

## Fraud is Expensive—But is it Expensive Enough?

Written by Administrator

Monday, 08 February 2010 00:00

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In October, 2009 we [wrote](#) about the serious fraud charges facing BAE Systems PLC. We noted allegations of “bribery and corruption in arms deals in South Africa, Romania, and the Czech Republic dating back to the 1990’s.” Britain’s Serious Fraud Office (SFO) was seeking an admission of guilt as well as payment of fines ranging from £500 to £1billion ( US\$1.6 billion to \$3.2 billion at the currency conversion rates in effect at the time).

At the same time, the U.S. Department of Justice (DOJ) was conducting an investigation into allegations that the US-subsiidiary of BAE Systems “used a U.S. bank to funnel bribes to Saudi Arabian officials.” We predicted that, “given the current U.S. government stance on contractor integrity and ethical conduct, a sustained finding in this area could prove problematic for the company,” since it derived slightly more than half of its £18.5 billion pounds annual revenue from U.S. operations.

[Reports](#) have emerged that on February 5, 2010, BAE Systems settled its case, agreeing to pay the U.S. \$400 million to settle charges of making a False Statement and agreeing to pay the SFO £30 million (US\$47 million) for improper

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accounting (“breach of its duty to keep [accurate] accounting records”) in connection with a payment to a former consultant in Tanzania. The settlement permits BAE Systems to avoid suspension or debarment, and thus to continue to bid on U.S. government contracts. As such, it is seen as a victory for the company; its stock price rose 1.6% on the day of the announcement.

According to the WSJ article linked above—

[BAE’s CEO] on Friday stressed that the transactions in relation to which the company pleaded guilty all occurred nearly a decade ago and outside the U.S. U.S. court documents detailed what prosecutors allege was BAE’s use of secretive offshore entities and shell companies, and its efforts to conceal where payments were going, in 1999 deals to lease fighter jets to Hungary and the Czech Republic. According to prosecutors, BAE avoided communicating with so-called ‘marketing advisers’ in writing and maintained scant information about its payments. After 2001, prosecutors allege, BAE made payments totalling more than £135 million and an additional \$14 million-plus to marketing advisers through one offshore entity, according to the court documents. The U.S. filing also alleges that BAE paid tens of millions of dollars to a Saudi government official and other associates, as well as to intermediaries, as recently as 2002. The payments were made as part of its management of a long-term agreement begun in the 1980s between the U.K. and Saudi Arabia to supply

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military hardware to the Saudis, U.S. prosecutors say.

‘Beginning in 1993, BAE [Systems] knowingly and willfully failed to identify commissions paid to third parties for assistance in the solicitation or promotion or otherwise to secure the conclusion of the sale of defense articles, in violation of its legal obligations,’ the court documents filed by Justice Department prosecutors said.

Interestingly, the false statement stemmed not from the payments themselves, but from management’s assertions and certifications regarding its commitment to ethical business conduct. As the WSJ article reports, “In the court documents, prosecutors allege that BAE promised to institute antibribery programs and filed false documents to the U.S. Defense Department stating it had implemented such programs when none existed.”

According to the [Financial Times](#), “BAE ‘undertook no adequate review’ of any of the services it gave the official, the DoJ said, even when the BAE employee who was handling the matter submitted \$5m in invoices. The DoJ

said that until early 2002, the company transferred millions more to an account in Switzerland controlled by an intermediary, though the company ‘was aware that there was a high probability’ that the payments would be transferred to the Saudi official.”

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We have discussed the [Foreign Corrupt Practices Act](#) (FCPA) before. We have also [discussed](#), in passing, the False Statements Act (18 U.S.C. 1001). This is an interesting blending of the two statutes. The U.S. DOJ certainly earned its \$400 million settlement.

In the U.K. though, watchdog groups are not as sanguine about the paltry settlement negotiated by the SFO. [This report](#) from the BBC states that the “Campaign Against the Arms Trade” (CAAT) was “shocked and angered” by the settlement, as well as “outraged and angry,” and ‘dismissed the UK fine as a “tiny p rice” for the lucrative deals the company struck. The CAAT spokesperson asserted that “Ultimately the charges that we see admitted are administrative charges, not charges of corruption.”

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[\*\*This Financial Times article\*\*](#) quotes a former African National Congress MP as calling the settlement a “travesty of justice.” Certainly, US\$400 million is no small fine—but does the UK settlement of \$47 million represent a mere slap on the wrist? What do you think? Members are encouraged to leave their comments below.