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Anti-Corruption Laws & Compliance by Infra Co's

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Anti-corruption prosecutions and the penalties associated with them, have reached new heights in recent months - US$1.7 billion in the first quarter of 2010 in the United States alone[1]. Not only have penalty amounts increased considerably, individual executives are now targeted for criminal punishment with greater frequency[2].

Moreover, the Dodd-Frank Act, the recently-enacted US financial reform legislation, specifically singled out energy and infrastructure companies by requiring the disclosure of royalties, licensing and other payments made by resource extraction issuers to foreign governments in relation to the "commercial development of oil, natural gas or minerals"[3]. The measure requires such companies to exercise an even greater degree of oversight and disclosure than is required under prior law, and has been criticised by industry groups for being anti-competitive[4].

The anti-corruption trend is not limited to the United States. The Organization for Economic Cooperation and Development (OECD) has promulgated an Anti-Bribery Convention that has been adopted by all 32 OECD member states and six non-member states[5].

The UK government recently passed, and is now on the road to implementing, the Bribery Act, which is in some ways more restrictive than US anti-corruption law[6]. In Germany, the number of corruption investigations increased seven fold from 2005 to 2008, from 12 to 88, while prosecutions rose from one to forty-three in the same period[7].

Recent Anti-Corruption Cases

The energy and infrastructure sectors have been especially prone to prosecution by anti-corruption authorities. According to one corporate investigative services firm, 39 per cent of the cases prosecuted under the US Foreign Corrupt Practices Act (FCPA) from 1999 through 2009 were connected to transactions in the energy sector. The infrastructure sector was the second most prevalent in FCPA prosecutions, accounting for 15 per cent of cases[8].

This high-degree of prosecution is connected to the participation of energy and infrastructure firms in activities where there is often a greater corruption risk. Specifically, the execution of complex projects of great value involves significant public-private interaction, often in less

than transparent settings. The broad range of countries covered by the energy and infrastructure sectors increases the number of risks even further.

These special risks are displayed in a number of recent cases. For example, witness the international investigation of bribes paid to public officials by the consortium of multinational energy services firms developing liquefied natural gas facilities on Nigeria's Bonny Island. There, a consortium made up of Kellogg Brown & Root, Inc. (KBR), Technip S.A., Snamprogetti Netherlands BV, and JGC Corporation, allegedly paid bribes to high-ranking Nigerian officials to secure contracts worth about US$6 billion.

In February 2009, KBR pled guilty to violating the FCPA. As part of its plea agreement with the US Department of Justice (US DoJ), in which it agreed to cooperate in the ongoing investigation, it paid a US$402 million criminal penalty and US$177 million in disgorgement of profits. The company's CEO resigned and has been separately prosecuted. Further, the company agreed to install an FCPA compliance monitor for a period of three years. Since the time of KBR's guilty plea, two other consortium partners, Snamprogetti and Technip, have also pled guilty, with fines to date totalling at least US$1.28 billion.

Another case highlighting corruption risk in this space is that of Frederic Bourke, founder of the well-known handbag company Dooney & Bourke. In August 2009, he was convicted of conspiracy to violate the FCPA in connection with his investment in a company seeking to purchase a stake of the state-owned oil company of Azerbaijan, Socar.

Bourke's partner, Viktor Kozeny, was found to have bribed high-level Azerbaijani officials. Despite the fact that the US DoJ did not show that Bourke actually knew of the bribery scheme, the court held that he should have known that Kozeny was bribing foreign officials[9]. Bourke was sentenced to one year and one day in prison, and was ordered to pay US$1 million in fines, in part because, in the words of the sentencing judge, "[such] bribery must and will result in a jail sentence."[10]

Why Are Compliance Programmes Needed?

The elevated legal risk associated with doing business in the energy and infrastructure sectors places special importance on compliance programmes for the companies carrying out these activities. So too do US government efforts to incentivise such programmes.

In prosecuting violations of the FCPA, the US DoJ and the US Securities and Exchange Commission (SEC) consider the presence of compliance programmes, especially in setting the amount of fines that would otherwise have to be paid[11]. These programs are also given credit under the US federal sentencing guidelines, which serve to guide federal judges on the appropriate sentences to hand down[12].

Moreover, the US government routinely penalizes companies for ineffective programs. In recent high-profile anticorruption cases against Daimler, Halliburton, and KBR, the US DoJ cited a lack of oversight and internal controls as aggravating factors in determining the

charges. In the Bourke case, the defendant was held responsible by the court for not carrying out adequate due diligence concerning the identities and activities of business associates.

Consequently, energy and infrastructure firms lacking a coordinated approach to anti-corruption compliance face growing incentives to create and maintain robust compliance programmes.

Key Program Elements

Discussed here are five elements common to such programmes.

Comprehensive Risk Assessment

First, companies must understand the corruption risks associated with the specific countries, regions and industries in which they operate. Studies have shown that the level of corruption in a given area correlates to a range of economic factors[13].

The presence of state-owned entities in the market may also play a role. Cultural factors loom large in settings where significant gestures of generosity bear social significance[14]. Certain industries may be particularly susceptible to improper behaviour on the part of unscrupulous officials, especially those involving large, complex projects and a high degree of host government involvement.

Given the range of variables at play, energy and infrastructure firms would be well-advised to undertake a comprehensive assessment of corruption risk. Such a review should seek to identify at-risk business units, employees, partners, projects, transactions and activities. The results of that review can be used to flag potential problem areas and shape the contours of an effective compliance programme. After an initial review is conducted, ongoing risk assessment mechanisms should be kept in place to identify and track these risks.

Meaningful Due Diligence

Second, effective compliance can only take place if one knows the identities of the relevant players in a transaction: company agents, employees, business partners, and other recipients of funds. Background checks often hold the key, helping to confirm the identity of an individual and to cross-check his or her name against lists of high-risk individuals.

Such checks are particularly important for energy and infrastructure firms making use of foreign representatives to gain access to new markets. While potential representatives are often selected for their connections, these very relationships may give rise to corruption risk if their use for business ends is not controlled and monitored. Background checks should be used to confirm the integrity of all foreign representatives.

Background checks should also be used to ascertain whether any individual receiving funds or benefits can in any way be considered a foreign official under the FCPA or other anti-corruption regimes. In countries where significant portions of the economy are controlled by

the state, status as a "foreign official" for the purposes of the FCPA may not be readily apparent[15].

Written Assurances or Certifications of Compliance

Compliance programmes typically include a requirement that, in business transactions, one or more parties provide written assurances of anti-corruption compliance. In other words, foreign representatives, agents, consultants and business partners should be apprised of the company's anti-corruption compliance policies and should be required to certify that they will not violate these policies.

Companies should also identify those company employees likely to encounter improper solicitation, apprise these employees of company policies and require a similar certification of compliance. All assurances and certifications should be made in writing and documented.

In a similar vein, language stipulating compliance with anti-corruption requirements should be included in contract documentation. Moreover, in public infrastructure projects, contracts between public and private entities should be as clear as possible with respect to the legal and regulatory rules under which the transaction will be structured. Clarity and transparency in public-private dealings can remove the ambiguity that might otherwise obscure improper behaviour. Where appropriate, contracts should allow for termination of the business relationship in the event of breach of any anti-corruption provisions.

Careful Monitoring of Payments

Anti-corruption laws require companies to track payments of money, goods and services. For instance, the FCPA states that listed companies "(A) make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; and (B) devise and maintain a system of internal accounting controls…."[16].

These provisions require attention to and consideration of accounting processes, controls and methodologies. While this requirement applies only to companies that have securities listed with the SEC, the US DoJ has been aggressive in its use of the FCPA, and at-risk companies would be well-served by complying with these provisions.

Furthermore, effective compliance does not stop at accounting; it requires policies that guide, control and monitor payment activities, especially high risk activities such as the use of corporate funds on expenses that may be used to mask improper payments, such as gift, entertainment and hospitality expenses. Oversight should be established over all high risk activities, requiring that all such payments be recorded and accounted for.

As discussed above, energy and infrastructure companies have reason to pay particular attention to payment monitoring, as US regulations are set to tighten due to financial reform legislation.

Senior Management Engagement

Finally - but most importantly - an effective anti-corruption compliance programme results from the active engagement of senior management committed to a culture of compliance. Authorities have affirmed the importance of the "tone at the top" by penalizing companies for lax corporate cultures, and by actively prosecuting senior executives as individuals[17].

For instance, in the case of Siemens AG, where a company-wide and decades-long record of bribing public officials around the world was revealed, the company ultimately paid more than US$1.6 billion in bribery penalties - an amount explicitly tied to the poor "tone at the top" of the company, which had allowed bribery to become "standard operating procedure."[18]

Engagement of senior management can be achieved in various ways, depending on the industry and company. The scope and complexity of most multinational energy and infrastructure businesses - and the heightened corruption risks they encounter - may call for the creation of a separate compliance department and the designation of compliance officers to oversee its activities.

For all companies, executive support for training initiatives will play an important role in achieving anti-corruption goals. Employees will require training in carrying out periodic risk assessments, due diligence, internal monitoring and audits. Likewise, senior executives may themselves need training in setting a tone supportive of compliance and oversight.

Conclusion

Not surprisingly, there is no 'one size fits all' anti-corruption compliance programme. Achieving effective compliance is a serious undertaking that requires a careful and company-specific approach.

For many companies this exercise will not be entirely new. Some firms have taken steps to institute compliance programmes related to anti-money laundering laws (AML). Indeed, AML compliance programmes may provide a blueprint for FCPA programmes[19]. But AML and anti-corruption programmes are not identical, and care should be taken to craft an approach to compliance responsive to the specific regulatory regimes at play[20].

Compliance with anti-corruption laws is a major concern for energy and infrastructure firms and requires time and effort to get right. Still, one thing is clear: there is no turning back the clock on anti-corruption enforcement. Across borders, authorities are waking up to both the costs of corruption on competition and development, and to the financial benefit of rigorous enforcement and hefty fines. Serious anti-corruption laws have become an inescapable 'fact of life' for energy and infrastructure companies. Those companies, now more than ever, have good reason to create and maintain effective compliance programmes.

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NOTES:

[1] Fiona Philip and Sasha Hodge-Wren, "What is Enough FCPA Due Diligence." Bloomberg Law Reports, Vol. 4 No. 20. Available here.

[2] See "But is it right?" The FCPA Blog. July 21, 2010. Available here.

[3] The US Securities and Exchange Commission is expected to issue a final rule no later than 270 days following the passage of the law, which took place on July 21, 2010. See Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. § 922 (2010). Available here.

[4] See Kara Scannell, "Oil Industry Gets Disclosure Jolt." The Wall Street Journal, August 11, 2010. Available here.

[5] See Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, Organization for Economic Cooperation and Development. Available here.

[6] Bribery Act 2010 (c.23). Available here.

[7] Fritz Heimann and Gillian Dell, "2006 TI Progress Report: Enforcement of the OECD Convention on Combating Bribery of Foreign Public Officials." Transparency International, 26 June 2006. Available here.

Fritz Heimann and Gillian Dell, "Progress Report 2009: Enforcement of the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions." Transparency International, 23 June 2009. Available here.

[8] "Where the Bribes Are," Global Fact Gathering. The James Mintz Group, Issue 4. June 2009. Available here.

[9] David Glovin, "Bourke Convicted of Bribery in Kozeny's Azerbaijan Oil Deal." Bloomberg, July 11, 2009. Available here.

[10] Chad Bray, "Bourke Sentenced to One Year in Azerbaijan Bribery Case." The Wall Street Journal, November 10, 2009. Available here.

[11] See The Principles of Federal Prosecution of Business Organization. US Department of Justice. Available here.

See also Exchange Act Release No. 44969. US Securities and Exchange Commission. Available here.

[12] See Chapter 8, US Sentencing Guideline Manual, Corporate Sentencing Provisions.

[13] "Economics and the rule of law: Order in the jungle," The Economist. March 13, 2008. Available here.

[14] F. Joseph Warin, Michael S. Diamant, and Jill M. Pfenning, "FCPA Compliance in China and the Gifts and Hospitality Challenge." Virginia Law & Business Review. Volume 5, Number 1.

[15] For instance, the US DoJ prosecuted AGA Medical Corporation for payments made to physicians at hospitals owned by the Chinese Government. See DOJ Release 08-491, "AGA Medical Corporation Agrees to Pay $2 Million Penalty and Enter Deferred Prosecution Agreement For FCPA Violations." US Department of Justice, June 3, 2008. Available here. See also Warin, Diamant, and Pfenning at 44.

[16] 15U.S.C. §§ 78dd-1, et seq.

[17] See DoJ Release 08-1105, ''Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations and Agree to Pay $450 million in Combined Criminal Fines.'' U.S. Department of Justice, December 15, 2008. Available here.

[18] See DoJ Release 08-1112, ''Transcript of Press Conference Announcing Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations.'' US Department of Justice, December 15, 2009. Available here.

[19] Robert M. Axelrod, "The Foreign Corrupt Practices Act and the Financial Services Industry: Towards Enhancing Compliance." Bloomberg Law Reports, Vol. 2 No. 11. Available here.

[20] See Martin T. Biegelman and Daniel R. Biegelman, "Foreign Corrupt Practices Act: Compliance Handbook." John Wiley & Sons: 2010 at 219.

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