Foreign Corrupt Practices Act – Are Grease Payments Really Allowed? Recent Developments in FCPA Enforcement

Presented by:

S. Lane Tucker, Partner Stoel Rives LLP (907) 263-8411 sltucker@stoel.com

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Foreign Corrupt Practices Act (FCPA)

- Anyone subject to U.S. jurisdiction
 - who, with corrupt intent,
 - makes a payment (or does some act in furtherance of an offer, promise, gift or authorization of the giving of anything of value)
 - to a foreign "official"
 - Directly or
 - Indirectly to anyone while knowing that it will go to foreign official
 - to obtain or retain business . . .
- . . . is liable under the FCPA.



Business Environment FCPA Red Flags

- Highly regulated industry or transaction
- Use of agents or third party intermediaries without formal agreements or use of "success fees"
- Excessive fees or commissions to agents, distributors, other intermediaries
- Subcontractors or consultants adding little value
- Cash payments requested
- Third parties recommending government officials or who are government officials

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Business Environment FCPA Red Flags

- Payments to third countries
- Multiple agents for same scope of work
- Use of shell companies
- Non-transparent or oral contracts
- Political contributions to a potential customer
- Refusal to sign FCPA certification
- Country has a reputation for corruption
- Excessive expenses requested by customer or agent
- Customer recommends the use of agent or subcontractor

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Problematic Regions, Common Schemes

- Deloitte 2009 Survey
 - FCPA issues perceived most likely in
 - Russia
 - China
 - Africa
 - Middle East
 - Most common schemes
 - Subcontractors who do not add value
 - Fraudulent training and travel expenses
 - Payments routed to, from or through foreign countries



FCPA Due Diligence: Know Your Partners, Know Your Subs

- Check publicly available information
- Ask for and check references
- Maintain records of checking and keep them for at least 5 years
- Use formal contracts with clear payments terms and defined SOWs
- Require signed FCPA certifications and include FCPA reps and warranties in contracts



FCPA Due Diligence: Know Your Partners, Know Your Subs

- Have third party contracts approved by legal counsel
- Know the project managers interview them and make sure they are competent
- Make sure third parties have their own code or are familiar with your company's Code of Ethics and Business Conduct
- Conduct, or require third parties to provide evidence of, anti-corruption training
- Retain audit rights in all third party contracts



What About Grease Payments? Case Study 1

- A subcontractor is advised by its prime subcontractor in China that it will need to make a large number of small grease payments (\$50-\$100) to expedite the issuance of visas and licenses
- The subcontractor advises that such payments are technically illegal in China, but permissible under the FCPA and suggests that the payments be accounted for as "visa fines" and "license fees"



The Grease Payment Exception

- The FCPA contains a "facilitation payment" exception:
 - Liability exemption where payments are made "to expedite or to secure the performance of a routine governmental action"
 - All facilitation (grease) payments must be properly accounted for as such



In Practice, the Grease Payment Exception May Be Illusory

- In the aggregate, small grease payments may be deemed to equal one large bribe
 - DynCorp International (2009) \$300,000 in total payments to subcontractors to expedite the issuance of visas and licenses triggered an internal investigation and the termination of top management – probably at U.S. Government request
- Even payments that comply with the FCPA may violate local law
 - China has stepped up internal anti-corruption enforcement

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In Practice, the Grease Payment Exception May Be Illusory

- FCPA accounting provisions still apply
 - Dow Chemical (2007) Failure to record and account for payments that were arguably FCPA-compliant resulted in \$325,000 fine

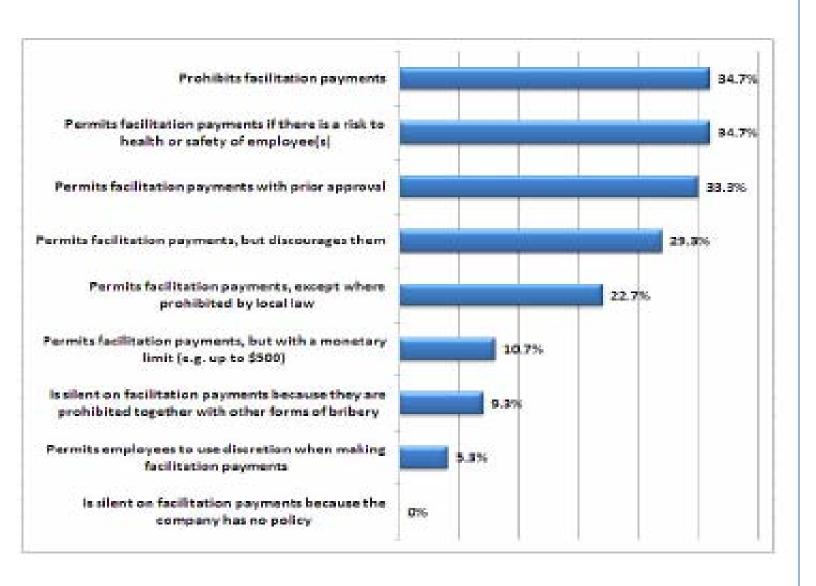


Grease Payments: Common Practice Is Changing

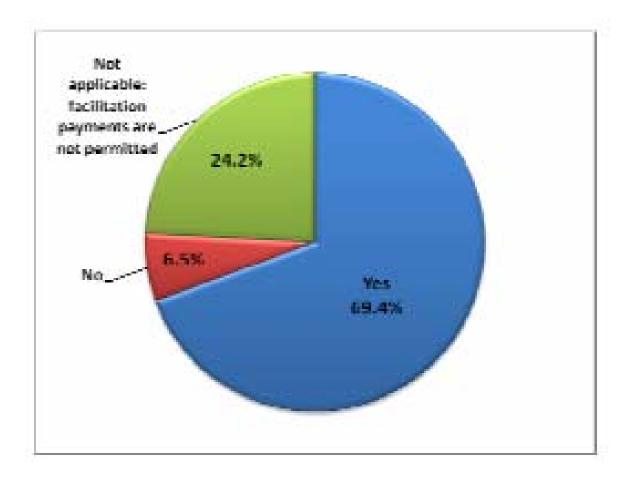
- 80% of U.S. companies have reportedly banned facilitation (grease) payments entirely
- Worldwide, companies are also trending away from permitting grease payments
 - 2009 Trace Survey (see following slides)



Which of the following BEST describes your company's policy with respect to facilitation payments, if any? (please select all that apply)



If your organization permits facilitation payments, with or without approval, does your organization require such payments to be recorded as "facilitation/facilitating payments" in your books and records?



Source: 2009 Trace Survey

Case Study 2 – Extortionate Payments

- Your company, which is operating in Kyrgyzstan, is told by local taxing officials that it must pay \$170,000 in fines for a failure to submit two reports
- The officials threaten that if the fine is not immediately paid that all of the monies in your company's local accounts will be immediately confiscated



Case Study 2 – A Bribe Is a Bribe

- Dimon International (2010)
 - The extortionate nature of the tax audits did not excuse the corrupt payments



Links to additional information:

- http://www.schiffhardin.com/binary/haysholmes_bloomberg_march2010.pdf
- http://www.mwe.com/info/pubs/Foreign_Corr upt_Practices_Act_Compliance_Issues.pdf
- https://www.traceinternational.org/documents/ /FacilitationPaymentsSurveyResults.pdf

