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FCPA: Baker Hughes Settles Bribery Charges

In yet another record-setting settlement in the Foreign Corrupt Practices Act (FCPA) area, the Securities and Exchange Commission (SEC or the commission) and the Department of Justice (Justice Department) announced, April 26, 2007, that Baker Hughes Inc. (BHI) and Baker Hughes Services International Inc. (BHSI), a wholly owned subsidiary of BHI (collectively, Baker Hughes), have together agreed to pay \$11 million in criminal penalties, \$23 million in civil disgorgement and prejudgment interest, and \$10 million for violating a 2001 commission cease-and-desist order prohibiting BHI from future violations of the books and records and internal controls provisions of the FCPA. *In the Matter of Baker Hughes Inc.*, Exchange Act Release No. 44784 (Sept. 12, 2001).

The total payment of \$44 million by Baker Hughes represents the largest combined penalty ever imposed in the FCPA area. The Baker Hughes settlement comes fast on the heels of the Feb. 6, 2007 settlement



in which three Vetco Gray International Ltd. subsidiaries, Vetco Gray Controls Inc., Vetco Gray Controls Ltd., and Vetco Gray UK Ltd., agreed to pay a combined \$26 million to settle charges that they violated the antibribery provisions of the FCPA. Justice Department Release No. 07-075 (Feb. 6, 2007).

Clear Message

The message from the Justice Department and the SEC is loud and crystal clear:

The Justice Department “will continue to hold U.S. companies and their subsidiaries accountable for foreign bribery[,]” and “[t]he record penalties leveled in [the Baker Hughes] case leave no doubt that foreign bribery is bad for business.” Justice Department Release No. 07-296 (April 26, 2007). The Justice Department’s view is that “[b]y enforcing the FCPA, [it is] maintaining the integrity of the U.S. markets and leveling the playing field for those companies that want to play by the rules.” For its part, the SEC takes the view that “[c]ompanies like Baker Hughes will be held accountable when they circumvent

the rules of fair play and honest competition by making improper payments to win business.” SEC Press Release No. 2007-77 (April 26, 2007).

Setting aside for the moment the philosophical debate about whether the United States should dictate how business is done around the world while ignoring the harsh realities of the environments in which U.S. companies operate, what is clear from these recent cases is that U.S. companies will continue to pay steep civil and criminal penalties if caught violating the strictures of the FCPA.

Additionally, the Baker Hughes and Vetco Gray settlements also illustrate the fact that repeat offenders face an especially daunting task in negotiating a favorable settlement, not the least of which is the real prospect of an injunctive action and criminal prosecution, both of which could have significant collateral consequences on a company’s ability to conduct its business.

Charges Against Baker Hughes

The SEC and Justice Department allege that, in late September 2000, BHSI acceded to a demand for illicit payments made by officials of Kazakh oil, the state-owned oil company of Kazakhstan. See SEC Civil Complaint, No. 07 Civ. 1408 (S.D. Tex. April 26, 2007); DOJ Criminal Information, No. 07 Cr. 129 (S.D. Tex. April 11, 2007).

Just prior to September 2000, BHI had received unofficial notice that it had prevailed in its bid, tendered through BHSI, to provide a wide range of oil-field drilling and production services for Karachaganak, a large oil and gas field located in Kazakhstan. (SEC Complaint, *supra*.) Notwithstanding this notice, a Kazakh oil official demanded

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that BHI hire a consulting firm located in the Isle of Man to assist its bid on the Karachaganak project and pay that firm a 3 percent commission on the profits earned by BHI on the Karachaganak project.

After receiving a threat that refusal to pay would jeopardize BHI's bid for the Karachaganak project and its chances of obtaining future work in Kazakhstan, BHSI agreed to pay a 2 percent commission to the consulting firm, which had provided no services in preparing the bid and provided no services to BHI or BHSI at any later point. The resulting payments—which were extended between May 2001 and November 2003—totaled approximately \$4.1 million.

BHI and BHSI were also alleged to have improperly characterized these payments as legitimate payments in their respective books and records, even though BHSI knew they were not compensation for legitimate services and, in fact, were intended to be transferred to Kazakh government officials.

The SEC complaint additionally alleges that Baker Hughes and its subsidiaries committed numerous other FCPA violations in Kazakhstan and elsewhere by paying bribes and making other payments to agents without obtaining sufficient assurances that these payments were not being passed to government officials. These allegations include charges that BHSI and a second BHI subsidiary paid over \$1 million in bribes to Kazakh oil officials in connection with separate transactions, that a BHI subsidiary extended over \$11 million in questionable payments to Angolan agents with close ties to government officials, and that BHI subsidiaries extended smaller amounts to officials in Nigeria, Indonesia, Uzbekistan and Russia, while ignoring signs that these

payments were intended to be transferred to government officials and failing to conduct the due diligence necessary to ensure that the payments were legitimate.

This record settlement was likely driven by several factors. First, and perhaps foremost, was the size of the contract and, consequently, the level of profits that Baker Hughes secured through its allegedly unlawful payments: Baker Hughes conceded that it had earned almost \$20 million in profits from its work on the Karachaganak project. BHSI's criminal penalty and BHI's disgorgement was largely derived from this profit calculation.

Second, the SEC clearly viewed BHI's violation of the cease-and-desist order imposed as a result of past FCPA violations as a sign that steep penalties were appropriate, particularly because the commission then went on to conclude that BHI's subsequent violations had been "widespread and egregious."

The message sent by the \$10 million civil penalty, according to SEC enforcement director Linda Thomsen, was that "recidivists will be punished." SEC Press Release No. 2007-77. Coming hard on the heels of the combined \$26 million fine imposed on three Vetco International Ltd. subsidiaries by the Justice Department in February 2007—still the record for purely criminal investigations—that message is now unmistakable.

Third, the record sanctions obtained by the government in this case also can be seen as a consequence of the coordinated civil and criminal investigation by the SEC and Justice Department. This tactic of conducting joint civil and criminal FCPA investigations (which ironically was first used against BHI in 2001, and has since been utilized by the government with increasing

frequency in recent years) permits the government to exert maximum pressure on companies by simultaneously unleashing all of its investigatory powers, and by placing the full panoply of possible civil and criminal sanctions on the negotiating table at the same time.

As both the SEC and the Justice Department have made clear, prosecuting violations of the FCPA is a priority for both agencies. What is of concern is that regulators appear to be uninterested in the reality on the ground in the many countries around the globe where paying to get things done is par for the course.

More and more cases are brought not for bribes paid to "obtain or retain business," but for routine payments made to get things done. See, e.g., *SEC v. Dow Chemical Company*, SEC Litigation Release No. 20000, Feb. 13, 2007 (charging that employees of fifth-tier foreign subsidiary level made payments to speed approval for sale of pesticide products); *In the Matter of Oil States International Inc.*, SEC Release No. 34-53732, April 27, 2006 (charging that consultant hired by company paid employees of state energy company to avoid unwarranted stoppages and delays).

Companies are advised to pay as much attention to these small, seemingly inconsequential payments—which are often made by low-level employees with little or no management input—as they do to requests for large payments from highly placed government officials when bidding for government projects.

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