Avoiding Fraud and Corrupt Practices

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Types of Corruption

- Bribery
- Embezzlement
- Extortion
- Grey Market
Avoiding Fraud and Corrupt practices

• Rules, protocols, guidelines!
• Organizational Culture.
• Legal contexts.
• Audit!
• Train staff.

• Trust everyone and no one.
Prevalence of Corrupt Practices

Perceived corruption levels by country and companies’ propensity to bribe

Source: Transparency International
Foreign Corrupt Practices Act

- Law in U.S. since 1977
- All OECD members have similar laws
OECD convention signers

Argentina
Australia
Austria
Belgium
Brazil
Bulgaria
Canada
Chile
Colombia
Czech Republic
Denmark
Estonia
Finland
France
Germany
Greece
Hungary
Iceland
Ireland
Israel
Italy
Japan
Luxembourg
Mexico
Netherlands
New Zealand
Norway
Poland
Portugal
Russia
Slovakia
Slovenia
South Africa
South Korea
Spain
Sweden
Switzerland
Turkey
United Kingdom
United States
Prevalence of Corrupt Practices

Perceived corruption levels by country and companies’ propensity to bribe

Source: Transparency International
Foreign Corrupt Practices Act, 1977, prohibits

- Any individual, firm, officer, director, employee, agent of firm, stockholder acting on behalf of firm, from
  - acting with corrupt intent, to make payment to a foreign official (regardless of rank), foreign political party or official, candidate for foreign political office,
  - To induce the recipient to misuse his official position or wrongfully direct business.
Sanctions

- **Criminal**
  - Up to 5 years in prison and up to $2 million fine.

- **Civil**
  - AG or SEC or Competitor may bring action to enjoin or punish.

- Those in violation may be barred from doing business with the Federal govt.
• U.S. Justice Department priority
• Greater enforcement
• Higher Fines
• Prosecution of businesses as well as officials
Exceptions to FCPA

- Size of payment
- Routine governmental action
- The seniority of the governmental official
- Discretionary or required approvals
- Third Parties
- Accurate recording
- Monitoring
Exceptions to FCPA

- *Routine governmental action* does not include any decision by a foreign official to award new business or to continue business with a particular party.
Private to Private bribery

- Criminalized in some countries including:
  - UK
  - Hong Kong
  - China
  - Malaysia
  - Germany
  - Spain

- United Nations Charter against corruption of 2005 mentions encourages criminalization
Extortion

- Fees demanded by dishonest officials for performing their duties.
- Fees demanded by representatives of purveyors for fulfilling their agreements.
Extortion avoidance

• Implement policy
• Reporting system
• Training
• good relations with governmental authorities
Extortion avoidance

- Discuss demands of local officials with higher authorities.
- Cooperate with local commercial associations to publish official procedures, time, and fees for approvals.
- Prohibit payment of non-documented expenses.
Responses to extortion

• Refuse to pay and explain that your organization doesn’t allow payments not required by law and official receipts are required.
• Report incident to higher management.
• Inform official that making payment is prohibited by your company and explain that you may be fired if you make a payment.
Responses to extortion

- Take the name of the employee and explain that all fees must be paid to the government office and that an official fee needs to be issued.
- If this can’t be done, request a receipt on the government letterhead.
Responses to extortion

- Identify a more senior official to approach.
Responses to extortion

• Seek assistance from other organizations, local universities, and trade organizations. Ask how they have responded to similar demands.

• Explain to the parties involved that the demand could endanger continued operations.

• Contact business groups and the U.S. embassy.
• Theft of cash or property in company’s possession.
• Skimming: Before cash gets on the books, stealing.
• Phony vendors: Company pays invoice and money is paid to employee.
Individual Warning signs

- No concept of right or wrong
- Troubling family and friend relationships
- Deceptiveness
- Resentment
- Build an image of trustworthiness
- Self confidence – belief they can get away with crime.
- Clever and creative
Behavioral Red Flags

- Failure to follow procedures and accounting rules
- Late submission of expenses
- Reluctance to reassign work
- High travel expenses.
- Failure to reply to inquiries related to expenses.
- Purveyors complain of late payments
- Divorce/Family problems
- Addiction problems
Remedies against employee theft

- Ethical organizational culture
- Good internal controls
- Timely submission and review of financial transactions
- Careful review of expenditures against budget
- Whistle blower policy
Over-invoicing is a popular mechanism used in both government organizations and private firms in China and the rest of the world to embezzle funds.
Over-invoicing

- Employee sent to purchase computer with authorization to spend $3000.
- Computer firm provides invoice for $3000 although computer lists at $2500
- Employee pockets $250
- Computer agent pockets $250
- Alternative: the Computer firm throws in a hard drive worth $250 to the employee.
Misuse of petty cash

- Employee takes petty cash to purchase office supplies.
- Store employee provides receipt for 25% more than the cost of the goods.
- Employee and store employee split the profits.
- Employee puts her share in the staff social fund.
Grey market

- Offshore payments
- Cash payments for services

Risks:
- Labor audits
- Disgruntled employees can sue—or inform government
Summary

Understand regulatory environment everywhere you operate.
Commit to honest operations
Understand risks to operations and reputation
Maintain compliance
Use experts when necessary
Educate staff
Culture of Compliance