

BAKER HUGHES TO PAY RECORD AMOUNT IN FCPA CASE

Baker Hughes Inc., a Houston-based oil field services contractor, agreed to pay a record \$44.1 million to settle a probe into alleged bribery in connection with its operations in Kazakhstan, Nigeria, Indonesia, Uzbekistan, Russia, and Angola. The settlement represents the highest total penalty ever paid in a bribery case under the Foreign Corrupt Practices Act (“FCPA”). Baker Hughes settled the case with both the Securities & Exchange Commission (“SEC”) and the Department of Justice (“DOJ”). The company’s wholly owned subsidiary, Baker Hughes Services International, Inc. (“BHSI”), also pleaded guilty to criminal FCPA violations in connection with the settlement.

In settling allegations with the SEC, Baker Hughes agreed to pay \$10 million in civil penalties and over \$23 million in disgorgement. In a plea agreement with the DOJ, BHSI pleaded guilty to (1) one count of violating the FCPA’s antibribery provisions, (2) one count of conspiracy to violate the FCPA, and (3) one count of aiding and abetting the falsification of an issuer’s books and records. As part of its plea agreement with the DOJ, BHSI agreed to (1) pay an \$11 million criminal fine, (2) serve three years’ probation, and (3) adopt a comprehensive antibribery compliance program. BHSI’s parent company, Baker Hughes, Inc., simultaneously entered into a deferred prosecution agreement with the DOJ. In doing so, the company agreed to hire an independent compliance monitor and to continue to cooperate fully with the government in investigating FCPA violations by individual employees.

In filing criminal charges against BHSI, the DOJ focused on the company’s activities in Kazakhstan. According to the charging documents, BHSI submitted in February 2000 a bid to perform oil field services in Kazakhstan for a company called the Karachaganak Petroleum Operating Company, B.V. (“KPO”). KPO was owned by a consortium of four major oil companies—BG Group, Eni, Chevron, and Lukoil. The consortium had the right to develop the Karachaganak oil field in Kazakhstan under a contract with Kazakhstan’s state-owned oil company—Kazakhoil. Kazakhoil did not own any shares in KPO, but it wielded significant influence in awarding contracts. According to the DOJ, contracts effectively required the approval of Kazakhoil officials.

After BHSI submitted its bid, Kazakhoil officials demanded that Baker Hughes pay “commissions” to a “consulting firm” located on the Isle of Man. The consulting firm performed no services for BHSI or Baker Hughes. In September 2000, however, BHSI agreed to pay a 2.0% commission on all revenues earned under the Karachaganak contract and a 3.0% commission on all revenues earned on future services that it performed in Kazakhstan. KPO awarded the contract to BHSI on October 23, 2000. In pleading guilty, BHSI admitted that it violated the FCPA by making \$4,100,162.70 in improper payments to the “consulting firm” between May 24, 2001 and November 25, 2003. In making the payments, BHSI understood that the firm would transfer the “commissions” to an undisclosed official or officials at Kazakhoil.

Baker Hughes and BHSI also failed to account for the payments properly. Instead, they improperly characterized the payments as legitimate expenditures for, *inter alia*, “commissions,” “fees,” and “legal services.” BHSI accordingly also pleaded guilty to aiding and abetting “books and records” violations by Baker Hughes.

According to the SEC’s civil complaint, other Baker Hughes entities made similar improper payments to third-party agents and consultants. For example, another Baker Hughes subsidiary, Baker Petrolite, made improper payments to an agent in Kazakhstan in 1998 and 1999. According to the SEC’s complaint, Baker Petrolite paid approximately \$1.05 million to the agent’s Swiss bank account while knowing that the agent’s representative was a high-ranking executive at a Kazakh state-owned company, KazTransOil. The payments purportedly helped Baker Petrolite obtain a large chemical contract. Like BHSI, Baker Petrolite inappropriately recorded the payments in its books and records as “commission” payments.

According to the SEC, Baker Hughes repeatedly violated the FCPA’s “books and records” and “internal controls” provisions in making improper payments to foreign officials. On September 12, 2001, in connection with an earlier FCPA case, the SEC issued a “cease-and-desist” order requiring Baker Hughes to comply with the FCPA. Despite the order (involving alleged bribes in Indonesia), however, Baker Hughes continued to make improper payments around the world, and failed both to keep accurate books and records and to implement sufficient internal controls. Baker Hughes allegedly made improper payments in Kazakhstan and Angola from 1998 to 2003; it allegedly made improper payments in Russia and Uzbekistan from 1998 to 2004; it allegedly made improper payments in Indonesia from 2000 to 2003; and it allegedly made improper payments in Nigeria from 2001 to 2005. Baker Hughes initiated an investigation in 2003, but the investigation failed to uncover or prevent these continuing violations.

In this settlement, the SEC and DOJ are signaling a “get tough” attitude on what they conclude to be corporate recidivism and in their continuing expectation that companies will devise and implement effective compliance programs and auditing procedures to uncover FCPA violations in their overseas operations. The agencies noted the companies’ exceptional cooperation and significant remedial action, which sent a strong message throughout the company that unethical and illegal business practices would not be tolerated. Nevertheless, as noted above, the companies were required to pay record amounts to settle the cases and to hire an independent compliance monitor for a three-year period.

The case also shows the types of problems that a company can experience when it fails to adopt sufficient internal controls. Corrupt officials and employees often use third-party agents and consultants to channel improper payments to government officials. Proper due diligence should have discovered that Baker Hughes’ suggested consultants performed no work for the company and that foreign government employees selected those consultants. Companies should be particularly watchful for potential FCPA violations in high-risk countries and high-risk industries.

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