POLICY BRIEFS ON LAVA JATO

Backgrounder on Lava Jato

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ABOUT THE PROJECT

Lava Jato or Operation Car Wash refers to Latin America’s largest known corruption scheme in living memory. Related events began unfolding in Brazil in March of 2014. Construction companies were colluding with employees of Brazil’s state-owned oil company to win public works contracts. The oil company’s employees took bribes, while politicians obtained kickbacks as personal gifts or campaign donations.

The relevant scholarship had warned that corruption could result in public works being constructed at inflated costs. However, such warnings were ignored, and so the people involved in the scheme managed to steal billions in state funds. Prosecutors further revealed that bribes paid by the region’s largest construction group extended to eleven other countries besides Brazil.

In spite of the continued interest among policy practitioners and academics, there are key questions about Lava Jato that remain unanswered. For instance, how did the construction company that led the corruption scheme choose the countries in which to do business? According to the international press, the scheme played a role in the 2014 World Cup, but was corruption also at work in the planning and execution of the 2016 Rio Olympics? Also, what is motivating some of the key actors fighting corruption in Brazil, and what can be done to avoid similar corruption scandals in the future?

To answer these and related questions, the Center on Global Economic Governance (CGEG) at Columbia University’s School of International & Public Affairs has collected a series of policy briefs on Lava Jato-related themes. This project is proudly cosponsored by the Center for Development Economics and Policy (CDEP), Columbia Global Center in Rio, and the Latin America Initiative at Rice University’s Baker Institute for Public Policy with the goal of shedding light on a complex problem that has affected the lives of millions.

Lava Jato or “Operation Car Wash” refers to Latin America’s largest known corruption scheme, which investigators in Brazil began to uncover in March of 2014. Prosecutors in the southern city of Curitiba were looking into the activities of black-market money dealers known locally as *doleiros*.¹ These *doleiros* were using gas and car wash stations to launder money, which is how the scandal got its name. As prosecutors deepened their investigation, they were surprised to find that a particular *doleiro* had links to Paulo Roberto Costa, a high-level executive of Brazil’s state-owned oil company Petrobras.²

Thus, what began as a local investigation into money-laundering, found extensive collusion between Petrobras employees and construction companies seeking contracts for public works projects. The oil company’s employees took bribes, while politicians obtained kickbacks. Investigators and prosecutors found that corrupt practices involving Odebrecht, the region’s largest construction group, covered a total of twelve countries—in alphabetical order: Angola, Argentina, Brazil, Colombia, the Dominican Republic, Ecuador, Guatemala, Mexico, Mozambique, Panama,

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² Ibid.
Peru, and Venezuela. Those involved in the scheme managed to steal billions in state funds, resulting in inflated costs for public works projects at the expense of taxpayers.

Some key questions about Lava Jato remain unanswered. Thus, aiming to address some of the gaps in our knowledge, Professor Jan Svejnar and I launched a project that collects a series of policy briefs. The goal is to inform the discussion about corruption, especially as it affects Brazil and Latin America. This document in particular provides background information about Brazilian politics and about the Lava Jato scandal itself.

From Scandal to Scandal

Brazilians have long had to accept corruption scandals as a chronic part of their government. Graft was present under military rule (1964–85), contrary, perhaps, to the beliefs of those who now hope for the return of authoritarianism. Corruption scandals have also plagued every presidential administration since civil order was reestablished in 1985. A congressional

While Luiz Inácio “Lula” da Silva was president (2003-2011), Brazil experienced a number of corruption scandals, including those known as Caixa Dois and Bingos. But the most important scandal was the one called Mensalão, a scheme in which coalition parties accepted large clandestine monthly payments (mensalão) in exchange for their support of Lula’s party, known as the Workers Party or PT. News about these illicit payments broke in 2005 when a legislator publicly accused Lula’s party of bribing its political allies. As The Economist explains:

The money [for the bribes] was said to have come from the public purse via fake advertising contracts signed by state-owned companies with corrupt advertising firms. […] Overlapping congressional inquiries ended up accusing 18 congressmen.

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10 Taylor and Buranelli (2007), 60.
11 Ibid.
of involvement in the vote-buying scheme. The biggest name among them was José Dirceu [...], who had been chief of staff to the president, Luiz Inácio Lula da Silva, until forced by the scandal to step down.\textsuperscript{15}

The Supreme Court eventually took up the \textit{Mensalão} case, but because of the court’s considerable backlog, the trials of more than three dozen politicians did not begin until mid-2012.\textsuperscript{16} In the meantime, the PT won two more presidential elections, the first re-electing Lula, and the second Dilma Rousseff in 2010.

Rousseff is an economist and politician who, in her youth, had been imprisoned and tortured by the military dictatorship.\textsuperscript{17} She began her tenure by firing over five ministers because they were suspected of corruption.\textsuperscript{18} However, these and other actions, such as the enactment of a major government transparency law,\textsuperscript{19} were by 2013 seen as insufficient, as Brazil’s economic

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outlook worsened. Crowds took to the streets to protest corruption, and in particular the billions spent on new football stadiums for the 2014 World Cup, among other issues.

Soon after the demonstrations, Rousseff stood for reelection in 2014; her margin of victory was the narrowest in modern Brazilian history. Against this backdrop of growing economic and political anger and anxiety, the largest corruption scandal in the country’s history unfolded.

### The Petrobras Scandal and Lava Jato

Petróleo Brasileiro S.A., known as Petrobras, is Brazil’s semi-public national oil company. Its contracts run into the billions of dollars annually. Looking to access this treasure trove, over a decade ago Odebrecht S.A. and other Brazilian construction firms colluded to ensure that Petrobras awarded them inflated contracts.

About three percent of the money from the contracts was paid as bribes, mainly to top-level Petrobras employees in order to ensure that the company allotted business to companies in

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the cartel. Politicians got kickbacks in the form of personal gifts and campaign donations. Bribes flowed through a complex network of offshore accounts and black-market financial operators. One of the contracts processed through the shady scheme involved the construction of the Arena Corinthians soccer stadium, a finding that seemed to vindicate the protests that had preceded the World Cup.

The scheme might have continued unhindered, if not for the investigation that became known as Lava Jato or “Operation Car Wash,” run by Brazil’s Ministerio Público Federal (MPF, the Federal Prosecutors’ Office). Federal Prosecutors, along with the Federal Police, the Federal Court of Accounts, and the Office of the Comptroller General, play a central role in the country’s system of accountability. Their agency enjoys significant institutional autonomy to investigate and prosecute corruption.

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In 2014, prosecutors decided to deepen an ongoing investigation when they discovered that a particular doleiro or black-market dealer named Alberto Youssef had given Paulo Roberto Costa of Petrobras a luxury SUV. The arrest of both Youssef and Costa began the process of uncovering an intricate corruption network involving managers, businesses, politicians, and doleiros. Petrobras executives, usually appointed by the political parties in the governing coalition, would share inside information with Brazil's largest contractors, including Odebrecht.

In his plea-bargain testimony, the then-CEO of Odebrecht finally admitted to prosecutors that the construction company had an entire department dedicated to bribery. The department was known as the Division of Structured Operations, and it helped fund the elections of a half-dozen presidents in Latin America. It also helped influence heads of state in Peru and Venezuela, as well as legislators across the region. All told, Structured Operations paid nearly 800 million dollars in bribes so as to secure government contracts worth over three billion dollars in profit for the company.

Now, Federal Prosecutors in Brazil cannot sanction wrongdoers: this is the responsibility of Brazil’s Judiciary. Historically, however, revelations of corruption have not always resulted in

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36 Ibid.
39 Ibid.
40 Ibid.
punishment for the corrupt.41 With Operation Car Wash this changed significantly. Federal and Supreme Court judges have examined extensive evidence, much of it obtained from subpoenaed bank records and from politicians and business people who, arrested on suspicion of corruption, agreed to testify in exchange for leniency. Members of the country’s elite found themselves arrested, charged, and jailed.

Among those sent to prison was Marcelo Odebrecht, the ex-CEO of Latin America’s largest construction group;42 José Dirceu, a former revolutionary who had been Lula’s chief of staff;43 Eduardo Cunha, a conservative politician who was speaker of the lower house of the Brazilian Congress;44 and even former President Lula himself.45

Sergio Moro is the judge who has overseen the Lava Jato prosecution.46 Many have celebrated Moro’s willingness to pursue members of the country’s elite.47 Some have even suggested that his actions will attract investors who prefer countries with reliable institutions.48

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Ribbons in Brazil’s national colors have reportedly been displayed around the courthouse where Moro officiates as an expression of approval.49

But not everyone supports Judge Moro. Some express due-process concerns.50 There are also those who question Moro’s impartiality, by pointing to the investigation’s focus on the PT and other left-leaning political parties.51 However, Moro insists that the prosecutions have simply followed the evidence.52 In fact, the evidence has pulled into court prominent conservative political leaders as well.53 Higher courts have upheld many of his rulings and his use of harsh tactics, such as pre-trial detention of suspects.54

The Impact of the Lava Jato Scandal

There is much controversy surrounding Lava Jato. A delegation representing the Latin American Studies Association (LASA), a professional organization of scholars who study Latin America, argued that the impeachment procedures against then-president Dilma Rousseff

represented an attack against democracy.\textsuperscript{55} Opinion pieces published in \textit{The New York Times}\textsuperscript{56} and \textit{The New Yorker}\textsuperscript{57} have expressed concern that Lula’s recent imprisonment could represent political vendetta. Some see injustice in the way that Rousseff’s unpopular successor, Michel Temer, avoided standing trial on obstruction of justice and corruption charges, by securing support among Brazilian lawmakers.\textsuperscript{58} Temer secured lawmakers’ support by allocating local projects and positions in government, as well by issuing favorable decrees.\textsuperscript{59} Anger about corruption appears to have fueled political support for the presidential candidacy of Jair Bolsonaro, a military veteran and right-wing populist whose disparaging comments against gays, women, and blacks when he was in Congress won him notoriety.\textsuperscript{60}

Notwithstanding such criticisms, the vast majority of Brazilians believe that the Lava Jato investigations should continue.\textsuperscript{61} Even the LASA delegation suggested that the corruption being uncovered by Brazilian investigators was \textit{real and serious}.\textsuperscript{62} Based on the strength of the evidence, the United Stated Department of Justice, in collaboration with Brazilian and Swiss authorities,
imposed a multi-billion dollar fine on Odebrecht.\textsuperscript{63} Eighty percent of that amount will be returned to Brazil.\textsuperscript{64}

Still, in spite of the prosecutorial success of Lava Jato, it remains to be seen whether Brazil will achieve sustained improvements to its level of governance. Lowering the level of corruption is clearly a difficult endeavor that, if achieved, will ensure a better standard of living for Brazilians in general.

In this sense, honest governance is a public good: that one law-abiding citizen enjoys the advantages of an accountable government does not in any way diminish another law-abiding citizen’s ability to enjoy the same benefits. But because honest governance is a public good, a majority of individuals in a society may prefer to free ride on the singular efforts of anticorruption advocates. It follows, then, that moving Brazil to a lower corruption equilibrium requires solving a major collective action problem.

However, achieving collective action to fight corruption is made difficult by the feelings of shared resignation that often follow scandal. Indeed, the unceasing revelations of corruption may make people feel disheartened. Our hope is that, by studying the problem, knowledge will help replace the sense of loss with a new sense of purpose and direction. Brazilians deserve a democratic government that has corruption under control.

\textsuperscript{63} DOJ. "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." Department of Justice, 2016. \(<\text{https://bit.ly/2icnvr5}>\).\textsuperscript{64} Ibid.