

The Anatomy of Corruption in Public Procurement

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January 17, 2012

Public procurement presents significant risk under the U.S. Foreign Corrupt Practices Act (FCPA). Cases like [Siemens Argentina](#), [Siemens Venezuela](#), [Johnson & Johnson](#), and [Tenaris](#) highlight the risk. Large amounts of money are at stake when the government procures things like roads, computer systems, oil extraction services, medical equipment, power stations, and textbooks. Companies must interact directly with government officials. And government officials have pockets of discretion that can give rise to manipulation of the process. When corruption is involved, procurement decisions are no longer based on price, experience, and quality.

I investigated corruption and fraud for The World Bank for several years in multiple countries known for high corruption risk. Almost every one of these investigations involved an expensive public procurement that The World Bank was financing in whole or in part. This financing is what gave The World Bank the jurisdiction to investigate and proceed against companies and businesspeople that we found to have engaged in wrongdoing.

Public Procurement is Common

Government procurement is more common than one might think. It [has been estimated](#) to account for 14 to 20 percent of a country's GDP, which would be between \$8.16 trillion and \$11.65 trillion worldwide each year. In Mexico, for example, the federal government spent about \$53 billion in 2008 on public procurements, constituting about 18.4 percent of Mexico's GDP. In 2009, it spent about \$78 billion.

Common Corruption Schemes in Public Procurement

Through my experiences in private practice and at The World Bank, I have seen several common corruption schemes in public procurements. Internal compliance officers should be especially vigilant when their companies engage in this area of work. Here are some common issues to watch for.

- Sometimes procurement officials require that bidders hire “consultants” as a way to funnel money back to the officials. This formed the basis of one [Baker Hughes](#) action and several of the [Siemens](#) actions.
- Sometimes companies will disguise direct payments to procurement officials as something else. In the [Johnson & Johnson](#) case, the company funneled money to procurement authorities at state-owned hospitals by using sales agents to award “civil contracts” to doctors, purportedly to conduct trainings for the company that never actually happened.

- Sometimes companies hire “experts” that, with or without the company’s knowledge, previously worked for the procurement agency itself. These individuals still have contacts in the procurement offices. Maybe they even designed the actual specifications of the tender at issue. As former officials, they know how to game the system.
- Sometimes improper payments, if made during the project design phase, will influence procurement authorities to narrowly design a project’s specifications to benefit the company making the payments.
- Sometimes project designers proactively seek to include complicated technical features in the tender. The more technical, the more room an official has to use discretion in the selection process to favor one bidder over another.
- Sometimes companies gain access to confidential information, such as getting to see the tender specifications before they are officially released. In the [Tenaris](#) case, the company obtained access to competitors’ confidential bid information and then revised its own bids accordingly to win.
- Sometimes procurement officials might choose to fully vet the bid of one company while giving a less rigorous review to the bid of another. In this way, companies that are unable to show appropriate qualifications and experience or the ability to deliver the appropriate product are still able to win the contract.
- Sometimes companies will learn early on that a government is considering the procurement of goods and will then seek to “entertain” procurement officials before the tender process even begins. During these periods, actors are able to develop complicated schemes to transfer improper payments and direct contracts in return.
- The World Bank does a good job in its publication, “[The Most Common Red Flags of Fraud and Corruption in Procurement](#),” of highlighting other red flag in procurement. For example, when a procurement authority does not select a lowest bidder, repeatedly awards contracts to the same bidder, or changes the contract terms and values after the process concludes, investigators know to take a closer look.

High Alert Needed

Compliance officers should be on high alert when dealing with procurements. The above themes can help in structuring their own compliance measures to respond to risk.

In addition to being mindful of these corruption schemes, companies should also be mindful of the books and records and internal controls violations that can be associated with them. They should put mechanisms in place to ensure that management authorizes any use of agents, third parties are fully vetted and trained, transactions are accurately recorded in the books, backup documentation is maintained to justify expenses, and justification is maintained for the amount of fees paid to agents.

Companies should also make sure they know and follow the rules of public procurements. Almost every country has in place detailed rules that govern this activity. The World Bank

requires countries to follow [Procurement Guidelines](#) for projects it finances. Companies should understand when they can and cannot interact directly with officials. They should know when it is appropriate to revise or clarify their bids. They should know and comply with timelines for submitting their bids, submitting clarification questions, and expecting procurement decisions.

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