

# Insight: The new anti-corruption rules

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## The new anti-corruption rules: what do they mean for multinationals with operations in Asia?

Managing liability risks under anti-corruption laws can be a daunting prospect for most corporations, but this task is particularly complicated for multinational corporations with operations in developing economies where history, culture and customs impact day-to-day business.

Several notable enforcement and legislative developments in recent months highlight this continuing challenge for multinational corporations.

- In early May, **Avon Products Inc.** fired four executives over bribes to Chinese officials according to a regulatory filing.<sup>1</sup> The four individuals, who were initially suspended in April 2010 during an internal investigation, included a general manager and former head of finance of the company's China unit. As part of its internal probe, Avon has reportedly discovered millions of dollars in questionable payments in India, Japan, Argentina, Brazil and Mexico. In February of this year, the company conceded that it could face substantial fines, civil and criminal penalties and other sanctions, depending on how the Foreign Corrupt Practices Act (FCPA) matter is resolved. The investigation is reportedly ongoing.
- **Citigroup** faces lengthy bans on its credit card and wealth management businesses in Indonesia over a case of alleged embezzlement and the death of a client following questioning by debt collectors. Citigroup has said it is working closely with Indonesia's central bank to address its concerns.<sup>2</sup>

These two examples are representative of the risks faced by corporations and the importance of compliance efforts to avoid liability under applicable anti-corruption laws. As Lanny A. Breuer, Assistant Attorney General for the U.S. Department of Justice Criminal



An entity may potentially face charges under the anti-bribery regimes of several jurisdictions. Prosecution in one jurisdiction for anti-bribery law violations does not preclude another jurisdiction from pursuing charges based on the same conduct, so long as the conduct properly falls within the jurisdiction of the nations' respective anti-bribery laws.

<sup>1</sup> Matthew Boyle & Joel Rosenblatt, *Avon says it fired four executives in China over Bribes*, Bloomberg, May 5, 2011, available at <http://www.bloomberg.com/news/2011-05-04/avon-says-it-fired-four-executives-in-china-over-bribes.html> (last visited June 7, 2011).

<sup>2</sup> Adriana Nina Kusuma & Neil Chatterjee, *Indonesia lashes Citi over embezzlement, debtor death*, Reuters, May 6, 2011, available at <http://www.reuters.com/article/2011/05/06/us-indonesia-citigroup-idUSTRE7451J120110506> (last visited June 7, 2011).

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Division, has stated: "I have spoken often and to a variety of audiences about the Justice Department's determination to prosecute – and prosecute aggressively – financial fraud and corruption in all its forms.... It is important not only because there is intrinsic value in being a good corporate citizen. It is important because of the globalization of business and the complexity of our financial markets – both of which combine to present serious risks for your organizations."<sup>3</sup>

The emphasis placed on anti-corruption by enforcement agencies is likely to continue, particularly in light of new anti-corruption laws in the UK and China. On May 1, 2011, China's new anti-corruption law came into effect, and the new UK Bribery Act became effective on July 1, 2011. These new laws, along with the FCPA, have some overlap in terms of the types of conduct that are prohibited by the statutes, but contain significant differences that may have far-reaching implications for businesses.

The challenge for corporations is to manage the risk of liability under these regulations aimed at preventing bribery and corruption on a world scale, while operating in markets in which bribes and other corrupt payments may be widely accepted as a means or cost of doing business.

As White & Case's Arthur Mitchell<sup>4</sup> stated at the recent Inter-Pacific Bar Association (IPBA) meeting in Kyoto: "If we were to stop and look at anti-corruption efforts by governments in many developing countries, they are highly political. Holistic attempts to solve the problems of poverty, culture and a history of 'favors' via anti-corruption measures, in many jurisdictions, simply don't work. They lack focus and enforcement and generally encounter effective political opposition."

As one senior executive interviewed summarizes: "In some parts of Asia, if you are a multinational operating with ethics

and following all the laws [as we are], you are at a competitive disadvantage!"

This article explores the challenges for multinationals doing business in the developing markets of Asia. It looks specifically at the increase in processes and procedures needed by corporations in order to comply with the new anti-corruption regulations coming online; and it looks at some of the tactics multinationals are using to address the challenges of doing business in Asia.

## Recent FCPA developments

In the US there is increased scrutiny under the FCPA of alleged corporate bribery of foreign officials, with enforcement actions reaching an all-time high. The US Securities and Exchange Commission (SEC) is also stepping up FCPA enforcement, and the agency has a new whistleblower program that may help the agency identify possible securities laws violations, including accounting provisions of the FCPA. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, qualifying whistleblowers will be rewarded between 10% and 30% of sanctions in cases where more than US\$1 million is collected in successful enforcement actions. This enormous financial incentive suggests the SEC will be well-informed of potential misconduct and the agency will be able to continue to expand its enforcement efforts.

The FCPA has been in force since 1977, but recent enforcement efforts of US authorities have made companies subject to the FCPA increasingly aware of the risks for significant liability under the statute. The FCPA prohibits companies and individuals from providing anything of value to a "foreign official" for the purpose of obtaining or retaining a business advantage. While it does not prohibit commercial bribery between private companies (which the UK Bribery Act reaches), the term "foreign official" is broadly interpreted by U.S. enforcement authorities to include

individuals working for state-owned entities. Recent enforcement actions confirm that businesses must be particularly sensitive to operations in countries with many state-owned entities, such as China.

The FCPA does not contain an adequate procedures defense, like the UK Bribery Act, but US agencies do take compliance and cooperation efforts of companies into account when making enforcement decisions. Such anti-bribery efforts can mitigate liability for companies in the event that misconduct does occur. Unlike the UK Bribery Act, the FCPA explicitly permits facilitation or "grease" payments. The contours of this exception, however, are not well-defined.

Companies paid a record \$1.8 billion in fines and penalties to settle FCPA-related charges in 2010, and both the DOJ and SEC have continued their aggressive enforcement efforts in 2011. So far this year, a number of companies have already entered into settlement agreements with US agencies.

The agencies' commitment to enforce the FCPA is further demonstrated by several recent trials involving individual defendants, who face both fines and imprisonment if found guilty of violating the FCPA.

## The UK Bribery Act

The UK Bribery Act, which became effective on July 1, raises enormous challenges for both UK and multinational companies.

The challenges, in part, arise from the broad jurisdictional reach of the new Act. "A company is covered by the Act should it fail to prevent bribery anywhere in the world, if it simply carries on business in the United Kingdom," states Charlie Monteith, formerly Head of Assurance in the UK Serious Fraud Office (SFO) and a key advisor involved in drafting the UK Bribery Act. Charlie joined White & Case's London office as counsel in January this year. The Act also prohibits a broader scope of conduct than other anti-corruption

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3 Lanny A. Breuer, Assistant Attorney General, Criminal Division, U.S. Department of Justice, presentation to *Compliance Week 2010* – 5th Annual Conference for Corporate Financial, Legal, Risk, Audit & Compliance Officers, May 26, 2010 available at <http://www.justice.gov/criminal/pr/speeches-testimony/2010/05-26-10aag-compliance-week-speech.pdf>.

4 Arthur M. Mitchell, former General Counsel of the Asian Development Bank (2003-2007), is based in White & Case's Tokyo office. He presented "Can we fight corruption successfully in Asia? What lawyers can do about it" at The Inter-Pacific Bar Association meeting held in Kyoto, Japan, on April 23, 2011.

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laws by criminalizing commercial bribery between private companies, a significant difference that creates additional liability risk under the Act in comparison to the FCPA. For example, a French or US company could be prosecuted in the UK for an act of bribery in China, even if the act was committed by an individual employee without the company's knowledge, so long as the company has an office or is registered to do business in the UK.

One defense a company can raise to an allegation of violating the Bribery Act is its previous implementation of adequate procedures to prevent bribery. Charlie is currently working with the compliance teams of numerous companies to create those procedures. In the event that misconduct does occur, he and his team will be conducting internal investigations and engaging authorities to resolve the matter, should it reach that point.

### China's new anti-corruption law

The Chinese government recently amended its Criminal Law to prohibit bribery of foreign officials. With this amendment, which became effective on May 1, China joined an expanding group of nations that prohibit such conduct and broadened its anti-corruption efforts beyond its own borders. Statements from China's Premier, Wen Jiabao, who has identified corruption by principal officials as a "primary task in 2011,"<sup>5</sup> suggest that enforcement of the new amendment will be a priority and its prohibitions must be taken seriously by corporations with operations in China.

The amendment prohibits individuals and corporations from providing "money or property to any foreign party performing official duties or an official of international public organizations" for the purpose of "seeking illegitimate business benefits." The amendment, however, provides little guidance on specifics such as the types of

conduct that might be considered a "bribe" and who might qualify as a "foreign official." This lack of clarity affords prosecutors a significant amount of discretion.

The new amendment will apply to companies organized under China's laws. Violations may result in "fines and a prison sentence of up to 10 years."

The head of White & Case's China practice, Xiaoming Li, remarks: "This amendment, if seriously enforced, would certainly help build China's position and reputation on the world stage, and on the back of its overseas investment and acquisition trail."

### Extraterritorial cross-over

So where do multinationals sit in terms of potential enforcement actions given the extraterritorial cross-over of the FCPA, the UK Bribery Act and China's new anti-corruption law?

We already know that prosecutions under the FCPA can result in millions of dollars in fines, amongst other penalties. The Siemens matter is the case in point – a US\$450 million fine described by Lanny A. Breuer as: "although quite substantial, [it] was a far cry from the advisory range of US\$1.35 to US\$2.7 billion called for in the Sentencing Guidelines"<sup>6</sup>.

Avon has reportedly cooperated with the DOJ and SEC to resolve its FCPA matter since the investigation began. The question is: will future cases involving alleged bribery of officials in China be subject to liability under several anti-corruption laws?

According to White & Case's Charlie Monteith: "There will clearly be overlap in anti-corruption enforcement between the US, UK and China. In terms of jurisdictional lead, the question of where to report will normally be resolved by negotiation at the starting point – engagement with the enforcement

agency where the offence takes place." Charlie was with the SFO when it signed a Memorandum of Agreement with China's enforcement authorities last year. The emphasis of the agreement was on intelligence sharing between enforcement agencies.

The definitive answer is that an entity may potentially face charges under the anti-bribery regimes of several jurisdictions. Prosecution in one jurisdiction for anti-bribery law violations does not preclude another jurisdiction from pursuing charges against an entity based on the same conduct, so long as the conduct properly falls within the jurisdiction of the nations' respective anti-bribery laws.

There are several examples of entities entering into settlement agreements with both US and UK enforcement agencies to resolve charges arising out of the same conduct. One notable case is that of BAE Systems plc, which agreed to plead guilty and pay US\$400 million to the DOJ and US\$47 million to the SFO to settle FCPA-related charges for activities in the Czech Republic, Hungary, Tanzania and Saudi Arabia.<sup>7</sup> The DOJ alleged that BAE Systems earned more than US\$200 million from contracts obtained through improper means. BAE Systems pled guilty to one charge of conspiring to make false statements to the US Departments of Defense and State. The government alleged that BAE Systems concealed and misreported corrupt payments made to foreign officials in lease applications and export license applications. BAE Systems' settlement with the SFO for accounting records violations is the largest SFO settlement in UK history.

Any organization under scrutiny by enforcement agencies of multiple jurisdictions is well advised to seek the best legal advice available, based on solid experience in all of the jurisdictions affected.

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<sup>5</sup> An Lu, *Chinese Premier renews call for fight against corruption*, Mar 25, 2011 available at [www.gov.cn/english/2011-03/25/content\\_1831956.htm](http://www.gov.cn/english/2011-03/25/content_1831956.htm) (last visited June 7, 2011).

<sup>6</sup> Lanny A. Breuer, *supra* note 3.

<sup>7</sup> See White & Case Client Alert, *2010: All Signs Point to a Record-Breaking Year of FCPA Enforcement*, Mar. 1, 2010, available at <http://www.whitecase.com/alerts-03022010/> (last visited June 7, 2011).

## Corruption in developing markets in context

An effective compliance and ethics program can help a corporation manage its risk of liability by preventing fraud and corruption in the first instance and identifying and remediating misconduct when it does occur. However, implementing such a program in developing markets presents challenges due to the types of corruption prevalent in such markets.

In order to address this, we first need to look at the nature of the problem.

### The cost of corruption to business

There are many estimates of the cost of corruption to businesses and economies. The World Bank estimates the figure at an extra 10% of the cost of doing business. The reality is that because the vast majority of corruption is kept secret, an accurate assessment of the true cost of corruption may not be possible.

But we all intuitively know that the direct and indirect costs are enormous. How we measure it depends upon how we define it.

While there are many definitions, acts of corruption may generally be placed into three categories.

- (a) In the narrowest sense, it is an official's appropriation of a public right for personal gain. This encompasses both petty corruption – such as a policeman shaking down a driver for a few dollars; as well as grand corruption – such as the President of a developing country demanding bribes to facilitate the construction of a major project.
- (b) A more robust definition is that of the United Nations Development Program (UNDP): the misuse of public power, office or authority for private benefit through:
  - Bribery
  - Extortion
  - Fraud

- Embezzlement
- Speed money (grease payments)
- Influence peddling
- Nepotism

- (c) An even more expansive definition might include entertainment and gift expenses incurred by businesses seeking to curry favor from other businesses or government officials.

### Laws and enforcement – a practical view

However defined, corruption exists in all countries today. In some places it is rather crude. In others, it is so sophisticated it is not even considered illegal.

Many countries have laws against corrupt acts like bribery, extortion, fraud and embezzlement, as discussed in the first part of this article. But the problem in many developing countries for multinationals is that even in clearly defined areas of illegal activity, there is a lack of enforcement.

For most corporations doing business in developing markets such as those in Asia, the primary problem, aside from reputational risk, involves the appropriation of bribes, the making of payments to senior officials in order to obtain legal concession rights, licenses or approvals and clearing goods through customs.

A direct correlation exists between petty corruption by police, judges, customs officials and tax collectors and the low salaries they are paid. Grand corruption is almost always directly related to the very structure of the political system that allows those who are in positions of authority to use corrupt payments to enforce the status quo.

President Aquino in the Philippines won the election last year in large part because of his stance against rampant corruption. Aquino used his position on corruption to encourage more foreign investment,

recognizing that “[y]ou cannot deal with a government where the right hand is offering a handshake while the left hand is trying to pick your pocket.”<sup>8</sup>

Tunisia and Egypt are the most recent examples of how both petty and grand corruption can lead to political instability.

### What can be done?

If we recognize the political nature of corruption, we must also recognize the political nature of anti-corruption efforts. In reality, this is why the problem is difficult.

International financial institutions such as the Asian Development Bank (ADB) and the World Bank, have devoted considerable efforts to reducing corruption in Asia.

It is interesting that their Charters require them to act in non-political ways – or at least rationalize their activities solely on economic grounds. Because of this constitutional requirement, they center on “governance” as a key development concept deserving prominence.

In his address to the IPBA, Arthur Mitchell stated: “In order to break the cycle of corruption, we need to recognize that there is a ‘market’ in corruption. That is, there is both a supply and demand side.”

Corporations doing business in Asia are on the supply side, as they are providing jobs, security and contributing to GDP.

They therefore must consider what tools are at their disposal to reduce the cost of “corruption demand.” These may include:

- (a) corporate codes of conduct
- (b) internal and external audits
- (c) publication and dissemination of anti-corruption policies
- (d) training of all employees from top to bottom
- (e) whistle blower protections and confidential “hotlines” for employees
- (f) enforcement of sanctions for violation of the rules.

<sup>8</sup> President Benigno S. Aquino, Speech at Opening of Infrastructure Philippines 2010: Investing and Financing in Public-Private Projects, Nov. 18, 2010, available at <http://ppp.gov.ph/2010/11/speech-of-president-aquino-during-the-ppp-conference-infrastructure-philippines-2010/> (last visited June 7, 2011).

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Moreover, senior executives, general counsels, heads of compliance and others should engage with experts in the field in order to stay abreast of the requirements of anti-corruption statutes in the country of their principal place of business, as well all other jurisdictions in which they conduct business.

**Collective action**

One of the most effective tools in addressing corruption is collective action. Corporations can benefit from the knowledge and experience of competitor corporations in evaluating anti-corruption efforts. Of course, any information sharing must be accomplished in compliance with relevant competition and antitrust laws and meetings must avoid discussion of commercially sensitive and non-public information. However, so long as antitrust considerations are properly accounted for, corporations may benefit from working with industry associations that could discuss best practices for managing compliance efforts under anti-corruption laws.

Some examples of industry associations working effectively in Asia include:

- **Food Industry Asia** consists of major food companies that strive to ensure that all laws and regulations governing the production, trade and marketing of food are feasible, practical and based on sound science.
- **Crop Life Asia**, focused on anti-counterfeiting, biotechnology, plant biotechnology and seeds strategy.
- **US-ASEAN Business Council**, an advocacy organization for US corporations in the dynamic Association of Southeast Asian Nations (ASEAN), is the only US organization to be given the privilege of being able to raise member company concerns in consultations with the ASEAN Finance and Economic Ministers as well as the ASEAN Customs Directors-General at their annual meetings.

Organizations such as these could provide members with valuable insight on compliance practices and should consider putting anti-corruption on their agendas so that anti-corruption can be dealt with from all angles, not only from a regulatory perspective.

Corporations should also be aware of the opportunities that may come about from working and cooperating with international financial institutions such as the Asian Development Bank, specifically in the area of institutional development in Asian countries. An example might be funding for training programs for government officials in customs and tax collection or public support for higher salaries for these officials.

In conclusion, while compliance requirements are on the rise, multinationals must continue to do their best to comply with the rules that regulate business operations in Asia. In terms of internal processes, a lot comes down to the education of employees – so that they can distinguish good behavior from bad. Nonetheless, cultural norms will always come into play and that is one of the key challenges of doing business in developing markets.

An effective compliance and ethics program can go a long way to preventing fraud and corruption. This, along with partnerships among businesses, government watchdogs (ombudsmen) and international financial institutions such as the Asian Development Bank, and efforts to promote good governance, are most likely to level the playing field such that corrupt conduct is no longer permitted or rewarded.