Effective Programmes to Combat Corruption
vs Programmes Intended Primarily To Satisfy SEC, DOJ or SFO

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Abstract

Most “how to kits” for anti-corruption programmes provide a “check the boxes” type of programme that do not often address many of the real issues regarding avoiding corruption. Training of employees on what constitutes corruption (often with focus on what are the maximum amounts for gifts, dinners, entertainment) is really not addressing the crucial issues. This article is based upon research conducted by the author with companies who claim to have robust anti-corruption programmes.

In order for an anti-corruption programme to have serious ability to stop corruption, the following types of issues must be addressed:

1. How to communicate with employees who may not understand English well (assuming that is the main language of the company) or may have very low levels of education and sophistication. How to impress upon them the importance of non-bribery when this is part of their cultural norm, and they will be likely not be penalized for bribing.

2. Looking at compensation for all employees to ensure that they are not financially penalized personally if they do not bribe.

3. Rewarding employees for whistleblowing regarding corruption, not just within the enterprise, but also, reporting demands for bribes by the host government officials as well as corruption by competitors. Without compensation for doing so, there is no reason for an employee to engage in advising of bribe demands.
4. Maintaining data bases for corruption demands, and using those as a tool to prevent corruption.

5. Corporate anti-corruption programmes also need to be wider than is the norm currently. The company must look at the various tools that are available to reduce both demands for bribes from government officials, as well as reducing the risks inherent to a company in refusing to pay a bribe. These tools include political risk insurance and financing programmes through powerful financiers.

1. Introduction

Companies are being consistently advised that they must develop an anti-corruption programme in order to prevent the company from running afoul of the anti-corruption laws, such as the FCPA in the USA, the CFPOA in Canada, the UK Bribery Act and other similar domestic legislation. This article will examine the question of whether these programmes are effective at combatting corruption, and suggest methods of improving such programmes.

2. Research Upon Which This Article Is Based

This article is based upon interviews with over 100 companies (primarily Canadian) as part of the course that the author teaches on international legal business risk for the Executive MBA programme at Athabasca University in Canada. These interviews consisted of in depth discussions with the students (all of whom are middle to senior management in their respective companies) regarding their company views and policies on issues of corruption and were conducted from June 2012 to August 2015.

One of the findings of the research was that many companies develop an anti-corruption programme that is primarily focused on “plausible deniability” rather than on actually stopping or reducing corruption within the company. The main goal is for the company to be able to demonstrate that it has a “robust programme” in place, and therefore, any corruption was engaged in by a “rogue employee” and the company should be forgiven for that. Thus, their understanding is that either the company will
be exonerated if corruption does appear, or will be given a very light punishment, because of their robust anti-corruption programme.

Rarely did companies that were canvassed worry about whether their programme will actually prevent or reduce corruption – the prime concern was the protective elements of the “robust programme” as they relate to possible prosecutions; there was a general consensus that in many developing states, it is quite impossible to function without engaging in some forms of corruption, and the prime purpose of the anti-corruption programme is to be used as a shield to protect in event that these acts of corruption come to the attention of the authorities in the home state.

Many of the companies confirmed that their Chief Compliance Officer had very little training or experience with issues related to compliance with anti-corruption – often the position was given to someone in the company merely to “show” to the outside world that there was someone in charge of such issues for the company.

3. Content of Existing Anti-Corruption Programmes

Most corporate programmes that were discussed in the interviews consisted largely of seminars or webinars with employees, explaining the basics of corruption issues, emphasizing such issues as warning employees against engaging in gift giving or dining with public officials or entertainment expenses that are outside the parameters permitted by the law and/or by the rules set forth in corporate policies.

One of the most shocking revelations was that some companies merely post their anti-corruption programmes on the corporate intranet, leaving it to the employees to view at their leisure. Yet, many of these companies have been touted in the media as being the models for others in anti-corruption training. (The reader can now understand why revealing the names of the corporations in this article is not permitted by the terms of the interview agreements – Chatham House Rules apply).

Often, the company requires its employees to “certify” that they will abide by the corporate policies on corruption, as a condition of employment; no effort is made by the company to determine the level of understanding employees have of those policies, prior to requesting them to “certify.”
4. What Should Be Added to Conventional Anti-Corruption Programmes?

Based upon the interviews, the following are some of the suggested recommendations for corruption programmes whose prime goal is to reduce corruption, not just reduce risk of punishments for corruption by authorities:

4.1 Compensation Programmes Must Be Structured to Reduce Corruption

Structuring compensation packages for all employees to ensure that they are not financially penalized personally if they do not bribe is a crucial element. While this is often considered in regard to top management, with potential for claw-backs for failure to control corruption, these concepts are not usually applied to those employees who are on the frontlines and face corruption demands regularly.

As a typical example of current corporate compensation practice, most companies will remunerate employees on the basis of “performance” which is usually defined exclusively or largely on financial indicators. For example, in sales departments, if the employee achieves a certain sales target, the compensation will increase via bonuses. Conversely, if the target is not achieved over a period of time (perhaps 4 consecutive quarters) then the employee may be faced with risk of dismissal.

In this circumstance, the employee is aware that while there are corporate policies against corruption, failure to achieve a sales target as a result of refusing to pay a bribe (frequent in situation where the company is engaged in government procurement projects) will result in immediate and certain loss of bonuses and perhaps loss of job. If he pays the bribe, there may be some (indeterminate) risk of negative repercussions to him in the future but that is highly speculative. The employee, therefore, is bearing most of the risks in relation to compliance with the anti-corruption policies personally. Given this scenario, can we realistically expect that the employee will refuse to pay required bribes, when this will result in certain financial detriment to him, balanced against a highly speculative risk of some negative repercussions to him in the future? Yet, that is the exact position that most employees are put into by a compensation package that rewards financial performance. It is not reasonable to expect that the employee will perceive that his obligation to comply with company policy against corruption will outweigh the risks that he will personally bare if he complies with that policy.
Thus, companies need to restructure compensation packages if they want to reduce corruption. Compensation packages can often be recast to reward non-financial goals or to reduce the emphasis on financial targets.

A recent article *Stop Paying Executives for Performance* (Cable 2016) written by faculty at the London Business School suggests that rewarding executives for performance is counter-productive. The authors suggest that rewarding learning is more beneficial to the company in the long term than rewarding financial targets being achieved. This article challenges what has been “conventional wisdom” regarding the importance of motivating employees through incentives for financial performance.

A contrary view, upholding the more conventional view of the importance of financial performance incentives is contained in *Performance-Based Pay for Executives Still Works* (Edmans 2016), also of the London Business School, who refutes some of the findings made by Cable and Vermeulen. Both articles are published in the same edition of the Harvard Business Review.

It is important however to note that neither of these studies discusses the corruption issue in relation to compensation for employees.

Transparency International has identified the importance of addressing the conflict between financial performance-based incentives and corruption in regard to bankers and financial services industry. In their Working Paper 02/15 “Incentivising Integrity in Banks”, they looked at the issue of remuneration for bankers in particular, and the effects of compensation packages on corruption issues as follows:

“Until recently, indicators for performance management have largely failed to account for non-financial performance such as behaviour or compliance, relying exclusively on short-term quantitative profit targets. This contributed to integrity failures. According to a 2015 survey of professionals working in financial services, a third of those surveyed said compensation structures or bonus plans pressure employees to compromise ethical standards or violate the law. To avoid these integrity failures, staff should be rewarded for sustainable risk management...
that includes compliance with the law, zero tolerance for anti-corruption and bribery, and ethical behaviour.” (page 3)

4.2 Rewarding Employees For Whistleblowing Regarding Corruption

Many companies have been advised to develop a programme for rewarding employees for whistleblowing regarding corruption. However, this issue needs to be considered more deeply. Firstly, whistleblowers perhaps should be compensated not just for reporting corruption within the enterprise, but also, reporting demands for bribes by the host government officials as well as corruption by competitors. Without compensation for doing so, there is rarely incentive for an employee to engage in disclosing bribe demands or payments by others. There are great disincentives for whistleblowing – loss of employment, career, reputation, and these need to be recognized; often, it is suggested that whistleblowers should come forward out of a civic duty to inform on wrongdoings, but in reality, we cannot expect a person to take the risks stated above, in order to comply notions of civic duty in the absence of compensation for those risks.

As an example of this issue, the author was recently involved as a consultant to a person who had “blown the whistle” on corruption and malfeasance by a government authority, for which she was constructively dismissed, regardless of the legal protections in place in Canada to protect whistleblowers. She was subsequently employed by a bank. While employed by the bank, she gave an interview to a television station about the corruption and malfeasance issues related to the government office. Before the interview aired, she mentioned the upcoming interview to her new employer, who immediately threatened her that if the interview aired, showing her as the whistleblower, she would be immediately dismissed from her job. This example illustrates the potential extreme repercussions that can result from a person acting as whistleblower.

Implementing a “whistleblower” policy that truly rewards whistleblowers and protects them from adverse repercussions can have a significant impact on decreasing corruption risk within the company, but this must be carefully considered against the following risks that such a programme brings:
(a) An empowered whistleblower can create significant problems for the company if the information is conveyed to government authorities, media or law enforcement in lieu of to those within the company that are tasked with dealing with these issues. This often results when the whistleblower provides the information to the company, which then takes no action, or insufficient action to deal with the issues raised. Thus, prior to instituting a whistleblowing programme, the company must be very sure that information received by a whistleblower from within the company is acted upon immediately, not ignored. This is a very difficult task.

(b) Scenario – Yco is engaged in a major construction project in a developing country, which employs thousands of people both in the host and home state. Yco obtained the contract through corruption. A whistleblower is aware of this and wants to disclose the corruption to the company and the relevant authorities. If the disclosure is made, this may result in the funders of the project declaring default under the loan agreement, thereby terminating the project, and causing all of the corporate employees to be terminated for lack of work. Should the whistleblower be encouraged to disclose, given the potential negative repercussions to all of the employees, who were innocent of wrongdoing? If the disclosure is made to the company, what course of action should the company embark upon, knowing the possible ramifications of this disclosure?

(c) How does the company deal with the norm in many societies that a tattletale is not to be tolerated? This is taught from childhood onwards and is ingrained in society. The protection of a whistleblower is contrary to this norm – how will it be perceived by fellow workers in the company? The author’s research indicated that in some situations, whistleblowers were ostracized by co-workers because this contravened a societal norm, and additionally, potentially put their jobs at risk. The fear is that if the company is shown to be engaged in corruption, it could jeopardize the long term financial viability of the company, and hence the employees of the company are at risk of losing their jobs.
4.3. Maintaining Databases For Corruption Demands

Databases for corruption demands can be an integral aspect of decreasing corruption globally. Such databases should be both internal to the enterprise as well as globally based. For example, an international agency or NGO, such as Transparency International, could undertake the role of repository of information on bribe demands globally. A corporate employee from whom a bribe has been demanded by a government official in order to obtain a supply contract would report that demand to the repository for input into the database. This would have a number of potential benefits to the fight against global corruption from the demand side:

(a) If a competitor obtains the contract, it can be surmised that competitor did pay the demanded bribe in order to obtain the contract. Thus, any competitor who is aware of this system of reporting would know that if they obtain that contract from the government official, there will be some degree of scrutiny of that situation by others. Hence this should result in reduction in the supply side of bribery.

(b) The name of the government official who demanded the bribe would be listed in the depository records. This “naming and shaming” could have a serious detrimental effect on that official, thereby reducing the probability that he will demand future bribes. Thus, the demand side of corruption would be reduced through the instituting of such a system.

This system would further the objectives as set out in the Recommendations Adopted by the OECD Council on 26 November 2009, Article IX on reporting foreign bribery. This is a crucial element in reducing corruption globally, but to date, has received little attention.

Reality however, is that this may be a problematic issue for the company. If it reports corruption demands by a government official(s) in the host state to the data base system, this will likely come to the notice of the government officials, who may then have motivation to damage the company in that host state as retribution. Conversely, the existence of this system may motivate governments to decrease corruption demands, knowing that such demands may become public knowledge, to the embarrassment

8
of the government officials involved. We are currently seeing the phenomenon globally whereby governments are being toppled as a result of disclosure of corruption by that government.

Implementing this type of reporting system may require some financial incentives being provided to employees to engage in reporting bribe demands.

4.4 Communicating With Employees Effectively

Often, the corporate anti-corruption programme is developed without serious consideration given to whether the audience for the programme will be able to understand the contents. For example, the programme will be written in English (assuming that is the main language of the company); yet, employees of the company may not understand English well. This is especially the case when the company has operations in various non-English speaking countries.

Not only must the programme be translated into the local languages of the employees, but the translations must be done with great care and consideration. Most corruption programmes have much “legalese” in them, often because lawyers help draft the programme. Translating “legalese” from English to another language is fraught with difficulties, unless the translators understands the legalese and legal concepts in both the English version and the language and legal culture of the translated version.

In addition, the employees may have low levels of education and sophistication. Thus, it is important that the programme be presented to them in a manner that is commensurate with their level of education and sophistication.

Cultural aspects often loom large. How does the company seek to impress upon employees the importance of avoiding corruption, when corruption is part of their cultural norm, and they will likely not be penalized for bribing in their home state? In some states, failing to provide the requisite customary gifts can be seen as an insult, at the very least. If the employee is a national of the host state and fails to conform to societal norms regarding customary gifts, he may experience societal disapproval of his actions.
5. Corporate Anti-Corruption Programmes Need to be Wider in Scope

Corporate anti-corruption programmes also need to be wider than is the norm currently. The company must look at the various tools that are available to reduce demands for bribes from government officials (demand side) as well as reducing the risks inherent to a company in refusing to pay a bribe (supply side), thereby strengthening the power of the company to resist paying bribes. These tools include political risk insurance, financing programmes through World Bank or other international development banks or export credit agencies which have the power to provide significant strengthening of the ability of the company to resist payment of bribes. These tools should be seen as fundamental to the anti-corruption programme; yet the author’s research suggested that these tools are virtually unknown to most companies.

5.1 Political Risk Insurance and Corruption Issues

Political risk insurance should be considered by the company as part of an effective anti-corruption programme if the company engages in foreign investment. Political risk insurance is insurance that provides protection against risks primarily related to the actions of a foreign government, such as expropriation, breach of contract by the government and numerous other risks. Policies are issued by international agencies, such as the World Bank, export credit agencies (such as OPIC and Export Import Bank of US, EDC in Canada), and commercial insurance companies (such as AIG, Lloyds, Zurich) and others.

The relationship between PRI and corruption can be briefly described as follows. If a company requires a business licence, operational permit or similar fundamental permission by the government, this is a very typical situation where a bribe is demanded by a government official, in order to issue the permit. Hence the existence of the exemption for facilitation payments in the FCPA which is a recognition of the ubiquity of this situation; this exemption allows a company to make such payments without contravening the law in some circumstances.

To illustrate, suppose that Xco has invested $1 million in the host state, to establish a factory, and Xco requires an annual operating licence to continue its operations. An official of the host state demands a
bribe payment of $1000 in order to issue the licence. We are assuming that there is no option but to pay or the licence will not be issued and the factory will cease to operate.

(a) The situation in the absence of political risk insurance is that if the company does not pay the bribe, it risks losing $1 million that has been invested, plus future profits.

(b) However, if the company has political risk insurance, that is well drafted to protect against government actions of this type, (typical is a 90% recovery clause) the company now is in the position whereby failure to pay the bribe will result in the loss of only $100,000 since the balance will be paid to it by the insurer. In this situation, the power relationship between the investor and the government official is quite different as the potential loss by Xco has decreased to only $100,000 if it fails to pay the bribe, thus giving Xco far more ability to resist that payment.

Not only does this situation increase the ability of Xco to refuse to pay the bribe, but it also greatly diminishes the power of the government official to extort the bribe. The official knows that if the company refuses to pay, and is shut down, the company will only suffer a 10% loss, because of the existence of the PRI policy. This can be sufficient deterrence to the official, as he knows that his bargaining position is quite weak now, resulting in withdrawal of the demand. Thus the existence of the PRI policy can reduce both the demand and supply side of the corruption equation.

Additionally, oftentimes the insurer itself will have strong leverage against the government of the host state to stop the bribe demands. For example, if the PRI issuer is the Multi-Lateral Guarantee Agency of the World Bank, it may be able to use its leverage to persuade the government to withdraw the bribe demand, lest it jeopardize its relationship with the World Bank and thereby lose the possibility of future funding of projects in that host state by the Bank.

PRI issued by export credit agencies ( ECAs) often have similar leverage, by enlisting the power of their home government against the host state, or threatening to refuse funding future projects in that host state.
Private insurers have leverage as well against host states often. Most PRI policies are issued by a syndicate of insurers, all of whom are part of the Berne Union, which consists of over 80 insurers, private and public, who issue export credit insurance. A host state government demanding bribe payments from an investor insured by a Berne Union insure will likely be faced with threats that the insurer will refuse to provide insurance products that will benefit the host state in future if they do not cease their bribe demands. This is also a powerful lever. Under the terms of the Berne Union rules, any member insurer is obligated to report issues such as corruption demands to all other members of the Union, resulting in collective efforts by the insurance companies against the host state.

5.2 Protection Against Bribe Demands Through Funding That Prohibits Bribery.

If a project is funded by financiers such as the World Bank, ECAs, or international banks, the funding contract will require the borrower to refrain from making any corrupt payments, failing which the loan can be called in by the lender for default under the loan agreement.

These lenders will often have leverage similar to the PRI issuers to persuade the host state to refrain from demanding bribes from their borrower/client.

Additionally, in many international investment projects financed by these international lenders, the host state is required to issue a guarantee to the international lender that if the project stops due to fault of the host state or for any other reason, the host state will pay to the lender the amounts then owing by the borrower to the lender. Thus, the host state becomes the guarantor to the lender for all or a portion of the loans; if the project stops as a result of bribe demands by the host state which are refused by the investor, the host state is liable for all outstanding debt of the investor to the funder. Thus, the existence of this situation is often sufficient to have the host state cancel any bribe demands, lest the state itself be liable for any financial damages resulting therefrom, and the reasons for the project being stopped become known to the public of the host state.
6. Tools Will Also Help Boards of Directors to Withstand Shareholder Pressures

PRI and funding agreements with prohibitions on corruption can be a powerful tool for boards of directors or management to withstand demands by shareholders for bribery in order to increase profits.

While there is much academic literature on pressure by shareholders to stop their boards of directors from engaging in corruption, the author has had ample anecdotal evidence through the interviews referred to above, that often the pressure is the other way. Companies are often pressured by shareholders to invest in countries with high corruption risks - usually because the competitors of the company are already operating in those countries and the shareholders do not want the company to lose market share and profits to those competitors.

When corruption demands are made by host state governments in order to provide necessary operating licences, shareholders sometimes equate the possible payment of fines for corruption with a cost of doing business, and therefore pressure the company to pay the bribes in order to increase profits. In order to resist that pressure from shareholders, the company may rely upon the following:

(a) PRI policies usually stipulate that if the company engages in corruption, the insurance becomes invalid.

(b) Similarly, international investment funding agreements usually provide that engaging in corruption is a serious breach of the agreement, permitting the lender to demand immediate repayment of the loan.

These provisions are often sufficient to empower a board of directors to withstand shareholder demands that corruption be engaged in as a means of obtaining higher profits. The risks to the company of engaging in bribery are not just those provided by the laws of the host and home state, but also, loss of PRI coverage or funding for the project.

(c) Arbitration provisions in foreign investment can be a significant tool for boards of directors to use as a rationale for refusing to pay bribes. Many foreign investments are made under the protection of a Bi-Lateral Investment Treaty, Free Trade Agreement or an international investment agreement made between the investor and the government of the host state. One of the key
protective elements of these BITs, FTAs or investment agreements is the right of the investor to submit any dispute between the investor and the host state to international arbitration, rather than to the domestic courts of the host state. However, the general principle in international arbitration jurisprudence is that if the actions of the investor are tainted by corruption, then the investor’s claim will fail. This in itself provides a very strong method of empowering the board of directors to withstand shareholder demands that the company comply with corruption demands in order to obtain higher profits. The loss of an arbitration claim worth $100 million due to acts of corruption engaged in by the investor will generally far exceed the profits that could be derived from the payment of the bribe demand. Unfortunately, many of the companies researched did not really grasp the importance of arbitration provisions as a means of dispute resolution between the investor and the state and thus, did not understand the concept of arbitration provisions strengthening the power of the board to withstand pressure from its own shareholders.

7. Conclusions

The development of an anti-corruption programme is far more complex than is usually recognized by companies. One of the crucial elements that underlay the development of an anti-corruption programme is the determination of whether the key purpose of the programme is to satisfy governmental authorities or whether it is a serious effort to stop corruption within the company. The programme will be quite different, depending upon which option is chosen. When the company is making that decision, it should also be aware that governmental authorities will likely become more sophisticated in their review of such programme in the near future, rejecting those that are not seriously focussed upon reducing corruption throughout the company. Thus, choosing the former approach is very short sighted, and extremely risky, but often far cheaper to develop and implement in the short run.

Once the focus is decided upon, and prior to deciding upon the content of the programme, the company must also investigate the corruption landscape in the various jurisdictions in which it intends to operate. This is often done in a very cursory manner by the company, relying primarily on internet searches, TI Corruption Indexes and publically available information. However, companies that were researched often stated that when they established in a jurisdiction after cursory investigation, they were shocked
to discover how serious the corruption risks they encountered that were not mentioned in the sources they consulted. They realized then that hiring professionals who have expertise in determining the corruption landscape that a company will likely face should have been a prime concern in the investigation stages.

Now they were faced with the a very serious predicament, as they had invested millions of dollars in the host state, only to find after the investment was made that it was virtually impossible to operate in that jurisdiction without engaging in corruption. They had to then choose between almost equally unpalatable options; abandon the investment or continue to operate by engaging in corruption in order to survive financially. If they choose the former, the shareholders and others will likely be extremely critical of the management, suggesting that they should have engaged in proper investigation of the corruption landscape in that host country prior to investing millions of dollars. If they choose the latter, they may be financially successful, thereby avoiding criticism by shareholders for not engaging in proper due diligence, while they confront the risks associated with being engaged in corruption activities. At that point, many companies come to the realization that no matter how strong the anti-corruption programme is on its face, the reality in a particular country is that complying with the policies of the programme will likely result in financial failure.

At that point in the cycle, the company begins to realize that there may be tools that could have been employed to reduce many of these risks, such as PRI or financing through international banks, for the reasons set out above. However, it may then be too late for the company to avail itself of such tools.

At the same time, the company often slowly realizes that the world of international investment is fraught with risks and concerns that they have not anticipated. The existence of BITs or FTAs are important to the protection of the investment, as is an understanding of the concepts of international investment arbitration, human rights issues (which are very closely connected to corruption issues), expropriation issues etc.
Thus, anti-corruption programmes should not be developed in a vacuum, but must be closely connected to the other risks that the company will encounter in that foreign investment, and employ all of the tools and techniques available to sophisticated international investors to mitigate risks.

References


Berne Union information can be accessed at http://www.berneunion.org/about-the-berne-union/