Facilitating Payments versus Bribes: Are We Sending Conflicting Ethical Signals in Accounting Education?

Randall B. Bunker, Ph.D., CPA.
Department of Accounting
Arkansas State University
USA

K. Michael Casey, D.B.A.
University of Central Arkansas
College of Business
201 Donaghey Ave., COB 102E
Conway, AR 72035, USA

Abstract
Due to the past decade of business scandals, ethics in accounting education has become an increasingly important topic in the academic profession. This increased focus on teaching ethics in academic programs can create challenges for education professionals, especially when unethical behaviors like facilitating payments (FPs) to foreign officials continue to be allowed under United States law. Facilitation, or ‘grease’ payments, remains one of the few exceptions from anti-bribery prohibitions of the law. While technically legal, facilitation payments are questionable at best from an ethical point of view and their legality creates obvious obstacles when trying to teach students the difference between ethical and unethical behavior. The legal code should be updated to create ethical consistency regarding this issue.

Keywords: ethics, accounting education, facilitating payments, FCPA, bribery

I. Introduction
Following the fraudulent scandals of the past decade (WorldCom, Enron, etc.), ethics in accounting education has become an increasingly important topic in the academic profession. In 2003, the National Association of State Boards of Accountancy (NASBA) addressed the ethics issue and initially recommended that two stand-alone college courses should be included in the education requirements to sit for the CPA exam. The NASBA proposal met with widespread criticism from accounting educators and the accounting profession, specifically the American Accounting Association (AAA) and the American Institute of Certified Public Accountants (AICPA) (Van Wyhe 2007). However Klimek and Wenell (2011) concluded that students who take a separate ethics course in accounting do seem to have higher ethical reasoning ability than students who have only had ethics integrated into their accounting courses. As of today, however, the vast majority of State Boards of Public Accountancy do not require stand-alone ethics courses in their educational requirements, but much more emphasis has been placed on teaching ethics in numerous college programs.

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2. Background and Literature
As a result of SEC investigations in the mid-1970's, over 400 U.S. companies admitted making illegal payments in excess of $300 million to foreign government officials, politicians, and political parties (DOJ 2011). The United States Congress enacted the Foreign Corrupt Practices Act of 1977 (FCPA) to bring a halt to the bribery of foreign officials and to restore public confidence in the integrity of the American business system (DOJ 2011). The FCPA is primarily known for its two main provisions, one that addresses the bribery of foreign officials and a second provision concerning accounting transparency requirements. The anti-bribery provisions of the FCPA make it unlawful for a U.S. person, and certain foreign issuers of securities, to make a corrupt payment to a foreign official for the purpose of obtaining or retaining business with any person.
Since 1998, the Act also applies to foreign firms and persons who take any act in furtherance of such a corrupt payment while in the United States. However, the FCPA does explicitly allow for the use of facilitation payments. The FCPA also requires companies whose securities are listed in the United States to comply with its accounting provisions. These accounting provisions require corporations covered by the Act to keep accurate records that reflect the transactions of the corporation and to devise and maintain an adequate system of internal accounting controls.

Facilitation payments are one of the few exceptions from anti-bribery prohibitions of the law. Facilitation payments are payments made to public officials to expedite government activities. Under the FCPA, a payment to a foreign public official is not a bribe if it is incurred for the sole or dominant purpose of expediting or securing the performance of a routine government action of a minor nature. Facilitation payments are typically viewed as a necessary business process that makes the bureaucratic process run more smoothly, however, according to Argandona (2005) facilitating payments are a widespread form of corruption. Facilitation payments often lead to more serious forms of corruption, impose additional costs on companies and citizens, and in the long run sap the ethical foundations of organizations (Argandona 2005).

Before the passage of the FCPA, the US did not allow deductions for bribes paid to foreign government officials if that bribe was a criminal offence. After the passage of the FCPA, US tax laws were changed to disallow tax deductions for payments if made to foreign government officials or employees and if unlawful under the FCPA, which makes facilitating payments tax deductible. While technically legal, facilitation payments are still considered to be questionable from an ethical point of view and they create obvious obstacles when trying to teach students the difference between ethical and unethical behavior.

Following the passage of the FCPA, Congress became concerned that American companies were operating at a competitive disadvantage compared to foreign companies who routinely paid bribes and were permitted to deduct the cost of such bribes as business expenses on their taxes (DOJ 2011). In 1988, Congress directed the Executive Branch to commence negotiations in the Organization of Economic Cooperation and Development (OECD) to obtain the agreement of the United States’ major trading partners to enact legislation similar to the FCPA (DOJ 2011). In 1997, the United States and 33 other countries signed the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

The OECD Anti-Bribery Convention establishes legally binding standards to criminalize bribery of foreign public officials in international business transactions. As of today, the 34 OECD member countries and four non-member countries - Argentina, Brazil, Bulgaria, and South Africa - have adopted this Convention. In 2009, the OECD Anti-Bribery Convention, in view of the corrosive effect of facilitation payments, made the following recommendations to Member countries: (1) Member countries should undertake to periodically review their policies and approach on small facilitation payments in order to effectively combat the phenomenon; (2) encourage companies to prohibit or discourage the use of small facilitation payments in internal company controls, ethics and compliance programs or measures, recognizing that such payments are generally illegal in the countries where they are made, and must in all cases be accurately accounted for in such companies’ books and financial records; and (3) urged all countries to raise awareness of their public officials on their domestic bribery and solicitation laws with a view to stopping the solicitation and acceptance of small facilitation payments (OECD 2009).

The accounting and recordkeeping provisions of the FCPA require companies making facilitation payments to accurately record them in their books and records. The OECD evaluators sought to understand the impact of this practice on overall FCPA enforcement of the foreign bribery offences, in particular, they questioned if companies were recording payments as facilitation payments, and if they did, whether the SEC would verify if the payment was in fact a bribe to a foreign public official in contravention of the FCPA (OECD 2010). The OECD evaluators also wondered if facilitation payments might be recorded as other expenses to conceal their purpose, and in such cases whether the SEC would take enforcement action for not accurately recording them in the books and records (OECD 2010). The SEC did inform the evaluators that SEC cases have been clear that in some instances where a company alleges payments are facilitation payments according to the FCPA, and the facts show that the payments are in fact bribes (OECD 2010). In addition, there were also cases that involved the misreporting of facilitation payments concerning customs, immigration and visa processing, inspections, training, gifts, travel and entertainment (OECD 2010).
The existing evidence suggests that companies are using the facilitation payment exception in the FCPA to illegally bribe foreign officials and take tax deductions for these payments.

In 2010, the OECD Working Group on Bribery in International Business Transactions issued a Phase 3 report in which it commended “the United States for its visible and high level of support for the fight against the bribery of foreign public officials, including engagement with the private sector, substantial enforcement, and stated commitment by the highest echelon of the Government” (OECD 2010, 4). However, the Working Group on Bribery recommended that the United States consider developing specific guidance on the application of the exception in the FCPA for facilitation payments and clarify “grey” areas identified by the private sector concerning facilitation payments (OECD 2010). One academic study by Bailes (2006) even suggested that firms be forced to make declarations about the use of FPs as a condition of listing on an organized stock exchange. However, at the present time it appears that the United States does not plan to eliminate the use of facilitation payments or provide additional guidance on this practice.

3. Conclusions and Comments

According to Dictionary.com, ethics is defined as the philosophical study of the moral value of human conduct and of the rules and principles that ought to govern it, and that branch of philosophy dealing with values relating to human conduct, with respect to the rightness and wrongness of certain actions and to the goodness and badness of the motives and ends of such. Ethics is a moral philosophy about the difference between right and wrong, and just because something is allowed under current laws does not mean that it is ethical. The majority of business professionals would likely agree that facilitation payments are unethical, even though they are technically legal under the FCPA.

Today, the topic of ethical behavior in business management is of great interest to the general public. Ethical behavior should be a core value for all US corporations and business professionals. The issue of how to best integrate ethical training in the educational curriculum is an important topic in the academic profession. It is an issue that is made more complicated by US laws that legalize unethical behavior in business like facilitation payments.

The AICPA developed a code of professional conduct for CPAs to follow and it informs them about the importance of ethics in the business environment. The AICPA lists several principles of professional conduct for CPAs to observe and follow. These principles include integrity, objectivity and independence, and due care. The code of professional conduct requires CPAs to maintain responsibility to their clients as well as the general public. Teaching accounting students ethical behavior should be paramount in every accounting curriculum, and US law should require companies to operate in an ethical fashion. Accounting professionals will have to adhere to a code of ethical behavior during their careers and US laws should be adapted to eliminate loopholes and exceptions that allow for unethical business practices. The FCPA should be amended to eliminate facilitation payments. The elimination of these unethical payments would alleviate the existing contradiction where US law legalizes unethical business practices, and make teaching ethical behavior in the classroom more transparent. And, given the list of recent FCPA violations (see Cleveland 2009) it is apparent that the current laws and guidelines are not sufficient to prevent illegal behavior. Perhaps if students were instilled with a less conflicting code of ethics on this issue it would become second nature to behave ethically.

Assuming no legal action to remedy this issue is forthcoming, the accounting profession needs to be proactive in addressing the ethicality of FPs. At a minimum there should be a standardized set of rules developed to clarify the “grey” areas mentioned earlier. For example, at exactly what amount does a facilitating payment become a bribe? Similar to the recommendations made by Aalberts and Jennings (1999) in their study of the ethicality of retail slotting fees, the accounting profession should mandate that companies that use facilitating payments should follow a standard set of guidelines for the payment and reporting of FPs. For example, perhaps the FP should be: 1) an amount linked in magnitude to the size of the business venture; 2) published and visible on a company’s website and disclosed via a prominent statement in the company’s annual report; and 3) applied in a uniform and consistent manner across all firms. This type of system would then allow the investing public and consumers to make more informed decisions about whether to support this practice with their investment and consumption dollars. Some clear guidelines would also make it easier to train future accounts in the appropriate ethical behavior.
References


