

RiseEngineer and the Foreign Corrupt Practices Act

Evan Mulbry and Andrew Sutherland

Marsha Jackson has just been promoted to the Head of Internal Audit in charge of financial controls for RiseEngineer Corporation, a NYSE publicly traded company that specializes in green design and construction. Started in 2003 by a graduate of MIT's Leaders for Global Operations program, the company has expanded from leading two suburban office building projects in New England to having nearly 50 high-rise office projects across the country. The company's growth led them to begin bidding on major international projects, one of which was in the country of Elysium.

As Head of Internal Audit, Marsha is responsible for ensuring the adequacy of internal controls over financial reporting (**Exhibit 1**) as well as compliance with the Foreign Corrupt Practices Act (FCPA) (**Exhibit 2**). Her oversight includes Elysium, a country she has neither visited nor done business with. Her research notes that it ranks low on Transparency International's Corruption Perceptions Index, meaning there is a high incidence of societal corruption.¹ RiseEngineer Elysium is the local subsidiary of the U.S. parent.

Shortly after her promotion, Marsha learns that an anonymous tipster left a message on RiseEngineer's whistleblower hotline, stating that "the big contract win in Elysium this year involved misconduct, and this was the only way I could tell someone."

¹ The Corruption Perceptions Index is a survey developed by Transparency International to assess the relative corruption of countries around the world.

This fictional case was prepared by Evan Mulbry and Professor Andrew Sutherland. Mr. Mulbry is an attorney with the United States Department of Justice. The views expressed are the authors', and do not represent the official position of the Department of Justice or any other Government agency.

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Marsha asks her compliance team to begin corroborating the whistleblower's claim. Their fact gathering unearths the following information:

1. The contract in question is an Elysium government tender to be performed over the next 12 months. RiseEngineer was one of five companies that bid for the contract. The bids ranged in value from \$800 million to \$1.25 billion. RiseEngineer's \$1.2 billion bid was accepted.
2. The following events related to the contract took place:
 - a. RiseEngineer managers took Elysium officials out to dinner at a Michelin Star restaurant. RiseEngineer managers and Elysium officials also exchanged small gifts on holidays and other occasions. Shared meals and gifts are custom in Elysium, and the competing local contract bidders were involved in similar activities.
 - b. RiseEngineer invited four Elysium officials to tour their Boston facilities. The officials brought their families, who explored the city while the officials were in meetings.
 - c. Each month, the Elysium government wired \$100 million to RiseEngineer's operating account in Elysium. Then, RiseEngineer Elysium's local finance director transferred \$90 million to RiseEngineer's main corporate account at the Boston headquarters.
 - d. A RiseEngineer Elysium employee wired \$3 million to an offshore account owned by TGH Consulting. TGH helps U.S. companies understand the local market and permitting process in Elysium, and provides government touch points. RiseEngineer hired TGH before the bid, as it was their first time doing business in Elysium.
 - e. RiseEngineer Elysium employees withdrew \$5 million in cash.ⁱⁱ
 - f. One email thread between RiseEngineer Elysium salespeople included the following: "I'm not sure I'm comfortable moving forward, I think we should run this by our General Counsel at headquarters," to which another salesperson responded "Call me."
3. RiseEngineer Elysium was its auditor's only client.
4. Two RiseEngineer Elysium employees raised the possibility that a disgruntled former employee made the whistleblower claim under false pretenses.

ⁱⁱ The local finance director stated only \$1,000,000 of cash withdrawals included documentation showing the withdrawals' purpose.

Internal Controls Report

Marsha's compliance team also returned with a report on the Elysium team to aid her assessment of the financial controls. Initially, they report that the head of RiseEngineer Elysium, Sarah Smith, was unhappy about their questions. Sarah said her subsidiary prioritizes profitability over paperwork.

The compliance team noted several additional facts. The Elysium sales team has five employees, each of whom has an uncapped commission. As a result of the contract in question, each salesperson received \$100,000 in commissions, which is double their \$50,000 base salary. Sarah stated her salespeople were "the goose that lays the golden egg," so she gives them substantial autonomy in developing relationships with customers, setting pricing, and hiring consultants. Moreover, Sarah said that when a conflict arises between sales and other departments such as finance, she almost always defers to sales because "we are in the business of making money."

Regarding the financial controls, the compliance team interviewed the Elysium financial manager to assess the current situation. The finance manager stated that he handles all accounting entries and the majority of banking transactions. He allows employees to withdraw cash from the business and initiate bank transfers with incomplete or no documentation. Moreover, the accounting manager does not require separate approval beyond the person's confirmation that the withdrawal or transfer relates to a specific client or potential client. When he is unsure about how to account for a particular transaction, he assigns it to an account based on his best estimate.

Exhibit 1 Background on Internal Control over Financial Reporting

Internal controls are the policies, processes, mechanisms, and procedures companies implement as part of their business processes to ensure the integrity of financial information and corporate assets. The Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) framework represents the industry standard for designing, implementing, and monitoring internal controls. The framework includes the following elements:

1. Control Environment
2. Risk Assessments and Management
3. Control Activities
4. Information and Communications
5. Monitoring Activities

Exhibit 2 The Foreign Corrupt Practices Act

Passed in 1977, the Foreign Corrupt Practices Act (FCPA) forbids U.S. citizens and firms from bribing foreign government officials in advancing their business interests. The FCPA applies worldwide and enforcement does not depend on local laws or customs. In other words, U.S. citizens and firms are prohibited from engaging in bribery even if it is widely accepted in the country. Bribes do not necessarily involve money; travel, scholarships, internships, charitable donations, and other benefits may also qualify.

The FCPA requires U.S. public companies and their subsidiaries to maintain transparent financial records and internal accounting controls providing reasonable assurance that:

- Transactions have been authorized;
- Transactions are recorded in a way that allows the firm to comply with the applicable accounting standards; and
- An authorization system is in place to monitor who accesses assets, and asset records are verified at reasonable intervals against actual assets.

Unlike most securities laws, the FCPA is enforced by both the Securities and Exchange Commission (SEC) and the Department of Justice (DOJ). Both civil and criminal penalties (i.e., prison time) can apply.

Discussion Questions

1. If you were Marsha, what additional information would you like to have to assess the credibility of the whistleblower claim?
2. What specific events and transactions do you view as most problematic?
3. If you were Marsha, what internal control and process changes would you put in place for future international bids? How do you balance the desire of headquarters to monitor against the international subsidiaries' pursuits of new contracts?
4. When thinking about RiseEngineer's activities in Elysium, what are the responsibilities and incentives of the following parties?
 - a) Auditors
 - b) RiseEngineer's board of directors
 - c) Regulators
 - d) Marsha Jackson
 - e) Sarah Smith
 - f) Shareholders