Drilling Down to Important Details

Why Enhanced Due Diligence is Critical to the Oil & Gas Industry

A LexisNexis® White Paper

Twitter®, 24-hour news channels ... in today's always-on world, businesses must stay on their toes if they hope to avoid negative publicity. The complex, global nature of extractives markets and increasingly stringent regulatory environment only raises the pressure on the oil and gas industry which is already hampered by poor public perception. In fact, according to the PwC 2014 Global Economic Crime Survey, energy/utility and mining industries are close rivals to state-owned companies when it comes to perceived risk of corruption.[1] Not convinced? Three of the eight Foreign Corrupt Practices Act (FCPA) enforcement actions taken by the US government in 2013 involved companies from the oil and gas industry.[2] As the saying goes, "Prevention is the best medicine." Is it time for you to re-evaluate the due-diligence process you depend on to protect your business from legal, financial and reputational risk?

Why is the Oil & Gas Industry Susceptible?

Despite public perception, the oil and gas industry isn't inherently corrupt. Why, then, is this sector so often in regulators' sights? The complexities of relationships oil and gas companies have with third parties worldwide make compliance with anti-bribery and other anti-corruption regulations more challenging. According to the *Resource Guide to the U.S. Foreign Corrupt Practices Act* published by the U.S. Department of Justice (DOJ), "Comprehensive due diligence demonstrates a genuine commitment to uncovering and preventing FCPA violations."[3]

FCPA Enforcement Actions taken by the United States in 2013

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> *"Comprehensive due diligence demonstrates a genuine commitment to uncovering and preventing FCPA violations."*
>
> U.S. Department of Justice

High-Risk, Emerging Markets

As oil and gas companies look for new reserves of natural resources to tap, they are finding themselves exploring and operating in countries that lack the political stability, infrastructure and regulatory environments of more established markets. The result? According to Transparency International's Corruption Perceptions Index, key growth markets for oil and gas—Africa, Latin America, Asia and the Middle East—come in at the lower end of the scale, indicating high levels of alleged corruption.[4] In addition, many of these emerging markets are at high risk of conflict, and the high value attached to oil and gas increases the risk for money laundering and corruption. When oil and gas companies operate in these countries, they must take care to ensure that their global business policies are enforced everywhere, despite the cultural differences encountered.

Interaction with Government Officials

In emerging markets, oil and gas companies often find themselves dealing with state-owned organizations. Whether wholly- or partially-owned, these organizations drive up risk because employees are considered foreign officials for the purposes of bribery and corruption regulations. Moreover, the need to frequently interact with government officials on local, regional and state levels exposes oil and gas companies to many situations where questionable practices—demanding cash payments to obtain border entry for equipment or securing work permits for employees, for example—are the norm.

Reliance on Third Parties

More critically, oil and gas companies often contract with third parties to operate on their behalf in these countries. Under the FCPA and other anti-corruption regulations, companies can be held responsible for any corrupt practices of the third party if it ultimately leads to a business advantage for the contracting company. And it's not just third parties within the emerging market that pose a risk. Recently, in response to regulator inquiries into market rigging—and more than $4 billion in fines for several large banks—British Petroleum announced it is reviewing its own foreign exchange unit because of customer relationships with 26 banks.[5] BP spokesperson Brett Clanton noted in an email that "BP has a robust framework of compliance requirements and internal controls which are constantly reviewed, and maintains an open dialogue with the appropriate regulators." Clearly, any third-party relationship increases risk potential for oil and gas companies.

Largest FCPA Fines to Date

1. **Siemens**: $800 million in 2008
2. **Alstom**: $772 million in 2014
3. **KBR / Halliburton**: $579 million in 2009*
4. **BAE**: $400 million in 2010
5. **Total S.A.**: $398 million in 2013*
6. **Alcoa**: $384 million in 2014
7. **Snamprogetti Netherlands B.V. / ENI S.p.A**: $365 million in 2010*
8. **Technip S.A.**: $338 million in 2010*
9. **JGC Corporation**: $218.8 million in 2011
10. **Daimler AG**: $185 million in 2010
11. **Weatherford International**: $152.6 million in 2013*

* Oil and Gas Industry

How Great is the Risk?

The financial risk is significant. Three of the top 10 FCPA fines imposed in recent years were levied against companies in the energy sector—Alstom, Total S.A. and Weatherford International—totaling more than a billion dollars. The industry will continue to be a prime target for FCPA and other regulatory enforcement actions precisely because it relies on a complex, global network of customers, venture partners, foreign government agencies and contractors.

In addition to the financial risk, the oil and gas industry must manage a reputation that the public already perceives as tarnished. Third-party misconduct could exacerbate the issue. Late in 2014, for example, a global oil company's third-party drill ship operator working off Alaska's Arctic coast pled guilty to environmental and maritime crimes.[6] While the drill ship operator claimed full responsibility for its actions and is paying more than $12 million in fines and community service payments, the incident fueled environmental activists already opposed to Arctic drilling—creating yet another hurdle for the oil and gas industry to overcome.

Enhanced Due Diligence Makes a Difference

Whether vetting potential customers, partners, third-party suppliers or contractors, companies in the oil and gas industry must establish a robust due-diligence process to mitigate risk. Relying on financial health information alone is not enough. Companies also need to look at sanctions and politically exposed persons data, country risk assessments, negative news, litigation history and more. In addition, companies need to maintain an auditable trail that demonstrates the due-diligence and compliance process is in place and being used. The DOJ's *Resource Guide to the U.S. Foreign Corrupt Practices Act* notes that "Businesses may reduce the FCPA risks associated with third-party agents by implementing an effective compliance program, which includes due diligence of any prospective foreign agents."[7] Recent actions confirm this position. One company that was the subject of an FCPA case earned a positive resolution based on the fact that it had "already significantly enhanced and is committed to continue to enhance its compliance program and internal controls," sending a clear message that due diligence is a valuable—and necessary—part of mitigating compliance risk.[8]

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U.S. Department of Justice

[1] http://www.pwc.com/gx/en/economic-crime-survey/
[2] http://www.sec.gov/spotlight/fcpa/fcpa-cases.shtml
[3] http://www.justice.gov/criminal/fraud/fcpa/guidance/guide.pdf
[4] http://www.transparency.org/cpi2014/results
[5] http://www.houstonchronicle.com/business/energy/article/BP-says-foreign-exchange-unit-reviewed-after-5988718.php
[6] http://bigstory.ap.org/article/143ba3f5733945dd86d4e1adc4cdb9b1/arctic-drill-ship-company-admitting-8-felonies
[7] http://www.justice.gov/criminal/fraud/fcpa/guidance/guide.pdf
[8] http://www.justice.gov/opa/pr/bio-rad-laboratories-resolves-foreign-corrupt-practices-act-investigation-and-agrees-pay-1435

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