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Fighting corruption in the Maritime Industry What you need to do to navigate in transparent waters

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A Point of View





The shipping and ports industry plays a crucial role in the Indian economy in sustaining the country's growth in trade and commerce. Currently ranking 16th among maritime countries, around 95 per cent of India's trade by volume and 70 per cent by value takes place through maritime transport¹.

The shipping industry has the ability to connect and influence all corners of the world. It is connected to all industries in some way or form, and as companies begin to grow and expand into other markets globally, shipping becomes an integral part of the day to day operations. A leading threat however, to this industry is corruption. While all industries are considered to have a level of corruption or bribery associated with it, some are affected more than others.

The United Nations (UN) estimates that corruption can add 10% or more to the cost of doing business internationally

In the maritime industry, with the advent of globalization, there has been a surge in global trade. It is estimated that merchandise exports of 160 World Trade Organization members in 2013 was USD 17.8tn². The logistics of maritime import and export of merchandise invariably involve considerable interactions with government officers of that country e.g., customs officials, import/ export licensing officials, product safety certification and standards officials etc.

New amendments to the Prevention of Corruption Act, 1988 provides for classifying corruption as a heinous crime and longer prison terms for both the bribe giver and the bribe taker. The measures approved include penal provisions being enhanced from a minimum 6 months to 3 years and from a maximum five years to seven years. The proposed amendment Act will also ensure speedy trial, limited to two years, for corruption cases. The ambit of the existing Act will be enhanced to make commercial entities liable for inducement of public servants. Under the present law, only individuals are liable. The proposed amendment also provides for issue of guidelines to commercial organizations to prevent persons associated with them from bribing a public servant.

¹ Source: Ministry of Shipping

² Source: World Trade Organization International Trade Statistics 2014

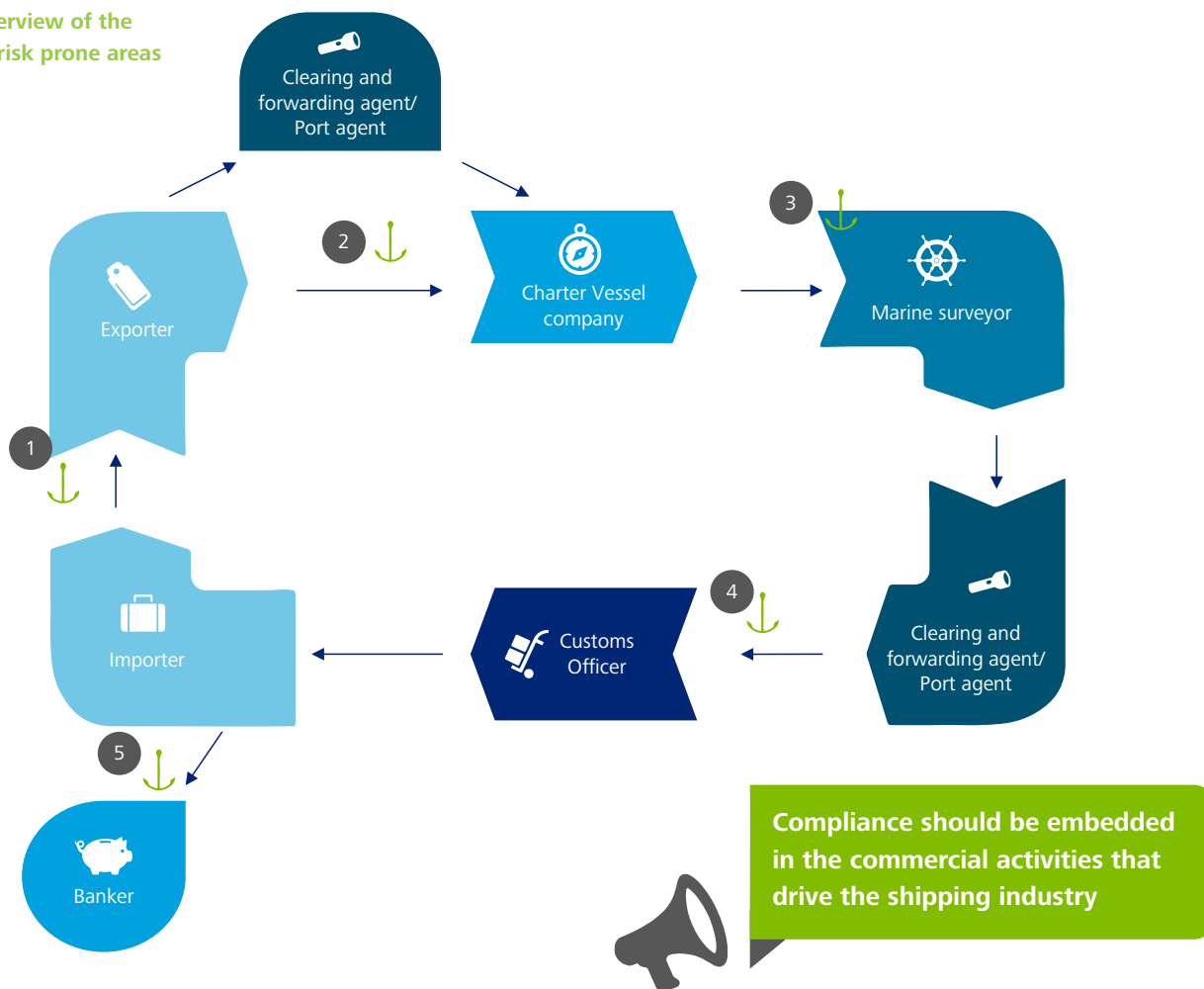


Many emerging countries have import and export licensing and other regulatory requirements that lack transparency and that make the movement of goods into and out of those countries time-consuming, burdensome, and costly. Considering these requirements, especially in 'high-risk' countries where local officials may be considerably underpaid and where corruption is routine, the temptation to pay bribes to those local officials in order to 'facilitate' or 'expedite' the import and export of merchandise may be very high³. As per a recent study by the Organization for Economic Cooperation and Development (OECD) the transport and storage industry is tied at second as the industry where the most bribes are paid⁴.

Shipping is a global business, with several stakeholders and jurisdictions involved in any single shipment. Even for a single shipment there are innumerable potential pitfalls where the dishonest seek to take advantage. As parties are often based in multiple locations in most cases they deal with each other through brokers and financial institutions⁵ increasing their vulnerability to regulations having an extra-territorial reach such as the US Foreign Corrupt Practices Act (FCPA) and the UK Bribery Act (UKBA).

It is the exposure to statutes such as these, combined with the weaknesses of the maritime import and export that draw uneasiness to this industry.

An overview of the fraud risk prone areas



3 Source: Foreign Corrupt Practices Act Compliance Issues for Import/ Export Operations by John F. McKenzie
 4 Source: OECD Foreign Bribery Report 2014, An analysis of the crime of bribery of foreign public officials
 5 Source: "Fraud in the Maritime Industry", Skuld



Understanding common fraud scenarios

1. Under-invoicing

The exporter may receive a request from the importer to declare on the invoice (sent along with the goods) that the merchandise is of lower value than the actual sale price. Typically, the purpose behind “under-invoicing” is to understate the declared value of the goods for local customs purpose to avoid customs duties and import taxes at the time of importation. The issuance of a false commercial invoice upon a purchaser’s request could constitute a violation of the books and records provision of the FCPA.

2. Bribes paid to gain contracts

Where large shipping and commercial vessel companies are involved, they very often bid for long term contracts from large scale manufacturers/ exporters. This bidding process can create opportunities for corruption, as the exporter could be induced to show favor to certain bidders.

Case study: According to the claims that emerged in May 2014 the Dutch logistics company, Maersk Group, bribed an official of Brazil’s state-owned Petroleo Brasileiro SA, (Brazil’s largest oil manufacturer) to grant shipping contracts to Maersk during a bid process. It is alleged that Maersk paid commissions to a Brazilian broker, Gandra Brokerage, who in turn bribed Paulo Roberto Costa, the then head of refining and fuel supply at Petrobras, in exchange for being awarded contracts for several years⁷. Investigators believe USD 2.1 billion in bribes were moved in the Petrobras corruption scheme⁸.

3. Illicit payments to Marine Surveyors

A marine surveyor is a professional who conducts inspections, examines marine vessels to assess and report on the condition of the vessel itself and the cargo on it. Marine surveys typically include the structure, machinery and apparatus (navigational, safety, radio, etc.) and general condition of a vessel and/ or cargo. One of the many duties of a marine surveyor includes the inspection of the vessel before it docks into the arrival port. At this stage a vulnerable marine surveyor may be compromised.

Case study: In late April 2015 an associate consultant with a marine surveying firm was charged by the Singapore High Court for soliciting bribes on three occasions from ship masters, for issuing positive inspection reports that would allow the ships to enter an oil terminal. On two occasions, the consultant overstated his findings by claiming some non-existent high-risk defects to prompt bribes amounting to USD 3,000 in each incident in exchange for a positive inspection report. On a third occasion, a sting operation organized by the Singapore Corrupt Practices Investigation Bureau, the surveyor attempted to elicit a bribe in exchange for which the consultant would issue a report failing to mention the real defects of the ship. In the present case the consultant was sentenced to 6 months imprisonment.

4. Illegal payments/ facilitation payments to Customs Officers

A big challenge in the shipping industry is the frequent and persistent demands for low value amounts demanded by public officials to facilitate port operations (“so called facilitation payments”). Customs administrations of emerging economies, in particular, have been ranked amongst the most corrupt government institutions (Transparency International 2008). The OECD estimates that customs clearance is the second highest reasons why bribes are being paid. The nature of corrupt activities that customs officials engage in typically vary from country to country and range from acts of extortion, patronage, nepotism, embezzlement, kickbacks and cronyism in exchange for rewards in cash or kind. These can largely be classified into three types:

- a) Routine corruption: This type of corruption pertains to instances when bribes are paid to customs officials to ensure customs procedures are completed or expedited.

Case study: In the case of Helmerich & Payne, Inc.’s (H&P) (an US based Oil & Gas-Exploration company) Venezuelan subsidiary, allegedly made improper payments through their agents to customs officials in Argentina and Venezuela to permit and expedite the import and export of equipment and supplies. Between 2003 and 2008 the Venezuelan entity paid Venezuelan customs officers (via their customs brokers) around USD 19,673⁹. The Department of Justice (DOJ) did not prosecute because of H&P’s prompt and voluntary disclosure as well as the considerable remedial actions taken, however did levy a USD 1 million penalty¹⁰.

7 Source: <http://www.ft.com/cms/s/0/947feb1e-e42c-11e3-a73a-00144feabdc0.html>

8 Source: <http://seafarersrights.org/petrobras-bribes-estimated-at-2-1-billion/>

9 Source: <http://fcpa.shearman.com/?s=matter&mode=form&id=224>

10 Source: <http://www.bu.edu/law/central/jd/organizations/journals/bulr/volume92n4/documents/STRAUSS.pdf>

- b) Fraudulent corruption: This type of corruption involves the persuading of customs officials to 'turn a blind eye' to certain procedural requirements in order to decrease tax liability or other import/ export obligations.

Case study: Emery Transnational a Filipino company which was a former subsidiary of Con-way Inc. (a US based freight transportation and logistics company) allegedly made improper payments amounting to USD 244,000 to officials at the Philippines Bureau of Customs and the Philippines Economic Zone area. These payments consisting of hundreds of small cash payments were made to induce officers to violate customs protocols, settle customs disputes, and reduce or not impose appropriate fines¹¹.

- c) Criminal corruption: This type of corruption occurs when criminal organisations offer payments to customs officials to enable the smuggling of illegal substances into the import country¹².

Refusing demands for facilitation payments can lead to commercial delays or even threats to crew, but allowing these to be embedded as a way of business can foster a system of corruption and inefficiency that is much costlier in the long-term.

5. Illegal purchase of letters of credit

The letter of credit (LC) has eased many of the problems relating to payments in international trade. The importer or customer obtains the LC in such a manner where payment is promised on presentation of certain documents which validate that the goods have been delivered in a satisfactory fashion. The importer may use monetary means to persuade a banker to issue an LC. This LC is sold to the importer or customer at a discounted rate. Thus when the exporter tries claim against the said LC he is defrauded. Obviously, if the banker is a government employee – which may be the case in many countries – and the inducement is anything of value, including a gift, the action may be interpreted as a violation of the FCPA and several other anti-bribery statutes.

Recommended action

Bribes are expensive - they add significantly to the basic cost of a transaction as well as devastating regulatory consequences when failing to meet anti-bribery compliance standards. From an ethical stand point, bribery and corruption undermine both democracy and law by directing money away from moral companies and governments and into the hands of corrupt officials and business owners. A lot of foreign bribery and corruption is hard to track however there are certain steps companies can undertake to help mitigate the risks.

- Implement a comprehensive anti-bribery and corruption compliance program across the business
- Periodically review policies and assess the effectiveness of such a program
- Policies and procedures must be clear and practical
- 'Tone from the top' - adopt a zero tolerance culture
- Strengthen internal controls by conducting anti-bribery trainings for senior management, employees, business partners and third-parties that act on behalf of the company.
- Perform business partner/ vendor assessments and risk evaluation
- Local consultants/ agents should not be engaged without a thorough due diligence
- Establish an effective and confidential whistleblowing mechanism to enable employees and other third parties to voice their concerns without the fear of retaliation

With legislative enforcement and collective action initiatives gaining ground, companies in all facets of the shipping industry should be diligent. One of the most challenging perhaps would be to change long-established attitudes towards bribery in the industry that "things are just done that way." It is however up to every stakeholder to think of bribery not as a cost but as an obstacle to doing business.

11 Source: <http://fcpa.shearman.com/?mode=form&id=167>

12 Source: http://www.worldcustomsjournal.org/media/wcj/-2013/2/WCJ_V7N2_Ndonga.pdf



Contact Us



Rohit Mahajan

Senior Director and Head,
Forensic, Financial Advisory,
Deloitte in India

T: +91 22 6185 5180
E: rmahajan@deloitte.com



Amit Bansal

Senior Director
Forensic, Financial Advisory,
Deloitte in India

T: +91 22 6185 6764
E: amitbansal@deloitte.com



Sushmit Bhattacharya

Director
Forensic, Financial Advisory,
Deloitte in India

T: +91 22 6185 5263
E: bsushmit@deloitte.com

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