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OCTOBER 1-2, 2012 HOUSTON

COMPLYING WITH THE FOREIGN CORRUPT PRACTICES ACT

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PRESENTERS



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- Represents companies and individuals in Foreign Corrupt Practices Act investigations and other criminal and SEC investigations



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- Leads BDO's Anti-Corruption Compliance & Investigations practice, conducting global Foreign Corrupt Practices Act and U.K. Bribery Act-related compliance, due diligence and investigations
- Has overseen numerous anti-corruption matters in Europe, Asia, Latin America and Africa
- Possesses significant hospitality industry expertise across several disciplines

PRESENTATION AGENDA

1. Overview of the US Foreign Corrupt Practices Act (FCPA)
2. FCPA Enforcement Trends and Developments
3. Assessing Corruption Risk
4. Q&A

WHY IS ANTI-CORRUPTION COMPLIANCE IMPORTANT?

ENFORCEMENT AND PENALTIES ON THE RISE

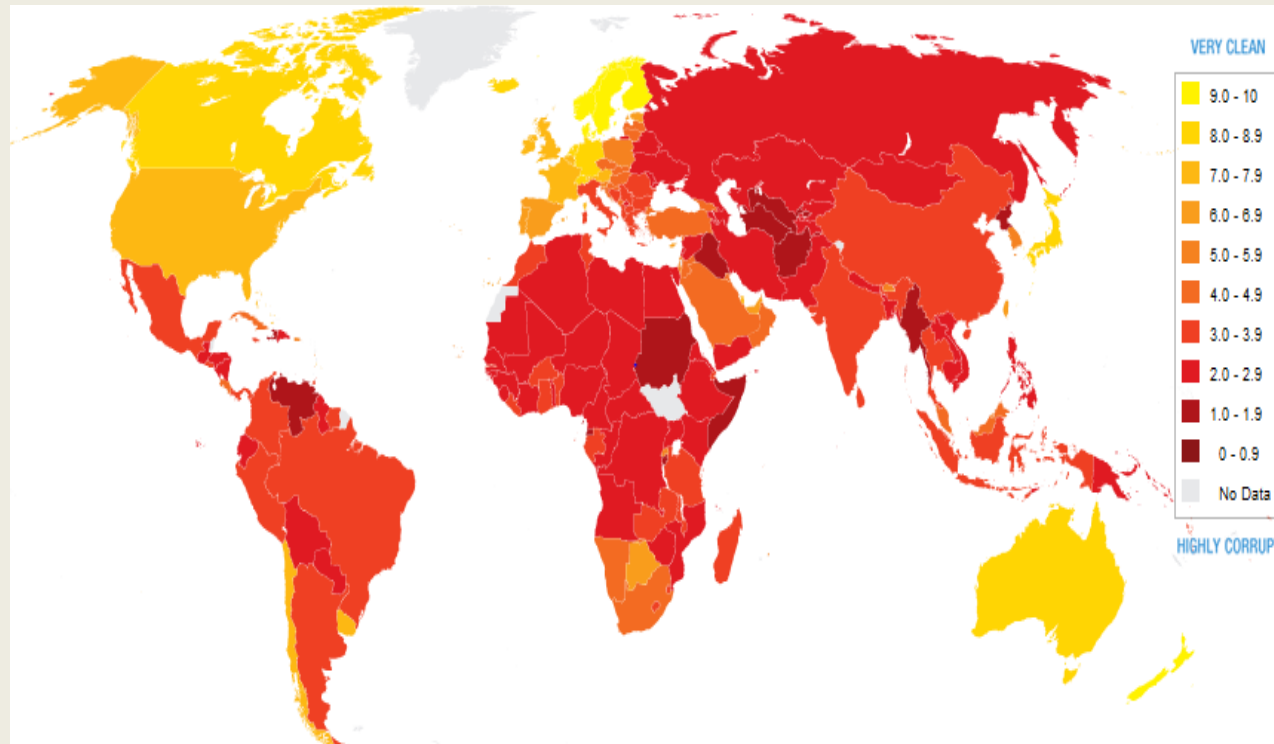


- Enforcement and investigations are increasing.
- Companies and individuals face serious consequences.
- First enacted in 1977, and amended since then, the FCPA is a focus of US Government enforcement:
 - Since 2007, the United States has settled FCPA enforcement actions with over 80 companies.
 - Over \$4 billion paid in penalties and disgorgements.
 - Over 85 companies world-wide currently being investigated.
 - Prosecution of individuals for FCPA violations and the length of prison terms are also increasing.
 - Huge costs in terms of money, time, careers and people's lives.
- Other countries ramping up their enforcement of anti-corruption laws.
 - U.K. Bribery Act

WHY IS ANTI-CORRUPTION COMPLIANCE IMPORTANT?

HEIGHTENED RISKS AROUND THE WORLD

- Transparency International's Annual Corruption Perceptions Index (CPI) ranks 183 countries based on perceived level of corruption.
- CPI is relied on by the U.S. government, the World Bank and others.
- 2011 CPI: Scale: 1 (most corrupt) to 10 (least corrupt)



Denmark: 2 (9.4)
Canada: 10 (8.7)
U.K.: 16 (7.8)
U.S.: 24 (7.1)
Oman: 50 (4.8)
China: 75 (3.6)
India: 95 (3.1)
Mexico: 100 (3)
Nigeria: 143 (2.4)
Libya: 168 (2)

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OVERVIEW OF THE U.S. FOREIGN CORRUPT PRACTICES ACT (FCPA)

THE U.S. FOREIGN CORRUPT PRACTICES ACT (FCPA)

- The U.S. FCPA is aimed at combating international bribery.
- The FCPA imposes three distinct requirements:
 - **Anti-bribery:** Prohibits giving, offering, or promising anything of value, directly or indirectly, to a foreign (non-U.S.) official for the corrupt purpose of obtaining or retaining business.
 - **Books and Records:** Public companies must keep books and records in reasonable detail that fairly and accurately reflect the transactions and circumstances of the company.
 - **Internal Controls:** Public companies must devise and maintain a system of internal controls that provides reasonable assurance of accurate books and records and GAAP compliant financial statements.

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION ANYTHING OF VALUE



- The term “anything of value” is broadly construed.
 - No materiality threshold
 - Includes non-monetary items, such as travel, food, entertainment, employment, discounts, charitable contributions, etc.



- If an official requests something, it is certainly of at least some “value” to him/her; otherwise, it would not be requested.

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

FOREIGN OFFICIALS AND OTHER RECIPIENTS

- **Foreign (non-U.S.) Officials:**
 - Any officer or employee of a government or any government entity, including:
 - National, local, provincial, regional, and state officials;
 - Immigration personnel;
 - Customs personnel;
 - Tourism or Visitor's Bureau personnel;
 - Airport personnel, including security;
 - Personnel of state-owned enterprises, such as national airlines, utility companies, hospitals, etc.
- **Foreign (non-U.S.) political parties, political party officials and candidates for foreign political office.**

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

CORRUPT INTENT

- **Payment must be made “corruptly.”**
 - **Intended to induce recipient to misuse position, for example:**
 - to direct business to payor or his client;
 - to obtain preferential treatment, legislation or regulations; or
 - to induce foreign official to fail to perform official function.

- **For the purpose of obtaining or retaining business.**
 - **Broadly interpreted to include advantages such as lower tax assessment than competitors.**

- **A corrupt act need not succeed:**
 - **An offer, promise, or even the authorization of or an agreement to make an offer or promise of a corrupt payment can be violation, even if no payment is made.**

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 1

- Hospitality Co. has decided to send one of its best and brightest, Moe Tel, to the country of Briberia to assist in managing the company's recently opened hotel there.

- Moe is on his flight on Briberia Airways, which is owned by the Briberian government, and Moe orders a drink. Moe tips the flight attendant to make sure he gets good service for the rest of the flight.
 - Has Moe violated the FCPA?

- On the flight, Moe is sitting next to an employee of the Briberian Ministry of Petroleum. The man lost his wallet and can't afford cab fare. Moe is being picked up by a company car and offers to give the employee a ride to his destination.
 - Has Moe violated the FCPA?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION IN ACTION – PART 1 (CONT'D)

- When Moe lands he is greeted by Briberian immigration officials who inform him that his work visa is invalid. He offers to give the officials a free stay at Hospitality Co.'s new hotel if they look the other way.
 - Has Moe violated the FCPA?
 - Has Hospitality Co. violated the FCPA in any of these scenarios?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION KNOWLEDGE

- FCPA prohibits corrupt payments to any person while “knowing” that payment, or portion of payment, will be directly or indirectly made or offered to a foreign official.
 - Example: Payments to agent with knowledge that the agent will make payments to foreign officials.
- “Head in the sand” approach unacceptable; “Knowing” includes conscious disregard or deliberate ignorance.
- Knowledge can be inferred from circumstances showing a high probability of improper payment.
 - Inference cannot be overcome by “deliberate avoidance of knowledge.”
 - Cannot ignore “red flags” that would create reasonable suspicion that illegal payments have been made.
- Red flags are viewed critically and in hindsight.

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

DIRECTLY OR INDIRECTLY

- FCPA prohibits direct payments to officials.
- FCPA also prohibits indirect corrupt payments made through agents and intermediaries, such as:
 - consultants,
 - independent contractors,
 - agents,
 - lobbyists, or
 - distributors.
- Company is liable if it:
 - Authorized the payment by the third party; or
 - Knew or consciously disregarded the high probability that the illicit payment would be made by the third party.



KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 2

- On Moe's first day as manager of the hotel in Briberia, he receives an email announcing a Request for Proposal from the Briberian Ministry of State for a contract to provide lodging for visiting dignitaries. Because Moe is new in Briberia, he wants a consultant to help him with the RFP.
- Moe interviews a consultant who says that he can guarantee success if hired, so long as he receives an up-front, one-time payment of \$50,000 deposited in an offshore bank account.
- Moe interviews another consultant, who is the niece of the Briberian Minister of State. Moe is concerned about hiring someone so closely affiliated with the Minister.

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 2 (CONT'D)

- Moe calls Hospitality Co.'s business affairs director to ask for advice. The director says, "hire the guy who guaranteed success because he is not affiliated with the government. If he ends up paying someone off, that's on him and we won't know anything about it?"
- Has the company adequately protected itself from an FCPA violation?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

AFFIRMATIVE DEFENSES

- **Two affirmative defenses:**
 - **Affirmative Defense No. 1:** Payment or gift was legal under written laws and regulations of host country (when made).
 - **Affirmative Defense No. 2:** Payment was for reasonable and bona fide expenditures incurred by or on behalf of recipient and directly related to:
 - Promotion or demonstration of goods and services; or
 - Execution or performance of contract with foreign government or agency.
 - Allows payment of reasonable travel and lodging expenses for a foreign official to visit facilities or meet with company representatives.
 - Allows payment of reasonable marketing expenses or other costs necessary to perform the contract.

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 3

- Hospitality Co. is competing for another contract with National Tour Co., a state-operated company that promotes tourism to Briberia. As part of its bid effort, Hospitality Co. has invited several executives of National Tour Co. to visit its flagship hotel property (upon which a new Bribieran hotel will be modeled) and headquarters in the United States to meet with Hospitality Co. executives.
- Hospitality Co plans to pre-book and pre-pay for the officials' airfare and hotel accommodations. It also plans to give each official a cash advance for miscellaneous travel expenses.
 - Does this raise any issues?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 3 (CONT'D)



- One of the executives of National Tour Co. says that he is bringing his wife on the trip and asks Hospitality Co. to provide airfare and hotel accommodations for her.
- A Hospitality Co. executive believes that the National Tour Co. executives would probably like to have some recreation time after the meetings with Hospitality Co. He suggests using the company's private plane to take the officials to Disney Land for a weekend.
- What, if any, issues do these scenarios raise?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 4

- Hospitality Co. lands the contract with National Tour Co. Hospitality Co. sponsors a charity golf event to commemorate the signing of the contract and has invited relevant representatives from private vendors that will work on the contract and from National Tour Co.
- Moe secures from the Marketing Department golf balls marked with Hospitality Co's company logo to gift to each of the attendees.
- Prior to the event, a representative of National Tour Co. publicizes that he and his son have been trying unsuccessfully to get a reservation for a tee time at a country club at which the Moe is a member.
 - Is it appropriate to provide the golf balls to the representatives from National Tour Co? What if, instead of golf balls, the gift was new golf clubs worth \$3000?
 - What should Moe consider before deciding whether to make a reservation for the National Tour Co. representative and his son to play at his country club? Would it matter if Moe accompanied them?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

FACILITATION PAYMENTS

- One Exception to the FCPA: The FCPA does not apply to facilitating payments made to a foreign official to expedite or secure performance of a “routine government action.”
- Excludes decisions to award new business or continue business.
- “Routine Governmental Action” includes obtaining permits, licenses or other official documents to qualify person to do business in foreign country, where the actions are of a non-discretionary nature.
- The UKBA, however, prohibits facilitating payments and, as a result, many companies prohibit facilitating payments.

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 5

- After Moe left for Briberia, Hospitality Co. shipped all of his furniture and other belongings to Briberia for him.
- A Briberian customs official calls Moe when the shipment arrives. He says that, due to a backlog, the shipment won't get through customs for three weeks.
- The official says he can get the shipment through customs in one week for an additional fee of \$3000 from Hospitality Co.
 - Should Moe pay the fee? What if it was \$300? Or \$3?
- While Moe is deciding what to do, the official calls back and says that if anything in the shipment is considered “contraband” then the shipment will not clear customs for six weeks. The customs official says he will pre-clear the shipment, thus expediting the process, if he receives an additional payment of \$1000.
 - Should Moe pay the fee? What if it was \$100? Or \$1?

KEY ELEMENTS OF THE ANTI-BRIBERY PROVISION

IN ACTION – PART 5 (CONT'D)

- Moe, wized since his early snafus in Briberia, contacts Hospitality Co.'s legal department for advice. They tell Moe that Hospitality Co. does not allow facilitation payments and instruct him not to make any of the additional payments to the customs official.
- Although later than desired, the shipment finally passes through customs. The customs official, upset that he did not receive payments from Moe, calls Moe to say that he will not release the shipment to Moe unless he receives \$5000 on top of the regular customs fees.
 - What should Moe do?
 - If any of these payments had been made, how should Hospitality Co. have recorded them in their books and records?

FCPA ACCOUNTING PROVISIONS

BOOKS AND RECORDS PROVISIONS

- **Require US issuers to maintain:**
 - **Accurate books and records**
 - Reasonable detail
 - **Adequate system of internal controls**
 - Policies and procedures
 - Documentation and certifications
 - Corrective action

FCPA ACCOUNTING PROVISIONS

INTERNAL CONTROLS

- Prohibits knowing circumvention of, or knowing failure to implement accounting controls.
- Prohibits knowing falsification of books, records or accounts.
- Issuer who owns 50% or less of voting power of domestic or foreign entity is required to use good faith influence to induce compliance.
- Issuer liable if foreign subsidiary creates false records to conceal illicit payment and issuer-parent then incorporates subsidiary's information into its books and records.
 - Several U.S. companies charged for actions of foreign subsidiaries, including Oracle Corporation, Dow Chemical, ABB, Schering-Plough, DPC, BJ Services, and others.

FCPA POTENTIAL PENALTIES

Companies

- Criminal fines up to \$2 million per bribery violation and \$25 million per accounting violation
- Civil penalties up to \$10,000 for a bribery violation and \$500,000 per accounting violation
- Additional penalties may include disgorgement of profits, placement of a corporate compliance monitor, required revision or enhancement of compliance policies, and reporting requirements.

Individuals

- Up to 5 years imprisonment plus criminal fines up to \$100,000 per bribery violation and up to 20 years imprisonment plus a \$5 million fine per accounting violation
- Civil penalties up to \$10,000 for bribery violations and \$100,000 for accounting violations
- DOJ and SEC are increasing focus on individual criminal prosecutions

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FCPA ENFORCEMENT DEVELOPMENTS AND TRENDS

ENFORCEMENT TRENDS

INCREASED ENFORCEMENT ACTIVITY

- As of June 2012, over 85 companies around the world are known to be the subjects of ongoing FCPA-related investigations.
- Including companies in the hospitality industry:
 - Las Vegas Sands Corp
 - Walt Disney Studios
 - Wynn Resorts Limited



ENFORCEMENT TRENDS: ESCALATING PENALTIES

- FCPA penalties for 2011 topped \$508 million.

- 8 of the 10 most significant penalties were imposed in 2010 and 2011.
 - JGC Corp. - \$218.8 million (2011)
 - Magyar Telekom - \$95 million (2011)
 - BAE - \$400 million (2010)
 - Snamprogetti - \$365 million (2010)
 - Technip - \$338 million (2010)
 - Panalpina and six of its customers - \$236 million DOJ/SEC (2010)
 - Daimler - \$184.6 million (2010)
 - Alcatel-Lucent - \$137 million (2010)

- Prior to 2010:
 - Halliburton/KBR - \$579 million (2009)
 - Siemens AV - \$2 billion (2008)

FOREIGN CORRUPT PRACTICES ACT

MONETARY PENALTIES – TOP TEN

Year	Company	Country	Penalty Amount
2008	Siemens	Germany	\$800 million
2009	KBR/Halliburton	United States	\$579 million
2010	BAE	United Kingdom	\$400 million
2010	Snamprogetti Netherlands B.V./ENI S.p.A	Holland/Italy	\$365 million
2010	Technip S.A.	France	\$338 million
2011	JGC Corporation	Japan	\$218.8 million
2010	Daimler AG	Germany	\$185 million
2010	Alcatel-Lucent	France	\$137 million
2010	Panalpina	Switzerland	\$81.8 million
2011	Johnson & Johnson	United States	\$70 million

ENFORCEMENT TRENDS

INCREASED ENFORCEMENT AGAINST INDIVIDUALS

- **Recent enforcement against individuals:**
 - **February 2012:** Albert “Jack” Stanley, former CEO of KBR, sentenced to 30 months in prison.
 - **On December 13, 2011,** 8 former executives and agents of Siemens indicted including a former member of the Board. First time a board member of a Fortune 500 company has been indicted for an FCPA violation.

- **Increased penalties extend to individuals:**
 - **November 2011:** Joel Esquenazi sentenced to 15 years in prison for FCPA and money laundering violations.
 - Co-conspirator sentenced to seven years in prison;
 - Defendants also ordered to forfeit \$3.09 million.
 - **March 2011:** Jeffrey Tesler agreed to forfeit \$149 million to settle FCPA charges.

- **Increased emphasis on prosecuting individuals, even non-U.S. citizens.**
 - Jeffrey Tesler and Wojciech Chodan (arrested and extradited in 2011)
 - Flavio Ricotti (arrested and extradited in 2010).

ENFORCEMENT TRENDS: A FOCUS ON GIFTS, TRAVEL, AND ENTERTAINMENT

CASE STUDY: AON CORPORATION - \$16.3 MILLION (2011)

- Aon, one of the world's largest insurance companies, used funds for sending Costa Rican and Egyptian officials to trainings in the insurance field to reimburse the officials (and sometimes their spouses) for dozens of trips to tourist destinations and for other "non-training activities."
- A substantial number of these trips were in connection with conferences and seminars, but Aon's records either failed to provide a business purpose for the expenditures or showed that the expenses were clearly not related to a legitimate business purpose.
- Even though the trips appeared to have "some business component," they "included a disproportionate amount of leisure activities and lasted longer than the business component would justify."

ENFORCEMENT TRENDS: A FOCUS ON GIFTS, TRAVEL, AND ENTERTAINMENT

CASE STUDY: DIAGEO PLC - \$16.4 MILLION (2011)

- From 2003 to 2006, Diageo, a producer of premium alcoholic beverages, made over \$2.7 million through its subsidiaries in improper payments to various government officials in India, Thailand, and South Korea to obtain sales and tax benefits.
- Diageo's South Korean subsidiary paid over \$86,000 in cash and over \$100,000 in travel and entertainment expenses to customs and other government officials as a reward for their roles in granting Diageo significant tax rebates.
 - On one trip, South Korean officials traveled with personnel from Diageo's South Korean subsidiary to Scotland to inspect a scotch distillery; however, the trip concluded with a "purely recreational side-trip" to Prague and Budapest.
 - Diageo also made hundreds of gifts, including traditional and customary presents known locally as "rice cake" payments, totaling over \$230,000 to South Korean military officials in order to obtain and retain liquor business.

ENFORCEMENT TRENDS: A FOCUS ON GIFTS, TRAVEL, AND ENTERTAINMENT

CASE STUDY: IBM - \$10 MILLION (2011)



- From 2004 to 2009, two IBM subsidiaries in China provided improper travel and other expenses to Chinese government officials and employees on at least **114** occasions.
 - The travel included side trips, sightseeing trips, or other trips with little or no business purpose.
 - In conjunction with the travel, Chinese government officials were sometimes given improper per diems and gifts.
 - The misconduct involved key management at the subsidiaries and over **100** employees.
 - The IBM subsidiaries designated certain travel agencies as “authorized training providers” and would record that payments to those agencies for improper trips were for “training services.”

ENFORCEMENT TRENDS: A FOCUS ON GIFTS, TRAVEL, AND ENTERTAINMENT

ROCKWELL AUTOMATION - \$2.8 MILLION (2011)

- RAPS paid \$450,000 to fund sightseeing trips for state-owned design institute employees to places such as New York City, DC, Hawaii, Germany, Australia and others.
 - These trips typically followed business-related travel, but “appeared to have no direct business component.”
 - E.g., one “business trip” was to New York City, but Rockwell had no facilities in NYC.
 - A Rockwell document said the trip was planned because “everyone likes New York.”

ENFORCEMENT TRENDS: A FOCUS ON GIFTS, TRAVEL, AND ENTERTAINMENT

CASE STUDY: VERAZ NETWORKS - \$300,000 (2010)

- Veraz Networks was a California-based telecommunications services provider.
- The SEC alleged that from 2007-2008 Veraz made payments and gave gifts to government-controlled telecommunications companies in China and Vietnam.
- Without admitting or denying the charges, Veraz consented to pay a civil penalty of \$300,000 to settle the allegations of books and records and internal controls violations.
- The SEC took action against Veraz despite the de minimus nature of the violations and Veraz's remedial steps.
 - Payment to the Chinese company in China was only \$4500.
 - The only gift given to the Vietnamese company that the SEC highlighted was flowers to the CEO's wife.
 - Veraz cancelled a contract with the Chinese company when it realized it had won the contract due to an illegal payment.

ENFORCEMENT TRENDS: A FOCUS ON GIFTS, TRAVEL, AND ENTERTAINMENT

CASE STUDY: UTSTARCOM INC. - \$3 MILLION (2009)

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- UTStarcom (UTSI) is a global telecommunications company that designs, manufactures and sells network equipment and handsets.
- Between 2002 and 2007, UTSI subsidiary—UTS China—paid nearly \$7M for hundreds of trips to popular US tourist destinations for employees of Chinese state-owned telecommunications companies.
 - The trips were recorded as “training expenses,” but UTSI had no facilities in the locations and conducted no training.
- In settlement agreements with DOJ and the SEC, UTSI admitted to the conduct, agreed to pay \$3M in fines (\$1.5M DOJ; \$1.5M SEC), and implement rigorous internal controls.

ENFORCEMENT TRENDS: NEW ENFORCEMENT TOOLS AND THEORIES

- **New Enforcement Units**
 - **FBI FCPA Task Force**
 - **SEC's new Office of the Whistleblower: Formed as part of the Dodd-Frank Act; Final rules took effect in August 2011.**
 - **DOJ and SEC emphasis on additional compliance requirements for violators: Increased imposition of monitors by the DOJ; SEC requirement for compliance reporting and certifications.**

ENFORCEMENT TRENDS: NEW ENFORCEMENT TOOLS AND THEORIES (CONT'D)

- **Expanded Theories of Enforcement**
 - Creative enforcement theories expand the potential scope of FCPA liability.
 - Commercial Bribery and the Travel Act
 - Travel Act prohibits traveling between states or countries or using an interstate facility in aid of any crime, federal or state.
 - Enforcement agencies have added Travel Act charges to FCPA charges.
 - Example: Control Components, Inc. - \$18.2 million (2009). CCI was charged and pled guilty to FCPA violations and Travel Act violations.
 - Control Person Liability
 - Control Personal liability may be based solely on supervisory responsibility over the managers and policies involved, and a failure to maintain an adequate system of internal controls.
 - Example: Nature's Sunshine Products - \$600,000 (2009).
 - Company's CEO and CFO were charged with violating the books and records and internal controls provisions of Section 20(a) of the Securities and Exchange Act of 1934 based on their position as "control persons."
 - The executives agreed to pay \$25,000 each in fines, despite a lack of knowledge or authorization of the payments.

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ASSESSING CORRUPTION RISK

COMPONENTS OF AN EFFECTIVE ANTI-CORRUPTION COMPLIANCE PROGRAM

- Clearly articulated corporate policy and procedures;
- Strong tone from the top;
- Designated compliance officer and an internal audit function trained in anti-corruption compliance;
- Appropriate due diligence for retention and oversight of agents and other third parties as well as for M&A transactions;
- Standard provisions in agreements, including but not limited to audit rights, with agents and other third parties;
- Appropriate processes for authorizations and documentation for relevant transactions;

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COMPONENTS OF AN EFFECTIVE ANTI-CORRUPTION COMPLIANCE PROGRAM (cont.)

- Periodic testing of transactions;
- Regular training for employees, agents, officers, directors involved in international activities;
- Well-communicated hot line and other reporting structures; and
- Appropriate disciplinary procedures.

RISK ASSESSMENT CONSIDERATIONS

- Does the Country have a reputation for corruption and bribery?
- Does the industry have a history of FCPA and anti-corruption problems?
- Does the company have a history of corruption issues?
- Is there heavy reliance on political or government contacts?

RISK ASSESSMENT CONSIDERATIONS (CONT.)

Third Parties

- Heavy reliance on agents, consultants, intermediaries and other third parties to conduct business:
 - Pre-retention due diligence, and post-retention oversight on agents, consultants, intermediaries and other third parties;
 - Representations and warranties regarding compliance with anti-bribery laws;
 - Audit rights of the third party's books and records; and
 - Right to terminate agreement or relationship as a result of failure to comply with anti-bribery laws or any breach of representations or warranties related to anti-bribery.

RISK ASSESSMENT CONSIDERATIONS (CONT.)

Policies & Procedures

- Gifts, travel and entertainment expenses, contributions to charitable organizations and political parties and facilitating payments;
- Payments in cash, manual checks and bank account reconciliations;
- Background checks on all relevant employees; and
- Hotline reports, SOX testing and internal audit testing.

PERIODIC TESTING AND MONITORING

Substantive Testing

- In audit parlance, substantive testing is thought of as a direct test of transactions and account balances;
- Substantive testing entails validating the propriety of higher risk transactions through examination of supporting documentation; and
- Continuous Controls Monitoring (CCM).

RED FLAGS OF CORRUPTION

- ❖ Customer name or address equals vendor name or address;
- ❖ Vendor payment to address in country of customer;
- ❖ Unusually large one-time payment;
- ❖ Round dollar payments;
- ❖ Several round dollar payments to a vendor within a short time frame;
- ❖ Payments slightly under enhanced authorization protocols;
- ❖ Several payments for identical amounts;
- ❖ Abnormal frequency/magnitude of cash transactions;
- ❖ Manual checks;
- ❖ Vendor Address = PO Box;
- ❖ Payee inconsistent with GL classification;
- ❖ Authorizing party inconsistent with classification of expenditure;
- ❖ Excessive payments to intermediaries;
- ❖ Payments in excess of budget; and
- ❖ Excessive charitable contributions, T&E, gifts
- ❖ Vendor address in different country than location of services

RED FLAGS OF CORRUPTION (CONT'D)

RECORDKEEPING AND ACCOUNTING VIOLATIONS

- Vague, non-specific description for payments made in entries;
- Payment descriptions that do not correspond to accounting classification;
- General purpose or miscellaneous accounts with significant activity;
- Missing invoices or other documentation; and
- Travel and expense requests with incomplete information.

RED FLAGS OF CORRUPTION (CONT'D)

THIRD PARTIES

- Known connections of agents, consultants, intermediaries and other third parties with foreign officials;
- Reluctance to agree with contract representations and warranties regarding compliance with anti-bribery laws;
- Lack of sound reason for use of intermediaries; and
- Requests for commissions to be paid in a third party country, to a third party, or in cash or untraceable funds.

RED FLAGS OF CORRUPTION (CONT'D)

ADDITIONAL RISK FACTORS OR INDICATORS

- Bank accounts in tax havens (Luxembourg, Switzerland, British Virgin Islands);
- Transactions routed through unconsolidated or nominee companies; and
- Violation or avoidance of internal controls (payment amounts slightly below authorization limits, manual checks, missing or incorrect approvals).

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QUESTIONS?