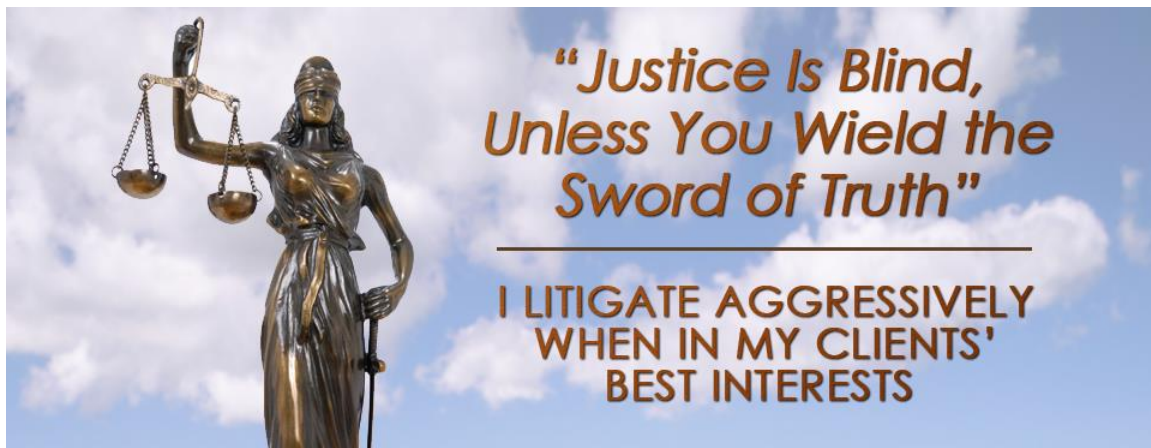




FOREIGN CORRUPT PRACTICES ACT AND ANTI CORRUPTION LAWS IN CHINA AND THE UNITED STATES



CHINA: BUSINESS CULTURE AND RULE OF LAW

BUSINESS CULTURE

- “Guanxi” — With the long influence of Confucianism in East Asia, the person you are isn't just who *you* are individually, but the *relationships* that you're a part of. It makes sense, then, that guanxi is such a significant part of professional life in China.
- But, a business culture – guanxi – that encourages a tradition of favors, nepotism, and connections can lead to infractions of government regulations.
- Foreign businessmen frequently get hit with requests for the “red envelopes” that are “necessary to doing business in China,” quoted in *China Law Blog, China Law for Business,*” Dan Harris on July 12th, 2012.

- **“The payment of bribes to some officials followed by the eventual decision to stop paying bribes to anyone led to “unfortunate delays” and “misunderstandings” from the unbribed (or insufficiently bribed) officials’ departments.” In every instance, a foreign businessperson giving grease payments to speed things up, [found instead that] things have taken significantly longer.” *China Law Blog, China Law for Business,*” Dan Harris on July 12th, 2012**

PHILOSOPHY OF TRUTH

According to cultural philosophers, Westerners and East Asians have had contrasting views about the concept of truth and how it works for thousands of years — and it shows up in present-day psychology.

It all goes back to the cradles of two civilizations: ancient Greece and ancient China.

It comes down to two different "laws":

- The Greeks followed the "law of the excluded middle," which states that if two people are debating, then one of them must be exclusively right and the other exclusively wrong.**
- The Chinese followed the "doctrine of mean," which states that if two people are debating, then they're probably both partly right and partly wrong — the truth probably lies somewhere in the middle.**

**These things have deep roots:
Agricultural economy and centralized control of society in China versus
Hunting, herding, fishing, grapes and olive oil in Greece**

The doctrine of the mean dates back to Confucius, who lived some 2,500 years

ago. It is "widely considered as the highest ideal in Confucianism." Li-Jun Ji, Albert Lee, and Tiejuan Guo, *The Oxford Handbook of Chinese Psychology*

RULE OF LAW

Given these philosophical differences, what role should the rule of law play?



VIGILANCE

“A great deal of facts tell us that the worse corruption becomes, the only outcome will be the end of the party and the end of the state! We must be vigilant!” *Xi Jinping, (11/19/2012)*

In the political arena in China, "the rule of law" is highly topical. The Fourth Plenary Session of the 18th Central Committee of the Communist Party of China, held from Oct. 20 to 23, 2014, decided comprehensively to advance the rule of law in China.



Xin Chunying, Vice-Chairperson of Legislative Affairs Commission of China's National People's Congress, Has Endorsed Rule of Law

The Plenary decision has seven relevant parts, including the decision to:

- **Set the general target of rule of law and to improve the system of laws;**
- **Improve constitutional implementation to promote administration by law;**
- **Promote respect for law in government and to safeguard judicial justice;**
- **Improve judicial credibility and to promote public awareness of the rule of law;**
- **Enhance the construction of a law-based society;**
- **Improve the professional competency of law-related personnel;**
- **Refine the CPC's leadership in promoting the rule of law.**

CHINA'S ANTI-CORRUPTION ENFORCEMENT: THE NEW REGIME AND CHANGES TO ANTI- CORRUPTION LAWS AND ENFORCEMENT

FOUR ANTI-CORRUPTION CHINESE ENFORCEMENT AGENCIES

1. Central Commission for Discipline Inspection (Main Agency)



2. Supreme People's Procuratorate (Prosecutor's Office)



3. State Council (Government Agencies)



- **Ministry of Supervision**
- **State Administration for Industry and Commerce (SAIC)**

4. Public Security Bureau (Law Enforcement)



SELECTIVE ENFORCEMENT

- **Confucian Model of Authoritarian Control:**

“While a lot of things are nominally illegal, within accepted limits the law can be irrelevant, so long as the target does not ‘rock the boat’ of the authoritarian state.” *Forbes Magazine, “How China's Culture Of Corruption Threatens U.S. Sovereignty,” (August 25, 2013)*

RECENT CHANGES TO ANTI-BRIBERY LAWS AND POLICIES INCLUDE:

- **Limits on party officials**
- **Increased criminal prosecutions**
 - **Incentives for confessing to bribery**
- **A new five-year plan**
- **Asset disclosure for public officials—Resistance**

UNITED STATES ENFORCEMENT OF THE FOREIGN CORRUPT PRACTICES ACT (“FCPA”) IN CHINA

US REGULATORY AGENCIES

DEPARTMENT OF JUSTICE



**Lanny A. Breuer, Assistant Attorney General, Remarks before
the 24th National Conference on the Foreign Corrupt
Practices Act (Nov. 16, 2010):**

**“[O]ur FCPA enforcement is . . . getting stronger. I am
aware that, for some of you, as we have become more
aggressive, *you have become more worried . . . I want to
tell you . . . that you are right to be more concerned*).**

**DOJ’s aggressive enforcement posture is characterized by
expansive interpretations of the Act that are a function of
prosecutorial charging discretion, industry sweeps, ever
increasing sums paid to settle and earn cooperation credit
and demands for longer prison terms.**

SECURITIES AND EXCHANGE COMMISSION



The United States SEC is expected to impose "blockbuster" fines under the Foreign Corrupt Practices Act (FCPA) on companies bribing foreign officials this year, with China a likely target of US investigations, lawyers say.

"US enforcement authorities have stated there are a number of very large settlements in the pipeline," said an SEC staff attorney. "Given the attention paid to China in recent years, it is a safe bet some of those large settlements will involve conduct in China."

The increased intensity over China by the SEC sprang from the SEC's action in 2014 to bar for six months of the mainland affiliates of the Big Four accounting firms from auditing US-listed Chinese firms formed through reverse mergers. "If US authorities are suspicious of the auditors, they will be suspicious of Chinese companies listed in the US."

Further, China's reputation as an emerging world economy has garnered the attention of US law enforcement, including the US Securities and Exchange Commission and the US Department of Justice, which has increased its prosecution of violations of the Foreign Corrupt Practices Act.

WHAT IS THE UNITED STATES FOREIGN CORRUPT PRACTICES ACT?

Congress enacted the U.S. Foreign Corrupt Practices Act (FCPA or the Act) in 1977 in response to revelations of widespread bribery of foreign officials by U.S. companies to obtain business. The Act was intended to halt those corrupt practices, create a level playing field for honest businesses, and restore public confidence in the integrity of the marketplace.

Here are the words of the United States Senate at the time of the Act's adoption:

“Corporate bribery is bad business. In the free market system in the United States, the sale of products should take place on the basis of price, quality, and service. Corporate bribery is fundamentally destructive of this basic

tenet. Corporate bribery of foreign officials takes place primarily to assist corporations in gaining business. Thus, foreign corporate bribery affects the very stability of overseas business. Foreign corporate bribes also affect the domestic competitive climate in the US when domestic firms engage in such practices as a substitute for healthy competition for foreign business.”

The FCPA has two topic areas:

- **Anti-Bribery Provisions: The FCPA prohibits corruptly giving, promising, or offering anything of value to a foreign government official, political party, or party official with the intent to influence that official in his or her official capacity or to secure an improper advantage in order to obtain or retain business.**
- **Accounting Provisions: The FCPA also requires issuers to maintain both accurate**

“books and records” and a system of effective internal accounting controls.

WHY RELEVANT TO CHINESE BUSINESS?

Several factors make China an environment in which FCPA violations are likely to occur and serve as a trap for the unwary:

- China’s unique political and economic system,**
- China’s business culture in which many forms of corruption (at least petty corruption) have been tolerated – known as “Guanxi,” and**
- China’s continuing attractiveness as a place to do business for multi-national corporations (“MNCs”).**

➤ **Wholly Owned Subsidiaries (Foreign Direct Investment)**

➤ **Joint Ventures created through combined investment capital and technology (usually 60% foreign, and 40% PRC SOE).**

• **Aggressive (and untested) interpretations by US Department of Justice**

HOW CAN THE UNITED STATES ASSERT “JURISDICTION” OVER ACTS IN CHINA?

• **“Issuers”**

➤ **Term of art under Section 30A of the Securities Exchange Act of 1934 (the “Exchange Act”)**

➤ **ADRs**

- **”Non-Issuer” Domestic Concerns.**
 - **Companies and Partnerships -- any corporation, partnership, association, joint stock company, business trust, unincorporated organization or sole proprietorship that is either (a) organized under the laws of the United States or any individual state, or (b) has its principal place of business in the United States.**

 - **Persons -- any person who is either (a) a citizen, national or resident of the US, or (b) an officer, director, employee, agent or stockholder, acting on behalf of a domestic concern, even if that person is a foreign national, foreign stockholder, or foreign company.**

- **Territorial Jurisdiction**

Since 1998, the anti-bribery provisions of the FCPA have applied to foreign persons and foreign non-issuer entities that (directly or through an agent) engage in any act in furtherance of a corrupt payment (or otherwise offer, promise, or authorize any such payment) while in any territory of the United States.

•Other Jurisdictional Conduct Inside and Outside the United States Involving the Use of an Instrumentality of Interstate Commerce

➤The FCPA's anti-bribery provisions can apply to conduct inside and outside the United States merely by use of the United States mails or "any means or instrumentality of interstate commerce."

➤Money flows through a US Bank

Statoil Case

Despite the conduct involving a foreign corporation's bribery payments in Iran, and with no immediately apparent connection to U.S. jurisdiction, and even though Norway had already taken enforcement action, US DOJ commenced enforcement action. The US government included in the DPA details about how Statoil had transferred \$5.2 million to its consultant's bank account in Switzerland via two bank transfers through US bank accounts. The Statoil employee did not even know that the money was going through the US banks.

➤ Agency Theory -- the DOJ has obtained jurisdiction over foreign persons and entities under the agency theory that the foreign

national was an “agent’ of the US subsidiary and thus a “domestic concern” under the FCPA.

•Conspiracy and Aiding and Abetting the FCPA Violation

A foreign national or company may also be liable under the FCPA if it aids and abets, conspires with, or acts as an agent of, an issuer or domestic concern, regardless of whether the foreign national or company itself takes any action in the United States.

WHAT DOES FCPA PROHIBIT?

First -- Anti-Bribery:

•General: prohibits corrupt payments to foreign officials for purposes of *obtaining or retaining business*

• **Business Purpose**

➤ **Statute**

Payments intended to induce or influence a foreign official to use his or her position “to assist ... in *obtaining or retaining business* for or with, or *directing* business to, any person.”

➤ **Examples**

- [?] **Winning a contract**
- [?] [?] **Influencing the procurement process**
- [?] [?] **Circumventing the rules for importation of products**
- **Reducing or eliminating customs duties**
- [?] [?] **Gaining access to non-public tender information**
bid
- [?] [?] **Evading taxes or penalties**

- **☐☐ Influencing the adjudication of lawsuits or enforcement actions**
- **☐☐ Obtaining exceptions to regulations**
- **☐☐ Avoiding contract termination**

➤ **Exception – Facilitation (Grease)**
Payments [See McKenna Aldridge PP, at 18-21]

Payments to non-discretionary, ministerial activities performed by mid- or low- level foreign functionaries to perform routine governmental acts

Examples:

- **Processing governmental papers, such as visas and work orders;**
- **Providing police protection, mail pickup and delivery, or**

scheduling inspections associated with contract performance or inspections related to transit of goods across country;

- **Providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration**

•FCPA Elements Unique to China

➤ **PRC government, department or agency**

PRC Officials

Ministry Heads (e.g., State Council) and their officers

Public Security Bureau (Law Enforcement)

➤ “Instrumentality” of Chinese Government

Any entity owned (in whole or in part) or controlled by Chinese government

SOEs and SCEs

**Effect of Privatization ?
Effect of Control by PRC**

All important sectors (e.g., banking, telecommunications, steel production and manufacturing, oil and gas exploration, health care and pharmaceutical, electricity and water supply, and train and air travel)

Question of Fact; Judge will order case to trial

➤ Who is a “Foreign Official”

Government Officials

Officers, Employees of SOEs or SCEs

E.g., doctors and laboratory personnel

DPC (Tianjin) Co. Ltd

Officers or employees of JVs

• Anything of Value

➤ The statute prohibits the corrupt “offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization of the giving of *anything of value* to” a foreign official. The words “anything of value” will include not only cash

payments (whether dubbed consulting fees, commissions, or forms of “case fees” charged by law firms that hire private investigators), but also travel and entertainment expenses (e.g., tickets to sporting events) and expensive gifts (e.g., watches).

➤The FCPA does not contain a minimum threshold amount for corrupt gifts or payments. The statute contains an exception for “reasonable and bona fide” expenditures if they are directly related either to (a) the promotion, demonstration, or explanation of products or services, or (b) the negotiation, execution, or performance of a contract with a foreign government or agency. Examples include payment of taxi fares, reasonable entertainment expenses (e.g., bottles of wine and dinners), and company

promotional items (e.g., pens). Further, travel and expenses paid for government officials to visit company facilities, receive training, or attend meetings are not likely to trigger enforcement action. But, “world tours” through Paris, Dubai, Beirut and New York City en route to the company’s plant are prohibited. The exception exists so that companies can “facilitate” appropriate business relationships with foreign officials in the course of conducting business.¹

➤ Providing valuable student internships to family members of foreign government officials affiliated with a sovereign wealth fund. [BNY Mellon Pays \$14.8 mm]

¹ Under Chinese law, Chinese (PRC) government officials (but not non-PRC officials) who receive gifts in excess of RMB200 (\$US23) are required to turn the gifts over to their supervisors. Gifts of cash and securities are strictly prohibited.



“The FCPA prohibits companies from improperly influencing foreign officials with ‘anything of value,’ and therefore cash payments, gifts, internships, **or anything else** used in corrupt attempts to win business can expose companies to an SEC enforcement action,” said Andrew J. Ceresney, Director of the SEC Enforcement Division. “BNY Mellon **deserved** significant sanction for providing valuable student internships to family members of foreign officials to influence their actions.”

• Knowledge

➤ ***Actual* knowledge of prohibited conduct is not required**

- Knowledge is “awareness,” which can be *imputed* where factual information possessed by company or person indicates a “high probability” that improper conduct may result or has occurred
- “Willful blindness” and “conscious avoidance”

•Corrupt Intent

- An *intent or desire to wrongfully influence* someone:

“The word ‘corruptly’ is used to make clear that the offer, payment, promise, or gift, must be *intended* to induce the recipient to *misuse* his official position; for example, *wrongfully* to direct business to the payor or his client, to obtain preferential legislation or regulations, or to induce a foreign official to fail to

perform an official function.”

➤ **Attempts**

➤ **Business Culture and Local Laws**

Written law or regulation

“Guanxi”

**Common illegal practices are
not lawful**

**Effect of China’s anti-corruption
initiatives**

**Effect of Sweden’s anti-
corruption laws**

**Second – Accurate Books and Records,
and Proper Internal Accounting
Controls**

**Of the more than 50 FCPA actions the
SEC has brought in the last five years,**

approximately 15 percent have been based solely on internal controls or books and records violations. Until the BHP Billiton case, however, only three of the companies targeted have had to pay penalties, and each of those amounted to \$300,000 or less. In BHP Billiton, the settlement announced May 26, 2015, the SEC's fined the company \$25 million, which is larger than all other previous internal controls cases, even those where millions of dollars were disgorged, and even though there was no allegation of bribery.

•To Which Companies Does SEC Law Apply?

“Issuers”

•What Does SEC Law Require

➤Make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect

**the transactions and dispositions
of the assets of the issuer**

➤ **All *transactions* must be executed
in accordance management's
general or specific authorization**

➤ **Transactions are recorded as
necessary to:**

**Permit preparation of *financial
statements* inconformity with
GAAP or other criteria
applicable to such statements,
and**

**Maintain *accountability* for
assets**

➤ ***Access* to company assets**

**Permitted only pursuant to
management's general or
specific authorization, and**

Recorded accountability for assets is *compared* with existing assets at reasonable interval and timely action taken for any differences

•No person shall *knowingly* circumvent or knowingly fail to implement a system of internal accounting controls or knowingly falsify any book, record, or account

- **Criminal Intent, including “conscious avoidance”**
- **Negligence – fraud and non-fraud**
- **No “sleep walking”**

•Billiton Case (Beijing Olympic Games)

On May 25, 2015, BHP Billiton, an Australian mining company and the largest mining company in the world, agreed to pay \$25 million to settle SEC charges for failing to have a proper system of internal

accounting controls in place to prevent the heightened risk of bribery when it paid for trips government officials (most from Asia and Africa) to attend the 2008 Beijing Olympic Games. The company invited 176 government officials and employees of SOEs to attend the Olympic Games at the Company's expense, and ultimately paid for 60 government officials and their spouses, paying as much as \$16,000 for each official and their guests. Travel packages included Olympic event tickets, stays at luxury hotels and sightseeing excursions. The SEC brought the case even though there were no underlying charges of any improper or *quid pro quo* payments, and the SEC never alleged that Billiton gained any specific contract or other business advantage. .



"BHP Billiton footed the bill for foreign government officials to attend the Olympics while they were in a position to help the company with its business or regulatory endeavors. The company recognized that inviting government officials to the Olympics created a heightened risk of violating anti-corruption laws, yet the company failed to implement sufficient internal controls to address that heightened risk." Statements of Andrew Ceresney, the SEC's Director of Division of Enforcement.

ROBUST COMPLIANCE PROGRAM

DOJ and SEC insist on a “robust” compliance program designed to stop problems from occurring

The company must customize its compliance program to fit the individual needs and subject matter of the business with which it is engaged. There is no “one-size-fits-all program”



*Scott W. Friestad
Associate Director
SEC Enforcement Division*

“There are significant consequences for public companies that fail to implement strong compliance programs and prevent corrupt payments to government officials.”

“Designed Carefully, Implemented Earnestly, and Enforced Fairly”

“Tone at the Top”

Global Compliance Checklist [MLA Booklet, at 10-11]

Due Diligence

- **Consultancy Agreements with Agents, Subagents and other Third Parties [MLA Booklet, at 5-8]**

- **Know who they are, what they are up to, whether any of them are full or part time employees of the foreign government or SOE, and**

how the terms of any consulting agreement may differ from standard company agreements

➤ **Consultant Information Package to Management**

➤ **Drafting a consultancy agreement – terms and representations**

- **M&A – how much due diligence is possible**

Policies Reflect Culture and Local Law

- **“Guanxi”**
- **Take account of China’s Anti-Corruption Law**

Code of Ethical Conduct

System of Internal Accounting Controls

- **Defined:** In its broadest sense, internal controls involve everything that controls risks to an organization. It is a means by which an organization's resources are directed, monitored, and measured. When defined in the context of accounting and auditing, it is a process for assuring achievement of an organization's objectives in operational effectiveness and efficiency, reliable financial reporting, and compliance with laws, regulations and policies. Thus, it plays an important role in detecting and preventing fraud and protecting the organization's assets and resources.

- Irregularities in invoicing, size of payments, method of payments, payments to third parties,

- **Internal Audit Review**

Protocols, Procedures, Education and Training

- **Educational and Training materials should identify “risks” the company is likely to confront**
- **Teach and reinforce proper procedures for reporting suspicious areas or “red flags”**
- **Employee “hotline”**

On the Ground Implementation

- **Designated FCPA Officer on Location**
- **Travel and Entertainment Policies**

- **Policies over Facilitation Payments**

- **Controls over Agents, Subagents, “middlemen,” and other 3rd Parties -- know who they are and what they are up to**

Credit When Problems Do Occur

- **Internal Investigation and Remediation to ensure that:**

- **Know what happened - Full Extent of Problem has been Identified**

- **Breakdown in Compliance Understood**

- **Wrongdoing has Ceased**

- **Evidence is Preserved – Document Retention**

- **New Compliance Procedures**
- **Improved Training of Employees**
- **Disciplinary Action Against Employees**
- **Disclosure to Government**
 - **“Candid, Complete and Timely Cooperation” [Leslie Caldwell, Assistant AG in Charge of DOJ Criminal Division (May 2015)]**
 - **Determine Which Jurisdictions Apply and Their Respective Interests**
 - **Cooperation with Government (PetroTiger Ltd, 2015)**

- **Ability to Answer Government's Questions**
- **Provide results of any Internal Investigation (Hyperdynamics Corporation)**
- **Little Privacy Protection**
- **Provide summaries of witness interviews**

- **Client Representations – company, officers or employees? Government “sensitive” to conflicts of interest.**

- **What “credit?”**

- **Declination or Settlement**
- **NPA or DPA**
- **Reduced Fines, CMPs or Disgorgement**

New Compliance Counsel Will Assess Effectiveness of Corporate Compliance Programs

In August 2015, the DOJ announced that it is hiring a compliance counsel to assist DOJ prosecutors in assessing the effectiveness of companies' corporate compliance programs. The announcement of this new hire underscores the fact that DOJ is placing significant and increased importance on the effectiveness of corporate compliance programs when assessing whether or not to charge corporations for failing to detect or prevent criminal wrongdoing by their employees.

REMEDIES AVAILABLE TO US GOVERNMENT

Criminal

- **Declination (disclosure, cooperation, and remediation)**

PetroTiger, Ltd (2015)

- **Fines and Incarceration**
 - **Individuals: \$100,000 and 5 years in jail**
 - **Company: Up to \$2 million per violation**
 - **Alstom S.A (\$772 million)**
- **Plea Agreements**
 - DPAs (PBSJ Corp)**
 - NPAs (Ralph Lauren)**

- **Independent Compliance Monitors**

Civil

- **Injunctions**
- **Civil Monetary Penalties**
- **Officer and Director Bars**

Collateral Consequences

- **Suspension or debarment from contracting with the federal government,**
- **Cross-debarment by multilateral development banks, including Overseas Private Investment Corporation**
- **Barred from receiving State Department export licenses, or**

**suspension or revocation of certain
export privileges.**

- **Barred from programs under CFTC**
- **Issuers will also be required to disclose the violations and may be disqualified from using various rules and exemptions when raising capital.**
- **Shareholder derivative suits against officers and directors.**