

Risk and Regulation  
Anti-corruption

# Corruption prevention in the Engineering & Construction industry





# Risk and Regulation

## Anti-Corruption

### The issue

Corruption in the global economy is a fact. No company is immune to risk, even if it operates in what appear to be relatively “safe” countries.

Transparency International – the global anti-corruption organisation – publishes a “Bribe Payers Index”, which identifies industry sectors most likely to bribe a public official: the Public Works Contracts and Construction sector emerges as being the most likely! This means that Engineering and Construction (E&C) companies face a disproportionately higher risk of being involved in corruption, and management need to ensure that this risk is both recognised and addressed.

### Why should this be?

E&C companies have a business model that exposes them to a greater proportion of the recognised corruption risks than almost any other industry sector. This is because they are involved in significant one-off long-term contracts, often for the public sector, using complex supply chains. If they operate abroad, the risk is even greater.

This creates an exposure therefore that regulators are only too well aware of, which is why they have made the industry sector such a focus of their attentions.

### How does this affect you?

“One of the most important trends in FCPA (Foreign Corrupt Practices Act) enforcement is the increased aggressiveness of Government....US law enforcement authorities are increasingly focusing on foreign corporations.” (Shearman & Sterling LLP Oct 2008)

The US regulators are probably the most active in this area, but those in other countries are catching up fast. Regulators around the world are cooperating with each other, sharing information and levying increasingly punitive fines. Often the same act can fall foul of multiple regulatory regimes, opening the opportunity for multiple fines.

### The enforcement regime

So far the most significant fines have been imposed by the US regulators. Other countries, however, notably Germany and France, are starting to impose increasingly heavy penalties. The following is a cross section of recent fines levied:

<b>Siemens – \$800m (Department of Justice and Securities and Exchange Commission, US) and \$569m (Office of the Prosecutor General, Germany)</b>	<b>Halliburton - \$559m (Department of Justice and Securities and Exchange Commission, US)</b>
<b>Aon - \$8m (Financial Services Authority, UK)</b>	<b>ABB - €65m (European Commission, Switzerland)</b>
<b>Alstom - €53,5m (European Commission, France)</b>	<b>Balfour Beatty - £2.25m (Serious Fraud Office, UK)</b>

Furthermore, there is a step change increase in the level of activity by regulators and legislators. In 2005, across the 37 countries that were party to the OECD Anti-Bribery Convention, there were 50 cases under investigation. By 2008 this had risen to 254! Interestingly the US represented 70% of the 2005 cases, but this had dropped to 41% in 2008 – even though their own rate of enforcement had increased by 300%. The fact that eight countries introduced anti-bribery legislation in 2008 and another eight had similar legislation pending, can only reinforce this trend.

### Other Costs

In addition to the financial penalties, must be added the legal investigation and remediation costs, litigation and potential loss of government business.

The CFO of Siemens publicly estimated that the total cost of the bribery to the company was around one third of the annual profits for at least two years in succession. On top of this has to be considered the damage to reputation, and the impact this has on customers, staff and potential recruits.

### New trends in enforcement

Regulators are increasingly turning their attention to the individuals responsible, rather than just the companies. Recently, the first extradition warrant was served on a UK citizen for an FCPA violation.

Another trend is a focus on the extent of companies' anti corruption measures when considering fines. The recently published UK draft Bribery Bill introduces the concept of "negligently failing to prevent bribery". This puts an increasing onus on companies not only to have an anti-corruption compliance framework but to ensure that it is robust from the regulators' perspective.

## Why is Engineering and Construction at particular risk?

As mentioned earlier, the Public Work Contracts and Construction sector is recognised as carrying the highest risk of corruption. What are the red flags that make the sector particularly vulnerable, and, accordingly, where should the compliance activities should be focused?

### Operating in high risk areas

Although corruption can happen anywhere, some countries are clearly more risky than others. On a scale of 10 (clean) to one (corrupt), 135 out of the 180 countries ranked in Transparency International's Corruption Perceptions Index have a score of 5.0 or less. The territories with increased risk include the major emerging markets, as well as parts of southern and eastern Europe.

It is in the nature of the E&C business model that the most lucrative contracts tend to be in those locations where the market is newly established or experiencing significant growth and therefore particular care needs to be taken.

### Business, or other interactions, with Government officials

Under the OECD convention, Government officials are considered to be a particular risk with regards to corruption because they have the ability to award valuable contracts, or grant favours, and yet are often paid relatively little. The definition of Government officials is also broader than at first apparent, including:

- Ministers and civil servants
- Government employees including doctors, law enforcement and military
- Employees of any enterprise majority owned or controlled by the state
- Tax authorities and local government officials.

Again, it is in the nature of the business model that E&C companies will be dealing with government officials in some shape or form, either directly or through agents.

### Large projects, tenders or long term contracts

Large scale or long term projects and contracts increase corruption risk because the sums involved make corruption more attractive and potentially easier to conceal. There are often a limited number of tenderers for major products and those tenderers would sometimes be well known to both officials and competitors.

### Use of intermediaries to do business

"Third parties used as intermediaries are one of the most common channels through which bribes are made." (Transparency International)

Often it is impossible to do business in a country without using an intermediary of some sort. It is therefore vital to ensure that an ethical due diligence has been performed and that all payments are closely monitored. (Corporates can end up suffering penalties as a result of inappropriate activities by their agents or intermediaries).

### Decentralised business model

Compliance regimes need to be driven from the centre in order to create an independent challenge to local management. The more a business is decentralised, (and this tends to be the model in the E&C sector), the more counter cultural this operational oversight and challenge becomes.

### Locally operated bank accounts

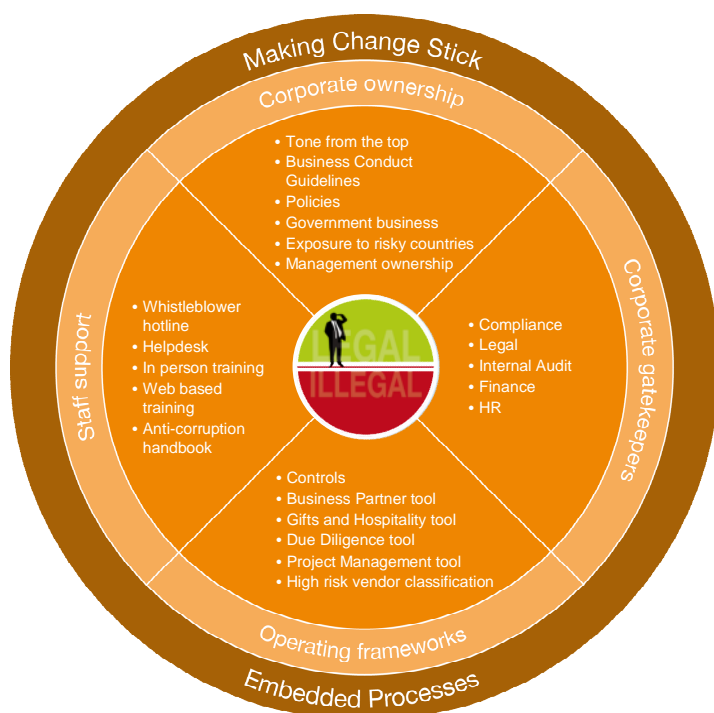
E&C projects usually require local funding. The less control you have over how bank accounts are set up and used, the greater the risk. This risk then increases further if it is easy for local management to use these accounts to make cash payments.

### Use of gifts, hospitality, entertainment or other benefits

Gifts, hospitality, entertainment etc that step over the dividing line from relationship building and good manners, into attempts to influence key decision makers, are also the focus of anti-bribery legislation. What may be regarded by the industry as normal business development practice could well be seen by a regulator as a bribe.

## What can you do about it?

Exposure to corruption cannot be avoided, but it can be managed. Those companies that have been caught and suffered the consequences were not fundamentally corrupt or even reckless. They simply had not taken effective measures to protect themselves, by implementing a proactive and comprehensive anti-corruption programme that addresses a company's culture, training, policies and controls. If your anti-corruption programme does not contain the component parts outlined in the model below, then you will be increasingly exposed to corruption risk.



## Are you risking it all?

Here are some questions you ought to be asking those in your company who have the responsibility of dealing with corruption risk:

- Do they perform an annual assessment to determine where the exposure to corruption exists?
- Is there an independent challenge when it comes to balancing commercial decisions with anti-corruption requirements?
- Are management comfortable that the typical employee will make the right ethical judgements in difficult situations and will know when and where to get support?
- How many intermediaries does the business use, what services do they provide and how much are they paid?
- How does management ensure the compliance framework provides the right balance of support and sanctions to prevent corruption?
- How do they restrict and eliminate the opportunities for corruption?
- Are performance targets set across the business considered in the light of corruption risk?
- Is the tone from the top right and do they know whether their people believe it?
- Do staff use the whistleblower hotline (assuming there is one), what is the pattern of cases and how are they followed up?
- When was the last time that key staff were trained and tested on their understanding of the anti-corruption requirements?

## How can PwC assist?

We believe we have some unique expertise in this area because we have direct experience of supporting our clients in two of the biggest and most successful compliance remediation programmes yet undertaken. This means that we understand the practical aspects of how to put things right, as well as the theory, and we know how demanding the standards for success can be.

We have a set of tools that help us move easily from risk assessment to diagnosis to design, and finally to implementation and testing. These principles can be tailored to any size of company and any size of exposure. Furthermore, once an appropriate compliance framework is in place, PwC can help ensure it is robust and sustainable.

Finally, and perhaps most importantly, we have a team of dedicated practitioners who solely work in the risk and regulation division, dealing with likes of anti-corruption on a day to day basis. This means they have the necessary experience to tailor the solutions to the specific needs of both the industry and the company. They will also ensure that their knowledge is transferred to your staff so that risks are minimised for the future.

If you would like to hear more information about this topic, a podcast is available for download on our website: [www.pwc.com](http://www.pwc.com) (within the Engineering & Construction pages – located under the 'Industry Sectors' tab).

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