Sierra Leoneans to legally extract diamonds through alluvial mining (ibid).

The reform was aimed at minimising illegal mining by making alluvial mining a legal option. In hindsight, however, the reform became a tool for President Stevens to further expand his patronage network by granting alluvial mining licences to allies and cronies. Stevens nationalised diamond mining by transforming the Sierra Leone Selection Trust into the National Diamond Mining Company. As part of the process, he granted himself and his key Lebanese advisor complete control of diamond mining (Maconachie 2009). The Lebanese minority in Sierra Leone has since established itself as a key player in the diamond trade. Under Steven's 17-year rule, official diamond exports fell from more than two million carats in 1970 to 595,000 carats in 1980 and 48,000 carats in 1988 (Temple 2006). This was because large amounts of diamonds were being smuggled through Liberia to avoid taxation.

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13 Diamonds are an important component of the Sierra Leonean economy, though not the only resource of importance. While diamonds receive a lot of attention, cocoa and plastic are by far the two biggest exports from Sierra Leone, followed by coffee, tea and rubber, according to the International Trade Centre (2016a). The country is mineral rich in general, and iron ore and coltan are becoming increasingly important to the economy. A recent case study by Hunter and Smith (2017), argues that the artisanal gold mining sector is also becoming increasingly important, primarily due to the scarcity of alluvial diamonds. There is, however, a general natural resource management issue in the country, which means that focusing exclusively on improving the governance of diamonds may help create opportunities for the exploitation of other resources.

Both the Alluvial Mining Scheme and the National Diamond Mining Company reforms relied on the Paramount Chief system established by the British colonial power, which granted licences to local chiefs to expand Stevens's patronage network (Maconachie & Binns 2007). Although the chiefs were often the targets of attacks by the RUF, they continued to play an important role in local governance (Bellow & Miguel 2009). In looking at the history of the diamond trade in Sierra Leone, it becomes clear that even before the civil war, there was very limited formalised governance of the diamond sector and that diamonds and other natural resources were used to build and sustain patronage networks or for self-enrichment. Accordingly, there was no formal functioning system to build on in the post-war period.

## The current diamond trade

Alluvial diamond mining is still an important source of employment in Sierra Leone and helps to provide stability and employment, especially among young men. Alluvial diggers rarely make a living on diamond mining alone and often also work on farms as a secondary source of income.<sup>14</sup> Numbers from the Sierra Leone government (2015) state that 17 small-scale mining companies and 200,000 artisanal miners operate in the country.

Quarrying/mining accounts for 20 percent of Sierra Leone's GDP, which makes it a significant economic sector for the country (AfDB, OECD, & UNDP 2016). Trade data from the International Trade Centre (ITC 2015a) shows that 76 percent of diamond exports from Sierra Leone goes to Belgium, a famous diamond cutting and trade hub. The second biggest export destination for Sierra Leone's diamonds is Mauritius, accounting for 8.7 percent of the trade. In total, Sierra Leone exported diamonds amounting to approximately USD\$127 million in 2015 (ITC 2015a). As a way to make the diamond trade more transparent, the Sierra Leone government (2016) set up an online repository from where it is possible to track income generated from mining concessions as well as the holders of both large-scale (kimberlite) and small-scale (alluvial mining) diamond concessions.

Sierra Leone suffers from a significant rural-urban divide. Poverty remains rampant in rural areas, whereas urban areas, Freetown in particular, are considerably more developed. Mining constitutes an important source of income for the poorer rural population in Sierra Leone (Fanthorpe & Gabelle 2013). In order to improve the sustainability of both diamond mining and the diamond trade, the Sierra Leonean government created the Diamond Area Community Development Fund (DACDF) in 2001. The fund aims to correct the power imbalances within the diamond trade, redistribute resources and promote political stability (Maconachie 2012). The DACDF has, however, failed to deliver the expected outcomes, partly due to the prevalence of embezzlement and patronage in the distribution of benefits (ibid). In a review of community mineral beneficiation schemes, Dupuy (2017) identifies a lack of transparency in the allocation of funds and vague targets in respect of the funds as key issues limiting the utility of the DACDF. In addition, the DACDF uses the old chieftaincy system to redistribute benefits from the diamond trade, which means that old patronage structures and dynamics are allowed to live on in the current system. In addition to corruption issues, DACDF is at times criticised for having a *destabilising* rather than a stabilising effect. This is mainly due to issues with limited public participation in decision-making regarding the funds, which tends to reinforce existing unequal power relations (Maconachie 2012).

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14 According to Engwicht (2016), the daily wages of diggers range between 1,000 Leones (approximately 20 cents US\$) and 7,000 Leones (approximately \$1.5 USD).

## How do diamonds divert from the legal value chain?

It is important to note that diamonds extracted through alluvial mining are not by definition illegal. There is a legal framework for alluvial mining in Sierra Leone, and small-scale miners can obtain licences (Levin & Gberie 2006). Diamonds from Sierra Leone more often divert at the point of extraction, close to its source, rather than later in the value chain. Miners and middlemen can, for several reasons, choose to trade diamonds illegally rather than using formal channels (Levin & Gberie 2006; Wilson 2011; Engwicht 2016). The motivation for choosing informal channels may be that they lack licenses for extraction, to avoid taxes, to achieve more lucrative prices on the informal markets or to smuggle the diamonds to a neighbouring country where the prices may be higher (Engwicht 2016). Wilson's (2011) field study found that better prices in neighbouring countries was the primary reason for smuggling diamonds out of Sierra Leone. The diamonds are then integrated in the legal value chain in the country of exchange, for example, in Guinea (ibid). The field study also identified the lack of monitoring as a key driver in illicit mining and that government officials often know of the illicit mining but choose not to interfere because of kicks-backs/bribes.

## The role of the civil war networks

During the civil war, the RUF and other actors used the export revenue from natural resources to buy weapons, supplies and ammunition, often in direct barter trading (Keen 2005). Throughout the war, close links developed between the RUF and the Liberian dictator Charles Taylor; these links also expanded to international arms traders and organised crime (Gberie 2002). To stop the revenue stream to the RUF and Charles Taylor, the UN sanctioned the rough diamond trade from both Sierra Leone and Liberia (UNSC 2000). Although the leaders from the civil war era, Charles Taylor (imprisoned) and Foday Sankoh from the RUF (deceased), are gone, established networks and trade routes are likely sustained by former fighters and diamond traders (PAC & Global Witness 2008).

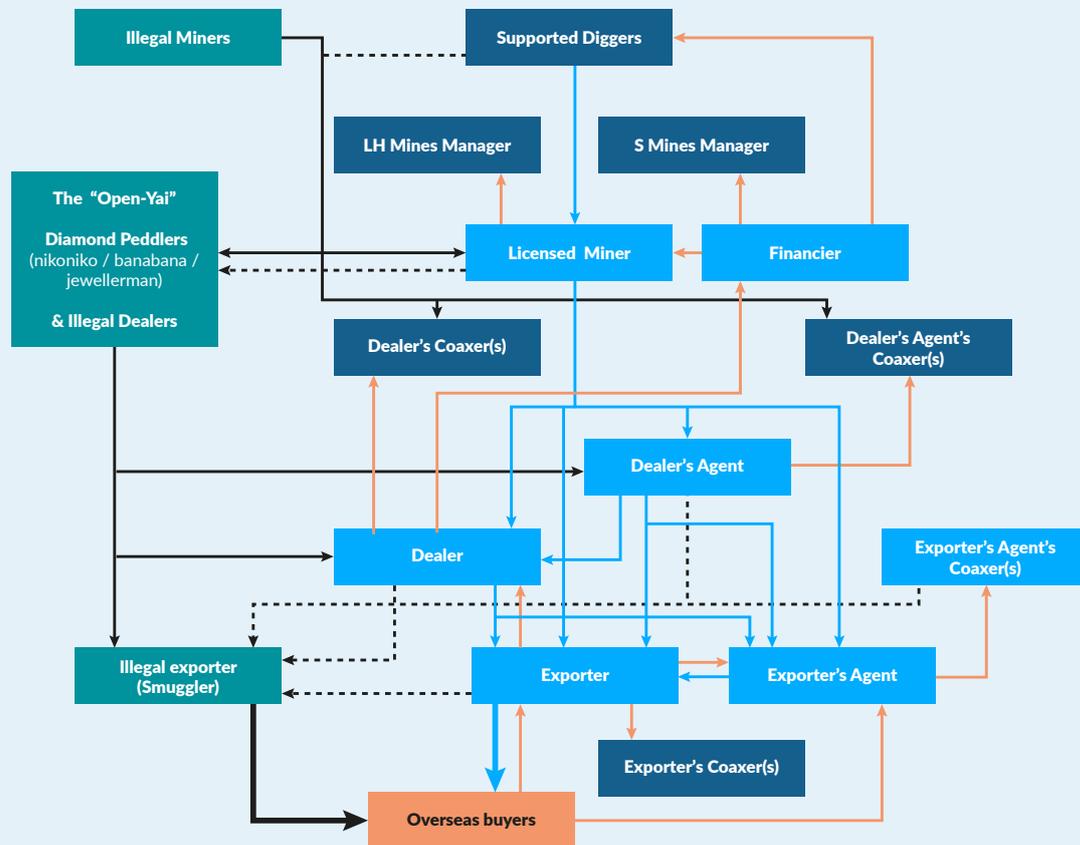
Civil wars tend to blur lines between illegal and legal activities, creating an acceptance of illegal behaviour (Williams & Picarelli 2005). Reno (2016) found that as key players from the civil war and previous authoritarian leaders still hold significant power in Liberia, there is a risk that groups from the old diamond elite also remain significant players within the diamond trade today. That old networks persist beyond the civil war is in no way unique to Sierra Leone, however, it is part of the growth-stability trade-off whereby powerful players are incentivised in post-conflict solutions to guarantee stability (Vorrath 2015). In fact, Engwicht (2016) found that the influence of the old networks is still present in the current diamond trade where diamonds are smuggled in and out of Sierra Leone by means of old established networks and transport routes.

## Diamond smuggling and informal diamond markets

Following the end of civil war, sanctions on Sierra Leonean rough diamonds were lifted by establishing the Kimberley Process Certification Scheme (KPCS). The KPCS is a certification process related to the place of origin of the diamonds to ensure that diamonds are 'conflict free'. According to KPCS statistics, the members of the initiative control 99.8 percent of the formal global production of rough diamonds (KPCS 2016). If numbers are accurate, this should make the diamond trade fairly well regulated, although the KPCS has been criticised for its limited scope, which excludes human rights abuses, and that diamonds from conflict areas can easily be mixed with diamonds from non-conflict areas (Howard 2015). However, studies have documented several issues relating to the KPCS. Estimates from Vorrath (2014), for example, indicate that 50-90 percent of diamonds from Sierra Leone's formal and informal small-scale mining operations are in fact not registered with the KPCS. Furthermore, large proportions of these diamonds are

also smuggled out of the country according to the same report (ibid). In Sierra Leone, however, the KPCS was initially successful in limiting opportunities for the illicit diamond trade and in reducing revenue flows to the parties to the former civil war. Yet, a 2015 evaluation of the KPCS showed that while the formal export of diamonds rapidly increased in the years following the implementation (Howard 2015), the quality (carat) of the diamonds remained low. This raised suspicions that the high quality diamonds were still being illegally traded (ibid). Reports have also pointed to the lack of transparency in the diamonds valuation process (International Consortium of Investigative Journalists 2016). Companies can lower their export values to avoid taxes and shift profits externally (ibid). While the KPCS has established a set of regulations for the diamond trade both in Sierra Leone and globally, it has been struggling with the

Figure 1: The Artisanal Diamond Chain, in practice



**Legend**

Legal transfer of diamond	Owns diamond (primary beneficiary)
Illegal transfer of diamond	Illegally owns diamond (primary beneficiary)
Illegal transfer of previously legal diamond	Involved in trading diamond and securing ownership, employed by superior in chain (secondary beneficiary)
Transfer of money	

Source: Levin & Gberie 2006

prevalence of fake export certificates, making it difficult for diamond traders to evaluate their authenticity (ibid). Resource traders may thus risk trading in conflict diamonds, even when they have followed the formal rules.

Engwicht's (2016) field research into the informal diamond trade reveals that diamonds found by diggers (alluvial miners) are traded in so-called 'Open Yai' (eye) markets by Banabanas (middlemen). According to the study, the trade is formally illegal but socially accepted; and it is informally approved by supervising authorities like the police and the Ministry of Mines and Mineral Resources. Engwicht (2016) found that Open Yai markets and middlemen have informal rules and honorary codes that traders follow. They also have collective funds for healthcare, weddings, funerals and elected chairmen. Middlemen facilitate the trade between diggers and high-end traders (both legal and illegal), and they arrange smuggling to neighbouring countries if the prices are higher or if a buyer prefers to make the deal in another jurisdiction (Levin & Gberie 2006; Engwicht 2016; Wilson 2011). According to Engwicht (2016), as well as other older studies, high-end traders are usually based in Freetown and are both foreign and Sierra Leonean (mostly from the Lebanese minority). Diggers and middlemen bribe officials to avoid a crackdown on the trade and can function relatively free of interference (ibid). In contrast to high-end traders who have licences and a wholesale approach to their trading, the Open Yai markets are an option for diggers – often young men who seek to profit from small-scale trading (Levin & Gberie 2006; Engwicht 2016).

In Levin and Gberie's (2006) field study for the Diamond Development Initiative, they illustrate the very complex relationships involved in the alluvial (artisanal) diamond trade (see figure 1).

As illustrated in Figure 1, the illicit diamond trade chain is complex, with a constant overlap between legal and illegal actors. The illustration dates back to 2006, but recent field research conducted by Engwicht (2016) found that the same structures still exist in Sierra Leone. According to both reports, while it is more common for diamonds to divert from the legal value chain at an early stage, it is an issue at all levels of the value chain. Open Yai markets and middlemen continue to play an important role in the value chain, suggesting that informal diamond trade outlets still exist in Sierra Leone. Importantly, if powerful informal networks, like chieftains, benefit from the current form of diamond trade, they are likely to interfere with or sabotage attempts to formalise the trade.

Figure 1 illustrates not only the complex structures of the diamond trade in Sierra Leone, but also the many diamonds can be diverted from the legal value chain. This is facilitated by the lack of oversight and enforcement of regulation, which is due to a combination of low governing capacity, lack of resources and bribery (Levin & Gberie 2006; Wilson 2011; Engwicht 2016).

## **Do diamonds finance illicit activity?**

The tendency to use diamonds to finance conflict in Angola, the Congo and Sierra Leone gave birth to the phrase 'diamonds are a rebel's best friend' (Olsson 2006). The high-value of diamonds, combined with the ease with which they are extracted and transported, make them attractive as tools to enable other illicit activity. It is well established that during the civil war, diamonds were used for illicit activity and self-enrichment (Keen 2005). However, the role that diamonds play in funding illicit activity in the post-civil war period is less understood.

### **The terrorist rumours**

Reports from the *Washington Post* in the aftermath of the 9/11 terrorist attacks connected Al-Qaeda to the diamond trade in Sierra Leone and Liberia (Douglas 2001). However, the reports were based on

limited anecdotal evidence. The proposed link is between Al-Qaeda via Lebanese diamond traders in West Africa to the RUF. There are also a few reports linking Lebanese diamond traders to the Lebanese terrorist group Hezbollah. These reports claim that Hezbollah used diamonds originating from Sierra Leone for funding and money laundering purposes (Douglas 2001; Levitt 2005a). Lebanese traders have come under increased scrutiny post-9/11, but the evidence remains anecdotal, and there is no solid proof that Lebanese traders have connections to Hezbollah or that Sierra Leone's diamonds are used for terrorist financing. These reports date back to the early 2000s, and there have been no later reports or court cases directly linking diamonds from Sierra Leone to terrorist financing. However as the FATF (2013a) points out, the characteristics of diamonds combined with the weak governance of the diamond trade create a *risk* that they may be used for the purpose of terrorist financing.

### The potential link to organised crime

Research by Engwicht (2016) and Levin and Gberie (2006) found that middlemen and high-end diamond traders engage with drug traffickers ('powdermen'), who then seek to buy diamonds for money laundering purposes. These studies reveal that high-end traders also engage in illicit trade whereby potential buyers, for unconfirmed reasons, are interested in acquiring diamonds. According to the FATF (2013a), the continued smuggling of diamonds in and out of Sierra Leone constitutes a significant money laundering risk. The FATF also acquired anecdotal evidence of people flying into the country with money and leaving with diamonds (ibid). There is a real risk that criminal networks still have contacts, and are involved, in the diamond trade. One such connection would be the case of Erez Daleyot, a Belgian-Israeli diamond tycoon, as revealed in the HSBC Leaks (or 'Swizz Leaks'). Bank documents show that Daleyot used the diamond trade to launder money for organised crime groups and corrupt politicians with links to Sierra Leone (International Consortium of Investigative Journalists 2015). In sum, unlike the risk of terrorist financing, there are reliable records of diamonds being used to launder money by persons connected to organised crime (ibid), although a substantial amount of this evidence is anecdotal.

In an attempt to address the illicit trade, in 2009, several UN agencies together with Interpol and the Economic Community of West African States (ECOWAS) created the West African Coast Initiative (WACI) to address the growing problem of illicit drug trafficking, organised crime and drug abuse in West Africa (UNODC 2017a). The initiative seeks to improve regional cooperation since the illicit trade often stretches across borders, and many of these countries, like Sierra Leone and Liberia, are closely connected.

### The use of secrecy jurisdictions

Research shows that in cases relating to illicit financial flows and corruption, jurisdictions with high banking secrecy are often used to hide the true beneficiary and origin of funds (Van der Does de Willebois et al. 2011; GFI 2015). An OECD report (2016c) on corruption in the extractives value chain shows that the use of secrecy jurisdictions is a common global phenomenon in corruption cases in the extractive sector. One example of the use of secrecy jurisdictions in Sierra Leone is a Subsidiary of OCTÈA Limited, also known as Koidu Holdings, which has a large kimberlite mining concession in Sierra Leone. According to the International Consortium of Investigative Journalists (ICIJ), OCTÈA Limited accounted for 50 percent or more of Sierra Leone's diamond exports, yet there is no data on how much the company paid in taxes. The agreement with the government states that OCTÈA Limited are subject to 35 percent tax on net profits. The company is located in a secrecy jurisdiction (British Virgin Islands), which makes it very difficult to access any financial data (ICIJ 2016). OCTÈA Limited was also ousted in the *Panama Papers* as being part of the controversial Israeli diamond trader Beny Steinmetz' company group (ICIJ 2016). Steinmetz was later arrested over a bribery case in Guinea, where he is also suspected of money laundering (*The Guardian* 2016). The example illustrates not only that diamonds are potentially used for corrupt

purposes but, also, the difficulty faced by the Sierra Leone government in generating the appropriate benefits from the diamond trade. It is important to note that Sierra Leone, as a signatory to the Extractive Industries Transparency Initiative (EITI), is actively working on addressing beneficial ownership issues. In 2016, the government published a roadmap towards a public beneficial ownership registry for the extractive sector scheduled to become available in 2018 (EITI 2016a).

## How is the illicit trade facilitated by corruption?

Informal networks continue to play a key role in distributing power and resources in Sierra Leone, as exemplified by the informal diamond trade systems and the role of chiefs in DACDF (Maconachie 2012; Engwicht 2016). Illicit trade, both current and past, has been facilitated by networks or informal settlements with vested interests in maintaining some level of informality in trade for personal gain (Levin & Gberie 2006; Engwicht 2016). A report on artisanal gold mining in Sierra Leone (Hunter & Smith 2017), found that bribes are paid to government officials in order to avoid interference in the illicit trade. Bribery can be used to access the resource by paying officials for a license to extract diamonds or to avoid interference in illicit extraction (Levin & Gberie 2006; Engwicht 2016). In the later stages of the trade, bribes/kick-backs may be paid to officials to access fake documentation or to smuggle the diamonds out of the country (Wilson 2011; Howard 2015; Engwicht 2016). Access to fake documentation facilitates the integration of illegally extracted diamonds to the legal value chain (Howard 2015). From a wider perspective, corruption plays a role in enhancing the prospects for criminal organisations to launder the proceeds of crime through the illicit diamond trade, as shown in the Swiss Leaks (ICIJ 2015). In addition, embezzlement and fraud limit the prospects of generating and distributing benefits from the diamond trade, as shown in the example of the DADCF (Maconachie 2012; Dupuy 2017) and the potential tax evasion case involving OCTÈA Limited (ICIJ 2016). This in turn forms part of larger systemic issues whereby exchanges of loyalty and favours take place outside the formal state system.

## Are reforms limiting the role of corruption in the illicit diamond trade?

There have been several attempts to curb the illicit diamond trade in Sierra Leone, such as the Kimberley Process, the DACDF and the EITI. Although these initiatives are directly aimed at targeting corruption, they all have components that are supposed to address corruption through certification, efforts to increase transparency as well as a more equal distribution of the benefits generated from the diamond trade. A Global Witness (2013) report on the timber sector in West Africa shows that permits have been abused by corrupt public officials. There are also reports of issues with fake Kimberley certificates in the diamond trade (Howard 2015). In addition, several reports also indicate that Sierra Leonean government officials are complicit in the trade and actively seek bribes/kick-backs (Wilson 2011; Howard 2015; Engwicht 2016). This can be partially explained by the fact that regulatory authorities like the police and the Ministry of Mines and Mineral Resources lack resources in terms of salary and equipment (Levin & Gberie 2006; Howard 2015; Engwicht 2016). However, the government's failure to address the informal diamond trade and to generate/distribute the benefits from the diamond trade suggests rent-seeking behaviour within institutions. This implies that there are more incentives for rent-seeking activities than the impartial delivery of services (Kolstad & Wiig 2009). To solve these issues, the underlying incentives for rent-seeking behaviour need to be addressed (ibid).

As shown by Wilson (2011), economic incentives play a key role in diamond smuggling, and a better distribution of diamond benefits can potentially curb some of the smuggling. Dupuy (2017) has pointed out that introducing greater transparency can be part of the solution to overcome the issue with the DACDF. More transparency into DACDF funds can be particularly useful at the local level where the community has a direct interest in the funds being distributed more equally. At the national level, an

online repository has been developed as part of the EITI framework, which enables media and civil society organisations to better monitor the licensing process in the diamond trade and extractive industry at large. However, as seen in the OCTEA Limited case, companies can still avoid revealing potential beneficial owners and tax payments. In order for transparency to be effective, measures are needed to ensure that the data provided is accurate. In addition, there is a need for a strong watchdog, such as civil society organisations and independent media outlets. A recent review by Rustad et al. (2017) shows that there are mixed results from revenue transparency projects like EITI. In addition, Vorrath (2015) points out that there is lack of trust in international arrangements in Liberia and that local informal extraction often enjoys more trust in affected communities.

The opportunity to smuggle and trade in diamonds in Sierra Leone is facilitated by a corrupt system. There is a need to better understand the incentives of the groups involved in this trade in order to design effective counter-measures. The informal diamond sector continues to play an important role in the illicit trade. Still, since alluvial mining and diamond trading are a source of revenue for many young men (Levin & Gberie 2006; Howard 2015; Engwicht 2016), if the informal sector is eliminated, there would be a need to find new sources of income for this group or to ensure their integration into the formal trade by providing economic incentives. Interestingly, in the absence of a formal regime, diggers and middlemen are already constructing their own redistribution channels and codes of conduct (ibid). These codes of conduct, unfortunately, do not include a ban on smuggling or the illicit trade in diamonds (Engwicht 2016), but there is probably a significant chance of eliminating some of the most harmful ways of trading by incorporating the group into the formal sector while still ensuring that the source of revenue does not disappear. To do this, there is a need for a better understanding of political economy and the interest/incentives of the stakeholders involved in the illicit diamond trade.

## Summing up

Diamonds remain an important resource in Sierra Leone, albeit a controversial resource that has consistently been used to build and nurture patronage networks and to finance armed groups. Diamonds have, as such, encouraged violence, corruption and the survival of influential networks that benefit from the illicit trade and, hence, will seek to retain a status quo. While diamonds are no longer directly funding conflicts in Sierra Leone, the findings in this paper indicate that the illicit diamond trade is still an issue in Sierra Leone, although it is not clear the extent to which it is used to finance organised crime and terrorism. In Sierra Leone, diamonds are easily accessible, and the fact that they often are extracted and traded outside supervision and regulation in an otherwise corrupt environment creates a risk that diamonds are exploited for money laundering, criminal activity and terrorist financing. Although the global diamond trade is regulated through the Kimberley Process, the system can be abused through forged documentation, which is used as a tool for integrating illicit diamonds into the legal value chain. This leaves diamond trading companies exposed, making it difficult to differentiate between legal and illicit diamonds. The illicit trade is facilitated by bribery whereby local officials are bribed to disregard the illegal extraction and trade. However, this is only one part of a governance system in which institutions fail to monitor and regulate trade as well as to generate and distribute the benefits from the diamond trade. The findings show that diggers, traders and state officials have economic incentives to engage in the illicit trade. To design effective interventions, the economic incentives need to be addressed in combination with the current power structures that benefit from maintaining the informal trade. Consequently, further in-depth analyses, such as political ecology or political economy analyses, are highly recommended before designing further interventions tailored to preventing diamonds from financing illicit activity on their way to consumer markets.

## 3.2 Liberia and timber: Rooting out the illicit trade?

### Context

Liberia, similar to Sierra Leone, has a history of patronage and a long civil war which lasted from 1989–2003. Both President William Tolbert (1971–1980) and President Samuel Doe (1980–1990) used natural resources to build patronage networks (Andersen 2010). Liberia's elite has been dominated by particular groups (mostly Americo-Liberians) who enjoyed privileges, such as the right to own land, often distributed and supervised by traditional chiefs (Beevers 2015).

The civil war was initially between Charles Taylor's National Patriotic Front of Liberia (NPFL) and Samuel Doe's loyal faction, the United Liberation Movement of Liberia for Democracy (ULIMO) (Gariba 2011). It began when Charles Taylor tried to grab power from the incumbent dictator, Samuel Doe. After years of fighting, Charles Taylor consolidated his power by winning a controversial election in 1997, held as an attempt to end the civil war.<sup>15</sup> Taylor established a 'warlord economy', a system based on the domination of a market established by violence rather than on state authority or political networks (Reno 2007). Taylor used his network to trade timber, gold, diamonds and rubber for weapons and supplies to sustain his network. This network also expanded to neighbouring countries like Sierra Leone and Guinea (Reno 1998). At the end of the civil war in September 2003, the UN installed its peacekeeping Mission in Liberia (UNMIL). The objective of UNMIL was to provide humanitarian assistance and security to stabilise the country as well as to improve governance of natural resources (UNSC 2003). In addition, the UN imposed a ban on trade with timber from Liberia in 2003, which limited Taylor's revenue sources and his prospects of continuing to finance the conflict (ibid).

Similar to Sierra Leone, there has been debate concerning the role of natural resources in explaining the war. Natural resources were seen by some as the root cause of war because it incited 'greed' (Collier 2000), while others saw the war as being motivated by 'grievance' related to the unequal distribution of natural resources (Ellis 1999). However, there are also alternative explanations to greed or grievance. The civil war in Liberia and Sierra Leone are not only connected because of geographical proximity and spill-over effects during the war; they are also connected because of a similar post-colonial neo-patrimonial rule that contributed to the civil war. Liberia suffered from deep problems with corruption, political violence and poverty (Utas 2003). These tensions, in combination with a weakened strongman rule, which was unable to maintain patronage networks, arguably contributed to the outbreak of the civil war (Bøås 2001).

In 2006, Liberia elected Ellen Johnson Sirleaf as president. Her first action was Executive Order No.1, which cancelled all existing logging concessions in Liberia. As such, all companies had to reapply for logging concessions (Beevers 2015). Johnson Sirleaf also inherited the Governance and Economic Management Assistance Programme (GEMAP), a major good governance programme with a budget of around USD\$500 million, which constrained the government's independence by placing external experts in key positions in government bodies (Reno 2008; Bøås 2009). The aim of the programme was to reconstruct the 'failed state' by providing funds and expertise and to limit official abuse of the system. GEMAP, in effect, put parts of the Liberian government under financial trusteeship to curb corruption for a limited period of time. Although the programme led to an immediate increase in government revenue, it proved unsustainable due to a failure to address the deeper social roots of corruption and because of its

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15 Not all rebel groups accepted the election result, and the Liberians United for Reconciliation and Democracy (LURD), fighting out of Guinea, and the Movement for Democracy in Liberia (MODEL), fighting out of the Ivory Coast, continued to engage in warfare against Taylor (Ford 2015).

short-term focus (Reno 2008; Bøås 2009). Ellen Johnson Sirleaf, still president of Liberia, has proclaimed zero-tolerance against corruption. Under her rule, Liberia has implemented several anti-corruption efforts such as the Liberian Anti-Corruption Commission (LACC), the General Auditing Commission, the Governance Commission, the Integrated Tax Administration System (ITAS), the National Land Commission and the Public Procurement and Concessions Commission (PPCC) (U4 2012). The results of these initiatives are mixed. On one hand, they have created solid frameworks and institutions, but according to Funaki and Glencorse (2014), many of these institutions struggle with effective enforcement due to issues such as bribery, nepotism, low salaries and lack of capacity. Enforcement is also criticised for being biased, only targeting out-of-favour politicians (Bertelsmann Stiftung's Transformation Index 2016b). Johnson Sirleaf has also appointed three of her sons in senior positions with significant economic power (ibid), a sign that the country is still struggling with patronage and nepotism.

## The importance of timber to Liberia

Liberia is rich in natural resources, with significant deposits of gold, diamond, rubber and timber. Despite not being the only important resource, timber remains significant to the economy.<sup>16</sup> Export data from 2015 show that, in 2015, Liberia exported around USD\$43 million worth of timber (ITC 2016b). According to Bickel and Cerutti (2017), the informal chainsaw milling sector provides between 19,000 and 24,000 more or less permanent jobs to individuals in urban and rural areas. According to calculations in the same report, the sector has an annual revenue between USD\$31 million and USD\$41 million, making it an important source of income for the rural population (ibid).

Liberia has historically had a liberal approach to trade and has long had an 'open door policy', inviting large foreign companies to invest in the country. After the civil war, the so-called 'conflict timber' was going to be transformed to 'peace timber' based on the 'three Cs' – conservation, commercial and community – and serve as a driving force in post-conflict reconstruction (Beevers 2016). Estimates from 2014 indicate that more than 50 percent of Liberia's land masses have been granted to commercial concessions, a figure expected to rise to 75 percent (De Wit 2014). The large concessions have, so far, mostly failed to translate into any significant benefits for local communities (ibid). This, among other factors, has led to low trust in international arrangements in Liberia (Vorrath 2015). Timber remains important to the Liberian economy, especially to the rural population, but logging has largely failed to benefit local communities to a significant extent (ibid).

## Reforming the timber trade

In 2006, Liberia passed the National Forestry Reform Law (NFRL), which led to a permanent lifting of the previous UN timber trade ban on the country (Government of Liberia 2006). Liberia has also signed the EITI and entered a Voluntary Partnership Agreement (VPA) with the European Union (EU) (Government of Liberia 2009). The VPA is a component of the Forest Law Enforcement, Governance and Trade Plan (FLEGT), an EU initiative that aims to reduce illegal logging by strengthening sustainable and legal forest management, thus improving governance and promoting trade in legally produced timber (European

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16 Since 2008, forestry has been a central component of Liberia's Poverty Reduction Strategy (PRS), especially for the economic revitalisation of rural areas (IMF 2008). Estimates from 2007 show that the formal logging sector provided direct employment for between 7,000–10,000 people in Liberia (Altman & Woods 2012). During the civil war, and in its immediate aftermath, logging for household and commercial purposes led to estimated losses of 33,000 hectares per year, and in 2005, approximately 4.5 million hectares remained (ibid). Despite the depletion of forests during the civil war and its aftermath, logging is still considered a major source of income for the government.

Union FLEGT 2016a). In 2014, Norway signed an agreement with Liberia to tackle deforestation in the amount of around USD\$120 million. The agreement seeks to improve forest monitoring and rural communities' capacity in sustainable forest management (Government of Norway 2016). These initiatives have contributed towards the establishment of a legal framework for the timber trade as well as steps towards greater accountability, community rights, public participation and transparency (Beevers 2016). Although there has been progress, Beevers (2016) points out that issues relating to contracting and land ownership remain.

The EU has been a key player in seeking to improve the governance of the timber trade in Liberia, mostly through the FLEGT project and the VPA with Liberia. The EU worked to improve the certification of timber from Liberia and assisted the country in prosecuting officials suspected of forestry crimes (European Union FLEGT 2016b). Nevertheless, export figures from 2014 show that around 85 percent of its timber exports go to China, while exports to the EU only amounts to around nine percent (ITC 2016a). The fact that China is the most important trading partner in timber exports can limit the EU's influence over Liberia's timber trade. Timber remains a key resource for Liberia, although the export pattern has changed, and it is doubtful whether the EU remains influential in the timber trade in Liberia. Exports to France, for example, decreased between 2011 and 2015 (ibid). In that sense, there is a discrepancy between the interventions that are primarily from the EU and the exports going primarily to China.

### **How does timber divert from the legal value chain?**

Estimates from 2005 show that half of the tropical timber in European and Western markets came from illegal sources (Jaakko Pöyry Consulting 2005). This was during a period when Liberia was still suffering from the aftermath of the civil war, and before most reform initiatives had been implemented. The situation is likely to be better today, but illegal timber trade remains a global issue (Interpol & United Nations Environmental Programme 2016). Between 2012 and 2014, the annual average of the global timber trade for primary and secondary (refined) timber products was USD\$360 billion (DESA/UNSD United Nations Comtrade Database 2016). This number highlights the magnitude of the global timber trade and adds perspective to the flows available to illicit groups that seek to exploit illicit timber.

According to Gan et al. (2016), chainsaw milling is a large source of illicit tropical timber, primarily because it does not require sophisticated technology. Chainsaw milling operates at a low cost but cannot supply timber on an industrial scale; thus, it is often used to supply the domestic market (ibid). A recent study by Bickel and Cerutti (2017) shows that domestic informal chainsaw milling is larger than official timber exports. Domestic informal chainsaw milling provides low quality timber for local construction, carpentry and furniture making (ibid). According to the study, local informal chainsaw millers have short supply chains without sawmills involved; thus, prices are low, and there is little added value to the primary product. Importantly, not all chainsaw milling is illegal, and there is in fact a legal framework for it in Liberia (Bickel & Cerutti 2017). It is therefore possible to get licenses for chainsaw milling under Regulation No. 115-11 administered by the Forest Development Authority (FDA) (FDA 2012). However, domestic informal chainsaw milling is not properly regulated, and a lack of understanding of potential economic gains from trading outside the domestic market limits the potential for economic growth related to timber (ibid). In contrast, Kishor and Lescuyer (2012) argue that illegal global timber traders are more sophisticated and have the resources to transport and launder illicit timber in the global supply chain.

## Illicit timber trade – A systemic issue

In Liberia, corruption is a systemic issue (U4 2012), which makes it difficult to assume that oversight and law enforcement will function in an unbiased and effective way. A review from 2005 shows that companies that held concessions owed the Forest Development Authority (FDA) over USD\$64 million in taxes and license payments (Altman & Woods 2012). The FDA also gave concessions for 10 million hectares of forest, even though the total amount of forest in Liberia at that point was 4.5 million hectares (ibid). This shows that the FDA had given the same concessions to several companies. The FDA's inability to control and monitor land concession thus frequently creates issues with contested land ownership due to several actors holding a claim to the same land. It also creates conflicts between communities and companies over contested land concessions (Beevers 2016).

As noted above, following the end of the civil war, significant efforts have been undertaken to improve the timber trade in Liberia. Beevers (2016) and Reno (2016) have however recently raised concerns about the limited impact of these reforms. They suggest that there is a risk that the timber trade is still used for patronage and that contracting/licensing processes are fraught with bribery issues. In the following section, some of these key issues are described in further detail.

## Fake licences and hacked databases

In Liberia, as well as globally, forgers play a key role in integrating illicit timber into formal/legal value chains. They create fake logging permits and timber certifications. Another type of illegal facilitator are computer hackers, known for their ability to make large quantities of illegal timber 'legal'. Computer hackers can illegally enter timber databases and adjust numbers in order to blend illegal timber with legal timber, a task often given to them by logging companies (Lawson & MacFaul 2010).

In 2009, the Swiss certification company Société Générale de Surveillance (SGS), together with the FDA, implemented a chain of custody (CoC) system to monitor timber logs bound for export from the point of extraction to the point of export in order to ensure that illegal timber does not enter logs (Bickel & Cerutti 2017). This system has been relatively effective in limiting the illicit trade, however, there are reports of issues with manipulation of log-tracing databases in Liberia, although the government claims that these issues are due to errors and not manipulation (Global Witness 2017a). The manipulated databases make it very difficult for traders to differentiate legal from illegal timber. Other efforts are also being prescribed to stop the problem at its core.<sup>17</sup> Another problem is that although most of the benefits generally go to local elites (Gan et al. 2016), local loggers are often paid slightly more for illegal logging, which gives them an individual incentive to engage in the illicit trade (Kishor & Lescuyer 2012).

In Liberia, there have been several issues with forged Private Use Permits (PUPs), which are issued to landowners, giving them the right to log. PUPs are under the supervision of the FDA and are aimed at minimising illegal logging. An investigative report by Global Witness (2012) shows that PUPs are regularly forged and signed with companies with secret ownership structures. In response, President Johnson Sirleaf issued Executive Order 44 in 2013, putting a temporary halt on all PUPs because they allegedly threatened Liberia's natural heritage (Beevers 2016).

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17 This includes GPS tracking systems to monitor forests and situational crime prevention that focuses on 'hot spots', periods of high activity, used by smugglers, mostly at night (Boekhout Van Solinge et al. 2016). The issue with this type of measure is that it requires the active participation of law enforcement and forestry departments, which, in the context with systemic corruption, are often part of the problem.

In the aftermath of the PUP scandal, the Forest Stewardship Council (FSC) disassociated the Danish Company Dalhoff Larsen and Horneman (DLH) Group after a complaint from Global Witness that the company had bought wood from three PUP concessions in Liberia after they exposed issues with the PUPs (FSC 2015). In order for the FSC to accept the DLH Group back into the council, the Group must, among other requirements, establish a due diligence system verified by an independent third party (ibid).

The PUP-related issues illustrate the difficulty of implementing certification schemes when corruption penetrates institutions. Traders are exposed because of the forged certifications and hacked databases, making it very difficult to distinguish legal from illegal timber. As timber companies are, in some cases, involved in these forgery schemes (Lawson & MacFaul 2010), enhanced due diligence can be a way for traders to identify suspicious counterparts and to protect their companies against fake or substandard licences.

### **Does timber finance illicit activity?**

Timber and natural resources more generally have been used to fund illicit activity in Liberia over a long period. The links between natural resources and conflict during the civil war have been well established. There is much more uncertainty about the role of illicit timber trade in contemporary Liberia.

#### **Enduring issues from the civil war**

Taylor used natural resources to fund conflict and to enrich his family, friends and network. His natural resource trade involved several foreign companies, one of the most controversial links being with the Malaysian Oriental Timber Company (OTC). OTC controlled 43 percent of Liberia's timber trade and had significant influence over the FDA. The OTC helped Taylor smuggle arms into Liberia through its ports and provided him and his family with significant bribes (Global Witness 2001). During the war, there were also reports of arms being traded directly for logging rights (Woods et al. 2008), arms which may have been used by the RUF to commit human rights violations.

Taylor established direct links to traders from Eastern Europe, who had close connections with organised crime, such as Victor Bout and Leonard Minin. Minin's case is a clear example of the close links between organised crime and the 'state' during Taylor's rule. Minin was a well-known arms dealer who provided Taylor, and an extension of the RUF in Sierra Leone, with arms. The fact that Minin also had a timber company, Exotic Tropical Timber Enterprise (ETTE), which was involved in the Liberian timber trade (Boekhout van Solinge 2008), is symptomatic of the civil war period. Police arrested Minin in Italy in 2001 with twenty grams of cocaine, USD\$150,000 in cash and more than half a million dollars worth of diamonds (Traynor 2001).

A recent report from Global Witness (2017a) shows that board members from the OTC are still involved in large logging concessions in Liberia. The same report also claims that virtually all logging concessions in Liberia are illegal due to the holders' failure to pay taxes and provide information on beneficial ownership, a claim that is strongly condemned by the Liberian FDA (FDA 2017). Some of the logging companies investigated in the report only consisted of a legal entity and not a natural person as the beneficial owner of the company, which violates the EITI principles and the FLEGT standard. The findings of the Global Witness report are contestable, but they do nevertheless illustrate that there is a risk that companies with secret beneficial owners can try to abuse the current system.

## The link to the illicit international trade

The current illicit trade is reportedly linked to Chinese criminal groups which use the previously established networks of illicit trade during the civil war (Vorrath 2014). The involvement of Chinese groups in the timber trade is most likely because the bulk of the current export is destined for China. However, it is difficult to determine which criminal networks immediately benefit from the illicit trade.

According to the findings above, timber is still a resource used in illicit trade, especially in the informal domestic trade. However, there are few clear links to international organised crime or conflict. The trade is facilitated by weak oversight and the lack of enforcement of legal measures due to a combination of low capacity and a culture of widespread bribery. Nevertheless, timber remains a key resource for rural Liberia as it is an important source of income. A sustainable timber trade is also crucial from both a social and environmental perspective.

## How is the illicit trade facilitated by corruption?

A failure to properly govern exploration, exploration rights contracts and concessions related to natural resources can fuel corruption and have significant negative impacts on the recovery of post-conflict states (Rustad et al. 2013). This has also been the case in Liberia, a country plagued by systemic corruption, with a lack of separation between power and the rule of law (U4 2012), and where natural resources have long been used to establish, maintain and expand patronage networks.

This has manifested in low-impact reforms and sustained problems with concessions, licences and certifications in Liberia (Beevers 2015). Bribery is important for ensuring non-interference in the illicit trade, which applies to both the illicit trade in timber and in other types of illegal trade, such as the drug trade (Vorrath 2014). Bribery can also be used by illicit traders to access fake documents and licences like PUPs. Bickel and Cerutti's (2017) study on informal chainsaw milling in Liberia found that in order to avoid state interference, informal taxes were paid to government officials, and bribes were frequently paid to police officers at checkpoints. A documentary by Global Witness (2016) showed that the British company Sabel paid bribes worth close to \$1 million to key actors close to President Johnson Sirleaf, including one of her sons, for the rights to a large iron ore concession. This is an indication that corruption still plays a role in natural resource management. It also reveals the existence of rent-seeking behaviour through which politicians and government officials seek to extract bribes or other forms of ill-gotten gains from the natural resource trade. This tendency goes beyond occasional bribery, and in order to address corruption, there is a need to better understand the underlying incentives and structures that lead to rent-seeking behaviour (Kolstad & Wiig 2009).

## Corruption and reform in Liberia

Liberia has been a recipient of substantial amounts of bilateral aid in the aftermath of the civil war, and as previously discussed, a great deal of the attention has been directed towards good governance initiatives. The GEMAP project alone cost around USD\$500 million. Although the project had some initial success, it failed to address the root causes of corruption (Reno 2008). Such projects might give rise to what has been called 'isomorphic mimicry', whereby the government implements reforms and sets up oversight that function like a façade, mimicking good governance, with marginal effect in reality (Pritchett et al. 2013). This was highlighted in a report by Global Witness (2013), which argues that reforms in the timber sector often have loopholes and/or that timber concessions are granted as political favours even though it is illegal. In the same report, PUPs in Liberia are showcased as an example of a reform that is abused for corrupt purposes.

Reno (2008) argues that the downfall of the previous centralised patronage system in Liberia has opened up space for previous fighters to establish themselves in an increasingly decentralised governance system. The decentralised patronage systems often revolve around illicit trade and control of resources (ibid). The new networks are likely to oppose any intervention that seeks to re-establish a more centralised system. As noted above, this may be because of rent seeking, whereby reforms decrease the opportunities to extract bribes or other forms of ill-gotten gains. In addition, reforms need to be considered against the 'growth–stability trade-off,' whereby they might have a positive impact on growth but a negative impact on stability or vice versa (Khan 2010).

Introducing measures designed to increase oversight of the timber trade is not likely to be sufficient to solve the issue, as contexts characterised by systemic corruption, in most cases, lack principled official, making oversight interventions inefficient (Marquette & Pfeiffer 2015). In the Liberian context, patronage and corruption issues are systemic. In the pre-civil war period, there was no robust rule of law system in the country. Beevers (2015) argues that the current forest governance interventions in Liberia were built on pre-civil war arrangements that were used for corruption and patronage, like the Chieftaincy system in the DADCF. Reforms aimed at addressing corruption in the timber sector have, according to reports, also failed due to a lack of 'political will' (Beevers 2015; Funaki & Glencorse 2014; Global Witness 2013). However, to state that lack of political will is the reason for the limited impact of anti-corruption reforms in the timber sector falls short of pinpointing the essence of the problem. In order to properly address corruption, there is a need to spend resources to unpack the black box of lack of political will.

## Summing up

According to the findings above, the illicit trade in Liberia is facilitated by neo-patrimonial societal structures in which there is a lack of oversight of the timber trade due to a combination of limited capacity and rent-seeking behaviour. This enables illicit traders to avoid prosecution as well as to access resources and licences/certifications that they have no formal right to access. Domestic informal chainsaw milling seems to play a significant role in the timber trade, but this paper found no evidence connecting it to organised crime or terrorism. However, the prevalence of fake certificates and issues regarding hacked databases are worrying and indicate that logging companies may be complicit in the illicit trade. The poor track record of forest governance interventions in Liberia shows that there is a need to better understand the underlying power structures and incentives that uphold the current system and the underlying incentives of stakeholders who engage or facilitate the illicit trade.

### 3.3 Mali – Golden opportunities lost?

#### Context

Prior to 2012, Mali was often presented as a showcase of African democracy. While such a picture was always greatly exaggerated (Harmon 2014), a series of events in 2012 radically changed that impression. A coup which overthrew the government of President Amadou Toumani Touré (ATT), the Tuareg rebellion and an Islamist takeover<sup>18</sup> of the north revealed that Malian institutions were weak, that mismanagement and corruption were rampant, that the state was in fact highly fragmented and that Malian democracy had largely been a ‘sham’ (Harmon 2014). The events demonstrated that the de facto governing logic was characterised by the interests of regional and national ‘big men’ (be they state officials, separatists, criminal entrepreneurs, terrorists or any combination of the above) (Bøås & Torheim 2013). Following an intervention by French Forces, a UN stabilisation mission, MINUSMA, was authorised.<sup>19</sup> However, it has struggled to achieve its goal to ensure the success of the Algiers Agreement, which offers Tuaregs and other northern groups some autonomy if they give up on independence (see, e.g. Reeve 2015). As of early 2017, however, violent clashes continued, with few solutions in sight.

Mali thus suffers from a range of serious challenges, including insurgency, terrorism, internally displaced persons, intercommunal violence, widespread crime, poor governance, political and socio-economic grievances and poverty. In the north, there is a lack of state penetration and a monopoly of violence; tribal leaders and armed groups compete for local power and control (Reitano & Shaw 2015). This has led the northern region to become especially susceptible to transnational threats, particularly those emanating from transnational organised crime (TOC), militants and insurgents. These vast desert and semi-desert areas are also home to ancient trade routes that connect West Africa with North Africa through the Sahara, which have made Mali an attractive transit country for the transport of a wide range of illicit commodities and contraband, including cigarettes, guns and drugs as well as human trafficking and migrant smuggling.<sup>20</sup> Facilitating these flows are long-established corrupt arrangements and dynamic networks involving state officials, members of the security apparatus, business people, tribal leaders, unemployed youth, Islamists, terrorists, militias, kidnappers, etc. These flows were originally established to facilitate cigarette smuggling but have proven adaptable to new flows of other illicit goods (ibid). According to Reitano and Shaw (2015) and Gberie (2016), the large benefits of these illegal flows have penetrated not only law enforcement institutions, but also political institutions and policymakers (Reitano & Shaw 2015).

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18 The Islamist groups included Ansar ed-Din, Al Qaeda in the Maghreb and the Movement for Unity and Jihad in West Africa (MUJAO) (Bøås and Torheim 2013).

19 The UN Multidimensional Integrated Stabilization Mission in Mali (MINUSMA) has been authorised to last until the end of June 2017 (MINUSMA 2017). France also maintains a parallel peace operation called ‘Barkahane’, and the European Union runs a training mission for the Malian army.

20 The most lucrative endeavour these days seems to be the illegal transport of migrants to Libya. This activity has provided new economic opportunities, as well power to tribes and groups residing in the area, and new sources of revenue to criminal networks and corrupt officials. According to UNODC interviews, there is a particular market for Malian documents, such as passports, which can be acquired from corrupt Malian officials. These passports are in demand as they give the right to enter Algeria, unlike ECOWAS documents (UNODC 2013, 29).

## The importance of gold to Mali

Mali is Africa's third largest gold producer, after Ghana and South Africa, and the fifteenth largest producer worldwide according to numbers from 2015 (Thomson Reuters GFMS 2016). Most of the gold is located in the south and south west of the country and, thus, outside the troubled northern part of the country. The gold sector in Mali consists of artisanal and small-scale gold mining (ASGM) as well as medium and large-scale gold mining (MLSGM), or what is often referred to as 'industrial mining'.<sup>21</sup> The exact figures of Mali's gold exports are somewhat uncertain, and different sources report slightly different figures. Reuters reports that industrial mining produced 46.5 tonnes in 2015, while artisanal mining produced four tonnes (Reuters 2016).<sup>22</sup> In 2012, the World Gold Council reported that gold accounted for 75 percent of Mali's foreign exchange earnings. According to ITC data, Mali exported gold worth USD\$570 million in 2015, exported primarily to Switzerland (85.2 percent) and India (14.6 percent) (ITC 2015b).

The 2012 crisis propelled a spike in artisanal mining, largely because of economic sanctions and the displacement of people seeking artisanal mining as a way to survive after the seizure of the north by Islamist groups. In 2013, the amount of gold produced by artisanal mining surged to 20.4 tonnes, only to drop back down to 7.4 tonnes in 2014 (Reuters 2015a; Schipper et al. 2015). One of the reasons for the sharp dip may be a ban that the government enforced on artisanal mining during rainy seasons in order to reduce accidents and to divert people back to agriculture. Another reason seems to be that there were crackdowns on artisanal mining sites located within permits held by large mining companies (Reuters 2015a). Despite these fluctuations, a Human Rights Watch report claims that reported figures for artisanal mining are notoriously low (HRW 2011).

While illegal and informal mining are often lumped together under the label artisanal ASGM, it should be noted that under Mali's Mining Code, artisanal mining is legal in designated geographical areas or gold mining 'corridors'. In reality, however, most artisanal mining sites lie outside these corridors. One expert held that 97 percent of artisanal mining sites were located outside of the legal corridors (HRW 2011, 18, 77). Still, the government tolerates most of the activity, including those outside the legal areas, partly because it provides revenues for many local government officials. These officials raise fees for shafts or get part of the gold production as customary land owners. Government officials occasionally serve as miners or organise miners to work for them (HRW 2011).

The lion's share of Mali's gold is produced in large industrial mines,<sup>23</sup> and a few international mining companies control most of the mining, including AngloGold Ashanti and RandGold (both South African), IAMGOLD, Avion Gold and African Gold Group (Canadian), Resolute Mining (Australian) and Avnel Gold Mining (British) (HRW 2011). These companies operate large mines such as Sandiola, Yatela, Morila and Loulo-Goukoto. The latter two are however joint ventures with the government of Mali (Investing News Network 2016). The Fekola mine, which is expected to have the largest deposits of its kind in West Africa, is anticipated to open in 2017 or later (Reuters 2015b).

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21 The differentiation between artisanal, medium- and large-scale mining operations is usually based on the method of extraction and annual output measured in metric tons per year. Large-scale operations usually have a minimum output of 500,000 metric tonnes per year, while medium-scale mining usually produces between 50,000 to 500,000 tonnes per year (UNICRI 2016, 24).

22 The official webpages of the Ministry of Mines or the Chamber of Mines intended to report these figures are strangely both blank.

23 The Malian Chamber of Mines states that there are nine operational mines in Mali, only five of which are named (Chambre des Mines homepage 2017).

## How does gold divert from, and reappear in, the legal value chain?

The value chains of artisanally and industrially mined gold are different. Nonetheless, each of them has junctures or transaction points that present the risk of actors diverting gold from the chain or reintroducing it to the chain. In the process, gold can be used to finance or facilitate illicit activity.

### Artisanal gold

Since the bulk of the artisanal mining is carried out outside the legal corridors, the bulk of this gold is not strictly legal. Still, exporters often have licenses which serve, at least in part, to legalise it. Much of the activity related to ASGM in Mali is thus informal, i.e. generally accepted, but technically illegal. The gold passes through a largely informal value chain until foreign traders import it.<sup>24</sup> An Associated Press study conducted in 2007 and 2008 found that gold that had been artisanally mined in Mali was sold via two to three middlemen before reaching its exporter. First, the gold was sold to local buyers at the mine; they would transport it to local traders in larger cities, who would transport it to Bamako. Buying houses in Bamako, often registered as limited companies,<sup>25</sup> would melt gold from several buyers into primitive bars at specialised smelting workshops before the bars were sold to an exporter (Callimachi & Klapper 2008).<sup>26</sup> Two more recent reports, both based on fieldwork in Mali, draw up an almost identical value chain (Schipper et al. 2015; Partnership Africa Canada 2017), suggesting that the local value chain of ASM gold has remained stable for the last decade. According to Partnership Africa Canada (PAC), each actor in the chain is usually pre-financed by an actor further up the chain, an arrangement which often also includes the exporter, who may be pre-financed by refiners abroad (PAC 2017, 18). Pre-financing schemes secure not only continued extraction, but also that the importer abroad receives a constant flow of gold. The Bamako-based exporter usually transports the gold as hand luggage on board commercial flights to trading houses, typically in the United Arab Emirates (UAE) or Switzerland and occasionally to traders in Belgium (Callimachi & Klapper 2008; PAC 2017; Schipper et al. 2015).<sup>27</sup> At times, foreign trading houses also travel to Mali to buy ASM gold directly from buying houses (Schipper et al. 2015). A Human Rights Watch (2011) report refers to export statistics obtained from the Ministry of the Economy and Finance of Mali to show that Switzerland is the most important trading partner in ASM gold from Mali.

The largely informal Malian export system of artisanal gold is apparently highly functional. In fact, it works so well that it also attracts substantial amounts of ASM gold from neighbouring countries like Burkina Faso and Côte d'Ivoire (PAC 2017). The porous borders of the region, the favourable application of tax laws in Mali, along with geographical concerns, have thus contributed to the establishment of Bamako (along with Ouagadougou to some degree) as an export hub for artisanal gold (ibid). There are also other indications that smugglers transport foreign gold to Mali to be illicitly exported from there. According to a calculation carried out by PAC, the UAE reports to have imported an amount of gold from Mali that exceeds some of the more conservative estimates of total gold production in Mali. According to the calculation, Mali produced 45.8 tonnes of gold in 2014, while the UAE reported to have imported

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24 For further elaboration on the distinctions between formal, informal and illicit artisanal gold mining, see the Global Initiative against Transnational Organized Crime and Estelle Levin Ltd. (2017).

25 There is no reliable information regarding the number of buying houses in Bamako, but guestimates place the number somewhere between 127 and 300 (Schipper et al. 2015, 46).

26 Over 100 exporters have a license to export, but the market is dominated by a handful (Schipper et al. 2015, 47).

27 Callimachi and Klapper (2008) referred to two small Geneva-based companies, Monetary Institute and Decafin SA traders, as the recipients of Malian artisanal gold.

59.9 tonnes of gold from Mali that same year (PAC 2017).<sup>28</sup> While there is considerable uncertainty regarding these numbers, they indicate that the UAE imports very large quantities of reportedly Malian gold, gold which may very well originate elsewhere in the region.

Once in the UAE, artisanal gold is often sold to gold buyers in Dubai's gold souk, bypassing the due diligence system established by the Dubai Multi-Commodities Centre (PAC 2017). Local refiners carry out the refining. One of them, the Kaloti Group, claims to account for close to half of all refining in Dubai's gold market (Bowers 2014). Actors like the Kaloti Group then redistribute gold via the international gold market or sell it at the souk, either as jewellery or per gram. The transaction from exporter or smuggler to buyer in Dubai often proceeds with no documentation requirements and is paid for in cash. In an inspection carried out by Ernest & Young Dubai, the Kaloti Group was found to have bought gold from 'walk-in' customers on a large scale. The average walk-in would carry about 2.25 kilos of gold, while the maximum amount recorded was 35 kilos (Bowers 2014). According to Ernest & Young's conclusions, the value of the company's cash-for-gold deals amounted to USD\$5.2bn in 2012, compared to the \$6.6bn worth of transactions involving conventional bank transfers. The same inspection also found evidence that large amounts of undocumented gold that had been smuggled via Morocco was traded by the same company at the souk (ibid), illustrating that the Souk functions as a hub for legally and illegally traded gold.

Studies of the value chain of artisanal gold in South Africa have shown that various international transit points (Dubai being one of them) often serve to produce counterfeit documentation, new analysis, pro-forma invoices and export documents (FATF & APG 2015; Cassara 2016). The forged paperwork enables all types of gold to be imported fully documented by buyers at the next point of entry. On verifying the legality of the shipment, the refinery or trading house would usually only check the import/export documentation and not further investigate the origins of the product (UNICRI 2016). However, even if international buyers 'asked the right questions', carrying out due diligence regarding ASM gold bought from Malian sellers is complicated. Malian ASM gold is particularly hard to trace due to the abovementioned smelting of gold from various traders and origins into rudimentary gold bullions taking place in Bamako.

ASM gold exported from Mali can thus be legally or illegally mined in Mali or abroad, and the delimitations between legal/illegal ASM gold are not easily identifiable once the gold is exported. This means that the Malian informal export system for artisanal gold facilitates illegally mined gold to be mixed with scrap gold, stolen gold or legal gold and to be sold to international buyers, who may or may not divert the gold into the legal value chain. This part of the value chain then easily encompasses a potential for a form of 'laundering' of gold from various origins and legal statuses.

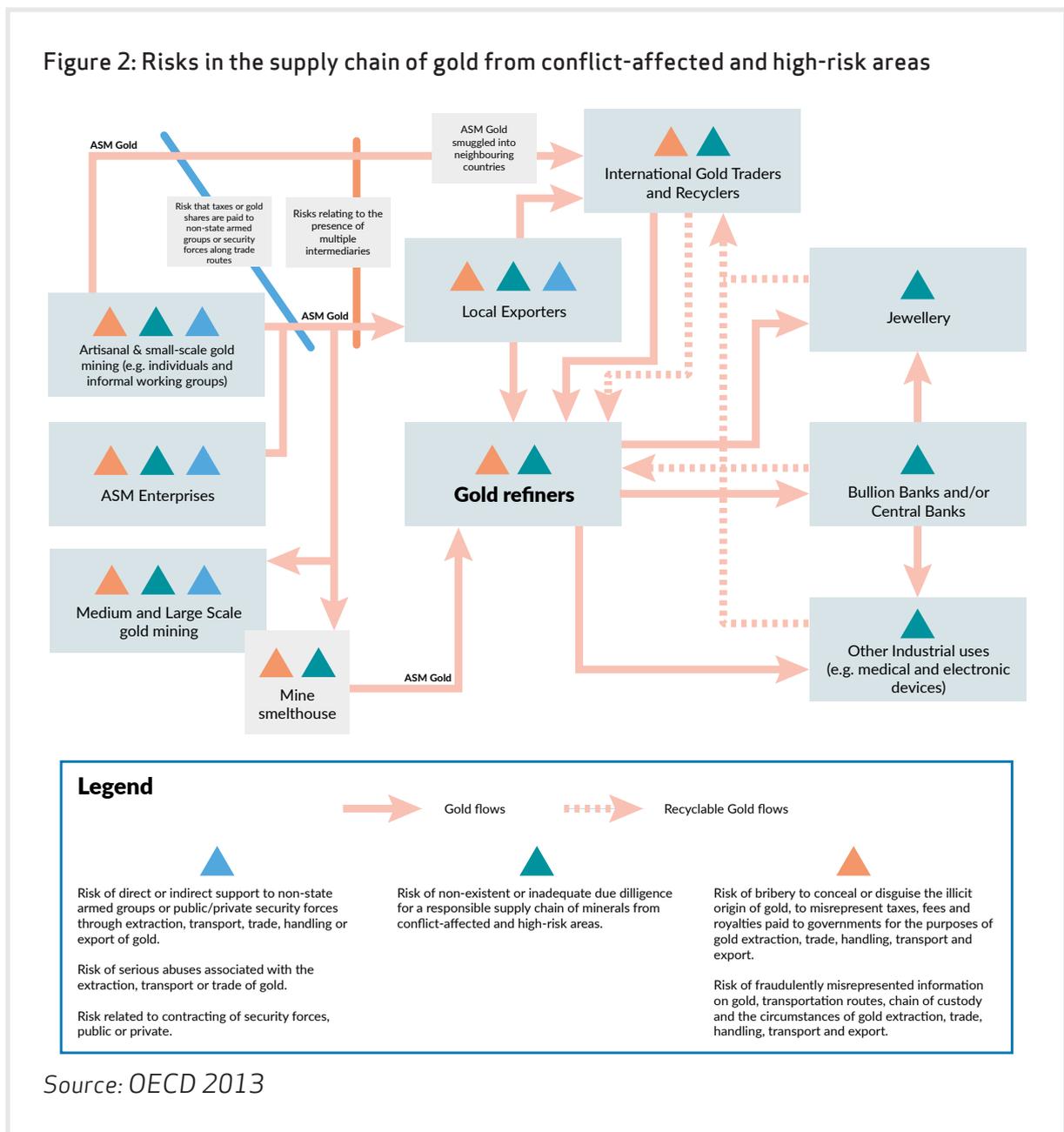
## Industrially mined gold

Large companies licensed to carry out extraction usually perform this on a large industrial scale. The main export destination for Mali's industrialised gold is, as mentioned above, Switzerland. For industrially mined gold exported to EU countries and Switzerland, due diligence and OECD compliant practices are most often put in place before it is refined and sold on to the international market (PAC 2017). Nevertheless, even MLSGM presents several opportunities for diversion from the legitimate supply chain, and there are risks associated with several steps of the chain.

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28 See UN Comtrade International Statistics Database. Available at <https://comtrade.un.org/>

One of the risks is associated with exporting unrefined gold. Gold mining countries often lack domestic gold refineries, which means that the gold needs to be transported abroad to be properly refined. Mali did not have a gold refinery until 2015, when two refineries opened, one owned by Swiss Bullion Co., the other by Marena Gold (CNBC 2016).<sup>29</sup> Prior to the construction of these refineries, all of Mali's gold was transported in an unrefined or semi-refined form across the globe to international refiners. In this shape, gold is particularly vulnerable to exploitation by, for example, organised criminal groups. The



29 The capacity of these refineries is above Mali's production as they also aspire to service other gold producers in the region (CNBC 2016).

new refineries may, as such, lower the risk that industrially mined gold is directed to illegal or semi-legal markets, such as in the case of the smuggled silver-coated gold sold in the gold souk in Dubai (see Bowers 2014).

The OECD has identified and illustrated the risks associated with the supply chain of ASGM and MLSGM, shown in Figure 2.

Arguably, the chart may represent a somewhat stylised value chain and there are likely to be contextual variations. Nonetheless, it illustrates the junctures and risks of diversion associated with the extraction, transport, trade, handling and export of gold. Not only is most of Mali's ASM gold, strictly speaking, illegal from the start,<sup>30</sup> the chart also illustrates that there are multiple risks of diversion, taxation by armed or criminal actors or other types of exploitation along the value chain, which could be used to finance other illicit activity.

The chart shows that even for gold mined on an industrial scale, there are risks that it may have financed illicit activity, crime or corruption on the way from a conflict affected and corruption riddled country like Mali. There is particular risk relating to the misrepresentation of gold or masking its origins or trade route in one way or another (OECD 2013), but there may also be outright theft taking place in the extraction of the mineral. Notwithstanding the risks associated with industrial gold mining and its value chain, this report has not been able to substantiate whether or how Malian industrially mined gold is being exploited for criminal or other illicit purposes. Despite the fact that Mali has been a member of EITI since 2007, and that it is commended in its most recent report for pursuing more openness and reform despite a difficult security situation (EITI 2015), this report has found that the available information on the MLSGM sector in Mali is very limited.

### **Does Artisanal and Small-scale mining gold from Mali facilitate illicit activity?**

Artisanal gold mining presents an option for people with few alternatives for subsistence, but it also presents opportunity for criminal exploitation. As pointed out in a recent study of financial flows linked to ASM gold mining, artisanal gold mining can directly generate IFF, or the sector can be utilised for money laundering or tax evasion. This means that gold can be a tool to facilitate IFFs generated by other criminal activity (Global Initiative against Transnational Organized Crime, GIZ, & Estelle Levin 2017).

Due to rising gold prices, artisanal mining has attracted increasing numbers of people to Mali and other parts of West Africa over the last decade (HRW 2011). The Malian Chamber of Mines estimates the number of artisanal miners to be more than one million (Chambre des Mines du Mali 2017), while Human Rights Watch reports a mere 100,000 to 200,000 persons engaged in artisanal mining in over 350 artisanal mining sites across western and southern Mali (HRW 2011), other sources claim that as of 2010, only 150 sites were actually active (Schipper et al. 2015). Precisely because illegal mines operate clandestinely and fail to abide by labour laws, the workers employed in informal or illegal mines are on average vulnerable to different forms of labour exploitation (Verité 2016). Child labour is banned by law in Mali (HRW 2011), but it is nevertheless socially widely accepted (Schipper et al. 2015), and an estimated 20 percent of artisanal miners are children. Children who migrate without parents are particularly vulnerable to trafficking and exploitation (HRW 2011) and are easily exploited as sex workers in mining areas. The pre-financing schemes described by PAC in Mali may as such facilitate workers in

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30 It should be noted that the lines between what is informal mining and illegal mining may be blurry in Mali's ASGM sector.

becoming indebted to patrons and being locked in debt bondage schemes (see e.g. UN Special Rapporteur on Contemporary Forms of Slavery 2016). On a general basis, one can say that artisanal gold mining attracts some ethically questionable practices such as child labour and prostitution and is, in general, often associated with human rights abuses (UNICRI 2016).

Since the supply chains in Mali, Burkina Faso and Côte d'Ivoire are tightly interconnected, artisanal gold exported from Mali may very well stem from any of these countries and, therefore, support illicit activity, criminal networks and wartime actors in these countries. In Côte d'Ivoire, the 'Forces Nouvelles', a rebel group that played a key role in the country's civil war during the 2000s, has been known to be intricately involved in gold extraction and smuggling. Interviews carried out in the region by PAC found that the networks and trading routes of the ex-rebels were still used in 2017 and that some of the former commanders of Forces Nouvelles continue to be heavily involved in the illicit gold trade, usually through the financing of middlemen (2017).<sup>31</sup> The mining sites controlled by one of them, Quattara Issiaka (or 'Wattao') are estimated to produce 2.5 tonnes each year, most of which, if not all, is believed to be smuggled out of Côte d'Ivoire (GIATOC & Estelle Levine Ltd. 2017). Considering the 'export hub' status of Bamako, there is accordingly a risk that ASM gold bought as 'Malian' may have sponsored former rebels in neighbouring countries on their way to international markets.

The fact that the artisanal gold mining sector occupies a murky spot in the economy, caught between the legal and illegal sector, makes it susceptible to exploitation by criminal syndicates. ASM gold can be a convenient means to launder money stemming from the illicit trafficking of drugs, weapons, humans or cigarettes, although this study has encountered little concrete evidence that Malian gold is used for these purposes. A 2015 FATF report characterised gold as an 'extremely attractive vehicle for laundering money' (FATF & APG 2015). Several general characteristics of gold and the gold market make it particularly enticing to criminal actors. One is the nature and size of the gold market itself, which is highly reliant on cash as a method of exchange. In fact, much of the international gold trade operates 'off the books' (UNICRI 2016), and cash for gold outlets flourish around the world. Another convenient characteristic is the anonymity generated from the properties of gold, which make tracking its origins very difficult. Gold is also a reliable medium of exchange as its weight and quality can be assured; gold prices are fixed in markets worldwide; and both the demand and the value of gold tend to be relatively constant (Cassara 2016).<sup>32</sup> These factors, and others, make gold highly attractive to criminal syndicates wishing to hide, move or invest their illicit proceeds (FATF and APG 2015).<sup>33</sup> In particular, UNICRI (2016) maintains that drug traffickers often form part of the early value chain of illicit gold. In a 2015 field mission study in Mali, the IMF found that transactions involving gold by jewellers was commonly conducted in cash, which led to the conclusion that these transactions may allow for the integration of the proceeds of corruption (IMF 2015). This situation was aggravated by a lack of effective supervision of the gold-related sectors, and although mining companies are supervised by the National Directorate of Geology and Mines, jewellers and artisanal gold-mining are not supervised (ibid), leaving a space for these sectors to function as money

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31 These ex-rebel leaders had often been given positions within the armed forces to make them answerable to the military hierarchy, often with the opposite effect (*New York Post*, 2015).

32 In contrast, gems and even diamonds may be of less universal value or commercial market pre-valuation as their value depends on more subjective expert criteria and less stable demand (UNICRI 2016; Cassara 2016).

33 While gold used to be smuggled out of Mali through caravans crossing the Sahara, there is little evidence of such practices being widespread today. A couple of sources claim that an unknown but considerable share of ASM gold is usually smuggled out of the country (HRW 2011; Schipper et al. 2015), but there is no evidence of who actually carries out this smuggling or for what purpose. In general, gold smuggling can serve the dual purpose of generating profits and moving funds; militants and terrorists, in turn, often benefit by taxing such flows (GIATOC & Estelle Levine Ltd. 2017).

laundering vehicles. At the same time, investigative authorities in Mali, according to the same assessment, are not trained or staffed to recognise 'white collar crime' and have limited international cooperation or information sharing arrangements. The IMF mission reported that as of 2014, no one has ever been sentenced in Mali for money laundering per se (ibid).<sup>34</sup> Similarly, no bank in Mali has ever been penalised for not observing anti-money laundering rules of those relating to combating the financing of terrorism (ibid). This in effect indicates that the risks associated with acts of money laundering are low.

The apparent sparse attention paid to money laundering stands in contrast with Mali's membership in the Inter-Governmental Action Group against Money Laundering in West Africa (GIABA), established by the ECOWAS. The purpose of the GIABA is to contribute to strengthening the capacity of member states towards the prevention and control of money laundering and terrorist financing in the region (GIABA homepage). In its most recent evaluation, conducted in 2013, Mali was rated as non-compliant on the majority of recommendations and as partially compliant on a handful (see GIABA 2014 for details).<sup>35</sup>

## How is the diversion of gold from the legal market facilitated by corruption?

Corruption in Mali is entrenched and endemic in the both social and political culture, notwithstanding the incumbent regime (Harmon 2014). This can be explained, at least in part, by the observation that in Mali, models of power and politics have carried over from pre-colonial and colonial times to the present (Murray 2016). Rampant corruption, clientelism and rent-seeking behaviours at all levels of society compromise the quality of state institutions and characterise the way the Malian state manages its resources, foreign donor funds and business relations. In public procurement processes, economic stakeholders are commonly bribed in exchange for competitive public offers (Bertelsmann Stiftung 2017). Not unlike many other neo-patrimonial systems, patronage, informality and corruption thus characterise the way in which society and governance work. In the northern part of the country, government officials serve as protectors and facilitators of activities by accepting a share of the profits (Reitano & Shaw 2013).

Patrimonial logics and rent-seeking behaviour are also likely to affect the distribution of returns associated with gold mining, especially in the informal or illegal gold mining sector. The Malian state has done little to formalise the ASM sector, or to close loopholes in legislation, which allows the illicit flow of gold to continue. Mali amended its Mining Code in February 2012, but there is still little de facto control over the actors managing the ASM sector. As a result, the exploitation of the mining sectors outside the legal corridors continue without authorisation or traceability (PAC 2017), leaving the impression that the activity is informal yet 'protected'. Mining licenses and informal permission for government officials to operate as tax collectors, organisers, buyers, etc. around artisanal mining sites are also likely to function as rents in a larger and deep-seated clientelistic system. This system may affect the priorities of law enforcement institutions and perceptions of what is considered serious criminal offenses. An IMF inquiry, e.g. found that investigative authorities, especially the police, the gendarmerie and customs services had few means and little tradition for investigating sophisticated economic and financial crimes in Mali. Instead, the perpetrators of such crimes were often lumped together with 'respectable persons' (IMF 2015), which indicates that there are also cultural or habitual reasons for the prevalence of corruption and economic crime in Mali.

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34 Prosecutors often report to prosecute for misuse of public property rather than money laundering as the penalties for misuse are more severe (IMF 2015, 38).

35 GIABA evaluates its member states based on 40 recommendations established by FAFT. Ratings range from compliant and largely compliant to partially compliant and non-compliant.

Tax legislation follows a similar pattern. While Mali, like most of its neighbouring countries, charges a three percent export tax, the particular application of the legislation provides for a convenient loophole. The export tax is only charged for the first 50 kilos of gold, which means anything above that amount can be shipped without paying taxes (PAC 2017). The Malian government has taken no steps to close the loophole despite concerns expressed by some neighbouring countries. Lenient tax regimes and a lack of political will to formalise the ASM gold sector are not proof of corruption in themselves. Still, this leaves sufficient leeway for networks of gold smugglers to operate, a favour which usually does not come without rewards and a distribution of gains in neo-patrimonial orders such as Mali's.

## Summing up

The artisanal mining sector in Mali is particularly susceptible to sponsoring illicit activity, mostly because of its informal character. Analyses of financial flows elsewhere exemplify how illicit financial flows tend to perpetuate and exacerbate informality in the artisanal gold mining sector (GIATOC & Estelle Levin Ltd. 2017). Particular characteristics of gold and the gold market also contribute to its utility for IFFs and rent seeking, which also create a resistance towards the formalisation of the sector, especially from those actors profiting downstream. The informality of the sector does, however, come at a price to artisanal miners upstream, as the endeavour is closely associated with environmental damage, human trafficking, child labour and prostitution, including child prostitution, as well as a general disregard for human rights and international labour standards. This study has not been able to verify that Malian gold is associated with criminal networks, militants/insurgents or that it is used for money laundering, probably partly due to the difficulty of following the disguised 'gold trail'. Still, the value chain of ASM gold, and the export system in particular, certainly represent opportunity structures that could potentially be used for money laundering, with relatively low chances of being prosecuted. This means that there is a considerable *risk* that gold exported through these channels is associated with illicit activity in Mali and elsewhere. Mali has made progress in terms of transparency measures (EITI 2015), but as long as the country is in a state of conflict, the measures taken are likely to be minimal. Perhaps somewhat contrary to expectations, the lack of transparency is seen particularly in relation to the industrial gold mining sector. This may also stem from the fact that there is increasing attention drawn to ASGM from actors and organisations engaged in detecting human rights violations in the artisanal mining sector. However, this attention has yet to be translated into concrete action by donors and policymakers.

### 3.4 Nigeria – Oil as lubricant for networks of grievance and greed

#### Context

The Federal Republic of Nigeria is the most populous country in Africa, with a population of about 178 million. Oil was first discovered in 1956, and Nigeria has since evolved to become the largest exporter of oil in Africa. In October 2016, the IMF projected that, despite challenges related to low oil prices, the Nigerian economy would grow by 0.6 percent in 2017 (IMF 2016). Nigeria is accordingly a very rich country in terms of human and natural resources, but it continues to suffer from low levels of development and high poverty rates (between 45 and 60 percent) (World Bank 2016). Political instability and poor governance continue to plague the country, and Nigeria is still ranked thirteenth on the list of most fragile countries in the world, despite being described as the ‘the country with the largest economic and power potential on the continent’ in a 2015 Institute for Security Studies publication (Colliers, Schünemann, & Moyer 2015). The 2015 presidential elections, which were deemed free and fair, were also considered a ‘glimmer of hope’ as this was the first time since independence that political power was transferred peacefully from one party to another as a consequence of free and fair elections (Amundsen 2017).

Still, Nigeria has a variety of complex problems, some of which are closely tied to its oil economy. The most acute challenge is the insurgency waged by the Islamic group Boko Haram in the northern part of the country and the ongoing refugee and hunger crisis caused by it. The violence perpetrated by Boko Haram has caused massive suffering and widespread violations of international human rights and humanitarian law, leading to the displacement of large numbers of people and a growing humanitarian crisis. In the three most affected states, Adamawa, Borno and Yobe, almost seven million people were in need of humanitarian assistance in early 2016 (OCHA 2016). The grave situation in the north is related to long-standing tensions between the predominantly Christian south and the northern part of the country, which is predominantly Muslim. More fine-grained ethnic divisions also characterise the situation across the country. These divisions are also exacerbated by oil, as oil is chiefly found in the southern states and thus benefits Nigerians unequally.

Violence and instability plague the Niger Delta<sup>36</sup>. Although the Delta holds an estimated 95 percent of the country’s oil and gas reserves, it is still characterised by widespread poverty, youth unemployment, political underrepresentation, crime, corruption as well as environmental devastation that destroys local livelihoods (Onuoha 2016; Boris 2015). These factors, along with more historical ones, contribute to an explanation of the so-called ‘petro-violence’ in the Delta (Obi & Rustad 2011). The violence is often spearheaded by local militias but has also involved government forces, community vigilantes and security companies. Several local militias have admitted to sabotaging as well as stealing and smuggling oil. While these groups have typically claimed that oil theft is motivated by ‘grievance’, there often seems to be a mixture of motivations.

The southern part of Nigeria and the Niger Delta are heavily affected by TOC. Nigeria is, in fact, considered a hub in the global cocaine market (UNODC 2013). Nigerian networks, along with Ghanaian ones, play a dominant role in migrant smuggling schemes and in weapons and ammunitions smuggling (UNODC 2013). The Gulf of Guinea (GoG) is also home to a variety of piracy activity.

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36 Which states actually make up the Niger Delta varies according to different sources, but the three states considered at the ‘core’ of the Delta are Bayelsa, Delta and Rivers. While ABia, Akwa-Ibom, Cross River, Edo, Imo and Ondo are sometimes counted, they are often considered more peripheral Niger Delta states (Boris 2015, 564).

## The importance of oil to Nigeria

Nigeria is not only the largest economy in Africa; it is also very dependent on oil. Since 2014, however, oil production has fallen, and in January 2017, oil production was down to 1.5 million barrels per day (bpd), about 30 percent below the targeted 2.2 million. According to some reports, most of the divergence was due to damage inflicted upon export terminals, damaged pipelines and militancy in general (Bloomberg 2017). Oil and gas account for close to 90 percent of exports and approximately 35 percent of Nigeria's gross domestic product (OPEC 2016). According to the ITC, India is the biggest export market for Nigeria's oil, accounting for 22.1 percent of total exports (ICT 2015c).

Large quantities of Nigerian oil are stolen each year. Estimates of exactly how much oil is stolen vary widely, as do estimates of the value of losses. Katsouris and Sayne's (2013, 15) in-depth study of oil theft estimates in Nigerian averages that 100,000 barrels per day (bpd) disappeared from facilities on land, swamps and shallow waters in 2013 (not including theft from oil terminals and at sea). Other sources quote numbers as high as 400,000 bpd (Gaskia 2013; Obado-Joel 2014). While oil theft is a large and continuous problem, there is little coherent evidence proving that oil theft is in fact a *growing* problem in Nigeria (Katsouris & Sayne 2013). Instead, analysts tend to agree that oil theft fluctuates, that at least a considerable part of it seems to be correlated with levels of discontent and instability in the Niger Delta (Obi 2010) and that spikes in production and oil prices, as well as political events such as elections also matter (ibid).

Oil theft infers large and direct economic losses upon the Nigerian economy. Some commentators claim that widespread theft has hindered Nigeria from exporting enough crude oil to meet budgetary provisions, causing domestic debts to rise (Olateju 2013; Boris 2015). This challenge to the country's external balance is exacerbated by the sharp decline in oil prices since the third quarter of 2014. On top of the direct losses, oil theft infers considerable indirect costs in its contribution to environmental damage and capital flight. It also negatively affects socio-economic development and supports a range of other types of international organised crime in the Gulf of Guinea. The low oil refinery capacity of Nigeria's four refineries is also costly for the Nigerian state, as it creates a situation in which Nigeria imports most of its fuel and resells it to its citizens (until 2016) at subsidised prices.<sup>37</sup> According to one source, Nigeria imports about 80 percent of its refined products (Berne Declaration 2013, 8). In addition, the subsidy mechanism was itself found to be one of the most monumental embezzlement schemes in Nigerian history, especially between 2009 and 2011 (ibid).<sup>38</sup>

While the most renowned form of oil theft is perhaps the siphoning of crude oil pipelines in small- or larger-scale operations in the Niger Delta, Nigerian oil is in fact stolen in several different ways, in varying quantities and at many points along the value chain. When referring to oil theft or illegal 'bunkering' in this report, we refer in general to all acts involving the theft, diversion and smuggling of Nigerian oil, usually either upstream or midstream. The next section takes a closer look at how oil is stolen.

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37 Nigerian refineries have a theoretical capacity of 445,000 bpd (NNPC 2017), but the aging plants rarely manage to produce 50 percent of this capacity (Berne Declaration 2013). In a bid to increase domestic refinement, licenses have been issued to 22 companies to establish refineries, which one hopes will raise the capacity to 2.62 million bpd in the medium to long term (Okere 2017). Distributors import refined products at international market prices only to sell them at a lower subsidised price, receiving reimbursements for the difference from a Nigerian National Petroleum Company subsidiary (Gillies 2009).

38 A total of USD\$6.8 billion was paid without proper justification (Berne Declaration 2013).

## How does oil divert from the legal value chain?

Compared to gold and diamonds, in particular, stealing large quantities of oil is a bit more cumbersome. It requires logistical structures, corrupt officials to turn the other way, an established market for the stolen product and ways to insert the product back into the legal value chain at a later stage. While one would think that stealing oil is a very visible endeavour, and hence a well understood phenomenon, there is limited knowledge of theft procedures and the intricate value chains of stolen oil (Katsouris & Sayne 2013). Nigeria's oil industry is among the world's least transparent, which leads to an often murky division between legal and illegal Nigerian oil. Furthermore, the oil sector in general is littered with corruption and fraud throughout the value chain (Gillies 2009), which facilitates oil theft on a massive scale.

The Nigerian oil and gas infrastructure consists of a complex system of facilities starting with drilling platforms on land or at sea, pipelines or tankers for transport, refineries and tank storage facilities, ports where petroleum is loaded onto ships and, finally, the transport by ship from Nigeria to international buyers. Each of these steps appear to have their own vulnerabilities to theft, and although there may be a myriad of ways to steal oil, this paper briefly describes four of the more common ones:

### Small-scale illegal bunkering of crude oil

Small-scale illegal bunkering is typically carried out by local groups and youths who siphon crude oil from pipelines, wellheads or other oil installations inside the Delta. To steal oil, pipelines are punctured, and illegal taps are sometimes installed. Oil is then artisanally and illegally refined locally, before being sold in local markets. Some of the product is blended with refined products or sold on the street as fuel (Katsouris & Sayne 2013).

### Larger-scale bunkering in the field

A similar type of theft is carried out on an industrial scale using more sophisticated tools and means of transport. Networks of workers operate onshore, in swamps or in shallow waters to siphon oil, using hoses to load the oil onto barges. The barges then transport the crude through the Delta and onto small tankers waiting at the coast. The tankers may carry the cargo to a refinery or storage tank elsewhere in the Gulf or simply to a local storage facility. Once there is enough oil, it is transferred to a larger coastal tanker or an international class ship waiting further ashore. This vessel will then either be filled from scratch or be topped up by the illegal oil, thus blending legal and illegal product. Most of these larger tankers are chartered for oil export and hence transport the oil to destinations outside the country (Katsouris & Sayne 2013).

### Ship seizure or cargo theft at sea

Oil products are also stolen at sea by pirates.<sup>39</sup> The preferred targets seem to be tankers carrying refined products rather than crude (UNODC 2013). A frequently used *modus operandi* is for a fast approaching smaller boat to launch an attack on the bridge and accommodation block of a subject tanker using automatic gun fire and threatening to use rocket-propelled grenades (RPGs) (Murphy 2013). After a

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39 Pirates attack ships carrying both legal and stolen products, but since the latter type of theft is unlikely to be reported, there is little knowledge of the extent of this practice (UNODC 2013, 50). It should also be noted that oil-related piracy is only one of several types of pirate attacks commonly found in Nigerian waters. Murphy (2013), e.g. identifies five types of piracy, only some of which are carried out by Delta militant groups or groups otherwise connected to oil theft.

forced boarding of the ship, the cargo is transferred to another smaller tanker. The receiving tanker is often owned by local companies or may, in some instances, itself be a hijacked vessel. The loot is then transported to fuel tanks on land (Hastings & Phillips 2015). In some instances, the entire ship is hijacked and temporarily seized while awaiting the loading of cargo.

## Theft at oil terminals

Compared to the types of oil theft described above, there is far less information on how theft takes place at export terminals, but there are two competing narratives. The first alleges that stolen oil is pumped onto tankers being loaded at terminals, facilitated by manipulating meters and falsifying documentation. The second suggests that oil is siphoned from storage tanks at the export terminals and loaded onto trucks (Katsouris & Sayne 2013).

## How is oil reintroduced into the legal value chain?

As a starting point, the light sweet oil stemming from the Niger Delta is generally attractive to the market and is often preferred by American and European refineries. However, reinstating larger amounts of stolen oil into legal value chains is challenging, most likely complex, and is subject to thick layers of secrecy. Thus, there is limited detailed knowledge available. Nevertheless, one way to do this is simply to transport stolen oil to foreign refineries for processing and sale while presenting forged paperwork to allow the oil to be accepted. This generally requires some level of cooperation or interaction with formal business networks and state institutions, if only for the infrastructure (ships, storage and refining facilities) and the institutions (local brokerage, oil processing, shipping companies, local and foreign buyers).

Another tactic is so-called 'co-loading', which involves mixing oil cargos carried by tankers from other oil fields or countries. Single tankers commonly carry 'split cargos', i.e. several 'parcels' of oil, each of which has its own bill of lading and pertains to different owners. While co-loading and split cargo are not illegal *per se*, they can be exploited as a way to disguise illegal oil (Katsouris & Sayne 2013). Stolen oil can also be transferred ship-to-ship at sea. Due to the shallow waters of Nigeria's port draughts, lighter vessels are needed to transport oil closer to shore. Thus, such transfers are not uncommon even with legal oil. Illegal oil can also be transferred to other ships at sea under the pretence that one is actually refuelling (ibid).

Illegal oil has also been known to be brought to storage facilities overseas or at sea, from where it is carefully mixed with other oil parcels over time. New paperwork can be issued before the parcels are eventually sold. This way, the origins of the oil are better disguised for future transactions. Storage facilities involved in this form of 'whitewashing' may be located far from the origins of the stolen oil, e.g. in the US, Singapore, China, India and various countries in Eastern Europe, while storage facilities with smaller capacities are likely to be located in West Africa (Katsouris & Sayne 2013) and owned by local oil companies (Hastings & Phillips 2015). While mixing legal and illegal oil may help mask the origins of the product, the downside of this practice is that suspicious oil tends to have a somewhat limited market.<sup>40</sup>

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40 A bad blend may ruin engines or make the oil unfit for many purposes. It also changes the oil's basic qualities and characteristics, which might facilitate it being detected as illegal. However, there are markets for this type of oil, especially in Eastern Europe and Asia (Katsouris & Sayne 2013, 32).

## Does oil theft finance other illicit activity?

Nigerian oil bunkering is often loosely coupled with a wide variety of illicit activities such as insurgency, violence, piracy, robbery at sea, hostage taking, sabotage, online scams, drug trafficking and sometimes terrorism.<sup>41</sup> While there is fairly strong evidence of the links to Delta militants and to diverse types of pirate activity, the links to the other activities appear weaker and, in some cases, close to undocumented (in the case of terrorism). This section will take a closer look at the links between illegal oil bunkering and some of the illicit activities listed above.

### Delta militants

The official rationale for militants, such as the Movement for the Emancipation of the Niger Delta (MEND), has been that oil theft, sabotage and kidnapping of international oil staff were a form of protest of the unfair distribution of Nigeria's oil wealth (UNODC 2013). Irrespective of the precise motivation, not only have these groups and loosely organised militia benefited significantly from organised oil theft, they have also benefited from government campaigns to stop illegal bunkering in the Delta. A government amnesty programme promised immunity from prosecution and financial and educational support towards finding alternative livelihoods for militants. Some 26,000 militants turned themselves in, among them prominent leaders (UNODC 2013). The amnesty allowed oil production to rise from about 700,000 bpd in mid-2009 to about 2.4 million bpd in 2011. However, the programme was costly as it offered monthly payments to ex-militants totalling about USD\$500 million per year. Several ex-militant leaders were also awarded controversial and lucrative contracts to guard pipelines under the amnesty (Onuoha 2016).

The benefits offered by the amnesty programme also attracted so-called third-phase militants who launched sporadic attacks in order to collect the rewards of the deal (UNODC 2013). President Goodluck Jonathan continued the amnesty, but following the election in 2015 of President Bukhari, cutbacks of about 70 percent to the programme and the termination of the pipeline protection contracts of several militants were introduced (Onuoha 2016). In mid-2015, violence resurfaced with detrimental implications for local residents in the Delta states as well as for international oil interests, shipping companies operating in the Delta and the federal government of the newly elected President Bukhari. The government has since launched a military counter-offensive both on land and at sea, however, this offensive is reportedly of limited success (Onuoha 2016). In the 2017 budget proposal, Bukhari's government proposed to restore the financing for the amnesty programme to pre-2016 levels to about USD\$215 million (Bloomberg 2017). Somewhat ironically, both oil theft and the political measures designed to stop oil theft can be said to sponsor the Delta militant leadership.

### Maritime piracy

The new surge in militant attacks inside the Delta has also affected maritime piracy in the Gulf of Guinea (GoG) (OBP 2016; UNODC 2013; Onuoha 2016).<sup>42</sup> In 2016, maritime piracy activity worldwide was at its lowest since 1996, with only 42 reported attacks. The trend in the GoG, however, was somewhat

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41 See, e.g. UN Security Council, 'Gulf of Guinea Piracy 'Clear Threat' to Security, Economic Development of Region; Countries Need United Front in Response, Top UN Official Tells Security Council,' SC10558, 27 February 2012. Available at <http://www.un.org/press/en/2012/sc10558.doc.htm>

42 According to some, approximately 70 percent of all piracy-related incidents in the GoG are directly related to Nigerian criminal gangs mostly originating from the Niger Delta (Onuoha 2016, 7), however, such numbers are generally beset by uncertainty.

different. The number of reported incidents increased from 14 in 2015 to 36 in 2016. These included nine of the 12 vessels fired upon worldwide in 2016. Some of the vessels were attacked almost 100 nautical miles from the coastline (International Maritime Bureau 2017), suggesting well-planned attacks and that pirates are in possession of rather seaworthy vessels. A notable trend was also that kidnap for ransom against merchant vessel crews increased significantly in these waters. Thirty-four crew were taken in nine separate incidents in 2016 in Nigerian territorial waters (IMB 2017). Some have suggested that kidnapping for ransom at sea should not be seen in isolation but, rather, as 'an extension of the land-based kidnappings' typically performed by Delta militants (Hastings & Phillips 2015).

A 2013 UNODC report found that a large share of the piracy attacks in the GoG targeted vessels carrying petroleum products. These vessels are attacked because there is a booming black market for fuel in West Africa, which makes the cargo easily tradeable. The market for stolen oil thus provides a market for piracy activities, especially those aimed at well-planned ships and cargo seizures. In these types of large-scale and highly organised attacks, the actual pirates only play a detached role as 'muscle' in a larger syndicate of financiers and brokers, politicians and international actors (Hastings & Phillips 2015). Stolen oil thus appears to fuel different types of maritime piracy and criminal networks operating at sea. However, oil in general, and the presence of the international oil industry in particular, appears to be pivotal in attracting many of these attacks.

### Transnational organised crime and terrorism

A UN report concludes that oil theft supports a wide range of transnational organised criminal activity in the GoG (UNODC 2013), and unconfirmed reports of such connections abound. Many reports have also recycled old claims that Lebanese nationals, possibly financing Hamas and Hezbollah, the Russian mafia and drug cartels, take part in the networks involved in oil bunkering in the Delta (see Murphy 2013). Unconfirmed reports claim that East European, Russian and Asian organised crime networks reportedly play a role in the international part of the value chain of stolen oil (Katsouris & Sayne), but details are sketchy. The literature on oil theft is thus rife with claims which sometimes appear to amount to mere rumours of how stolen oil benefits criminal networks. What can be established is that there are high *risks* that trafficking networks that manage sophisticated illegal supply chains may also be implicated in other types of illegal activities, such as oil theft. Overall, however, there is little proof of the connections between oil theft, insecurity and TOC (Katsouris & Sayne 2013). Importantly, the lack of hard evidence should not be interpreted to mean that such connections do not exist.

If the links between networks involved in smuggling drugs, migrants and arms are weak, the connection between oils theft and terrorism are even weaker, though not entirely absent. Katsouris and Sayne found a few suspect business links that would suggest that oil theft helped fund terrorist groups and that terrorist groups took part in schemes to launder money stemming from oil theft (2013). However, little detail is available on these links. Scholars and studies investigating the financial sources of Boko Haram have found that its sources of revenues are elusive and diverse, but oil theft or oil smuggling is rarely reported to be central (see, e.g. FATF 2015, 2016)

## How are oil theft and related illicit activity facilitated by corruption?

Corruption in Nigeria is generally acknowledged as pervasive at all levels of government, and Nigeria is a clear example of a neo-patrimonial system (Bøås 2011; Oarhe 2013; U4 2014).<sup>43</sup> Corruption is as such not an irregularity; it is a governing logic or social mechanism that permeates the Nigerian state and society. Petroleum riches have significantly facilitated the neo-patrimonial system, as it provides a resource that can lubricate clientelistic networks and informal institutions. In fact, oil revenues may be said to function as a political glue among the political elite in an otherwise divided federal state. Traditionally, the president and his top advisors have constituted the core team of decision-makers in the oil sector, concentrating the power of oil income in the hands of a small and privileged circle (Gillies 2009; see also Global Witness 2017b).

The four types of oil theft described in this paper are all dependent on corrupt officials either turning a blind eye or, more often, taking part in the networks that carry out illegal extraction or theft. At the local level where small-scale theft takes place in local Delta communities, the protagonists are reportedly Niger Delta youth and community leaders (who condone the practice). However, several studies also point to the key facilitating role played by law enforcement agencies, in particular, the Joint Task Force (JTF) (Katsouris & Sayne 2013; Pérouse de Montclos 2012). The involvement of the JTF is key since it is, in fact, especially tasked with patrolling for evidence and the seizure of perpetrators, vessels and equipment used to steal oil in the Delta states (Katsouris & Sayne 2013). Rent-seeking police and member of the army are also complicit by protecting oil theft networks for a cut (Pérouse de Montclos 2012). In addition, there are claims that local employees of the oil industry are complicit (Vrej 2012) and that politicians or government officials in some cases oversee the practice (Gillies 2009). Bribes thus appear to be a common facilitating tool in terms of small-scale oil bunkering.

At the more industrialised level of oil bunkering, a more complex web of actors is at play. Some sources point to members of the executive and legislative arms of government, oil companies, including the Nigerian National Petroleum Corporation (NNPC),<sup>44</sup> businessmen, retired and serving military officers and militants, among others (Asuni 2009). It is not only the JTF, which is usually thought to be extremely corrupt, the same goes for the navy (Pérouse de Montclos 2012).<sup>45</sup> Larger-scale bunkering networks are also reportedly obliged to pay a fee to the navy for free passage off the coast (ibid).<sup>46</sup> This goes to show that Nigerian law enforcement agencies in all parts of the operational spectrum play a role within these networks, either as partners or by receiving bribes, including those tasked with preventing theft, with intelligence gathering, detaining and arresting thieves and with investigations and prosecutions. Nevertheless, it is important to note that these institutions tend to cater to different needs and are

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43 Nigerian elites have long been known to pilfer national coffers. By some estimates, close to USD\$400 billion in public funds were stolen between 1960 and 1999 (UNODC 2017b).

44 For more details on issues relating to the NNPC, see e.g. Sayne, Gillies and Katsouris (2015).

45 See, e.g. Ingwe (2015) for examples.

46 Other law enforcement agencies that apparently play a considerable role in oil theft networks include the Nigerian Maritime Administration and Safety Agency (NIMASA), which licenses, inspects and clears vessels and seamen in Nigerian territorial waters. It is also responsible for general surveillance and maritime domain awareness, carrying out some patrolling, detention and arrest functions (Katsouris & Sayne 2013, 19). The Nigeria Security & Civil Defence Corps (NSCDC) and the Economic and Financial Crimes Commission (EFCC) are also both complicit according to Katsouris and Saynes (2013, 19). The NSCDC is an important facilitator as it is tasked with policing pipelines to prevent theft and sabotage and with arresting and handing over offenders for prosecution, while the EFCC is responsible for developing financial intelligence on oil theft networks and investigating and prosecuting cases of oil theft and related crimes (2013, 19).

involved in both the facilitation of oil theft *and* in constraining it (see Hastings & Phillips 2015). The complicity of politicians may be less visible than that of law enforcement institutions and the judiciary, but politicians remain the greatest beneficiaries (Murphy 2013). Oil theft reportedly spikes during periods of high political competition, such as around elections, suggesting that stolen oil in part pays for political campaigns and other politically-motivated actions like targeted killings and violence aimed at disrupting voting (Katsouris & Sayne 2013).

Oil theft at sea is facilitated by complex networks of actors. These networks are comprised of state institutions and institutions of the formal economy, along with a diverse set of national and international criminal groups or networks (Hastings & Phillips 2015). The navy, customs and port authorities reportedly inform pirates and militants of the location of ships and their cargo and, hence, facilitate and protect oil theft at sea and pirate attacks. According to Pèrouse de Monclos (2012), some of them also provide pirates with bills of lading in order for them to have exact details of the potential loot.

### Oil related fraud schemes

As illustrated above, oil can be stolen in a plethora of ways on its way to oil terminals. However, large amounts of oil revenues also disappear in relation to export and concessions. Starting with export, Nigeria has a complicated system for selling oil, which tends to hinder transparency and facilitate corruption. Under President Goodluck Jonathan, for instance, there was a proliferation of middlemen and companies involved in selling Nigeria's oil, which resulted in confusion regarding ownership structures. On average, however, the NNPC is responsible for selling about half the total amount produced (Sayne, Gillies, & Katsouris 2015).<sup>47</sup> Complicating matters even more, each new regime tends to rewrite the list of companies allowed to sell Nigerian crude. This not only allows every regime to reward its cronies, but also to further thwart transparency for traders wishing to buy legal petroleum products.

International petroleum traders are heavily involved in the export of Nigerian oil. Swiss companies bought 36 percent of the oil put up for sale by the NNPC in 2011, and if Swiss subsidiary companies are counted, the number rises even further (Berne Declaration 2013). Considering that the NNPC is characterised as opaque, mismanaged, subject to high corruption risks and that it fails to maximise returns for the nation (Sayne, Gillies, & Katsouris 2015), there is also a considerable risk that international traders function as vehicles to support the theft of oil revenues and to launder the proceeds of corruption.<sup>48</sup> Information gathered for the Berne Declaration (2013) shows, for example, that there have been instances where two Swiss traders have bought oil from the NNPC at prices lower than market rates (Berne Declaration 2013).

As pointed out above, due to low refining capacity, Nigeria also imports large amounts of refined products. The subsidy system has in the past proven to facilitate large-scale embezzlement involving local importers and their foreign subsidiaries.<sup>49</sup> One study found that 10 percent of the importing companies

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47 This has also fostered oil fraud schemes whereby companies claiming to have close ties to the NNPC offer to sell oil at too-good-to-be-true discounts (Farge 2012). In many of these cases, there may be no oil for sale whatsoever. However, such schemes are also suspected of helping resell illegally bunkered oil from the Delta (ibid).

48 Large shares of the oil revenues have gone missing from the NNPC. In 2014, the Nigerian Central Bank governor raised the alarm that USD\$20 billion in NNPC oil sale revenue was in fact missing (Sayne et al. 2015)

49 For more details see the report of the ad hoc committee 'To Verify and Determine the Actual Subsidy Requirements and Monitor the Implementation of the Subsidy Regime in Nigeria', April 2012. Available from <http://www.sahara-group.com/docs/hrr.pdf>, Report of the Technical Committee on Payment of Fuel Subsidies, June 2012.

had subsidiaries in Switzerland and that Swiss traders dominated the market of deliveries to Nigeria.<sup>50</sup> A Swiss company found to be implicated in the fraud held that it had followed Nigerian regulations and had adjusted to 'the demands of the marketers' (Berne Declaration 2013). This indicates that oil traders outside Nigeria form intrinsic parts of oil-fuelled corruption and embezzlement in Nigeria.

Government officials have also been known to fraudulently grant oil concessions to small companies owned by themselves or their associates, only to sell them on to major multinationals, thus robbing the state of considerable income. A recent report by Global Witness (2017b) details how Shell and ENI knowingly paid \$1.1 billion in 2011 to a former oil minister's shell company for the rights to one of Africa's most valuable oil blocks. Substantial amounts of this money were to be transferred on to other key politicians, among them, President Goodluck Jonathan. The mutually beneficial ties between Shell and the Nigerian state apparatus appear to be deep-seated. As expressed by Shell's former Executive Vice President for Africa, Ann Pickard, Shell 'had seconded people to all the relevant ministries' in the country and that 'Shell consequently had access to everything that was being done in those ministries' (ibid. 5).

President Bukhari, who assumed office in May 2015, launched a massive crackdown on corruption, with some notable results. The beefed-up Nigerian anti-corruption agency, the Economic and Financial Crimes Commission (EFCC) has, for example, arrested dozens of public officials and their cronies (*The Economist* 2016) and cut the number of passive middlemen that profit from oil sales (Sayne & Gillies 2016). The management of the NNPC oil sales has also improved slightly under Bukhari, after having worsened in the years prior to his tenure (especially between 2010 and 2015) (Sayne, Gillies, & Katsouris 2015; Sayne & Gillies 2016). There has also been improvements in NNPC reporting, which means that small steps have been taken to improve transparency in the opaque NNPC (Sayne & Gillies 2016). The top brass of the NNPC was also sacked in 2015 (Kazeem 2015). Still, several problems persist, such as the NNPC spending billions of dollars that it could not account for. In the last half of 2015, i.e. under Bukhari's rule, only a third of the NNPC's oil sale revenues were transferred to the national treasury, meaning that the corporation withheld a 10 percent higher share in that period than in 2013 and 2014 under Goodluck Jonathan (Sayne & Gillies 2016). While some of these funds are most likely spent legitimately, corruption is found to explain at least part of the missing funds (ibid). The NNPC thus appears to be a key vehicle for diverting the proceeds of oil in Nigeria. Nigeria has however made progress according to the requirements established by EITI, and the overall assessment is that Nigeria has made 'meaningful progress' in terms of improving the public debate and 'satisfactory progress' in collecting 'in-kind revenues'.<sup>51</sup> There has been 'inadequate progress' in terms of the 'policy on contract disclosure' (EITI 2016c). Despite some progress, the task of eradicating corruption in a political culture where corruption forms the lifeblood of the political and social machinery proves to be a daunting task, especially since corruption also paralyses the state's efforts to fight and prosecute crime.

## Summing up

Corruption in Nigeria not only facilitates oil theft and cripples law enforcement, but also enables a wide variety of other illicit activities, some of which appear to be linked to oil theft networks. This situation has led Nigeria to become a hub for TOC syndicates attracted not only by easy access to oil theft and scams, but also by weak or corrupt law enforcement structures and ample possibilities to operate freely or for a fee. The above analysis shows that oil is stolen at most levels of the value chain in Nigeria. It

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50 See Berne Declaration 2013 for more detail on the role of Swiss traders.

51 In-kind revenues refer to revenues paid in the form of oil or gas, which the state then sells on (see EITI 2016c for a thorough explanation).

also shows that various forms of corruption, including bribery, embezzlement and document forgery are instrumental in the relentless occurrence of theft and fraud. In addition, it shows that as oil and oil products reach the point of export and later, import, corruption evolves into large-scale embezzlement and fraud schemes, often carried out through complicated operations to create confusing and complicated paper trails. These lucrative schemes involve the NNPC, local Nigerian companies, politicians, Nigerian elites as well as foreign traders and often subsidiaries located in tax havens. These schemes are criminal in their own right, but this report has found little evidence to support that they subsidise other illicit or illegal activity such as terrorism, militancy and drug smuggling.

### 3.5 Summing up the findings

This paper has found that diamonds, timber, gold and oil are all illegally extracted in the four respective countries addressed. Resources with a high value density, such as diamonds and gold, are naturally more attractive for illegal or illicit artisanal extraction than resources with a lower value density and are thus extracted illegally on a small scale. The paper found no evidence of industrial-level illegal diamond and gold extraction, but the lack of such information should not be interpreted as proof that it does not exist. Instead, more research is needed into the gold industry in Mali and the diamond industry in Sierra Leone to determine whether gold and diamonds could also be diverted from the value chain flowing from the formalised sectors. In the case of Nigerian oil, it is not illegally extracted; rather, it is stolen after one of the multinational oil companies has extracted the oil. Theft happens both on a small scale within the Delta (i.e. close to the point of extraction) and on a larger and highly organised scale inside and outside the Delta, at several stages of the value chain, both near to and far from the point of extraction.

While the distinction between illegal and informal extraction is often unclear (e.g. for artisanal gold mining in Mali), this study found that a large share of the extraction of lootable resources like diamonds, gold and timber is carried out informally. This is to say that it is part of the informal economic sector (Engwicht 2016; Bickel & Cerutti 2017; the Global Initiative against Transnational Organized Crime, GIZ, & Estelle Levin Ltd. 2017). Informal extraction is often driven by poverty and economic incentives due to lower transaction costs or higher prices in the informal and illicit trade (Wilson 2011; Bickel & Cerutti 2017). The artisanal mining industry in Mali is mainly informal, and so is a large part of the timber trade in Liberia and the diamond trade in Sierra Leone. This means that both of these particular value chains represent a chance for poor people to make a living, but they also serve as sources of income for corrupt officials and present a potential for money laundering and/or exploitation by criminal groups.

Illicitly or illegally extracted natural resources are traded in informal markets locally, smuggled to regional markets or exported, often using forged documentation. Timber is sold in informal domestic markets or smuggled out of the country using fake certifications or by hacking timber databases. Diamonds and gold are smuggled out of their respective countries, sold in illegal markets, used for money laundering schemes or exported through informal channels, as is often the case with ASM gold in Mali. This paper finds that corruption also plays a role in accommodating the informal trade, sometimes due to the lack of enforcement of the limited regulation that actually exists. In fact, there is no shortage of regulations, but partly due to the availability of rents and the weakness of the formal system as such, there is a lack of incentive to enforce those regulations. In Nigeria, the regulatory system is bloated and often times made too complex to navigate. In such a context, where the formal and informal systems work in intertwined ways, most of the stolen Nigerian oil appears to be sold illegally in regional or international markets through various complex, fraudulent arrangements, often necessitating the complicity of corrupt high-level government officials, politicians or sophisticated document forgery, as in the case of potentially hacked timber databases (Global Witness 2017a; Lawson & MacFaul 2010). Smaller amounts of stolen oil are also sold in illegal markets locally in Nigeria. As oil is neither particularly value dense or easy to smuggle, common to all types of oil theft is the involvement of networks of actors; including government officials, elites, politicians and people functioning as 'muscle' to protect and facilitate the endeavour.

The lootable natural resource trade, in many cases, began as legal (they are legally extracted), only to be diverted or stolen from the value chain at a later stage. While diamonds and gold are more susceptible to diversion from legal value chains due to high value density and that they are easy to extract and transport, this paper did not find evidence of gold or diamonds being stolen from the legal value chain. Conversely, oil is stolen at multiple stages of the value chain, and the study found little evidence to support that timber is stolen after being harvested.

Whether a natural resource is illegally/illicitly extracted or stolen at a later stage of the value chain, there are a plethora of ways to reinsert illegal or illicit resources back into the legal value chain in order for it to be sold 'legally' on international markets. This study found that the forging of documents and certificates is a key facilitating measure in ensuring that oil, diamonds, gold and timber can be traded at market prices. The paper also found that higher demands on supply chain control, in combination with interventions aimed at promoting licensing, may have led to a new market for forged licenses. One example of this is the abuse of Private Use Permits in Liberia, whereby bribes are exchanged for permits. In Nigeria, there seems to be intricate schemes for document forgery that appear to enable both grand theft- and grand corruption related to oil.

Another method frequently used to insert informal or illegal resources into the legal value chain is by blending legal and illegal resources. The study found that there is a high degree of ingenuity involved in devising ways to do this, especially in terms of mixing batches of oil.<sup>52</sup> Junior companies appear to be convenient vehicles for illegal transportation, storage, corrupt transactions and document forgery. These companies may be of concern for larger multinational companies with high compliance pressure and reputational awareness. In addition, there have been several indications that small companies involved in the lootable resource trade in the countries examined in this issue paper have links to politicians or use secrecy jurisdictions to cover beneficial ownership structures. In Nigeria, for instance, small companies found to be involved in illegal storage and transportation, as well as oil fraud schemes, are often owned by government officials or politicians (Hastings & Phillips 2015). Both beneficial ownership structures and the existence of tax havens thus play a key facilitating role in the large-scale looting and diversion of natural resources. The lack of due diligence on behalf of traders who import these resources further enables both large-scale and small-scale looting as well as the illegal and illicit exploitation of natural resources from West Africa.

Apart from informal exploitation and trade in natural resources, the study identified the *risk* that high-value resources are also used in direct barter arrangements whereby resources can be traded for arms, drugs or other resources. Thus, these resources need not enter the legal supply chain to be traded. The trade can be carried out completely outside the formal system, which makes it very difficult to detect and control. More investigative research is however needed to establish these patterns empirically.

In contrast to recent discussions on terrorist financing in West Africa and the Sahel, this paper found little real evidence in the literature linking terrorist organisations to the lootable resource trade in the four countries studied. Importantly, however, the absence of evidence in this paper should again not be interpreted to mean that there are no such links. Organised crime seems to be more closely intertwined with the trade in lootable resources, especially because high-value resources such as diamonds and gold are attractive for money laundering purposes (although such money laundering is not documented in this study). Nonetheless, it should be noted that several studies have concluded that high-value resources like diamonds and gold carry a particularly high risk of being exploited to launder money (FATF 2013a; Engwicht 2016; Hunter & Smith 2017). A forthcoming U4 and Public Eye study (2017) also shows that the commodity trading sector lacks strong anti-money laundering requirements and that FATF recommendations are mainly applicable to financial institutions. Yet, using commodities for money laundering falls under a larger trade-based money laundering concept, which has been identified by Global Financial Integrity (2015) as the largest source of illicit financial flows from developing countries.

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52 Gold is also known to be mixed and masked in a wide variety of ways, but this study found little documentation on whether this is the case in terms of gold originating in Mali.

This suggests that more attention ought to be devoted to West African countries and their development donors.

Figure 1: Summary matrix

	Legal or Illegal small-scale extraction	Illegal Industrial Extraction	Stolen later	Traded illegally	Funds other illegal activity (terrorism, organised crime or conflict)	Mode of operation to enter legal value chain (forged certificate/licenses, mixed in with legal resources)
<b>Timber in Liberia</b>		(X)		Sold at illegal markets	Organised crime	Forgery; mixed with legal resources
<b>Diamonds in Sierra Leone</b>	Both			Smuggling; money laundering; sold at illegal markets	Organised crime	Forgery
<b>Gold in Mali</b>	Both			Smuggled, probably barter		Mixed with legal resources
<b>Oil in Nigeria</b>	Illegal	(X)	Illegal bunkering; theft	Smuggled; sold at illegal markets; exported using forged documents	Organised crime	Forgery; mixed with legal resources

The matrix only displays findings that are considered well documented. In many cases, there are claims and anecdotal evidence suggesting further connections and conclusions could be drawn on a less secure basis.

## Conclusions

Sierra Leone, Liberia, Mali and Nigeria all have large reserves of valuable natural resources that are traded both legally and illegally on international and local markets. The fact that large shares of these commodities are traded partly outside of formal market structures makes them vulnerable to exploitation by criminal networks and armed actors, such as militants, pirate syndicates and terrorists. In neo-patrimonial systems such as these, where resources are governed both by formal and informal institutions, often in complex interaction, corruption becomes crucial and widespread. This means that corrupt practices facilitate

natural resource theft; but perhaps more worrying is that it facilitates opaque market structures which in turn leave room for a wide variety of illicit private gains. Not only does this deprive local populations of the benefits of natural resources, it also breeds more corruption, the hollowing out of state institutions, nourishes shadow economies and secrecy jurisdictions and helps hide and wash the profits stemming from other criminal behaviour. These structures may also constitute convenient avenues for clandestine organisations seeking to undermine state projects and law and order, such as regional or global terrorist networks. Rent seekers and criminal exploiters of natural resources often use ingenious methods and work out sophisticated systems of how to carry out their operations undisturbedly. Making sure that a lucrative set-up is not interrupted or impeded necessitates a certain distribution of benefits to a variety of actors, including political elites, law enforcement personnel and members of the judiciary. The fact that natural resources are exploited in ways that ensure that large networks profit, to some extent, is not only a core characteristic of neo-patrimonial networks, but also what makes devising effective countermeasures complicated. This is why this paper insists that in these types of governance systems, interventions be tailored in accordance with intricate understandings of the value chains. Interventions that fail to take profit patterns and structures into account may risk that value streams simply mutate to accommodate new obstacles, that established networks find ways to capitalise on these new obstacles by acting as gatekeepers, that efforts and interventions become irrelevant and hence contribute to fatigue on the part of donors or, worse still, on the part of local stakeholders and societies.

The country chapters in this paper have all concluded that few or no explicit links between natural resources and terrorism have been found. Still, 21st century organised crime and terrorists alike are organised in decentralised networks which operate in increasingly similar and indeed interconnected ways to earn money. In many instances they even converge and cooperate (see Matfess and Miklaucic 2017). Considering that the natural resources looked at in this paper lend themselves well to illegal exploitation, there is little reason for optimism what concerns the chances that gold, diamonds, timber and oil are not exploited by terrorists. The lack of clear evidence *may* be ascribed to the vexing challenge of mapping and understanding these purposefully opaque networks.

The realities described in this paper certainly seem a far cry from the African Mining Vision agreed by all heads of African states in 2009, which is aimed at a 'transparent, equitable and optimal exploitation of mineral resources to underpin broad-based sustainable growth and socio-economic development' (Africa Mining Vision 2009). Instead, both illicit and illegal natural resource exploitation continues much to the benefit of the few. The four countries included in this study in fact go a long way in representing near-ideal conditions for exploiters of natural resources, as they are characterised by low risk and high potential for profit. More precisely, they are characterised by porous borders, deficient state monopolies on the use of violence, often deficient territorial control, weak law enforcement structures and endemic corruption. These factors enable illicit, or partially illicit value chains, which in turn bring natural resources onto the market place. These findings are important for economic, development and security reasons. Quantitative research shows that countries where officials steal natural resources have higher incidences of rebellion and violent crime (Katsouris & Sayne 2013), which means that poor resource governance in West Africa is also real obstacle to peace and security. In states that are in some form of ongoing conflict, such as Mali and Nigeria, criminal networks often choose to support antigovernment or terrorist groups in order to prolong or sustain the very conflict environment which enables their own predatory activities (Deville 2013). This may have grave consequences for stability, but also for the prospects of a viable state able to provide rule of law. In addition, shadow value chains also require protection, which in many cases leads to increased levels of criminal violence.

The gravity of the consequences of illicit exploitation of West African natural resources points to the need for tailored policy prescriptions. Although there are no panaceas available to societies where corruption

form the lifeblood of economic, social and political life, this paper recommends that interventions be built on robust contextual analyses of the structures that benefit from exploitation and the shadow value chains that enable natural resources to reach markets. Recognising that shadow value chains of natural resources transcend individual state boundaries and that international actors play crucial roles in these value chains, successful countermeasures should not address the local parts of the value chains only, but action needs to be tailored to all stages of the value chain. Adding to that generic recommendation, the next section will provide some modest suggestions that may be relevant when designing interventions to diminish the exploitation of lootable natural resources and to curb the corrupt networks that facilitate and gain from this activity.

## 4. Entry points for external actors

In the types of governance systems described in this paper, traditional policy recommendations focusing on support for law enforcement agencies, licensing schemes and establishing accountability measures will often times only have limited effect (Booth 2012). At worst, they will have detrimental effects as they may serve to reinforce rather than weaken the neo-patrimonial networks involved. There is also empirical evidence suggesting that placing increased demands on governments can cause more effective clientelist relations rather than foster good governance (Booth 2012). By channelling money into state structures which are themselves associated with informal exploitative networks, donors may unintentionally help create opportunities for innovation and the further persistence of these networks. A weakness of some of the approaches that aim to build stronger accountability is that they do not necessarily build on context-specific understandings of corruption (Johnsøn, Taxell, & Zaum 2012). This has sometimes led them to the assumption that anti-corruption interventions will succeed if they can strengthen the abilities of the authorities to monitor and hold agents accountable for their actions. Such approaches often take for granted that the principals themselves have no political will or incentive to establish a transparent system (Marquette & Pfeiffer 2015). In contrast, state actors who rely on natural resources to uphold or build patronage networks usually have few incentives to effectively regulate the trade unless it coincides with personal gain. In order to devise sensible interventions, we need to develop a better understanding of the intricate dynamics, including the state and non-state actors involved in governing and exploiting the resources at hand. To do so, we need to pay attention to the underlying distribution of power and patronage, track changes to it and try to understand the sources of power at play (Kahn 2012). This is, however, no simple task as power tends not to be distributed once and for all, but to be continuously renegotiated. This requires not only outside intelligence efforts, but also local insights and knowledge of the dynamics at hand. Even though gathering such information is both resource demanding and complicated, and despite the fact that powerful networks may also be willing to use a range of means to protect their interests (Reitano & Shaw 2015), such insights are key to unpacking the oft-cited black box of 'lack of political will', which is often an important explanatory factor in failed reform attempts.

### What does this diagnosis of complexity mean for interventions in general?

A set of more specific recommendations are given below, but on a general level, one could say that there are four aspects of the cases at hand that have particular and direct implications for interventions and that should thus be kept in mind when designing interventions:

1. In these cases, mixed informal power distributions typically trump formal rules. This means that the impact of legal approaches may be limited and that the enforcement of such measure will most likely be selective and have limited effect at best.
2. State actors gain from and are complicit in the informal power distributions. This means that law enforcement is limited and that there is a collective action problem. This complicates the identification of interventions that actually incentivise people in power.
3. Non-state actors (companies, commodity traders etc.) also play a role in the networks, which means that their potential for disciplining public institutions is limited.
4. Civil society tends to be weak in these systems, and therefore, social accountability demands are constrained. Issues related to missing incentive structures often also apply to civil society. This means that demand side approaches alone may not work.

## 4.1 Recommendations

Pinpointing exactly ‘what works’ is a difficult endeavour as we are dealing with flexible value chains and complex networks of beneficiaries, often with few incentives to contribute to delimit their own revenues. The following recommendation may make a modest contribution to considerations of how to devise interventions aimed at limiting the illegal trade in lootable resources and the related sponsoring of other illicit activities in the four cases in question.

### Identifying entry points, areas of reform and partners

In each of the four countries studied in this issue paper, corruption represents the norm rather than a deviation from an ideal type of governance system. This suggests that corruption is not only part and parcel of the illegal lootable resource trade, but most likely also part of the legal trade in these resources (although this has not been sufficiently demonstrated in this paper). As shown, for example, in the case of diamonds in Sierra Leone, corruption is part of a workable system with informal rules and regulations. **To design more effective natural resource management interventions, there is a need to understand the actors involved, their incentives and how their networks function.** A few donor agencies already have frameworks for political economy analyses, such as the Swedish International Development Cooperation Agency (2013), power analyses and DfID’s Driver of Change analysis (DfID 2009). These frameworks, however, do not go as deeply into the links between political, economic and social factors in relation to environmental issues and changes as the political ecology analysis recommended in Williams and Le Billion (2017). They nevertheless provide a starting point for thinking about how to produce ‘thick’ contextual descriptions and a greater understanding in order to devise sensible and tailored interventions. This type of analysis is also in line with a point made in the 2017 *World Development Report*, which stresses the need to recognise power distributions in policy arenas before designing policies, as these power relations may affect policy design and implementation (World Bank 2017). Gaining a more holistic understanding of local power distributions and patronage systems does not, however, imply that sweeping reforms or interventions addressing corruption at all levels of society should or could be designed. In fact, according to Khan et al. (2016), research shows that corruption interventions with a sectoral approach have greater prospects of achieving change. In addition, taking the OECD’s mapping of corruption risks along extractive value chains into account could help identify entry points for intervention. This should include scrutiny of the part of the value chain that involves international actors as they are often times closer to the consumer point of the value chain. Consequently, **a point of departure for the design of interventions seeking to address the illicit trade in natural resources in any country could be to focus on a specific sector, with particular attention paid to highly exposed points of the value chains, based on a comprehensive contextual analysis.**

### Decreasing the tolerance for neo-patrimonial corruption

One way to weaken corrupt neo-patrimonial networks is by decreasing the public’s tolerance for corrupt practices. **An increased awareness of the gravity and unfairness of the system can be created by sharing political economy analyses with ordinary citizens (Cammack 2007). By displaying how values are stolen, how much is diverted from state coffers and exploited for private gain by elites, local communities may gain a better understanding of local informal power structures and how they undermine development and democracy (ibid).** These types of political economy analyses can however be highly controversial and can potentially cause security concerns or societal unrest. Provided that considerations are made regarding whether this could potentially impact local stability, making available information on corrupt practices may thus also inspire the intelligentsia, media, NGOs and others to engage in peaceful rights activism, which could help strengthen weak civil society structures and help

improve the potential for community engagement initiatives. Such measures should however be cognisant of the fact that one of the reasons that corruption goes mostly unpunished is that it is not necessarily perceived as a dysfunctional system but rather one that works according to a different logic (Cassara 2016; Cammack 2007). **Interventions should thus recognise that all forms of corruption are not necessarily perceived as deviant or illicit but, rather, as ‘business as usual’ and that it may even form part of long-established norms.** They should also reflect that in societies characterised by widespread corruption and patronage, civil society often has limited capacity to mobilise.

### Community engagement/local problem-solving

Communities are often engaged in reform initiatives such as community mineral beneficiation schemes, an example of which is the Diamond Area Community Development Fund (DACDF) in Sierra Leone. The results of these community-based initiatives are mixed, and they often become highly political, with limited community influence. **One way to ensure the utility of these community initiatives is to make them inclusive not only in terms of consultation but also in actual design and possibly even redesign.** This is also in line with the suggested approach to more effective governance interventions according to the ‘thinking and working politically’ paradigm, according to which local problem-solving is seen as a preferred tool to more effective interventions (Dasandi et al. 2016). This becomes especially important in contexts with limited statehood, such as the countries studied in this issue paper. **One prerequisite for local engagement is, however, increased transparency in how the authorities govern resources. The concerned authorities should thus, e.g. be encouraged to improve transparency in decision-making regarding the issuing and revoking of extraction licenses in order to prevent these from functioning as ‘currency’ in privileged clientelistic networks. It is thus recommended that donors continue to provide assistance in compliance with GIABA, EITI and FATF standards in Sierra Leone, Liberia, Mali and Nigeria.**

### Capacity building and awareness training of law enforcement

‘Strengthening the rule of law’ is a generic recommendation that, as this paper has warned, runs the risk of exacerbating corruption unless incentive structures and governing logics are properly understood. Provided that there is a comprehensive understanding of how patronage structures affect law enforcement, selective measures to build awareness and capacity to detect white collar crime may be helpful. As suggested by the IMF (2015), for instance, Malian law enforcement often lacks awareness of money laundering as a criminal endeavour and also lacks training in economic and financial crime detection, investigation and prosecution. **Considering that this paper has pointed to the high risk that Malian ASM gold is used for money laundering, tailored measures to capacitate law enforcement in Mali on the matter should be taken (provided due caution is taken) in order to hinder natural resources from being associated with impunity.**

### Promotion of regional cooperation

As the four cases show, illicit trade often has regional links through which lootable resources are being smuggled in and out of countries to later be sold in the most lucrative markets or to be exported from more convenient jurisdictions. Factors such as lower export taxes in neighbouring countries can thus create economic incentives for smuggling. **Regional efforts and organisations such as ECOWAS can serve as platforms to harmonise regulations in the region and to promote better border control. Such cooperation and harmonisation may serve to limit smuggling as well as to address some of the economic incentives that serve as drivers of the regional illicit trade.** In the case of Mali, the loophole in the way in which export tax law is practiced in relation to ASM gold should be closed. This means

that tax should be paid on the full amount of gold exported. This measure may help curb the illicit entry of ASM gold from neighbouring countries and control the export of ASM gold from Mali. As Reuters (2017) points out, there are limited prospects for commodity-based money laundering being regulated on a national level in developing countries because of the fact that local elites are often involved in illicit financial flows. Promoting regional efforts may not solve this issue entirely but may point fingers at regimes that avoid taking part in such initiatives.

## Due diligence

The pervasiveness of forged certifications and licenses often makes it difficult for resource traders to distinguish between legal and illegal commodities. To make it even more problematic, legal and illegal resources can be mixed in gold bars, oil shipments or through hacked timber databases. In addition, there is a trend in commodity trading, especially in mining, for smaller companies to often be involved in resource extraction. These smaller companies are, in general, less concerned about reputational risks and operate under less compliance pressure than larger companies. Issues regarding the forgery of licenses/certifications, combined with the increased role of junior companies, complicate transparency and exacerbate the need for effective due diligence. As pointed out elsewhere, **due diligence obligations that are applicable throughout the supply chain, from extraction to consumption, are needed in order to establish greater transparency in the flow of commodities** (see, e.g. Berne Declaration 2013). Nevertheless, establishing workable measures to that end may be difficult in practice. The OECD (2017) recently published a report with guidance for meaningful stakeholder engagement in the extractive sector. The report also includes guidance on stakeholder engagement with artisanal/alluvial miners. These guidelines make a healthy starting point for thinking about how to best manage supply chain risks.

The findings in this issue paper suggest that there is still a need to place strict demands and control routines on importers of gold, diamonds, timber and oil. The analysis shows that although some measures are in place, importers can easily establish informal routines in order to buy lootable resources from random sellers (such as in the case of 'walk-in' gold vendors trading considerable amounts of undocumented gold for cash in the UAE) or from informal artisanal exporters (such as those selling Malian artisanal gold to Swiss trading houses). One focus of attention for investigative authorities should be to scrutinise import transactions that include less known junior companies and especially companies that lack information about beneficial ownership structures, as this may be an indication of corruption. In general, both local and international actors, public and private, need to be the focus of anti-corruption measures.

## Multinational enterprises: Agents of change?

Multinational enterprises (MNEs) themselves can also positively contribute to foreign business environments by setting best practice incentives that resonate along global supply chains. In order to achieve this, there is a need for smart approaches that take into account the incentives of MNEs. International monitoring mechanisms need to take into account the conflict of interests that MNEs often face when trading in natural resources emanating from conflict or corruption prone states. **Ensuring regulation that does not shield MNEs from public naming and shaming is one important step. Self-regulatory mechanisms could be an additional measure** (see, e.g. the Maritime Anti-Corruption Network). These may have the disadvantage of appealing only to big actors who 'can afford to care', while leaving other segments of companies to cater to less conscientious clients and thus create a two-tiered market. Self-regulatory measures may nevertheless serve to raise awareness and raise standards of due diligence and facilitate critical inquiry into the business activities of MNEs by outsiders and/or clients. **In Sierra Leone, Liberia, Mali and Nigeria, there are already platforms for collective action cooperation, such as EITI, which could be further developed to increasingly serve as drivers for improved business**

**practices.** In a recent change, EITI now requires oil, gas and mining companies to disclose payments to governments for each project they operate. This represents an important improvement, which could also impede corrupt transfers for extraction licences. At the same time, however, a vote in the US Congress to overturn the implementation rule (1504) of the Frank Dodd Act represented a step in the opposite direction, as it will make it more difficult for the public to gain insight into the payments of extractive companies for extractive rights.

MNEs can also encourage trading partners to establish higher reporting standards. Commodity traders, both those involved in the export of Nigerian oil and the import of petroleum products into Nigeria, should, e.g. place demands on the NNPC and its subsidiaries for better reporting, provided that they are *not* themselves willingly implicated in corrupt practices. This could help decrease the risk of being used as vehicles for corrupt transactions and to cover up the theft of oil revenues. In order to improve transparency, commodity traders themselves should also improve their own reporting by publishing more details about their transactions and trade in lootable natural resources (see, e.g. the Publish What You Pay network agenda). It has also been suggested that traders should be obliged to carry out due diligence on their commercial partners (Berne Declaration 2013). This would include identifying red flags and exercising due caution when doing business with risky junior companies, so-called ‘politically exposed persons’, individuals who are or have been entrusted with a prominent public function (FATF 2013c) as well as companies with opaque ownership structures.

## Regulating commodity trade: Formalising informal value chains

Informal extraction and trade in natural resources often have a low entry barrier and, as such, may serve as a temporary or permanent solution for people in need of an income. However, **formalising, e.g. the artisanal gold mining sector in Mali would help ensure better working conditions for miners.** It could also help close some loopholes that currently facilitate corruption, illegal exploitation, tax evasion and potentially also the financing of illicit activity. One formalising measure could be to establish state-run buying centres for ASM gold. Another would be to enforce stricter regulation of the export system for ASM gold. While formalisation is a political and legal process that can only be decided by Malian authorities, there may be a need for advice on the design of legal measures as well as on the implementation of new regulation. One step in the right direction could be to opt for an assessment to be carried out by the Mining Policy Framework (Mali is already a member of the Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development, IGF). This process is intended to identify measures for improving mining governance through capacity building and technical support and has reportedly been of use to other countries in the process of reforming their mining sector.<sup>53</sup> Nonetheless, these measures are only fully helpful when there is due recognition of the incentive structures involved in these informal value chains. When making concrete recommendations, attention should thus also be paid to measures that maintain low transaction costs. Unless a considerable increase in transaction costs is avoided, there will be an economic incentive to engage in informal trade and to find new ways to continue to informally exploit natural resources. Interventions that encourage additional regulation and legal measures should also take into account that regulations do not solve much unless there is a local will to implement and enforce them. In order to avoid formalisation processes simply leading to informal trading structures being adapted or reinvented, one should also **consider providing education on how to make a living in a licit economy.** This is especially relevant when informal trade is widespread or has been long-lasting.

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53 See, e.g. the statement made by Senegal’s Director of the Control of mining Operations, Rosaline Mbaye, on the output of Senegal’s assessment (IGF Bulletin 2016, 6).

## Regulating the commodity trade: Trade transparency units

As noted in Longchamp and Perrot's (2017) report on corruption in commodity trade, the current FATF anti-money laundering requirements do not apply to commodity traders. Trade-based money laundering involving natural resources is, according to Global Financial Integrity (2015), a major source of illicit financial flows from developing countries, thus heightening the need to regulate the trade. As this issue paper points to the difficulty of establishing effective law enforcement in countries with systemic corruption issues, a potential measure to regulate the trade is by improving regulation in countries that are major importers or trading hubs for commodities, such as the UK, Switzerland and the UAE in the case of gold (Longchamp & Perrot 2017). So far, the focus of EITI has mainly been on producer states in publishing revenues and payment receipts for licenses and exploration rights; however, there is still a gap in trade reporting, especially purchasing companies' payments (ibid). According to estimates from EITI (2016b), only 10 out of 49 EITI-implementing countries publically reported sales.

In order to prevent and detect money laundering, many countries have established financial intelligence units (FIUs) responsible for examining suspicious transactions and information exchange. These units are most often based on international best practices identified by FATF and are in accordance with the requirements of the EU Anti-Money Laundering Directive. Modelled after the FIUs, Cassara (2016) recommends **establishing trade transparency units (TTU) for examining suspicious trade and to exchange information with customs agencies in different jurisdictions**. A TTU has been implemented under the US Immigration and Customs Enforcement (ICE) with impressive results (ibid). The US TTU has established information exchange with 11 countries and, according to Cassara (2016), seized assets worth more than USD\$1 billion. TTUs are not a viable option in any of the four countries due to financial and capacity constraints, however, major commodity trading hubs like the UK and Switzerland should consider this as an option.

## Addressing pertinent knowledge gaps

Illicit natural resource extraction is enabled by corruption and exploited by TOC in complex and dynamic arrangements. Anti-corruption interventions in this sector therefore have the disadvantage of aiming at 'moving targets'. **Building solid understandings of different aspects of how natural resources may help finance other types of illicit and illegal activity is therefore a continuous endeavour that requires constant attention to change**. This fluidity generates a near constant need for updated empirical knowledge of how natural resources are illicitly exploited on their way to legal or illegal markets worldwide. However, there are also a few notable and more generic knowledge gaps that should be closed in order to identify ways to prevent lootable natural resources from sponsoring illicit activity. Some of these gaps are identified and summarised in the following section.

## 4.2. Some key issues that merit further attention

### The role of money laundering in value chains

Money laundering is regarded as a major risk in relation to all the resources studied in this paper. Diamonds and gold, in particular, have been identified as highly valuable resources that are difficult to trace and, therefore, attractive for money laundering purposes. The FAFT (2013b) has published guidelines to prevent diamonds from being used for money laundering, but there is still a knowledge gap in relation to each of the four contexts studied in this paper. In particular, there is little knowledge of which actors use gold or diamonds for money laundering purposes and how this is done in practice, both locally and internationally. For donors who intend to introduce measures to curb the illicit flow of lootable natural resources into legal markets, understanding the mechanisms and vehicles used for money laundering is key. Learning more about money laundering can, as such, help devise ways to encourage greater transparency in the ways in which natural resources are extracted and traded. This in turn will likely help strengthen the capacity of commercial traders to carry out due diligence and to reduce the risk of becoming complicit in money laundering and potentially sponsoring additional illicit activity. Some have also called for a better understanding of country-level drivers of money laundering in order to make progress on the illicit financial flow agenda (Forstater 2016).

### The roles of illegal markets and formal industries

There is still a need for more research on the illegal (or grey) markets associated with each of these resources and their revenue flows. For instance, how and where are stolen oil products sold internationally? This means that more attention should be paid to understanding the particular value chains of each of the four resources studied in this paper. Some attention has fortunately been devoted to artisanal mining and related value chains. In terms of artisanal gold or diamond mining, there is a fair amount of research emanating from, for example, the literature on human rights/human security, development and the 'resource curse literature' (HRW 2011; Schipper, de Haan, & van Dorp 2015; Partnership Africa Canada 2017; Maconachie & Binns 2007). In the case of Mali, this literature seems somewhat detached from the literature on the current conflict in Mali and the disorder in the northern part of the country. This may simply be because there are actually few connections between illegal gold mining and the separatist and terrorist groups operating in the north of the country (FATF-GIABA-GABAC 2016), or it may be due to the difficulty of establishing such connections. Perhaps the most striking 'gap' in the literature concerning gold in Mali is, however, related to the state-controlled gold industry. Knowing that corruption is endemic in political and economic life and that Mali possesses large amounts of gold, corruption within the large industrialised gold sector and its potential links to criminal or separatist groups does merit a lot more attention. In both Mali and Sierra Leone, there is a particular need for more knowledge on whether industrially mined minerals (not just artisanal gold or diamonds) are stolen, used to support illicit activity and/or exploited in money laundering schemes.

### Opaque ownership structures/beneficial ownership

This paper points to the need to remedy weaknesses regarding licenses and certification schemes as part of efforts to ensure that resources are not stolen or illegally/illicitly traded. Licencing and certification schemes often provide a false sense of reliability due to weak oversight mechanisms and their susceptibility to forgery. When licenses and certification schemes are ineffective, there is a need to find solutions to ensure transparency in supply chains. Placing enhanced due diligence requirements on counterparts can be a way for traders to protect themselves against being complicit in illicit trade. However, more knowledge is needed on what exactly works in this respect. Global Witness (2017) found that companies

with secret ownership structures held several logging concessions in Liberia. Previous reports, like the Puppet Master report (Van der Does de Willebois et al. 2011) and the Panama Papers (2016), show that secrecy jurisdictions and corporate vehicles are widely used to transfer/hide illicit funds generated from corruption or other forms of criminal activity. Although this is covered in the EITI framework, there is still a need to further examine the use of corporate vehicles, especially due to the number of small actors with complicated ownership structures involved in the trade in lootable resources. There is a need for more knowledge of how to avoid opaque ownership structures in becoming a useful tool to cover up the looting of natural resources

### Manufactured goods imports originating from lootable resources

The direction of trade has changed over the last 15 years, with more exports of natural resources going to the so-called BRIC countries. For example, China is now a major importer of natural resources from Africa and is often a more significant trading partner than, for example, the EU. China generally has lower documentation requirements concerning origin and natural resource management than many other importers. Often, supply initiatives like the Kimberley Certification and FLEGT stem from the EU and do not necessarily impact trade with countries like China or the UAE. The fact that a major goods manufacturer like China or a trade hub like the UAE maintains lower documentation requirements than other importers causes problems for secondary imports to markets that maintain stricter demands on imports, such as the EU. Diverging requirements increase the risk that manufactured or processed import might stem from illicit trade. Once illegal natural resources are manufactured into products, the origins and value chains of the resources are very difficult to trace by individual companies. This also means that there is a need for more knowledge of ways to better control lootable natural resources, not only at their first stages of the value chain, but also after they have been processed and re-exported.

### Relating knowledge of neo-patrimonial governing logics to both the diagnosis of the problem and the design of interventions

As highlighted in this paper, the success of different oversight, licensing and certification interventions informed by simplified perceptions of corruption is often limited. There is a wide and general knowledge gap relating to anti-corruption reform and what potential effective alternatives to the traditional principal-agent approaches could look like. A proposed solution is to design interventions that are built on local problem-solving and to a greater extent on practical governance realities (Dasandi et al. 2016). However, local solutions are of little help unless they have established an understanding of the incentive structures at work, which are also applicable for local actors and populations, as they are usually not exempt from neo-patrimonial structures and logics. In countries such as the four studied here, corruption should be studied *not* as a deviation from established governing norms but, rather, as *the* governance system. While there is a fair amount of research on these systems, they need to be paired more concretely with the anti-corruption knowledge base. In order to address the knowledge gap of 'what works' in these types of systems, there is a need for more research to understand the interests and incentives of political settlements. A possible starting point would be to study existing informal structures like the Open Yai markets in Sierra Leone. From a practical perspective, doing this would require more in-depth and holistic approaches, especially to avoid the unintended consequences of creating a system that might further entrench corruption.

### Adaptive management: Learning from failure

There is a need for more knowledge of anti-corruption interventions related to lootable natural resources, which were of limited success. This is especially relevant for interventions in complicated neo-patrimonial social structures. Building a more systematised knowledge based on cases that failed to have the desired

effect would enable decision-makers to make more informed choices when designing interventions. While there is of course a need to avoid sweeping generalisations, a greater focus on what did not work could help advance the research field by enabling researchers to more systematically pinpoint key variables and combinations of variables, which may provide the best (or worst) potentials for different types of interventions. Learning from negative examples is usually a challenge in most policy fields, as failures are not published as widely as (moderate) success stories. In this respect, there may also be something to learn from the concept of 'adaptive management' within the field of development. While this is not an entirely new or widely accepted concept, it recognises that when dealing with complex challenges, iterative and adaptive approaches that are mindful of what seems not to have worked may be useful. Adaptive approaches that allow space for incremental learning may still not be dominant within the development field, but they could nevertheless serve to inspire less fixed approaches to learning within other fields. The United Kingdom's Department for International Development (DfID) has applied adaptive management to two major programmes, the State Accountability and Voice Initiative (SAVI) a demand-side good governance project in Nigeria, and Legal Assistance for Economic Reform (LASER), a climate reform programme implemented in eight countries (Derbyshire & Donovan 2016). The initial evaluation indicates that implementation was successful, although it demands significant operational and technical expertise (*ibid*). Gaining more knowledge on what this means in practice when designing interventions aimed at hindering West African natural resources from being looted, exploited by corrupt officials and even used to finance other illicit activity could be beneficial.

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Illicit natural resource trade continues to benefit corrupt officials, criminal and terrorist networks and divert resources away from development, security and the common good in West Africa. How are Liberian timber, Sierra Leonean diamonds, Malian gold and Nigerian oil traded outside, and intertwined with, legal value chains before ending up in what is often legal consumer markets? By collating recent knowledge of the 'shadow value chains' of these resources, this paper seeks to explore if and how illegally traded natural resources sponsor other types of illicit activity, such as organised crime and terrorism. Furthermore, how are these activities facilitated by corruption in the different cases? The paper gives a number of recommendations. The perhaps most important one is that in order to improve interventions, in-depth understanding of local power relations and incentive structures in these individual shadow value chains is crucial. Such knowledge should be paired with increased attention to how international actors and networks facilitate and accommodate illegitimate private gains stemming from lootable West African natural resources.



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