

Recent Corruption Scandals in South America and Their AML Impact on the Region

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Table of Contents

Executive Summary	3
Background	3
Multinational Scandals	4
Odebrecht S.A.	4
National Scandals	7
Brazil: Petróleo Brasileiro S.A., PetroBras, and Operação Lava Jato (Operation Car Wash)	7
Venezuela: Petróleos de Venezuela S.A., PdVSA (Petroleum of Venezuela)	9
Colombia: Refinería de Cartagena, Reficar (Refinery of Cartagena)	12
Argentina: Los Cuadernos de la Corrupción (The Notebooks of Corruption)	13
Legislative Impact	14
AML and Audit Impact	16
Banking With High-Risk and Cash-Intensive Industries	16
Banking With Politically Exposed Persons and Sanctions	16
Training and Communications With Senior Management	17
Record Retention	17
Conclusion	17
References	19

Executive Summary

This white paper focuses on the impact that corruption has on assessing AML impact in South America for local and foreign financial institutions.

Latin America remains an area of potential expansion for U.S. banks and financial institutions as the region has been dominated previously by regional and European banks.¹ As this occurs, these U.S. firms must remain vigilant about corruption, which clients are onboarded, and finally, how this may affect the design of AML programs that abide with both local and U.S. regulations.

The goal of this whitepaper is to utilize a recent multinational as well as four national (Argentina, Brazil, Colombia, and Venezuela) corruption scandals in order to demonstrate how they took place, the potential cost of corruption, political ramifications, and finally, how funds were laundered. Prior to the whitepaper's conclusion, a section called "AML and Audit" will summarize the four major takeaways that local banks and foreign banks that are establishing correspondent banking relationships should keep in mind.

It is evident through the research performed that many of these schemes were able to continue for extended periods of time through well-known schemes and methods, such as the use of offshore or well-known tax havens or the three stages of money laundering. This indicates that a continued and thorough review of a financial institution's AML program, locally and abroad, is paramount to tackle corruption.

Background

For foreign banks hoping to establish a local presence or correspondent banking relationships, the size of the South American market, in addition to the geographical proximity and the influence of the 56 million Hispanics in the United States as of 2016,² represents a major opportunity for expansion. Currently, the seven largest banks in South America have USD 2.2 trillion in assets.³ The region's GDPs for 2016 and 2017 were the following:

- 2016: USD 3.6 trillion⁴
- 2017: USD 4 trillion in 2017, an increase of 11%

For comparison, in 2017, the GDP for Africa and Oceania were:

- Africa: USD 2.2 trillion⁵
- Oceania: USD 1.6 trillion⁶

¹ "Leading Banks in Latin America in 2017...", Statista, 2019. See the References section for full hyperlink.

² "How the U.S. Hispanic Population Is Changing," by Antonio Flores, September 18, 2017. See the References section for full hyperlink.

³ "The 10 Largest Latin American Banks." See the References section for full hyperlink.

⁴ "List of South American Countries by GDP," International Monetary Fund. See the References section for full hyperlink.

⁵ "List of African Countries by GDP," International Monetary Fund. See the References section for full hyperlink.

⁶ "List of Oceanic Countries by GDP," International Monetary Fund. See the References section for full hyperlink.

South America is a region that presents challenges for U.S financial institutions as they must tailor their AML programs to account for widespread corruption and increased AML risk. The countries for which corruption scandals have been selected (i.e., Argentina, Brazil, Colombia, and Venezuela) have all experienced a decrease in the AML risk ratings from 2017 to 2018,⁷ thanks in part to increased government enforcement and creation of tighter anti-money laundering regulations.⁸

According to Moody's, the risk of corruption remains a risk to the credit rating for the majority of Latin American countries.⁹ According to Transparency International,¹⁰ 53% of those surveyed feel that their governments do a bad job at tackling corruption; the percentage within the countries reviewed in this whitepaper are the following:

- Venezuela: 76%
- Colombia: 59%
- Brazil: 56%
- Argentina: 42%

As anti-money laundering regulations continue to be enforced, and attitudes change towards corruption in the region, South American societies will hopefully be able to enjoy safer societies with better investments in basic services and an increase in foreign investment.¹¹ Corruption and its AML impact can simply be summarized as "systematic corruption impedes a developing economy from reaching potential development goals."

Multinational Scandals

Odebrecht S.A.

Odebrecht S.A is a multinational construction company founded in Brazil in 1944. As per its most recent annual report of 2017–2018, the company reported revenues of USD 18.5 billion, have 58,000 employees, and is present in 14 countries.¹² Before the scandal, Odebrecht had 180,000 employees and reported revenues over USD 40 Billion.¹³ On December 21, 2016, the U.S. Department of Justice (DOJ) released a statement in which Odebrecht, along with a Brazilian petrochemical company (Braskem S.A.), pled guilty to one count of violating the anti-bribery provisions of the Foreign Corrupt Practices Act (FCPA). These companies agreed to pay at least USD 3.5 billion in global penalties after admitting they had paid upwards of USD 788 million in bribes across various countries in Latin America.¹⁴ This scheme is

⁷ "Basel AML Index...", International Centre for Asset Recovery. See the References section for full hyperlink.

⁸ "Anti-Money Laundering in Latin America," *Financier Worldwide*, February 2012. See the References section for full hyperlink.

⁹ "5 escándalos de corrupción que ensombrecen a América Latina," *AltoNivel*, May 18, 2017. See the References section for full hyperlink.

¹⁰ *People and Corruption: Latin America and the Caribbean*, by Coralie Pring, October 9, 2017, Transparency International. See the References section for full hyperlink.

¹¹ "Effects of Corruption on the Economy of Latin America," by Megan Prenatt, April 19, 2018, *Panoramas*, University of Pittsburgh. See the References section for full hyperlink.

¹² *2018 Annual Report*, Odebrecht, S.A. See the References section for full hyperlink.

¹³ "Odebrecht Case: Politicians Worldwide Suspected in Bribery Scandal," *BBC News*, December 15, 2017. See the References section for full hyperlink.

¹⁴ "Global Implications of the Odebrecht Corruption Scandal," *A2 Global Risk*. See the References section for full hyperlink.

considered the largest foreign bribery case in history.¹⁵ It is important to note that the U.S. DOJ indictment is the first of many: 11 attorneys general in other countries, including nine from Latin American countries agreed to cooperate and handed down indictments in their respective countries with disastrous consequences to the firm itself and politics in South America.

Which countries are linked to the Odebrecht scandal?

Spread of Odebrecht scandal



Total bribes paid by Odebrecht (\$USm)

Admitted		Alleged	
Brazil	\$349m	Antigua	\$10.5m
Venezuela	\$98m	El Salvador	
Dominican Republic	\$92m		
Panama	\$59m		
Angola	\$50m		
Argentina	\$35m		
Ecuador	\$33.5m		
Peru	\$29m		
Guatemala	\$18m		
Colombia*	\$11m		
Mexico	\$10m		
Mozambique	\$1m		

*Colombia - a further \$16m is alleged by prosecutor

Source: US Department of Justice, El País, La Prensa Gráfica, Brasília declaration of judicial co-operation, signed by prosecutors



Odebrecht utilized common methods of money laundering such as shell companies that utilized offshore bank accounts. What made this scheme unique was that senior members of the firm and various co-conspirators created a division within the company, the division of structured operations, to conceal their activities and have them off of Odebrecht's financial statements. Members of this group created a separate system that allowed those of the division to communicate with co-conspirators outside of the organization through the use of e-mails and instant messages. All messages were codified with the use of code names and passwords. In addition, the divisional structure operations used a shadow budget for these operations. These operations were hard to track through Odebrecht financial statements, given

¹⁵ "Odebrecht and Braskem Plead Guilty and Agree to Pay at Least \$3.5 Billion in Global Penalties to Resolve Largest Foreign Bribery Case in History," Office of Public Affairs, December 21, 2016, U.S. Department of Justice. See the References section for full hyperlink.

that transfers were performed with offshore entities that were not included in its balance sheet. Payments were distributed primarily to foreign government officials and other senior political members. The bribes would reach them after the funds were layered by passing through as many as four bank accounts in various countries.

A related company, Braskem, was also involved in this operation; through that company there is a connection between Odebrecht S.A. and Brazil's Operation Car Wash, which is further explained in the next section. Braskem's, a petrochemical company, along with Petrobras, Brazil's state-controlled oil firm, political parties, and various politicians, were ultimately able to receive government concessions including:

- favorable legislation that allowed them to reduce their tax liabilities,
- preferential prices for raw materials, and
- construction contracts with Petrobras.

These bribes helped Odebrecht secure contracts throughout all of Latin America with minimal oversight. The local population and companies were greatly affected as major projects did not go through a fair bidding process, and the final contract would have its value inflated to ensure additional profits for the firm.

Ramifications of this scandal have been massive for the region and the firm. In addition to the fines by the U.S. Department of Justice and ongoing investigations in other countries, the CEO, Marcelo Odebrecht, was sentenced in 2017 to a 19-year sentence, and 76 other executives in the firm have signed plea deals in which they will provide further information in hopes of reduced sentences.¹⁶ At one point, a third of Brazil's government ministers faced investigations as a result. The following list describes some of the effects of this corruption scandal in other countries in the region:

- **Ecuador:** Jorge Glad, the country's vice president, was sentenced to six years in prison in December 2017 for accepting USD 13.5 million in bribes.
- **Peru:** Three prominent politicians in the country have been implicated in this scandal. Former president Alejandro Toledo is accused of taking USD 20 million in bribes and is currently at large. Ex-president Ollanta Humala was placed on pretrial detention for accepting bribes that were utilized for his presidential campaigns in both 2006 and 2011. The daughter of former President Alberto Fujimori, Keiko Fujimori, has been implicated in the scandal as well, due to notes on Marcelo Odebrecht's phone.
- **Colombia:** The presidential campaign of Ex-president Juan Manuel Santos, a Nobel Peace prize winner, is alleged to have been funded in part through various bribes by Odebrecht. This allegation was made by the finance chairman of his campaign.
- **Venezuela:** The former chief prosecutor, Luis Ortega, who is currently in exile, accused the current president and vice president (Nicolas Maduro and Diosdado Cabello respectively) of receiving USD 100 million in bribes. In recent developments, unfinished projects and assets of the firm have been nationalized.
- **Chile:** An anti-corruption investigation has started with the raiding of the company's offices.

¹⁶ "Odebrecht, el mayor escándalo de corrupción de América Latina," AmericaTV, February 23, 2017. See the References section for full hyperlink.

- **Countries outside South America:** The Dominican Republic, Mexico, and Panama have had corruption scandals linked to Odebrecht. Another 29 countries have requested assistance from Brazil for their own investigation on the firm.

This scandal is still ongoing but shows the importance of a financial institution performing appropriate due diligence on multinational companies. These companies, especially those that utilize offshore companies, should receive high-risk scoring so they undergo annual renewal and review of the client's know-your-customer (KYC) file on record.

National Scandals

Brazil: Petróleo Brasileiro S.A., PetroBras, and Operação Lava Jato (Operation Car Wash)

The aforementioned Odebrecht scandal was discovered as a result of Operation Car Wash in Brazil, a scandal that at the time was considered the worst corruption scandal in Brazil's history.¹⁷ The scandal, uncovered in March of 2014, started with the investigation of auto repair shops, gas stations, and car washes in Brasilia and São Paulo. It is alleged that the illegal scheme had been running for upwards of 10 years. News reports indicate that between 2004 and 2005, USD 2 billion were paid in bribes to politicians and business associates, who would, in turn, launder the funds into foreign accounts.¹⁸

The scheme worked by funneling illegal funds through cash-intensive businesses (auto repair shops, gas stations, and car washes) and reporting said funds as earnings of the firm. In effect, the laundered cash was distributed to top executives in Petrobras, politicians at all levels of the government, and heads of criminal organizations.

When PetroBras, Brazil's semipublic petroleum company and the largest of its kind in Latin America, had an upcoming construction project, they would open said project's construction up to bidding. The purpose of this process is to lower the price of construction and make the process open to the public with full transparency. Major construction and engineering firms in Brazil circumvented this process by forming a construction cartel in which they did not compete with each other but, instead, rotated the construction contracts. The firm that received the bid overcharged PetroBras, resulting in billions of dollars in profits for the winning construction firm but also billions in bribes to those involved in the scheme. For example, the Comperj refinery in Itaboraí was slated to originally cost USD 6 billion, but PetroBras paid Odebrecht USD 15 billion by 2015.¹⁹ Odebrecht laundered some of the proceeds through outside businesses, as mentioned in the previous section, before paying bribes to members of PetroBras, the criminals who laundered the funds, and politicians across all levels of the Government.

The scheme became a cycle of corruption and overpriced contract. Petrobras executives would provide construction contracts only to the cartel members. Those companies in turn would take turns submitting a winning bid, in exchange for bribes. Politicians in turn, would accept bribes in exchange for influence in Petrobras itself, one of the largest companies in Brazil, a company that could bring thousands of jobs to

¹⁷ "¿Cuál es la relación entre "Lava Jato" y el escándalo de Odebrecht?," Diario Las Americas, April 12, 2017. See the References section for full hyperlink.

¹⁸ "Corrupción en América Latina: La plaga que se expande," Telesur TV, December 9, 2017. See the References section for full hyperlink.

¹⁹ "The Biggest corruption scandal in Latin America's History," Vox Atlas, October 26, 2018, You Tube. See the References section for full hyperlink.

a region through a new construction project. The bribes helped secure re-election or the rise of political figures that could potentially help secure these new construction projects in the future.

The scandal started in March of 2013 when a banker and known money launderer, Alberto Youssef, gifted a Range Rover to Roberto da Costa, an ex-director of Petrobras. Authorities immediately questioned why a banker would gift such an expensive vehicle to a Petrobras executive? Two days after receiving the vehicle, Da Costa was arrested by authorities after they discovered he was destroying evidence with regards to his relationship with Albert Youssef. After this arrest, the initial phase of the operation resulted in the asset forfeiture of USD 5 million in cash, 25 vehicles, cell phones, jewelry, works of art, and, more importantly, 80,000 documents that helped provide a clearer picture to investigators.²⁰ In August 2014, feeling the weight of a major prison sentence, Da Costa and Youssef decided to cooperate with authorities in exchange for a reduced sentence. Ominously, Youssef told prosecutors, "If I speak, the republic is going to fall."²¹

Around the same time in March 2014, Brazil's Financial Intelligence Unit, operating under the country's Finance Ministry authority, identified suspicious transactions that involved both Petrobras and the largest member of the construction cartel, Odebrecht S.A. As of October 2018, this anti-corruption operation has "... resulted in more than two hundred convictions for crimes, including corruption, abuse of the international financial system, drug trafficking, and money laundering."²²

This scandal has had social, political, and economic consequences that are still resonating throughout Brazil. Recently, it played a role in the election of the current Brazilian president, Jair Bolsonaro, who ran a far-right campaign that promised the Brazilian electorate that he would be a hardliner as it relates to crime and corruption in the country.²³ Evidence of this is the rise of Judge Sergio Moro to a cabinet post in the new Brazilian government, at the helm of the Justice Ministry. This is the judge who famously sentenced the former president of Brazil and member of the opposition party, Luiz Inácio Lula da Silva, better known as Lula, to 10 years in prison for corruption and money laundering charges. The charges stem from receiving USD 1.1 million to renovate a beachfront apartment; in exchange, the construction company received lucrative contracts from Petrobras.²⁴

Lula's successor, Dilma Rousseff, would ultimately be impeached in 2016, be removed from office, and replaced by Michel Temer, both of whom were accused by Marcelo Odebrecht of receiving USD 48 million in illegal campaign contributions.²⁵ He would ultimately be cleared by a panel of judges determining that he had not violated campaign finance laws.²⁶ In addition to potential campaign violation laws, Rousseff's political downfall as a result of Operation Car Wash centers around her intention to include Lula in her cabinet and, thus, providing him immunity. During this process, Judge

²⁰ "Lava Jato: El arresto que cambió un continente para siempre," by Rodrigo Cruz, August 3, 2017, *El Comercio*. See the References section for full hyperlink.

²¹ "Brazil's Petrobras scandal, explained," by Zack Beauchamp, March 18, 2016, *Vox*. See the References section for full hyperlink.

²² *Brazil's Corruption Fallout*, by Claire Felter and Rocio Cara Labrador, November 7, 2018, Council of Foreign Relations. See the References section for full hyperlink.

²³ "Brazil's new far-right president had an alarming first week," by Jen Kirby, January 8, 2019, *Vox*. See the References section for full hyperlink.

²⁴ "Ex-President of Brazil sentenced to nearly 10 years in Prison for Corruption," by Ernesto Londoño, July 12, 2017, *The New York Times*. See the References section for full hyperlink.

²⁵ "Brazil Corruption Scandals: All you need to know," BBC News, April 8, 2018. See the References section for full hyperlink.

²⁶ "Court in Brazil Clears President Michel Temer in Campaign Finance Case," by Simon Romero and Dom Phillips, June 9, 2017, *The New York Times*. See the References section for full hyperlink.

Sergio Moro released a wiretapped conversation between Lula and Rousseff that mentioned the use of the political post in a bid to receive legislative immunity and, thus, avoid criminal prosecution for Lula. The graphic below summarizes the political ramifications of Operation Car Wash so far.



As Brazil continues to grapple with the widespread corruption within its political and economic system, these new investigations and operations have started as a direct or indirect result of Operation Car Wash:

- **Operation Weak Flesh:** Investigation into JBS and BRF, the world’s largest beef and poultry exporters respectively, accused of bribing health and safety officials to approve the sale of spoiled meat products. It is alleged that USD 600 million was paid out to 1,829 politicians.
- **Operation Panatenaico:** Investigation into potential bribes paid by construction companies to secure stadium construction contracts for the World Cup.
- **Operation Greenfield:** Investigation into fraud related to the pension funds of state-run corporations.
- **Operation Zelotes:** Investigation into bribes by various companies, including JBS (the world’s largest meat processing company) and Ford to tax officials in order to reduce their tax liabilities.

Venezuela: Petróleos de Venezuela S.A., PdVSA (Petroleum of Venezuela)

Any recent story involving Venezuela must take into consideration the economic and social deterioration of the country. The country is in the middle of a humanitarian crisis and an economic death spiral of high unemployment and hyperinflation, estimated to be at 1,000,000% as of 2018.²⁸ Given the economic crisis, access to foreign currency is restricted. The dollar is traded at both an official rate and black-market rate; both rates diverge wildly and present opportunities for those in government

²⁷ “The Biggest corruption scandal in Latin America’s History,” Vox, October 26, 2018, You Tube. See the References section for full hyperlink.

²⁸ “IMF projects Venezuela inflation will hit 1,000,000 percent in 2018,” Reuters, July 23, 2018. See the References section for full hyperlink.

positions to abuse. In 2017, the Financial Crimes Enforcement Network (FinCEN) issued an advisory to “alert financial institutions of widespread public corruption in Venezuela and the methods Venezuelan senior political figures (and their associates and front persons) may use to move and hide corruption proceeds.” The advisory warned about potentially suspicious activity from Venezuelan government officials occurring specifically within the United States in South Florida and Texas.²⁹

The FinCEN advisory implicated the country’s vice president at the time, Tareck El Aissami, and others of corruption and criminal activity. Part of these illicit activities included activities related to the state-owned PdVSA. In August of 2017, President Trump issued Executive Order (E.O.) 13808, which imposed additional sanctions related to PdVSA, the E.O. prohibited certain debt, equity, profit, and dividend disbursement activities. Subsequently, the president of Venezuela, Nicolas Maduro, ordered an investigation and restructuring of PdVSA. The investigation was ordered due to alleged losses due to corruption estimated at USD 17 billion in local currency over the span of six years, between 2011 through 2017.³⁰ As a result, 60 people in the government and PdVSA have been arrested.

The corruption in PdVSA continued to unfold in 2018 when U.S. authorities arrested two suspects in Miami for their involvement in a criminal case regarding money laundering USD 1.2 billion of funds from the oil company. The report alleged that the differences between the official and black-market exchange rates were used by corrupt officials and executives to launder illegal funds. The activity in question took place between December 2014 and May 2015, utilizing two businesses based in the United States. The article states that “these companies loaned PdVSA 7.2 billion bolívares utilizing the black-market rate at the time. When the loans were repaid at the official exchange rate it would be 14 times higher, a total of 102 billion bolívares. This converted to 512 million Euros from the initial loan principals of 36 million euros, which were sent to the suspects in 10 separate transfers.”³¹

Laundering of the funds took place using the three stages of money laundering. First, placement of the funds took place by sending the funds to well-known tax havens and European countries. Within the United States, some of the companies that assisted with this scheme were registered in Delaware, Florida, and New York.³² Second, layering of the illegal proceeds continued as funds were utilized in various investments, further hiding the original proceeds of the funds. The final and third step, integration, took place by using the funds to purchase real estate.

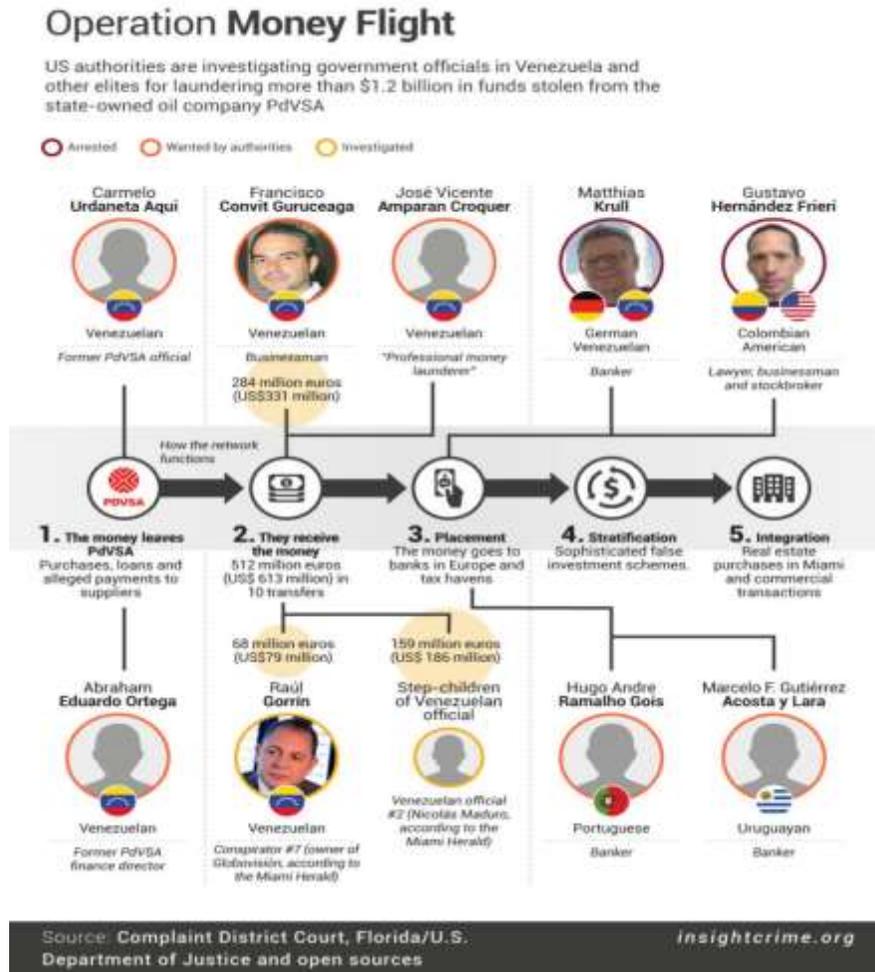
²⁹ “Advisory to Financial Institutions on Widespread Political Corruption in Venezuela,” Financial Crimes Enforcement Network, September 20, 2017. See the References section for full hyperlink.

³⁰ “Corrupción en América Latina: La plaga que se expande,” TeleSur, December 9, 2017. See the References section for full hyperlink.

³¹ “Weekly InSight: Corruption, Money Laundering and Bribery at Venezuela’s PdVSA,” InSight Crime, August 3, 2018. See the References section for full hyperlink.

³² “Treasury Targets Venezuela Currency Exchange Network Scheme Generating Billions of Dollars for Corrupt Regime Insiders,” U.S. Department of the Treasury, January 8, 2019. See the References section for full hyperlink.

The graphic, Operation Money Flight, provides a visual on how the operation worked and those implicated in the operation:



This scandal is also marked by the involvement of PdVSA and construction projects with Odebrecht. In Venezuela, the construction firm was involved in 23 projects that would ultimately be halted and nationalized.³³ Business with Venezuela in general is becoming more difficult for countries, companies, and banks. The FUI unit of Argentina announced on January 18, 2019, a red alert to their local banking institutions against working with Venezuela. This alert was disseminated to banks, car dealerships, public accountants, currency exchange offices, casinos, and other industries as part of Article 20 of local Argentinian Law 25.246. The alert warns against performing business with, by name, the current president, Nicolas Maduro, the vice-president, Delcy Rodriguez, the president of the National Assembly, Diosdado Cabello, among others.³⁴ This is in addition to the implementation of U.S. sanctions against 7 individuals and 23 businesses noted in the press release as per E.O. 13850.³⁵

³³ "The Biggest corruption scandal in Latin America's History," Vox Atlas, October 26, 2018, You Tube. See the References section for full hyperlink.

³⁴ "La UIF emitió una "alerta roja" a bancos y financieras para evitar negocios con Venezuela," iProfessional, January 18, 2019. See the References section for full hyperlink.

³⁵ "Treasury Targets Venezuela Currency Exchange Network Scheme Generating Billions of Dollars for Corrupt Regime Insiders," U.S. Department of the Treasury, January 8, 2019. See the References section for full hyperlink.

Colombia: Refinería de Cartagena, Reficar (Refinery of Cartagena)

Refinery of Cartagena is a subsidiary of EcoPetrol, Colombia's petrochemical company, which was established in 1957.³⁶ The refinery is located in the industrial sector of Cartagena on the country's Caribbean coast. When founded, the refinery had a capacity of 26,300 barrels per day, supplying most of the energy needs of the north and west of Colombia. In November of 2007, a construction and engineering company specializing in the petrochemical industry, Chicago Bridge & Iron (CB&I), which also merged with McDermott, was awarded the primary contract that would allow the increased production of the refinery by an additional 165,000 barrels per day. At this point, due to subsequent expansions and advances in technology, the refinery was producing 80,000 barrels per day.³⁷

Work started on the project in 2007 and was scheduled for delivery for 2012. The project was finally delivered in 2015. The project was meant to cost USD 3.993 billion, but the final tally was a total of USD 8.016 billion, which was double the initial quoted amount.³⁸ The scandal was uncovered after Colombia's attorney general's office published a report in which the various misdeeds that occurred during the project's construction were listed. The report placed blame on two Colombian presidencies, those of Alvaro Uribe and Juan Manuel Santos, in addition to the over-charging by CB&I.³⁹ CB&I submitted bills for labor and materials multiple times, purchased incorrect materials, and awarded a total of 2,460 subcontracts. Many of these contracts resulted in subpar quality or some work not being completed at all. One of the more scandalous items in report alleged that USD 16 million of Colombian tax funds were used by Reficar executives on parties, alcohol, and prostitutes.⁴⁰ This has been considered the largest discovered case of corruption in Colombia.

The contract established with Reficar was called a Cost Reimbursable Contract, a contract in which "...the contractor is reimbursed the costs they incur carrying out the work. The price is not defined at the outset, but at the end of the project."⁴¹ These types of contracts are ripe for corruption and embezzlement as the contractor can bill for nonexistent work, delay progress of completed works, etc. Allegations of corruption were also compounded by the transition of government that occurred in the country, from Alvaro Uribe to Juan Manuel Santos in 2010. One Colombian senator stated, "the ministers and members of the boards of Reficar and Ecopetrol knew what CB&I were doing and did not denounce it."⁴²

In 2018, Colombia's attorney general's office started the trial of those arrested in connection to this scandal:

³⁶ "Refinería Cartagena," EcoPetrol, 2018. See the References section for full hyperlink.

³⁷ "Refinería de Cartagena S.A. (REFICAR) Expansion," McDermott, 2016. See the References section for full hyperlink.

³⁸ "Guía para entender el robo al estado en Reficar," El Pais, February 3, 2016. See the References section for full hyperlink.

³⁹ TeleSur TV, "5 casos recientes de corrupción en Colombia", See the References section for full hyperlink. (August 25, 2018).

⁴⁰ "Colombian Corruption: How 7 Scandals Have Rocked a Nation and Eroded Faith in Justice," by Mark Kennedy, December 7, 2017, LinkedIn. See the References section for full hyperlink.

⁴¹ "Reficar: Colombia's 'biggest corruption scandal in history' good for a \$16M prostitution bill," by Thomas Graham, May 5, 2016, *Columbia Reports*. See the References section for full hyperlink.

⁴² "Reficar: Colombia's 'biggest corruption scandal in history' good for a \$16M prostitution bill," by Thomas Graham, May 5, 2016, *Columbia Reports*. See the References section for full hyperlink.

- Masoud Deidehban, previous project director for CB&I, a dual Irani and U.S. citizen who remains outside of Colombia and has yet to be extradited back
- Orlando Jose Cabrales, both ex-minister of mines and ex-president of Ecopetrol
- Pedro Rosales Navarro, ex-executive vice president of Downstream for Ecopetrol
- Carlos Alberto Lloreda, ex-auditor of Reficar
- Philip Kent Asherman, ex-legal representative of CB&I during the project's construction
- Reyes Reynoso Yañez, president of Reficar from 2012 through 2016
- Felipe Arturo Laverde Concha, ex-vice-president, Legal⁴³

It is important to note that Colombia is a country which Basel has lately reduced the AML risk of the country due to an increase of AML laws in the country; any charges related to money laundering can result of upwards of 64 charges according to Article 323 of the penal code.⁴⁴ This is indicative of the pervasiveness of corruption not in only in Colombia but in the region, and how a robust AML legal framework is not indicative of diminished AML risk.

Argentina: Los Cuadernos de la Corrupción (The Notebooks of Corruption)

Argentines were shocked at the revelations discovered in August 2018 in notebooks kept by the chauffeur of Ex-minister Julio De Vido, Roberto Barrata, and other politicians.⁴⁵ The chauffeur had kept a meticulous record in schoolbooks of bribes that took place over a period of 10 years (2005 through 2015).⁴⁶ This scandal has become known as the Notebooks of Corruption; the Spanish newspaper *El Diario* and Argentinian Judge Claudio Bonadio⁴⁷ received a total of eight notebooks broken down by the following dates:

- Number 1: February 2 through October 16, 2005
- Number 2: October 17, 2005, through June 29, 2006
- Number 3: July 1, 2006, through January 11, 2008
- Number 4: January 26, 2008, through April 12, 2009
- Number 5: April 13, 2009, through May 13, 2010
- Number 6: May 14 through December 21, 2010
- Number 7: May 6 through October 31, 2013
- Number 8: June 2 through October 22, 2015

Information on the contents of the notebooks was not published until information in the notebooks could be corroborated. The contents of the notebooks are listed in the entirety, freely accessible, and hosted by the Argentinian newspaper *La Nación*.⁴⁸ The notebooks are filled with notes documenting

⁴³ "Juez ordena detener a exdirector de CB&I por el desfalco de Reficar," *El Tiempo*, January 17, 2018. See the References section for full hyperlink.

⁴⁴ "Lavado de Activos," Unidad de Información y Analisis Financiero, Republica de Colombia, November 26, 2018. See the References section for full hyperlink.

⁴⁵ "Grandes escándalos de corrupción marcan a los países de América Latina," *El Universal*, August 13, 2018. See the References section for full hyperlink.

⁴⁶ "Las claves de los 'cuadernos de la corrupción' en Argentina: El caso perjudica a Cristina Kirchner y también a Mauricio Macri," by Cristina Pozo Garcia, August 8, 2018, *Eldiario.es*. See the References section for full hyperlink.

⁴⁷ "La 'causa de los cuadernos' un viaje al corazón de la corrupción en Argentina," by Federico Rivas Molina, August 19, 2018, *El Pais*. See the References section for full hyperlink.

⁴⁸ "Los Cuadernos de las Coimas," *La Nacion*, 2018. See <https://www.lanacion.com.ar/2159636-los-cuadernos-de-las-coimas-hojea-los-cuadernos-como-si-los-tuvieras-en-tus-manos>

hundreds of trips with bags filled with cash and alleged bribes from construction companies to secure government construction contracts. The scheme is alleged to have funneled approximately USD 160 million from various construction companies to various politicians in the country, primarily the two ex-presidents and Nestor and Cristina Kirchner, a married couple. The scheme was set up as follows:

- Bribes were paid by construction firms that held state construction contracts. According to the Judge Claudio Bonadio, the amount ranged from 10% to 20% of the initial value of the secured contracts.
- Bribes were transported by the driver, Oscar Centeno, to his boss, Roberto Baratta, the coordination secretary for the Ministry of Planification.
- Funds ultimately passed to the minister of Federal Planification, Julio de Vido, the person alleged to be responsible for controlling the fund collecting all bribes.
- Funds flowed through Julio de Vido and Daniel Muñoz, the private presidential secretary to Nestor and Cristina Kirchner.
- Nestor Kirchner ran this alleged corruption ring until his passing in 2010, at which point his wife took over this scheme. It was confirmed with persons close to the case that the funds were used during Kirchner's electoral campaigns.⁴⁹

Within two weeks of this scandal's publication, 14 people were detained by Argentinian law enforcement, 13 people came forward willing to collaborate in exchange for leniency, and 43 received criminal charges. On September 18, 2018, Ex-president Cristina was given a preventative jail sentence, which was not enforced due to her legislative immunity as a result of being an active senator in Argentina. Although she could not be arrested, by law, the investigation is still ongoing, and she could face jail time once she exhausts all legal options including a potential appeal to the country's supreme court.⁵⁰

Legislative Impact

The legislative impact of these corruption scandals has been felt most in the political upheaval and rapid changes that have pervaded many societies in South America as a result of these scandals being made public. Many elections in South America have been marked by allegations of illegal campaign funds, which have resulted in impeachments and possible jail sentences for many politicians. Anti-corruption campaigns and, by extension, money-laundering prevention are quickly becoming a way for politicians to demonstrate to their constituents that they are tough on crime and are fulfilling many of the campaign promises that brought them to power in the first place.

In Argentina, accusations of money laundering from bribes continue to plague Ex-president Cristina Kirchner and her family. On December 21, 2018, two prosecutors, Gerardo Pollicita and Ignacio Mahiques, requested that local justices place the Kirchners on trial. This is due to a direct request of the current Argentinian president, Mauricio Marci, who has been in power since December 2015.⁵¹ Given

⁴⁹ "La 'causa de los cuadernos' un viaje al corazón de la corrupción en Argentina," by Federico Rivas Molina, August 19, 2018, *El País*. See the References section for full hyperlink.

⁵⁰ "La Justicia argentina procesa a Cristina Kirchner por los cuadernos de la corrupción," by Mar Centera, September 18, 2018, *El País*. See the References section for full hyperlink.

⁵¹ "Piden juicio oral para Cristina Kirchner y sus hijos por lavado de dinero," RT, December 21, 2018. See the References section for full hyperlink.

the public outrage at the scandal unleashed by the Cuadernos de la Corrupción, the president has continued to crack down on corruption in the government and corruption from previous administrations.

In Brazil, Jair Bolsonaro, an ex-military captain, was sworn in as Brazil's president on January 1, 2019. His election is a direct result of Brazilians being fed up with their government and the pervasive corruption in their society. President Bolsonaro ran on a campaign of anti-corruption, intent on bringing back Brazil's economy from one of its most prolonged periods of recession. His new finance minister has floated the possibility of fully nationalizing units of Petrobras and the power utility Centrais Electricas Brasileiras SA (Electrobras).⁵² The new government is hopeful that the crackdown on corruption in addition to a reduction in taxes can lead to an economic boom that includes gains in infrastructure, a sector of the economy greatly affected by the Odebrecht and Operation Car Wash scandals.

In Colombia, the new government of Ivan Duque, sworn in to the presidency in August 2018, created a commission shortly after his inauguration to fight contraband, money laundering, and tax evasion. In December 2018, the commission stated that they had started to produce results that included the creation of a monitoring center, creation of a specialized unit within both the attorney general's office, and the treasury department, and most importantly, the start of talks with foreign intelligence agencies to secure knowledge and implementation of best practices.⁵³ Most Colombians are seeing the efforts of the current administration to prevent money laundering as one more tool that can help the Colombian government maintain the peace that was secured with the peace deal with the narco-terrorist organization known as Fuerzas Armadas Revolucionarias de Colombia or FARC. Laundered funds continue to be used to sponsor illegal activities, bombings, purchase of real estate, and continued bribery of politicians. For example, during their political careers, Ex-presidents Juan Manuel Santos and Alvaro Uribe have been repeatedly accused of bribery and fraud related to their election campaigns.

Changes in Venezuela related to corruption may not come for a long time, given the current president, Nicolas Maduro who started his new six-year term in January 10, 2019. The current president enjoys limitless power in the country after he dissolved the country's National Assembly by decree of the Supreme Court. The decree states that all powers of the dissolved assembly were to be transferred to the Supreme Court, a governing body that has been "stacked with government loyalists."⁵⁴ As a result of that decree, the country is now under control of the United Socialist Party. Recent developments related to the economic situation in Venezuela include the self-declaration of Juan Guaidó, the president of Venezuela's dissolved National Assembly, as interim president. Since this declaration on January 23, 2019, he has been recognized as the country's legitimate president by the United States and the European Union.⁵⁵ As of the writing of this white paper, the country's constitutional, humanitarian, and economic crises are ongoing and unresolved.

⁵² "Far-right Bolsonaro rides anti-corruption rage to Brazil presidency," by Anthony Boadle and Gabriel Stargardter, October 27, 2018, Reuters. See the References section for full hyperlink.

⁵³ "Contrabando y lavado de activos: ¿Cómo concluye la lucha del gobierno contra estos dos flagelos?," Actualicese, December 27, 2018. See the References section for full hyperlink.

⁵⁴ "Venezuela's high court dissolves National Assembly," by Rafael Romo, March 30, 2017, CNN. See the References section for full hyperlink.

⁵⁵ "Juan Guaidó se juramenta como presidente encargado de Venezuela," by Ana Vanessa Herrero, January 23, 2019, *The New York Times*. See the References section for full hyperlink.

AML and Audit Impact

The AML Audit lessons and guidance that resulted from these five scandals are divided between the local financial institutions and the foreign financial institutions that are considering establishing a correspondent banking relationship with local entities.

Banking With High-Risk and Cash-Intensive Industries

Local Bank: When establishing relationships with high-risk industries such as oil, construction, or nongovernment organizations, local entities should ensure that they understand the purpose of the account and whether it will be used only locally or abroad as well. Audit should verify through testing if there are sufficient policies and procedures to vet new high-risk clients, according to local regulation and the firms' risk appetite. Once the customer is active, periodic reviews should be performed to understand if the activity is in line with the expected activity. Audit should include in annual AML/KYC audits sample testing of new high-risk or prohibited clients. The testing should review the approval process of the client, adherence to onboarding procedures, and appropriate record retention of this information. Finally, Audit must test and verify that risk assessments performed in the year are taking into consideration these new clients like these and ensure that the bank is not operating outside of its risk tolerance.

Foreign Bank: Foreign banks must first ensure that adequate policies and procedures are in place to start a correspondent banking relationship with any local banks. Auditors should test whether these policies and procedures were implemented and properly approved prior to starting any such relationships. Any new client approval should take into consideration the regional risk appetite of the foreign financial institution. The foreign bank must also ensure that the local banks allow audit staff, wherever possible, to have visibility and oversight of processes related to high-risk and cash-intensive clients. The onboarding of local clients who want to use services outside of the jurisdiction must have commensurate approvals documented; this process should undergo reviews in global audits. Audit should implement test steps that review whether these clients submitted for approval the countries they want to work with, and if any are well-known tax havens or offshore banking centers.

Banking With Politically Exposed Persons and Sanctions

Local Bank: Given the high incidences of corruption in the region, a limited number of these accounts should be opened with approvals from the highest levels of Compliance and Management. Audit should test whether the bank has the appropriate monitoring and screening systems for these types of clients. Test steps should also be built in relation to testing access to these systems, given the sensitive information of these clients and the potential reputational risk to the bank. Screening against certain lists, according to the jurisdiction, and ongoing negative news media reviews should be in place and tested on a set frequency. The local audit team should compile a list of corruption or political scandals throughout the year, test whether there was communication between Compliance and Management, and document the result of these conversations.

Foreign Bank: Audit should test the sanctions screening processes in place, specifically the frequency that the client base is testing against these lists and how often the screening lists are refreshed. Sanctions reviews should take into consideration the population of PEPs and any new sanctions established in any country in which there is a correspondent banking relationship with the firm. Similar

to how a local bank should review, if sanctions apply to their jurisdiction and their client, the foreign bank should test whether Compliance and the business address these matters. Testing could potentially review the meeting minutes of AML operating committees (AMLOCs) or any other meetings where the business relationships may be altered if new sanctions are enforced.

Training and Communications With Senior Management

Local Bank: Audit should test whether local training is occurring on a set frequency and is catered to the unique risks and needs of the country in which it is operating. Testing should also determine if this training places emphasis on local AML requirements and provides relevant examples. For example, local AML training in Brazil should take into consideration major local industries such as cattle and oil. Testing should also include verifying that the training materials underwent appropriate approvals, is taken by all requisite staff, and that there are commensurate penalties for not taking this training. Finally, Audit should test whether Compliance and Management discussed any major ad-hoc changes that occurred locally and whether any decision made was performed according to the local bank's risk appetite.

Foreign Bank: Global Audits must review the contracts that are in place with local banks and ensure that training and sharing of training content and results are shared with the foreign bank providing correspondent banking services. Approvals from all the local heads of Compliance and Training must be documented and reviewed. Testing should be performed to ensure that global requirements for testing were adhered to and that any requested changes were integrated to the latest training version. Any major mandates from the foreign bank to the local institutions such as ceasing of a product or service or closure of certain accounts should be tested by Audit to confirm that these orders were implemented.

Record Retention

Local Bank: Testing should determine if record retention requirements for AML-related documentation is in line with local regulatory requirements and is readily available to external auditors. Records in relation to high-risk clients or PEPs should have additional security protocols in place that are tested on a regular basis.

Foreign Bank: Testing should confirm whether the contract with the local financial institution allows for global auditors to have access to local data, either in a remote or local headquarters. The foreign bank should verify whether the local record retention requirement is commensurate with global standards and that the local financial institution is adhering to the stricter requirement.

Conclusion

South America is a region that, separate from the risks highlighted in this white paper, presents a growth opportunity for many local banks and foreign financial institutions that would like to establish correspondent banking relationships there. The goal of this white paper was to highlight through the use of five scandals, the societal, economic, and political effects that they have had on their societies. The goal was not to dissuade financial institutions from investing in the region. On the contrary, the hope is that increased information on the region can help further regional investment and assist companies with implementing adequate controls. Lessons learned can be summarized as follows:

Anti-corruption drive: The region is experiencing an increase of anti-corruption initiatives that should lead to an increase in foreign investment and financial services offerings. Depending on the efficacy of these campaigns, the region can experience GDP growth. The campaigns can also increase the complexity of existing corruption and money laundering schemes. Banks and financial institutions must remain vigilant of governmental accounts, PEPs, and high-risk industries.

Record retention: Firms should maintain stringent record-retention programs to ensure that sufficient documentation is rapidly accessible in case of any future scandals.

Risk assessments: Risk assessment should accurately reflect the risks that the region presents and the risk appetite of the financial institutions. Products and services offered should be in line with assessment's results.

Sanctions: All lines of defense, including Audit, should be aware of sanctioned companies and individuals in the regions in which their financial institutions operate. Efforts should be made across the organization to understand the impact of new sanctions to the financial institution. Ad-hoc updates and potential continuous audit monitoring of high-risk customer files should protect the firm from reputational and regulatory risk.

Training and communications with senior management: Tailored curricula should be developed and disseminated on a regular interval to specific lines of businesses. Training materials should include relevant and timely examples that can help personnel identify potentially suspicious activities that can expose the firms to fines and additional risks.

Transaction monitoring: Typologies within the transaction monitoring system should take into consideration consumer habits of the region. South America is well known for being cash-intensive societies. This may lead to the creation of period account reviews for high-risk accounts; this can help ensure that activity is in line with the customer's profile.

The design of comprehensive AML programs and, more importantly, AML Audit testing that takes into consideration corruption and other unique aspects of South America can allow for the increase of financial institutions in the region. The proper design of these programs can allow for expansion without an outsized increase in risk. Finally, further integration of South America into the U.S. financial system will allow for more stringent review of transactions, increased escalation to the country's financial intelligence unit, and cooperation with U.S. regulators. Even when taking AML risks and corruption into account, investing in a region so close to home can represent a large economic benefit to various financial institutions.

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