The Energy Business & Bribery Legislation

by

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Introduction

In the 1970s, the SEC undertook investigations that revealed that over 400 US companies had made illegal or questionable payments to foreign government officials, politicians or political parties, totaling over US$300 million.

The reasons for the payments included everything from facilitation payments to make sure that government officials performed certain ministerial or clerical duties, to payments to senior officials to secure favourable government action.

The US Congress saw this as a threat to the integrity of American business and, in 1977 enacted the Foreign Corrupt Practices Act ("FCPA") making such practices subject to criminal and civil enforcement actions.

The FCPA has had a much wider impact than one would originally have thought. It was the beginning of an international trend to increase transparency in international dealings in extractive industries such as oil, gas and mining, particularly with respect to the role that certain payments might play in winning and retaining the right to extract valuable minerals.

The purpose of the these pieces of legislation is stated to be to create a level playing field for international companies, to prevent and punish corruption, and to help developing nations be in a position to distribute the mineral wealth of their countries more evenly.

This paper offers a review of the major pieces of anti-bribery legislation, assesses their impact, and discusses future legislative trends in this area.

US Foreign Corrupt Practices Act

FCPA compliance consists of two key sections. The first comprises the anti-bribery provisions; the second consists of the record-keeping and internal controls provisions.

The anti-bribery provisions make it unlawful for any public company to offer, give, promise, or authorise the giving of anything of value to:

- a foreign official,
- any political party, party official or political candidate,
- any person who is going to pass it to one of the above,

to

- influence his official actions,
- influence that official to do or omit any act in violation of his official duty,
- secure any improper advantage,
- induce the official to influence any act or decision of a governmental entity,

in order to obtain, retain or direct business.

To whom does the FCPA apply?

The FCPA prohibitions apply to payments to any public official regardless of rank.

Generally, the FCPA prohibitions apply to actions by any firm, individual, officer, director, employee or agent of a firm, and any stockholder acting on behalf of a firm. It can also catch anyone who orders, authorises or assists anyone in violating FCPA's prohibitions.

Where does the FCPA apply?

The geographic reach of US jurisdiction under FCPA depends on whether the actor is an "issuer", a "domestic concern", or a non-US national or business.

An "issuer" is anyone who has issued securities registered in the US, or who must file periodic reports with the US SEC.

A "domestic concern" is anyone who is a citizen or resident of the US, any business entity, in any form, that has its principal place of business in the US, or an entity that is organised in US territory.

What activities does the FCPA reach?

FCPA covers all acts furthered through any means of communication that comprise the instrumentalities of interstate commerce.

FPCA prohibits payments made for purposes of obtaining or retaining business. This "business test" is interpreted broadly, and the business in question does not have to be with a government or government-owned entity. It can be with any private business.

The non-US persons reached by the FCPA

In 1998, FCPA was amended to cover any foreign person or business organisation that causes an act in furtherance of a corrupt payment, in US territory.

US parents can also be liable for violations by foreign subsidiaries if they authorise direct or control those activities, as can employees or agents of those subsidiaries.

Joint Ventures

One factor that becomes critical in the face of the bribery prohibitions such as those found in he FPCA, is that one must know joint-venture partners well enough to be confident that they are not going to land a joint project in FCPA hot water.

Improper payments through third parties or intermediaries are prohibited. Such intermediaries can, of-course, be joint-venturers or agents.

In order to avoid being held liable for being involved in illegal payments, companies will need to show that they exercised due diligence by taking all necessary precautions to make sure that they are operating with reputable, and qualified joint-venture partners and agents.

In performing due diligence, a company may wish to consider: investigating potential partners. There are firms that specialise in providing background intelligence on persons and companies in different parts of the world. A company will also have to determine whether their potential business partners or agents have any personal or professional ties to the government which may increase the likelihood of improper payments or other favors being demanded or given. Other due diligence inquires will include finding out who the client clients of potential business partners are, and what sort of reputations those client have.

One source of information about the reputations of the potential partners will be the local US Embassy or consulate. Other sources can include with local bankers, your own clients or associates, if you have any with local knowledge.

When negotiating a business relationship, one should also be aware of certain "red flags" that may appear during the negotiation process. These can include:

- unusual financial arrangements or payment schedules;
- a history of corruption in a particular country;

- a refusal by a potential business associate to sign a declaration that they will not be involved in any corrupt arrangements;
- unusually large commissions;
- lack of backup information to support expense claims;
- poor qualifications in a potential business associate; and
- whether the potential business associate was introduced or recommended by a government official.

FCPA Exemptions

One category of business payments to foreign officials that is permitted under FCPA is “facilitation payments”. These are payments to expedite performance of "routine governmental actions".

The examples FCPA lists of such permissible payments include:

- obtaining licenses, permits, or official documents;
- processing visas and work orders; providing police protection, mail service, phone service, power and water;
- loading or unloading cargo, preserving perishable goods, undertaking contract performance inspections;
- permitting transit of goods; and similar functions.

If one has any doubt as to whether a particular activity falls within this exemption, one should consult counsel, or consider using the DOJ's Opinion Procedure (discussed in more detail, below).

However, keep in mind that any decision by a government official to award or permit continuation of business will never be within this “facilitation payment” exemption.

Affirmative Defences

FCPA does allow for certain defences to be claimed if one is charged with a violation.

One defence that the payment was lawful under the written laws of the country in question.

Another is that the money was spent demonstrating a product or to fulfill a contractual obligation.

But note that because these are "affirmative defences", which means that the burden of establishing that the payments were proper is on the defence. The prosecution does not need to prove, initially, that the payments were not proper.

Sanctions and Enforcement

The FCPA provides both criminal and civil sanctions for violations.

Criminal sanctions against businesses can consist of fine of up to $2 million, with individual penalties for responsible officers, directors, employees, agents and shareholders of up to $100,000 and prison terms of up to five years.

Fines may, under some circumstances, actually be a lot higher than the amounts designated under the FCPA. There is another statute, the Alternative Fines Act, which allows fines to be imposed equal to twice the amount of the financial benefit the defendant hoped to obtain by paying the bribe.

Please note that fines imposed on individuals may not be paid by their employer or principal.

The Department of Justice (“DOJ”) conducts criminal prosecutions; and the Securities Exchange Commission (“SEC”) has created a special unit responsible for civil administrative enforcement. They both maintain FCPA websites.

The DOJ or the SEC may also bring civil actions against companies and persons who violate the FPCA seeking fines of up to $10,000.

In addition the SEC may bring an enforcement action in which the court may impose fines for the greater amount of the gross amount of gain sought by the defendant through the violation, or between $5,000 and $100,000 for an individual, and between $50,000 and $500,000 for a business organisation.

The DOJ or the SEC can also seek injunctive relief requiring a firm to cease any activity that is, or is about to be, a violation of the FCPA.

Perhaps just as seriously, depending on the nature of one's business, any person or firm found guilty of a FCPA violation may be barred from doing business with the US Government. Even an indictment for a violation can result in suspension of government business. Also, under Presidential order, no person or entity can participate in government business if they have previously been barred from such business.

There are also a number of other disadvantages that may be suffered from being found guilty of violating the FCPA:

- a guilty party may be ruled ineligible to receive export licenses;
- the SEC may suspend persons from the securities business and it may impose civil penalties on those in the securities business found guilty of violations;
- the Commodity Futures Trading Commission and the Overseas Private Investment Corporation can suspend or debar persons found guilty of FCPA violations; and
- a payment made to a foreign official in violation of the FCPA cannot be a legitimate tax deduction as a business expense.

In addition to government sanctions, violations of the FCPA can also permit private individuals to bring suits for treble damages under the Racketeer Influenced and Corrupt Organizations Act ("RICO"). Such a claim could be

brought by a competitor alleging that bribery by the defendants unfairly led to the defendants winning a foreign contract.

The FCPA has had a significant impact on American firms doing international business. A number of firms have been the subjects of criminal and civil enforcement actions resulting in sometimes-huge fines and suspension or disbarment from federal procurement contracting. A number of their employees and directors have gone to jail. As a result many international companies have instituted detailed compliance programs to prevent their involvement in any improper payments by employees or agents.

Some examples of FCPA cases against oil and gas companies

FCPA enforcement actions have averaged about 17 cases a year. A number of them have involved oil and gas industry companies. Some examples are:

- 2012: Three oil company executives charged with bribing Nigerian officials to obtain illicit permits for oil rigs
- 20ll: A pipeline company paid $5.4 million to settle charges that it bribed officials in Uzbekistan during an oil and gas pipeline bidding process
- 2011: An energy products manufacturer, paid over $14 million to settle charges that it bribed Chinese officials to obtained business with state-owned entities
- 2010: Seven oil services and freight-forward companies, were charged with widespread bribery of customs officials in more than 10 counties to receive improper benefits.
- A power and automated products company paid $39.3 million to settle charges that it was paying bribes to officials at Mexico's largest power company, and kickbacks to obtain contracts under U.N. Oil for Food Program.
- A former manager of one of the world's largest offshore drilling companies, was charged with authorising bribes to government officials in Venezuela to extend drilling contracts and to obtain other favours.

- 2009: An oil and gas services company, paid $402 million to settle FCPA charges. Their CEO pled guilty to criminal charges, faced years in jail, and personal liability for $10 million.

DOJ Opinion Procedure

The Department of Justice Opinion Procedure has been set up for anyone who has any questions as to application of FCPA with respect to issues such as who constitutes a "public official".

In summary, the Attorney General will issue an opinion in response to a specific inquiry within 30 days of the DOJ's receiving a completed request. If the DOJ issues an opinion stating the proposed conduct conforms with current DOJ enforcement policy, the person receiving the opinion will be entitled to a presumption, in any future enforcement action, that his conduct was permissible under the FCPA. Details of the Opinion Procedure can be found in the Code of Federal regulations (28 CFR Part 80).

To see what kind of opinions have been issued by the DOJ in the past, releases about previous opinions have been made available on the DOJ's FCPA website (http://www.justice.gov/criminal/fraud/fcpa/).

If parties that require further information, both the DOJ and the Department of Commerce will supply additional guidance about the FCPA. Information about how to obtain the guidance can be found on their websites. (see DOJ site, above, and http://www.commerce.gov/category/tags/fcpa).

Response to the FCPA by other countries

The FCPA provoked an enormous outcry from US firms doing international business claiming that the legislation would put US firms at a significant disadvantage when dealing around the world, because they would be competing with foreign firms that were not restrained by the FCPA from paying foreign

bribes, and that such foreign competing firms often were allowed to deduct the payments as business expenses from their taxes.

Congress became concerned that American companies were being disadvantaged compared to their foreign competitors who routinely paid bribes and, in some cases, were permitted to deduct the cost of such bribes as business expenses from their taxes.

Consequently, Congress requested the Executive Branch of government, in 1988, to begin negotiating with the Organization of Economic Corporation and Development (OECD) to get agreements from the US's principal trading partner countries to enact similar legislation. This process took about 10 years, but in 1997 the US and 33 other countries signed an OECD Convention Combating Bribery of Foreign Public Officials in International Business Transactions. Implementing legislation was enacted in the US 1998. However, other countries have taken different lengths of time to implement appropriate legislation of their own to combat foreign bribery involving their business organizations. The anti-corruption trend is now supported by further international cooperative efforts such as the OECD Working Group on Bribery in International Business Transactions (http://www.oecd.org/daf/briberyininternationalbusiness/), and The UN Convention Against Corruption (2003) (http://www.unodc.org/unodc/en/treaties/CAC/).

UK: The Bribery Act 2010

One country that is particularly relevant in the international energy business is the UK. In 2010 the UK enacted The Bribery Act 2010, which came into force on 1 July 2011.

Main points

Key points of the Act are:

- A bribery offence can be active or passive:

    - Active: promising or giving financial or other advantage;
    - Passive: agreeing to receive or accepting a financial or other advantage;
- a business can be liable for failing to prevent a third person from bribing some one on their behalf if that third person is performing business services for the business entity in question;
- it is a defense to Bribery Act violations if a business can show that it put in place adequate procedures to prevent bribery (although putting such procedures in place is not mandatory if there is no risk of bribery of a company's behalf);
- provision of "hospitality" is not a violation of the Act; but,
- in contrast to what is permitted under the US FCPA, "facilitation payments" are bribes under the Bribery Act.

Under the UK That, "bribery" is generally defined as providing someone with a financial or other advantage to encourage that person to act improperly or to reward the person in question for having acting improbably. For example, a business organization could be held liable where an employee or agent pays a bribe to get, keep or gain a business of advantage.

Defense of adequate procedures in place to prevent bribery

However, it is a complete defense to Bribery Act offences if a business organization can show that it had adequate procedures in place to prevent bribery.

What constitutes having "adequate" procedures in place will vary with the nature, size and complexity of the business in question. A small or medium-sized business, facing small bribery risks, will only need to institute minimal procedures.

The Ministry of Justice has published a list of six principles to followed in order to ensure that the business has adopted "adequate procedures" to prevent prosecution under the Bribery Act.

The first principle is "proportionality". The procedures adopted should be proportionate to the risks faced and the size of the business.

The second principle is "top level commitment". Those at the top business organisation need to be committed that their business shall be conducted without bribery.

The third principle is "risk assessment". A reasonable assessment needs to be made of risks a particular business, in a particular market segment, may face.

The fourth principle is “due diligence”. It is important to get sufficient information about potential business partners so that one understands the reputation and backgrounds of the persons one is dealing with. Otherwise, it is difficult to know whether they pose a bribery risk. A firm intending to do international business should ask appropriate questions and perform some relevant checks before joining another firm in business transactions, or retaining an agent to act on their behalf.

The fifth principle is “communication”. Make sure that anti-bribery policies and procedures are adequately made known to employees and others acting on behalf of the business. Depending on the characteristics of one’s business, distributing written statements, getting signed acknowledgements of receipt and understanding, and/or providing additional training might be considered.

The sixth principle is “monitoring and review”. The character of a business and the risks run are likely to change over time. Therefore it is important to establish a policy of periodic reviews and adjustments to a firm's anti-bribery policy, communication and training. This is particularly necessary when entering new markets.

Assessing the level of risk

The Ministry of Justice has been quite clear the amount of effort that a business needs to put into its anti-bribery arrangement depends on the size and nature of the business. If a business is in low risk countries, or market sectors, that may require only minimal anti-bribery precautions.

There are also a number of simple and obvious procedures that can be performed to check the status of companies or persons one hopes to do business with. Internet searches can be a good place to start. Inquiries can also be made at embassies and consulates. UK Trade and Investment can also be consulted (http://www.ukti.gov.uk/uktihome/item/129961.html), and the there may be business, or chamber of commerce type, groups in the relevant countries that can provide information (see Section 3, above).

To be able rely on the defence of adequate procedures, one need only to have procedures in place that are proportionate to the risk.

One needs to consider due diligence only for those that are working for you or on your behalf. Generally, you will not need to perform due diligence on suppliers to you.

Any business is permitted to use its own judgment as to the level of bribery risks it faces. It is not necessary to obtain outside verification (for example, by lawyers or accountants) that the anti-bribery precautions it has taken are adequate.

Hospitality and facilitation

Reasonable business expenditures such as genuine hospitality or promotional activity are not forbidden by the Bribery Act. However, such expenditures have to be at a level that is proportionate for your business. Expenditures that are significantly out of line may be suspected of being a cover for bribery.

Unlike, the US FCPA, the UK Bribery Act considers "facilitation payments", which are payments to induce officials to perform routine functions that they are other wise obligated to perform, to be bribes. There are no exemptions. The only payments of this type permitted are legally required administrative fees or fast-track services. These are not considered “facilitation” payments.

Penalties

The penalties for offences under Act can be as much as 10 years in prison with an unlimited fine.

Jurisdiction

The Act reaches not only crimes committed in the UK, but crimes committed abroad as well.

Application

The Act applies to UK citizens, residents and companies established in the UK, and can apply to a non-UK company that fails to prevent bribery on its behalf, if that company does business in the UK.

Companies can also be liable for bribery committed for their benefit by employees or other associated persons, including third parties acting on a company’s behalf.

Companies can be level for board-level complicity in bribery, and senior directors who turn a blind eye to bribery can be personally liable.

Basic conditions for prosecution

No one can be prosecuted for an offence in England or Wales unless:

- one of the two most senior prosecutors (either the Director of Public Prosecutions or the Director of the Serious Fraud Office) is satisfied that a conviction is more likely than not; and
- the prosecution is in the public interest.

Prosecutions under the Bribery Act

Although the Bribery Act came into effect in 2011, there has only been one prosecution under it, and that had nothing to do with the oil and gas industries. In the spring of 2012, a court clerk in London was convicted under the Bribery Act for helping offenders avoid prosecution for driving offences in exchange for payoffs of up to £500. He was originally sentenced to six years in prison, but that sentence was found to be excessive and was later reduced to two years.

However, one should not be complacent. On 9 October 2012, the Serious Fraud Office issued a press release restating its commitment as an investigator and prosecutor of fraud and corruption including offences under The Bribery Act 2010. In particular the SFO's statement focused on facilitation payments, and business expenditures for hospitality. These press releases emphasised that the SFO considered facilitation payments to be bribes about although hospitality can be considered a legitimate business expense, the SFO takes note of the fact such payments can sometimes be used to disguise bribery. So, although there have been no oil and gas related prosecutions as yet under the Bribery Act, one should not lose sight of the fact that the SFO has this legislation in its sights.

Those who wish further guidance on corruption can consult the Ministry of Justice (http://www.justice.gov.uk/legislation/bribery), and use the tools available on the Business Anti-Corruption Portal (http://www.business-anti-corruption.com/), which provides "corruption profiles" of over 60 countries.

The Ministry of Justice has also published a 45 page guidance booklet on The Bribery Act that is available online, as well as a shorter "Quick Start Guide" also available online (http://www.justice.gov.uk/legislation/bribery).

US Reporting Legislation

Dodd-Frank, section 1504.

One might think that the above legislation provides adequate protection against bribery being conducted by or on behalf of US or UK companies, but apparently the US Congress did not think that this was enough.

In order to make bribery even more difficult, section 1504 of the Dodd-Frank Act was signed into law in July 2010. This law requires oil, gas and mining companies, registered with the SEC, to publicly report how much they pay to governments in connection with natural resource extraction.

Other countries have now enacted similar laws.

Regulations implementing this provision were published on 22 August 2012. Under these regulations, such companies must publicly disclose all taxes, royalties, fees, production entitlements, bonuses, dividends and payments for infrastructure improvements. Fees that must be reported include rental fees, entry fees, and concession fees. Also bonus payments are required to be reported including signature, discovery, and production bonuses.

The threshold for reporting is $100,000. All payments (whether a single payment or series of related payments) over that amount must be reported.

Payments to the US government, all foreign governments and all subnational governmental bodies are included.

These regulations cover above 1100 international oil gas and mining companies including such major companies as Chevron, Exxon, BP, Shell, Rio Tinto, Vale, BHP Billiton, Petrobras, Sinopec and Petrochina.

Lawsuit against the SEC

It would be putting it mildly to say these new reporting regulations upset the natural resources companies. As an indication of their displeasure, the number of trade organizations such as the American Petroleum Institute, the Chamber of Commerce of the US, the Independent Petroleum Association of America and the National Foreign Trade Council launched a lawsuit on October 10, 2012 in the US District Court for the District of Columbia, against the SEC demanding nullification of Dodd-Frank section 1504.

The plaintiffs claim that these disclosure rules will,

> "cost US public companies at least $1 billion in initial compliance costs and 2 to 400,000,000 in ongoing compliance costs and could have billions of dollars of additional costs through the loss of trade secrets and business opportunities."

The lawsuit alleges that the actual costs to US oil, gas and mining companies will be much greater, because US companies will be forced to allow competitors access to sensitive commercial information, and that US companies will have to abandon projects of those foreign countries that forbid such disclosures or that will refuse to do business with US companies because they do not wish such disclosures to be made. The companies claim that it is actually impossible to quantify how many billions of dollars the implementation of these rules will cost.

The plaintiff's grounds for seeking nullification of these rules is that the Commission misinterpreted the rule requirements of section 1504, and it failed to properly consider the impact of these rules.

Is there a decent chance that this suit will be successful under these rules will be overturned? In the opinion of this writer, that is highly unlikely.

It is much more likely that these rules will continue to stand and that a large number of international companies in the mineral extractive industries will be required to disclose their foreign government payments. But the writer admits he can be wrong, so we will see over the next year how this case is resolved.

EU transparency requirements

The EU, inspired by US reporting law, issued draft directives in October 2011, proposing to modify both the existing Transparency and Accounting Directives, to require companies listed on EU stock exchanges and other large companies based in member states to disclose their government payments for oil, gas, timber and minerals by country and by project.

The standards proposed by the EU are similar, in many ways, to the US reporting standards, but there are important differences. The EU directive includes not only publicly held companies but other large private companies as well, whether or not they are publicly held. A "large" company is defined as one which exceeds two of the three following measures:

- turnover, €40 million;
- total assets, €20 million and
- employees, 250.

The EU directive also covers timber as well as oil and gas and minerals.

The EU standards with regard to coverage of oil, gas and minerals do not reach as far as Dodd-Frank. The EU standards cover exploration, discovery, development and extraction of oil, gas and minerals. The US standards cover not only those activities but also cover processing and export of those minerals.

Also, the US rules offer no exemptions to its reporting requirements. The original EU proposal to make an exception for countries where complying with the disclosure requirements is a clear violation of the criminal law of the country concerned. However, the EU proposals noted that there are very few such countries, and that exemption now looks like it will not make it into the final regulations.

On 18 September 2012, a European Parliamentary committee agreed a version of the directive to be sent for negotiation with the European Council Ministers so that a final version of the directive can go to a full European Parliamentary vote sometime towards the end of this year.

The most significant modification of this version is that it deleted the exemption for reporting with regard to payments to governments where the regime has outlawed such reporting.

One of the important purposes of this version was to bring it closer to US regulations so that, as stated by Arlene McCarthy, the Parliamentary Rapporteur on the EU transparency law, Europe would be,

> "on track to create strong global transparency standards, with equivalent rules in the EU and the US."

Conclusions

Anyone operating in the global oil and gas industries out of Europe or the United States, or that is a company subject to registration because it is offering its shares for sale in either US or Europe, or because it is a company doing business in those areas, will need to be aware that may be subject to anti-bribery and/or reporting regulations because of its dealings, with foreign governments or government officials.

Therefore, it should do two things. First, make a good assessment of risks it faces with respect to bribery. This will involve looking both of the countries in which it does business and those will be doing business with or those that will be doing business on its behalf. If the Company determines the some risk of bribery, it should put in place measures to prevent it getting involved in bribery, and introduce training and communication measures to make it clear to which employees of those who does business that will not get involved in bribery. Second, it will need to establish what it's reporting obligations are with respect to payments to governments, and then place the necessary systems and mechanisms to make certain that the required reports are made in an appropriate and timely fashion.

Failure to do this can result in a company falling into situations where it, or its employees or directors, may be subject to fines, prison sentences for being barred from important business opportunities.

So, be careful out there.

Dr. Swan is U.K. Managing Director and International General Counsel at IX Power Ltd, and a leading international expert and advisor on energy policy, law and regulation. He has been adviser to the European Commission, Council of European Energy Regulators, national governments, energy markets, energy traders, and major energy firms. He has also been a partner at three major international law firms, where he advised on all aspects of the energy business including contracts, joint ventures, concessions, production, refining, purchasing, shipping, trading, environmental issues and litigation. Ned is also a visiting professor at the Faculty of Law at University College London where he originated, and taught the LLM (Master's degree) course in Regulation of Financial Markets. He is admitted to the New York and US Federal Courts, and is a member of the Energy Institute, and the UCL Energy Institute. The Legal 500 has praised… 'Ned Swan's impressive energy related work.'