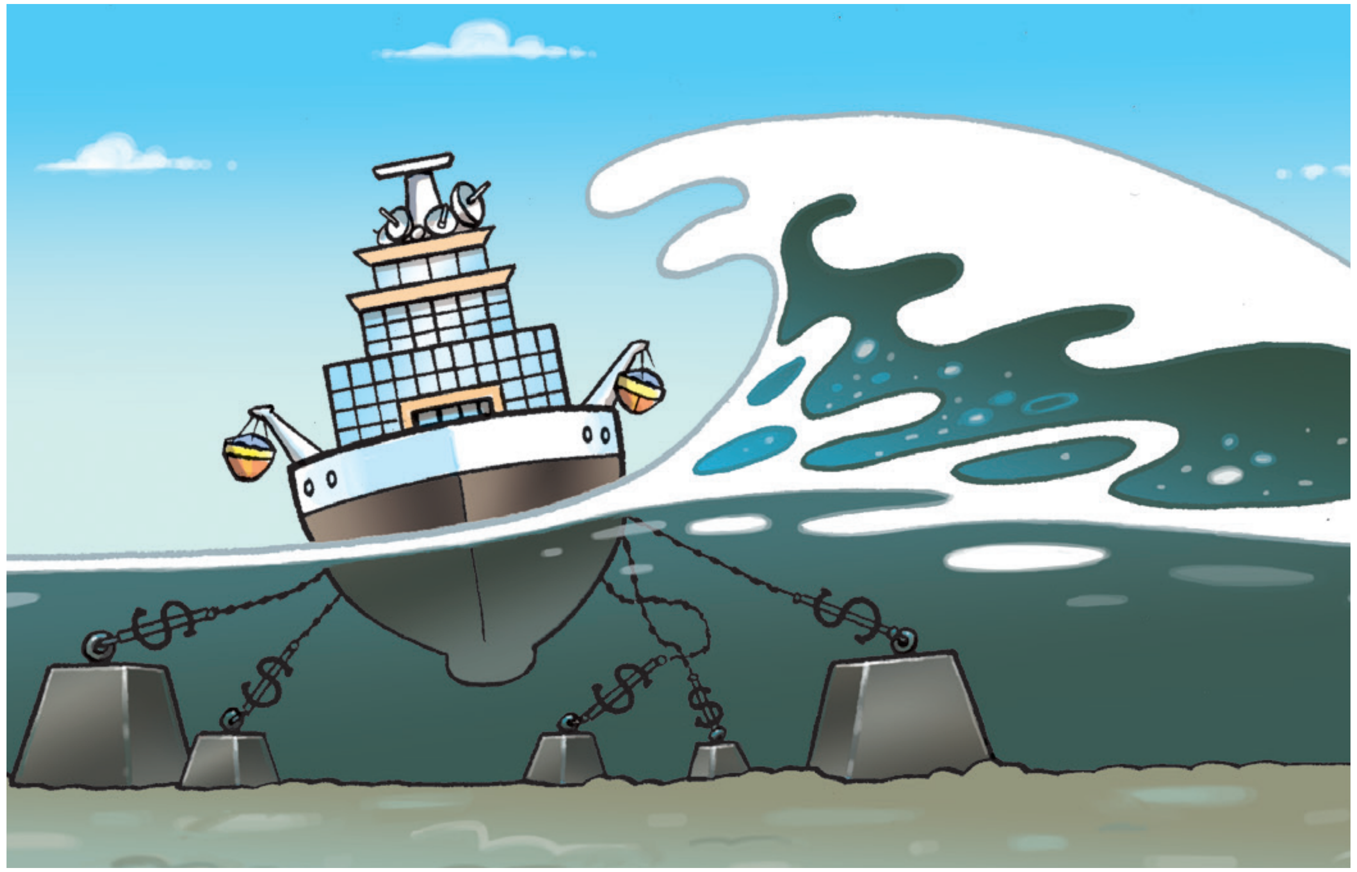

THE RISING RISK TIDE

The Increasingly Global Hazards of Doing Business with State-Owned Enterprises

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Compliance professionals have long known that doing business with state-owned enterprises poses a potential risk under the Foreign Corrupt Practices Act (FCPA). Under the FCPA, the term "foreign official" includes officers or employees of a department, agency, or instrumentality of a foreign government.

Although not explicitly defined in the statute, since the FCPA's enactment in 1977, the United States Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) have interpreted the term "instrumentality" to include certain state-owned and state-controlled enterprises. Indeed, the second ever FCPA case charged by the DOJ, in 1982, involved bribes paid to officials of Pemex, the Mexican national oil company, and the most recent DOJ FCPA resolution, against Alstom SA and several of its subsidiaries in December 2014, involved tens of millions of dollars in bribes paid to officials of state-owned electricity companies in countries such as Indonesia, Egypt, and Saudi Arabia. Recently, a federal appellate court agreed with the DOJ's and SEC's interpretation of "instrumentality" holding, in *United States v. Esquenazi*, that officers and employees of Haiti's national telecommunications company were "foreign officials" for purposes of the FCPA when they received bribes from a Miami-based telecom company. Thus, for companies within the jurisdiction of the FCPA, doing business with state-owned enterprises has posed, and continues to pose, a real risk from a US law enforcement perspective.

But what about the risk of enforcement by authorities in the state-owned enterprise's home jurisdiction? How likely is it that a bribe paid to an officer or employee of a state-owned enterprise will be detected, investigated, and prosecuted by domestic law enforcement authorities? To be sure, many countries include employees of state-owned enterprises in their ethics and bribery laws, meaning that such a risk was at least possible. But whether domestic authorities would enforce those laws as vigorously as US authorities enforced the FCPA was, in many places and at many times, unclear. Recent anti-corruption campaigns in China and Brazil suggest, however, that this might be changing in several important markets.

Enforcement Ramps Up Outside the US

In April 2015, China prosecuted the former Chairman of the China National Petroleum Corporation for his allegedly corrupt activities, which included accepting millions of dollars in bribes while working at that state-owned enterprise. This prosecution appears to be part of a wider anti-corruption campaign aimed at the country's largest state-owned enterprises. The widespread campaign seems to be gathering momentum as Chinese authorities recently announced that the Assets Supervision and Administration Commission has appointed seven audit companies, including a US Big Four accounting firm, to investigate the offshore holdings of the major state-owned enterprises.

Meanwhile, beginning in early 2014, Brazilian law enforcement authorities, as part of "Operation Car Wash," have taken dead aim at alleged corruption in Petrobras, that country's national oil company. According to an internal audit led by the former Minister of the Brazilian Federal Supreme Court, some 2,000 Petrobras employees are now under investigation. The government's crackdown on corruption, however, does not seem to be focused only on Petrobras. At least one Brazilian official has noted that Petrobras' allegedly corrupt "business model" is also followed in other parts of Brazil's public sector.

These crackdowns on alleged corruption in state-owned enterprises in China and Brazil suggest that multinational corporations doing business with these entities may be facing an increased risk that their dealings will be scrutinized not only by US authorities, but also by the domestic law enforcement authorities where those entities are based.

Not All Bad News for Companies

Increased vigilance by authorities around the world has resulted in mounting fear by multinational companies of having to answer to foreign regulators. Companies operating in countries where anti-corruption enforcement is on the rise worry that conduct that previously may have gone undetected will now surface or that—even when there is no improper conduct—the company will nonetheless be swept up in a widespread public scandal.

While companies have good reasons to be concerned, from a compliance perspective, the rise in global enforcement actually presents significant opportunities for positive change. For one, there is the harmonization of laws across the globe. While laws in different countries will inevitably vary in certain details, the growing trend is for countries looking to enhance their anti-corruption enforcement to pass conceptually consistent laws. This consistency means that a well-designed corporate compliance program should be able to address the patchwork of global laws. For a company, this makes the implementation of a compliance program easier in that it can roll out a uniform program that applies across its global operations. The rules are the same no matter where the employees are located. It may be that specific procedures to implement the program will need to take into account the varying legal requirements. However, companies should be thinking about their overarching anti-corruption compliance program as a comprehensive global program, not just from the perspective of any one particular jurisdiction.

Having anti-corruption enforcement no longer be a "US problem" also makes compliance easier to sell to the company's foreign operations. Historically, companies implementing an anti-corruption compliance program have struggled with getting foreign employees to buy into the notion that they need to comply with a US law. Why would a manager in Brazil who is conducting business in Brazil and making payments with Brazilian real be concerned about liability under US law? But the company's policy prohibiting such conduct will seem much more relevant for a manager who sees that the same conduct that would be prohibited under US law is also prohibited—and enforced—under Brazilian law. In this way, implementation of the company's anti-bribery compliance program will likely be more effective.

There should be real incentives for companies that decide to tackle slavery in the supply chain. It's unrealistic to expect that they will spend money to map their supply chains if competitors who choose to do nothing can easily get away with it and rake in more profits.

Building Awareness of Risks Posed by State-Owned Enterprises

There are additional steps that companies can take to address the increasing risk of domestic supervision of state-owned enterprises. Companies should ensure that their policies clearly provide that employees at any level of state-owned enterprises are to be treated as "officials" and thus that any rules applicable to government officials apply to them. Companies should also develop mechanisms to educate employees as to which companies are state-owned. This can be done, for example, via a company look-up tool, by attaching to the compliance policy a list of state-owned enterprises with which the company does business, through employee training programs, and with assistance from the legal department.

To the extent that companies were operating under the assumption that the risk of dealing with state-owned enterprises was lower than dealing with government agencies or that the risk was limited to the FCPA, those assumptions—if ever viable—are no longer. Effective compliance professionals can use this development to increase the quality and effectiveness of their compliance programs.

Author Biographies

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