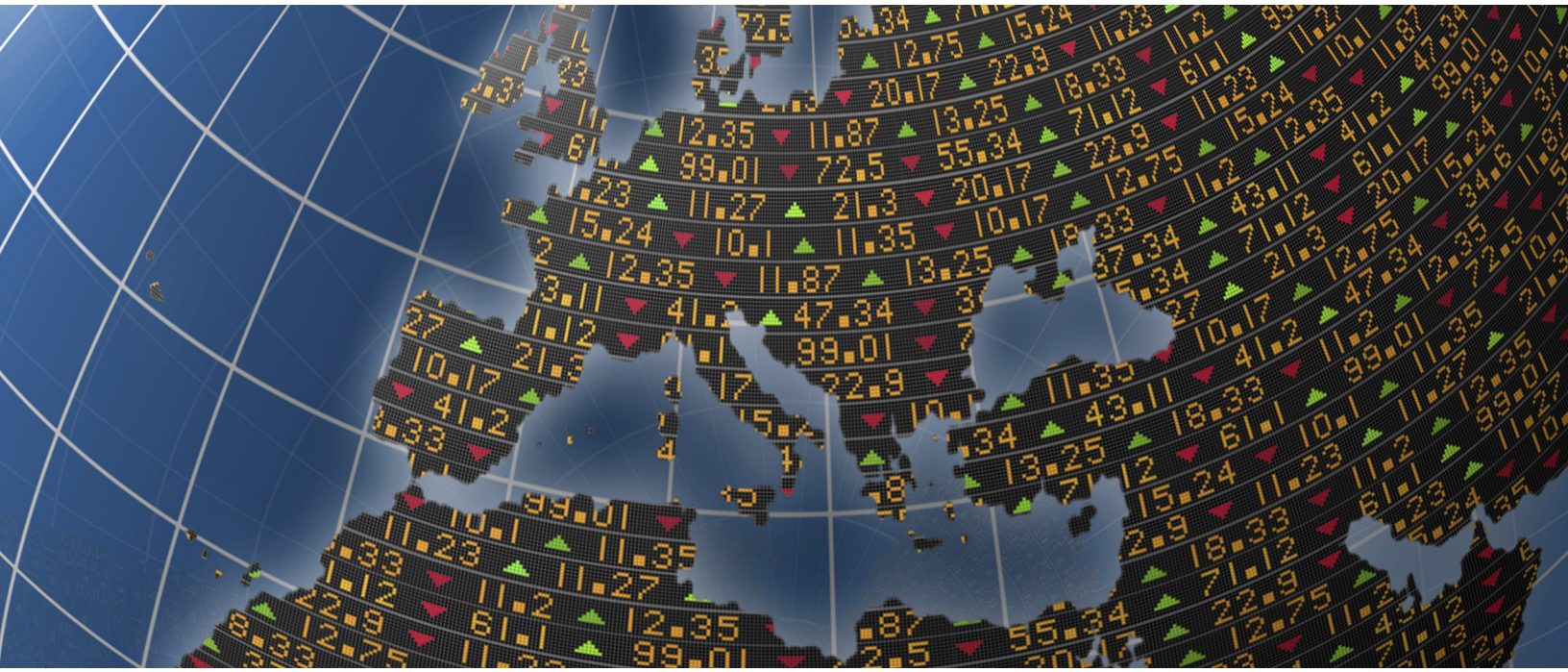
FCPA Update

A Global Anti-Corruption Newsletter



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Between a Rock and a Hard Place: Anti-Corruption Compliance and Antitrust Law in Russia

Anti-corruption compliance programs of multinational companies – and, specifically, policies relating to the selection and monitoring of third parties – have found an unlikely arbiter in Russia. Following a similar decision in 2011, in two recent cases the Russian Federal Antimonopoly Service ("FAS") and the commercial courts to which the FAS's decisions were appealed have undertaken a detailed analysis under Russian anti-corruption and antitrust laws of distributor selection policies of two multinational pharmaceutical companies.

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The decisions generally increase the risk that these policies could be deemed to violate Russian law. When carefully considered, however, they also provide guidance as to how companies can mitigate that risk by making targeted, Russia-specific changes to global anti-corruption compliance procedures.

This article sets forth the cases at issue and then lists steps that companies operating in Russia may consider taking in their wake.

I. The Novo Nordisk Case

As we have previously noted,[1] in January 2011 the FAS held that OOO Novo Nordisk ("NN"), the Russian subsidiary of the Danish global pharmaceutical company, was a dominant entity and violated the Law on the Protection of Competition ("Russian Competition Law")[2] by improperly refusing to contract with a number of potential distributors.[3] Among other things, the FAS faulted NN for promulgating anti-corruption compliance policies that were too onerous because compliance with them was not required by Russian law. The FAS also ruled that NN did not clearly articulate the criteria that distributors had to meet, which resulted in NN rendering case-by-case and possibly arbitrary decisions.

NN was fined 85 million Rubles (approximately $3 million at the time).[4] NN initially appealed the FAS decision to the Moscow Arbitrazh Court, but in July 2011 settled with the FAS, revising its commercial partner policy to list nine apparently exclusive reasons upon which NN may rely to refuse to contract with a distributor.[5] The policy did not contain any provisions relating to anti-corruption compliance audits of distributors.[6]

By December 2014, the FAS and NN were at odds again. In a second round of regulatory action, NN was fined for violating the Russian Competition Law by, among other things, forcing unprofitable and arbitrary conditions on a potential distributor after NN attempted to enforce its anti-corruption compliance policy.

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1. *See* Bruce E. Yannett, Sean Hecker, Alyona N. Kucher, James B. Amler, Jane Shvets, and Anna V. Maximenko, "Anti-Bribery Compliance in Russia: One Step Forward, Two Steps Back?," *BNA White Collar Crime Report* (Oct. 21, 2011).
2. Law on the Protection of Competition, No. 135-FZ (July 26, 2006).
3. *See* FAS Press Release, "FAS Russia Fined 'Novo Nordisk' Over 85 Million Rubles for Unlawfully Evading Contracts for Supplies of Medicines" (Jan. 24, 2011), http://en.fas.gov.ru/news/news_31180.html. For the full text of the Oct. 6, 2010 liability decision, *see* http://www.fas.gov.ru/solutions/solutions_31980.html?isNaked=1 (Russian); for the full text of the Jan. 20, 2011 damages decision, *see* http://www.fas.gov.ru/solutions/solutions_31981.html?isNaked=1 (Russian).
4. *Id.*
5. *See* Yannett, *et al.*, note 1, *supra*.
6. *See* "OOO Novo Nordisk's Policy Regarding Commercial Partners" (July 25, 2011) (on file with authors).

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NN's latest antitrust troubles began in August 2013, when it halted sales of certain medications to one of its distributors, ZAO Severo-Zapad ("SZ"), claiming that SZ violated the anti-corruption clauses of its distributor contract. On September 30, 2013, the FAS issued a warning notice to NN.[7] In the notice, the FAS requested, *inter alia*, that NN exclude from its distributor contracts (*i*) an anti-corruption audit clause;[8] and (*ii*) a clause allowing NN to refuse performance if it determined that it was "probable" that the distributor violated its obligations ("justifiable non-performance clause").[9] The FAS did not request that NN remove from its distributor contracts a clause requiring distributors' compliance with applicable anti-corruption mandates.

"[T]he court was not persuaded by NN's argument that the Russian Anti-Corruption Law rendered anti-corruption audit clauses non-arbitrary and legitimate."

NN appealed the warning notice to the Moscow Arbitrazh Court, making two principal arguments. First, NN argued that it was allowed to include the two clauses at issue in its distributor contracts pursuant to the July 2011 settlement with the FAS. Second, it argued that the anti-corruption audit clause was not an arbitrary condition because it was in accordance with Russian law, citing two provisions of the Russian Federal Law on Anti-Corruption Practices ("Russian Anti-Corruption Law"):[10]

- Article 14 of the Russian Anti-Corruption Law, which provides that a company can be held liable for corrupt acts taken by a third party "in the name of or the interests" of the company; and

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7. Under the Russian Competition Law and FAS procedures, the warning notice is a prerequisite for commencing a case for violating certain provisions of the Competition Law by dominant entities. The FAS can initiate such an action only if the company does not cure the alleged violation within the period provided.
8. Clause 11.3 of the distributor contract between NN and SZ provided that, at NN's request, SZ must furnish its books and records relating to the contract performance to an independent auditor selected by NN. If the results of the audit revealed violations of anti-corruption laws listed in the contract, SZ would have to pay the costs of the audit. *See* Moscow Arbitrazh Court Decision, Case No. A40-154847/2013, at 6 (Mar. 25, 2014).
9. *Id.*
10. Federal Law No. 273-FZ on Anti-Corruption Practices (Dec. 25, 2008).

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- Article 13.3, enacted in January 2013, which requires all companies operating in Russia to develop and adopt measures aimed at preventing corruption, including development and introduction of standards and procedures aimed at ensuring compliance.[11]

On March 25, 2014, the Moscow Arbitrazh Court rejected NN's positions. With respect to the prior settlement with the FAS, the court found that NN had promised to remove anti-corruption audit clauses from its distributor contracts, but had failed – at least in SZ's case – to do so.[12]

Most significantly, the court was not persuaded by NN's argument that the Russian Anti-Corruption Law rendered anti-corruption audit clauses non-arbitrary and legitimate. The court emphasized that, pursuant to Article 14, a company is liable for unlawful acts of a third party only if those acts are taken "in the name of or in the interests" of the company.[13] Under Russian contract law, the court observed, distributor agreements do not create the type of legal relationship that would make the distributor's actions attributable to the seller. Because SZ's actions would not be attributable to NN, the latter did not have a non-arbitrary reason, grounded in the Russian Anti-Corruption Law, to force SZ to submit to anti-corruption audits.[14]

On June 30, 2014, the Ninth Arbitrazh Appellate Court upheld the lower court's decision, but focused on different aspects of NN's distributor contracts. Rather than striking the anti-corruption audit clause as arbitrary in principle, the appellate court observed that NN (*i*) did not specify the anti-corruption laws that would serve as the compliance benchmark in any audit pursuant to the clause; (*ii*) failed to demonstrate why striking the clause would harm NN; and (*iii*) did not explain why NN could not demand SZ's compliance with anti-corruption law without including the anti-corruption audit clause.[15]

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11. *See also* Paul R. Berger, Dmitri V. Nikiforov, Bruce E. Yannett, Jane Shvets, and Anna V. Maximenko, "Anticorruption Compliance Programs Under Russian Law: Article 13.3 and the FCPA/UKBA Experience," *FCPA Update*, Vol. 4, No. 9 (Apr. 2013), http://www.debevoise.com/insights/publications/2013/04/fcpa-update.
12. *See* Moscow Arbitrazh Court Decision, note 8, *supra*, at 8.
13. *See* Moscow Arbitrazh Court Decision, note 8, *supra*, at 9.
14. *See* Moscow Arbitrazh Court Decision, note 8, *supra*, at 8-10.
15. Ninth Arbitrazh Appellate Court Decision, note 12, *supra*, at 3.

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Similarly, the appellate court ruled that the justifiable non-performance clause was vague and arbitrary because it did not include the criteria by which NN would determine that the distributor had "probably violated" its obligations under the contract. The court observed that the vagueness of the clause had the effect of allowing NN to cease performance under the contract at any time and for any reason.[16]

While its appeal was pending, NN agreed to remove the contract clauses at issue from its distributor agreements, but continued to refuse to execute a new contract with SZ.[17] Among other arguments, NN cited its Policy on Commercial Partners, which provided that NN can terminate a distributor if it had received information about possible violations of business ethics by that distributor. NN claimed that SZ had been subject to a government raid and search of its premises.[18]

The FAS did not credit NN's arguments, noting that it had requested information from the relevant authorities about any cases against or investigations of SZ, and was told that there were no such cases or investigations.[19] Accordingly, on August 25, 2014, the FAS issued a decision against NN, subsequently imposing a 30 million Ruble (approximately $48,000) fine on the company,[20] as well as a 20,000 Ruble (approximately $326) fine on NN's former CEO in her individual capacity.[21]

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16. *Id.*
17. *See* FAS Decision, Case No. 1-10-349/00-18-13, at 6 (Aug. 25, 2014), http://solutions.fas.gov.ru/ca/upravlenie-kontrolya-sotsialnoy-sfery-i-torgovli/18-36159-14 (Russian; English translation on file with authors).
18. *Id.* at 8.
19. *Id.* at 8-9.
20. FAS Fine Decree, Case No. 4-14.31-589/00-18-14 (Dec. 8, 2014), http://solutions.fas.gov.ru/ca/pravovoe-upravlenie/ak-50389-14 (Russian).
21. FAS Fine Decree, Case No. 4-14.31-600/00-18-14 (Dec. 15, 2014), http://solutions.fas.gov.ru/ca/pravovoe-upravlenie/ak-51729-14 (Russian).

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II. The Baxter Case

NN is not the only pharmaceutical company recently in the FAS's crosshairs. In 2013, the FAS initiated proceedings against ZAO Baxter Company ("Baxter"), the Russian affiliate of the U.S. pharmaceutical company headquartered in Deerfield, Illinois. Like NN, Baxter was ruled to have held a dominant market position with respect to sales in Russia of certain pharmaceuticals, including Extraneal, a drug used to treat renal failure.[22]

The FAS proceedings against Baxter stemmed from the company's refusal to sign a distributor contract with Medical Services Company ("MSC"), following what Baxter claimed to have been MSC's failure to pass Baxter's due diligence procedure.

In early March 2012, as part of its application to become Baxter's distributor, MSC filled out Baxter's due diligence questionnaire and its CEO was interviewed by Baxter's representatives.[23] Two weeks later, Baxter informed MSC that its application was rejected for two principal reasons. First, Baxter claimed, MSC provided "incomplete and inaccurate information in the Application Form and in the subsequent interview." Second, Baxter stated, the information provided gave "reasonable grounds to believe" that MSC had been involved in "anticompetitive actions" in connection with a public auction.[24]

In September 2013, days before its warning to NN, the FAS issued a warning notice to Baxter, stating that it could not refuse to contract with MSC because its third-party selection procedure "does not contain clear criteria for the selection and approval of counterparties."[25] After Baxter still refused to contract with MSC, the FAS initiated proceedings against the company for violating the Russian Competition Law. Like NN, Baxter argued that Articles 13.3 and 14 of the Russian Anti-Corruption Law mandated its due diligence procedure and refusal to contract with MSC. Using the same reasoning as the Moscow Arbitrazh Court in the NN case, the FAS found that argument unpersuasive.[26]

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22. *See* FAS Press Release, FAS Warned 'Baxter' Not to Violate the Antimonopoly Law" (Sept. 24, 2013), http://en.fas.gov.ru/news/news_33220.html.
23. FAS Decision, Case No. 1-10-248/00-18-13, at 2 (Apr. 8, 2014), http://solutions.fas.gov.ru/ca/upravlenie-kontrolya-sotsialnoy-sfery-i-torgovli/18-13495-14 (Russian; English translation on file with authors).
24. *Id.* at 3.
25. FAS Press Release, note 22, *supra*.
26. *See* FAS Decision, note 23, *supra*, at 6-7.

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Having determined that the Russian Anti-Corruption Law did not require Baxter to submit MSC to a due diligence procedure, the FAS noted that Baxter may nevertheless be innocent of an antitrust offense if it selected counterparties using transparent, concrete, and nondiscriminatory criteria and procedures.[27] The FAS went on to perform a detailed analysis of Baxter's third-party selection process, postponing its consideration of the case to give Baxter an opportunity to provide additional documents. The FAS found that the documents furnished by Baxter did not contain adequate criteria for selection or approval of distributors and thus did not sufficiently demonstrate how and why Baxter decided not to contract with MSC.[28]

"The NN and Baxter cases are the first in which Russian regulators or courts closely analyzed Russian Anti-Corruption Law and its requirements with respect to distributors and other third parties."

The FAS also conducted an in-depth analysis of Baxter's allegations regarding the likely anticompetitive and corrupt activities of MSC in prior public tenders. Although the extensive redactions in this section of the publicly available copy of the decision make it difficult to follow, the FAS ultimately found Baxter's arguments unpersuasive, emphasizing that Baxter did not contemporaneously cite the prior alleged misconduct in its decision not to contract with MSC and did not bring that activity to FAS's attention until late in the process.[29]

In July 2014, the FAS assessed a 9.23 million Ruble (approximately $151,000) fine on Baxter for disregarding its warning and continued refusal to contract with MSC, calculated as 1% of Baxter's 2012 revenues from the sales of Extraneal.[30]

Baxter appealed, arguing that the FAS exceeded its authority in ruling on Baxter's anti-corruption compliance measures. In October 2014, the Moscow Arbitrazh Court affirmed the FAS's analysis, as well as its own reasoning in the March 2014 NN decision. It held that a distributor contract does not create a relationship

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27. *Id.* at 8.
28. *Id.* at 8-12.
29. *Id.* at 12-17.
30. FAS Fine Decree, Case No. 4-14.31-198/00-18-14 (July 1, 2014), http://solutions.fas.gov.ru/ca/pravovoe-upravlenie/ats-26886-14 (Russian).

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between the seller and the distributor that could give rise to liability of the former for the corrupt activities of the latter under Russian Anti-Corruption Law.[31] The court upheld the FAS decision and reasoning in all other respects, but disagreed with the fine calculation method and reduced Baxter's penalty to 1.32 million Rubles (approximately $22,000).[32]

On February 26, 2015, that decision was affirmed in all respects by the Ninth Arbitrazh Appellate Court, which fully endorsed the lower court's reasoning.[33]

III. Implications for Multinational Companies Operating in Russia

The NN and Baxter cases are the first in which Russian regulators or courts closely analyzed Russian Anti-Corruption Law and its requirements with respect to distributors and other third parties. The detailed nature of the analysis – which is in marked contrast with several recent regional court decisions finding companies guilty of Article 13.3 violations[34] – and similarities in the reasoning used in both cases suggest that the decisions are a product of thoughtful deliberation likely to form a foundation for future decisions. As such, multinational companies operating in Russia would be well-advised to pay close attention.

Russian Anti-Corruption Law, as interpreted by the FAS and the Arbitrazh courts, clearly demarcates which types of third-party relationships may (and may not) give rise to liability for third-party misconduct. Both the NN and Baxter cases took a formalistic approach to interpreting whether acts of a third party are or can be taken "in the name of or in the interests" of the company. Rather than considering all the facts surrounding the third-party relationship at issue – here, that between a supplier and a distributor – the courts held that, by its contractual nature, a distributor agreement does not create a relationship that would make the distributor's actions attributable to the seller.

That approach is in tension with the consideration of facts often deemed relevant in FCPA liability determinations. Companies subject to the FCPA can be held liable for FCPA violations if other statutory elements are met and company employees know of or purposefully avoid learning of improper payments made by their

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31. *See* Oct. 29, 2014 Moscow Arbitrazh Court Decision, note 13, *supra*, at 10.
32. *Id.* at 16.
33. *See* Ninth Arbitrazh Appellate Court Decision, note 13, *supra.*
34. *See, e.g.*, Tver District Court, Case No. 2-2459/2014 (Dec. 19, 2014); Murmansk District Court, Case No. 2-4321/2014 (June 23, 2014); District Court of Bazamiy Sizgan, Case No. 2-1099/2014 (May 19, 2014).

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distributors, agents, or other third parties, regardless of the particular contractual arrangement in place.[35] In fact, third-party due diligence and monitoring – including the very steps that NN and Baxter took – have long been staples of corporate compliance policies under both the FCPA and the UK Bribery Act ("UKBA").

The Russian courts' interpretation of the Russian Anti-Corruption Law should not, in and of itself, prevent companies from implementing global third-party due diligence and monitoring programs in Russia, so long as those companies do not hold a dominant market position for competition purposes.[36] For companies that do hold a dominant market position or could be viewed as holding one by the FAS – in particular pharmaceutical companies that may be deemed to have a "dominant position" with respect to particular drugs given the lawful monopolies provided by patents – the NN and Baxter decisions present a serious challenge.[37] Companies operating in Russia would therefore be well advised to determine whether they hold a dominant market position on any particular market – or are at a risk of being deemed dominant by the FAS – and to adjust their antitrust and anti-corruption compliance policies accordingly.

Under the NN and Baxter decisions, a company with a dominant market position cannot defend the conditions it places on its distributors by appealing to the Russian Anti-Corruption Law requirements. Thus, if the FAS finds those conditions to be arbitrary and economically unjustifiable, that company could find itself with a choice of either (1) complying with Russian Competition Law by removing those conditions, potentially compromising its third-party due diligence and monitoring program; or (2) maintaining its program but facing FAS enforcement actions.[38] The latter can result in fines against the company and its employees who are deemed responsible for the antitrust violation, and potentially disqualification of those employees from service in certain positions for up to three years.[39]

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35. *See* Resource Guide to the U.S. Foreign Corrupt Practices Act, at 21-23 (Nov. 14, 2012), www.justice.gov/criminal/fraud/fcpa/guidance/guide.pdf

36. Under Article 5 of the Russian Competition Law, an entity or a group of entities hold a dominant position in the market for certain goods if they are able to (*i*) exercise a dominant influence on the general conditions of the circulation of such goods in the market; or (*ii*) force other entities out of the market; or (iii) impede other entities' access to the market. Generally speaking, most commercial entities are deemed to have a dominant market position if their share of the market exceeds 50%. The FAS can, however, rule that an entity with less than a 50% market share is nevertheless dominant if, for example, its market share is very stable over time or its market share is large compared to its competitors, or based on other criteria.

37. Under Article 10 of the Russian Competition Law, a dominant market player is generally prohibited from, *inter alia*, refusing to enter into agreements with third parties on any grounds that are not technologically or economically justified.

38. NN appears to have selected the first option, agreeing to remove the offending contractual clauses from its distributor agreements, though continuing to refuse to contract with SZ. *See* FAS Decision, note 17, *supra,* at 6-7. Baxter, on the other hand, has so far has refused to comply. *See* Ninth Arbitrazh Appellate Court Decision, note 13, *supra.*

39. As a general rule, company fines range from 1% to 15% of the company's annual revenues from the sale of goods/services on the relevant market. *See* Art. 14.31, Russian Code of Administrative Offenses. Individual fines range from 20,000 Rubles to 50,000 Rubles. *Id.*

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As we had previously noted in connection with the 2011 FAS decision against NN,[40] the conflict between Russian Competition Law and FCPA/UKBA compliance may lead to a revival of local law defenses under the FCPA/UKBA regimes. The conflict here, however, is more nuanced than a "classic" scenario in which an otherwise corrupt payment is lawful under the written laws or regulations of the foreign country, and the U.S. authorities have signaled that they would construe the local law defense narrowly in these circumstances.[41] Accordingly, it seems unlikely that merely citing the NN and Baxter decisions will persuade U.S. enforcement agencies to let companies off the hook when it comes to monitoring their sales channel in Russia.

"[C]ompanies are well advised carefully to consider privilege issues in structuring their anti-corruption compliance processes and related documentation."

That said, the difficult position in which companies dominant in the relevant product market in Russia may find themselves could be viewed, depending on the facts, as a mitigating factor in cases of alleged anti-bribery liability arising from the actions of third parties. It may even prove exculpatory with respect to allegations that an issuer under the 1934 Securities Exchange Act violated the FCPA's internal controls provisions, which require only those controls that are "reasonably designed" in light of the circumstances to prevent bribery.

The good news is that the NN and Baxter decisions do appear to leave some room for companies to comply with both Russian Competition Law and non-Russian anti-corruption legislation, or at least to minimize risks under both. The key requirement under the Russian Competition Law is that a dominant market player cannot place arbitrary or discriminatory conditions on its distributors. Although simply citing a desire to comply with anti-corruption laws is no longer an acceptable way to justify conditions placed on the distributors, there may be other ways to show that those conditions are reasonable and fair attempts to minimize attendant risks.[42]

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40. *See* Yannett *et al.*, note 1, *supra.*

41. *See* Resource Guide, note 35, *supra*, at 23-24.

42. Although the most prudent course may be to consider these risks before the FAS comes knocking, the FAS warning procedure, *see* note 7, *supra*, gives companies some time to evaluate its options before the FAS initiates a case.

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First, companies should set forth clear, consistent, and well-defined criteria for selecting counterparties and for post-selection monitoring processes. The NN and Baxter decisions indicate that Russian courts will not be satisfied with a general reference to a company's anti-corruption policies and procedures, and will delve into the details to determine whether they are sufficiently clear and substantiated. For example, the decisions noted that (*i*) the anti-corruption audit clause in NN's distributor contracts did not list the specific laws compliance with which would be audited;[43] (*ii*) country-specific regulations contemplated by Baxter's global anti-corruption and due diligence policies were not in place;[44] and (*iii*) the term "red flags" was not defined in Baxter's policies.[45]

Second, the Baxter and NN decisions demonstrate the importance of documentation to justify third-party selection and monitoring processes. They signal that Russian courts will not rely on a company's post-hoc statements and will require very detailed documentation of every step taken by the company with respect to its distributors. In the Baxter case, for example, the FAS requested "documents confirming every stage of the procedures" relating to the decision not to contract with MSC and was not satisfied with Baxter's explanation that the decision was made in discussions among Baxter's management.[46] As is the case more generally under Russian law, proof that certain actions were taken, and the reasons for them, often has to be in a particular documented form. That focus on documentation may seem technical and formulaic to non-Russian companies but, as these cases show, could affect significantly a company's ability to defend compliance decisions in the face of a legal challenge in Russia.

Third, companies are well advised carefully to consider privilege issues in structuring their anti-corruption compliance processes and related documentation. It appears that at least some of the documentation the FAS requested from Baxter, including the due diligence report on MSC, was not provided as a result of a determination that doing so would waive the U.S. attorney-client privilege.[47] Further, FAS's document request included a demand for copies of correspondence among Baxter's in-house legal counsel as well as external legal advisers.[48] These

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43. Ninth Arbitrazh Appellate Court Decision, note 12, *supra*, at 3.
44. *See* Ninth Arbitrazh Appellate Court Decision, note 13, *supra*.
45. *Id.* at 5-6.
46. FAS Decision, note 23, *supra*, at 10-11.
47. *Id.* at 11.
48. FAS Request for Additional Documentation, Case No. 4-14.31-243/00-18-14 (July 21, 2014), http://solutions.fas.gov.ru/ca/upravlenie-kontrolya-sotsialnoy-sfery-i-torgovli/18-29172-14 (Russian).

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requests indicate that companies should add Russian antitrust compliance to the list of the considerations to be weighed in deciding which material they can and should seek to protect under U.S. law, given that it likely would not be protected under Russian law.

Fourth, companies should consider timely reporting evidence of corrupt activities of their distributors or other third parties to Russian authorities. Although doing so may not be advisable in every instance due to a host of considerations, the NN and Baxter decisions make it clear that the courts and the FAS will discount a company's claim that its refusal to contract had to do with improper activity of the third party if that activity is not reported to or investigated by competent authorities in a timely manner. In the Baxter case, the appellate court emphasized that Baxter did not proactively approach Russian authorities with the evidence of MSC's alleged improper activities.[49] In the NN case, the FAS went so far as to request from the relevant authorities information regarding any investigations against SZ, and was told that no such investigations were under way.[50]

Finally, companies should also consider ways to minimize potential personal liability of their managers under the Russian Competition Law. As noted above, the FAS initiated cases against the CEOs of both NN and Baxter. The NN CEO was assessed a fine because she was the sole executive decision-maker, pursuant to NN's Charter, at the time of the antitrust violations.[51] In the case against Baxter's CEO, the FAS requested a list of all individuals involved in the decision not to contract with MSC, suggesting that cases against other Baxter employees were also a possibility.[52] Although the fines may be small, the individual managers also face disqualification and reputational risks. Decisions against individual employees, as well as those against companies, are made public, and the FAS has been known to emphasize its fines against individuals at public events. Companies should keep this in mind when structuring the decision-making processes around third-party

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49. *See* Ninth Arbitrazh Appellate Court Decision, note 13, *supra*, at 6.
50. *See* FAS Decision, note 17, *supra*, at 8-9.
51. FAS Fine Decree, note 21, *supra*.
52. *See* FAS Request for Additional Documentation, note 48, *supra*.

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selection and monitoring.

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The NN and Baxter decisions directly apply only to companies that are deemed to hold a dominant market position under the Russian Competition Law, and they ultimately resulted in relatively small fines (in comparison with the fines typically levied by U.S. and certain other regulators). Nevertheless, they provide a rare glimpse into the way Russian courts are likely to evaluate multinational companies' anti-corruption compliance policies and procedures. When carefully considered, they also provide welcome guidance on the way the companies can craft Russia-specific policies and actions to reduce their risks of adverse proceedings in Russia without compromising their global anti-corruption efforts.

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Brazil Issues Long-Awaited Decree Implementing the Clean Company Act

On March 18, 2015, Brazil's President, Dilma Rousseff, signed Decree No. 8,420 further implementing Law No. 12,846, the so-called Clean Company Act (the "Act"), which became effective on January 29, 2014.[1] The Decree took effect on March 19, 2015, when it was published in Brazil's Official Gazette.[2]

Awaited for more than a year, the Decree is part of a recently-announced "package" of new anti-corruption legislation being advanced by the Brazilian federal government.[3] Of particular significance, the Decree regulates the process for imposing administrative liability on legal entities for acts of bribery or corruption under the Act, both within and outside Brazil. It also sets forth guidelines for calculating fines and establishes rules that will govern leniency agreements and the criteria Brazilian regulators use to assess anti-corruption compliance programs, among other topics.

The Decree is a critical step in Brazil's implementation of the Act, which was enacted on August 1, 2013. Reflecting the growing political, economic, and social forces within Brazil that place increasing pressure on the government vigorously to prosecute corrupt acts, the Decree provides ever more reason for companies operating in Brazil to take further steps to review their compliance programs to assure appropriate alignment with the requirements of the Decree, and the Act itself, as well as other applicable anti-corruption laws such as the U.S. Foreign Corrupt Practices Act and the U.K. Bribery Act 2010.

I. The Decree's Role in Implementing the Clean Company Act

The Act (also known as Brazil's Anti-Corruption Law) imposes strict civil and administrative liability on corporate entities doing business in Brazil for corruption or bribery of Brazilian or foreign public officials, as well as fraud in connection with public tenders. It applies broadly to corporations, partnerships, and proprietorships, and to other for-profit and non-profit entities. The Act provides for monetary fines ranging from 0.1% to 20.0% of a company's annual gross revenues.

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1. *See* Andrew M. Levine, Bruce E. Yannett, Renata Muzzi Gomes de Almeida, Steven S. Michaels, and Ana L. Frischtak, "Brazil Enacts Long-Pending Anti-Corruption Legislation," *FCPA Update,* Vol. 5, No. 1 (Aug. 2013), http://www.debevoise.com/insights/publications/2013/08/fcpa-update.
2. The Decree is available at https://www.planalto.gov.br/ccivil_03/_ato2015-2018/2015/decreto/d8420.htm.
3. In addition to signing the Decree, President Rousseff submitted legislative proposals embodying the government's "anti-corruption package," following nationwide protests against corruption. These proposals address, among other topics, slush funds, money laundering in political campaigns, and stricter screening and conflict-of-interest rules for public servants.

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Although the Act's January 2014 effective date was a major milestone, many aspects of its implementation remained uncertain, as Brazil's federal government had yet to promulgate the required implementing regulation. The Decree at least partly achieves this critical step, especially with respect to federal administrative actions. While further clarifications of the Act may be issued by federal, state, and municipal authorities that share concurrent authority to enforce the Act, the issuance of the Decree is an essential development for companies conducting business in Brazil or that are otherwise subject to Brazilian law.

II. Key Provisions of the Decree

A. Overview & Jurisdiction

Among its most important provisions, the Decree establishes an administrative liability process ("Processo Administrativo de Responsabilização" or "PAR") for assessing the administrative liability of legal entities under the Act. The Decree requires the PAR to be concluded within 180 days from the date of the official publication that the process has been initiated, though extensions of this deadline are authorized. The Decree expressly provides for the possibility of searches and seizures in connection with investigations, upon request to the competent authorities. It also states that conduct charged by the government as violating the Act and Brazilian legislation on public bids and government contracts shall be adjudicated in a joint proceeding.

The Decree provides that the Comptroller-General of the Union ("CGU") shall have jurisdiction over enforcement involving alleged bribery of foreign (*i.e.*, non-Brazilian) public officials and, along with other federal governmental entities, concurrent jurisdiction over corruption cases involving Brazilian federal officials. The CGU is also empowered under the Decree to act in extraordinary circumstances, such as in the event of inaction by the authority originally tasked with handling the PAR, or in "complex" or "relevant" matters. There remain important questions as to how those potentially broad terms will be defined in the first instance by the CGU and then by any reviewing courts.

B. Fines & Other Sanctions

Implementing the Act's sanctions provisions, the Decree articulates the potential consequences for companies that violate the Act, including: *(i)* fines; *(ii)* publication of the decision sanctioning the breaching company in each of a local or national newspaper, notices at the company's headquarters, and on its website; and *(iii)* debarment, in the event of conduct that violates the Act and Brazilian legislation on public bids and government contracts.

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In perhaps its most detailed provisions, the Decree sets forth specific rules for calculating fines. The Decree provides detailed guidance for setting the maximum and minimum permissible fines as well as a methodology for calculating the fines actually to be imposed.

The Decree specifies that the maximum fine shall be set at the lower of: *(i)* a percentage of a company's gross revenues, capped at 20% thereof based on the presence of specific aggravating and mitigating factors; or *(ii)* three times the value of the benefit obtained or sought through the misconduct.[4] To facilitate calculation of the former figure, the Decree sets out methods for assessing aggravating and mitigating factors, such as the involvement of the company's senior management in the misconduct and the existence of a compliance program. To facilitate calculation of the latter figure, the Decree enables accused parties to deduct legitimate costs and expenses when the benefit sought or obtained is assessed, thus avoiding a windfall to the government if a bribe was paid but valuable goods or services (such as a stadium timely built to specification) were provided by the bribe-paying party.[5]

"Companies and individuals subject to the Act and, now, the Decree have more reason than ever to take stock of their existing practices and to assess how improvements can be made to assure compliance with not only Brazilian law, but also other anti-corruption laws that may apply to their conduct."

The Decree likewise establishes minimum fine levels, at the higher of: *(i)* the value of the benefit intended or obtained; or *(ii)* 0.1% of gross revenues, or BRL 6,000, when it is not possible to utilize the company's gross revenues. Companies that enter into leniency agreements might benefit from a reduction of up to two-thirds of the "applicable fine," as calculated under the Act and the Decree.

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4. This formula may well have important effects on how cases adjudicated under the Act are litigated. If the benefit obtained or sought exceeds the 20%-of-annual-gross-revenue figure, for example, the detailed rules for calculating the default fine will place significant pressure on accused parties and the government alike to learn the facts relevant to the various aggravating and mitigating factors that could affect the fine calculation. And, because calculation of benefits sought or obtained can also be the subject of dispute, it is possible that both alternative fine calculation methods may be litigated. Similar considerations will animate determinations of the minimum fine amounts if there is controversy over pertinent facts.

5. This approach for calculating "benefit" is roughly similar to the method utilized by U.S. federal courts to calculate the "gross gain" to be considered in the federal sentencing statute, 18 U.S.C. § 3571, which permits fining corporate and individual defendants convicted of a bribery or other offense up to twice the "gross gain" or "gross loss" caused by the crime of conviction.

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A table setting out the method identified in the Decree for calculating fines appears at the end of this article.

Additionally, the Decree specifies the operation of national registries publicizing details about individuals and companies that have been sanctioned under the Act or debarred.

C. Leniency Agreements

A company that has violated the Act or certain provisions of Brazil's legislation on public bids and government contracts may enter into a leniency agreement as a means to mitigate possible sanctions. Under the Act and the Decree, entry into a leniency agreement requires cooperating with the government's investigation and administrative proceeding, identifying other involved parties, and expeditiously providing information and documents evidencing the misconduct to the government. Specifically, under the Decree, in order for a company to enter into a leniency agreement it must: *(i)* take the initiative of approaching the authorities, when doing so is relevant; *(ii)* have ceased involvement in the misconduct; *(iii)* admit its participation in the misconduct; *(iv)* "fully and permanently" cooperate with the authorities; and *(v)* provide proof of the misconduct. As set forth in the Decree, the CGU may execute leniency agreements relating to conduct at the federal level or involving foreign governments, but it remains unclear whether – and, if so, to what extent – this authority will be shared with other law enforcement authorities, such as federal prosecutors.

Although the Act provides that a company will not be released from providing appropriate compensation for the damages it caused, it may benefit under the Decree from one or more of the following outcomes by entering into a leniency agreement: *(i)* exemption from publication of the decision sanctioning its conduct; *(ii)* exemption from the prohibition against receiving incentives, subsidies, subventions, donations, or loans from government bodies, public entities, or financial institutions owned or controlled by the government; *(iii)* reduction in the fine imposed; or *(iv)* exemption from, or mitigation of, administrative sanctions set out in certain statutes governing public tenders and government contracts. A leniency agreement may extend to legal entities belonging to the same "economic group" (*i.e.*, corporate family), provided those entities jointly execute the agreement.

D. Compliance Programs

The Decree contains several provisions relating to compliance programs. With regard to leniency agreements, the Decree requires a provision mandating the adoption or improvement of an existing compliance program by the breaching

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company. Also, as noted above, the Decree provides that the adoption and implementation of a compliance program will be a mitigating factor when calculating fines.

Consistent with best practices, the Decree recognizes that an effective compliance program must be risk-based, tailored according to factors such as a company's size, structure, and industry; jurisdictions where it conducts business; reliance on third parties; and the degree of interaction with government entities, among other considerations. The Decree also sets out parameters for assessing the effectiveness of a compliance program, including: *(i)* the commitment of the company's upper management to the program; *(ii)* the standards of conduct and codes of ethics applicable to employees, managers, and, as appropriate, third-party service providers; *(iii)* periodic training; *(iv)* internal controls; *(v)* specific procedures to prevent fraud and wrongdoing in the context of bidding procedures and the performance of government contracts, among other contexts; *(vi)* the independence and authority of the internal body responsible for applying and overseeing the program; and *(vii)* disciplinary measures applicable in the event of violations of the program.

As expected, these criteria largely parallel guidance previously provided by other regulators, such as the U.S. Department of Justice and the U.S. Securities and Exchange Commission in their November 2012 guidance,[6] and the U.K. Ministry of Justice in guidance issued in 2011,[7] as well as in pronouncements of the Organization for Economic Cooperation and Development.[8] The Decree also expressly states that the CGU will issue further regulations and guidelines that govern in more detail the assessment of compliance programs.

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6. *See* U.S. Dep't of Justice and U.S. Secs. and Exch. Comm'n, "A Resource Guide to the U.S. Foreign Corrupt Practices Act" (Nov. 2012) at 56-66, http://www.justice.gov/criminal/fraud/fcpa/guidance/.
7. *See* U.K. Min. of Justice, "Bribery Act 2010: Guidance to Help Commercial Organisations Prevent Bribery" (Mar. 2011) at 20-31, https://www.gov.uk/government/publications/bribery-act-2010-guidance.
8. *See, e.g.,* OECD, "Good Practice Guidance on Internal Controls, Ethics, and Compliance" (Feb. 2010), http://www.oecd.org/investment/anti-bribery/anti-briberyconvention/44884389.pdf.

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III. Conclusion

Issuance of the Decree is a long-awaited step in implementing the Act and underscores ongoing attention in Brazil to anti-corruption enforcement. Companies and individuals subject to the Act and, now, the Decree have more reason than ever to take stock of their existing practices and to assess how improvements can be made to assure compliance with not only Brazilian law, but also other anti-corruption laws that may apply to their conduct. While the enforcement environment in Brazil, as elsewhere, remains dynamic and subject to a variety of political, economic, and social forces, the promulgation of the Decree is proof that Brazil is taking clear steps to implement strong anti-corruption laws and that those ignoring best practices when operating in or from Brazil may be doing so at their peril.

We will continue to monitor the actions taken by the government in Brazil as it works to implement the Act and the Decree.

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Table 1

Maximum and Minimum Fine Amounts		
The *maximum* fine amount shall be set at the *lower* of:	20.0% of a company's gross revenues;* or	
	Three times the value of the benefit intended or obtained through the misconduct.**	
The *minimum* fine amount shall be set at the *higher* of:	The value of the benefit intended or obtained through the misconduct;** or	
	0.1% of a company's gross revenues;* or BRL 6,000, when it is not possible to use the company's gross revenues.	
Factors for Initial Fine Calculation		
The fine calculation begins by adding and subtracting amounts corresponding to percentages of a company's gross revenues;* calculated by reference to the following aggravating and mitigating factors:		% of company's gross revenues*
Aggravating Factors	Continuous misconduct	1% - 2.5%
	Involvement or knowledge of company's senior management	1% - 2.5%
	Interruption of the provision of public service provided or performance of construction work	1% - 4%

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	Company has solvency and liquidity ratios above 1, and reported net profits in previous fiscal year	1%
	Recidivism within 5 years	5%
	Contracts over BRL 1,500,000	1%
	Contracts over BRL 10,000,000	2%
	Contracts over BRL 50,000,000	3%
	Contracts over BRL 250,000,000	4%
	Contracts over BRL 1,000,000,000	5%
Mitigating Factors	Non-consummation of the violation	1%
	Company provided compensation for the damage caused	1.5%
	Company cooperates with the authorities, independently of a leniency agreement	1% - 1.5%
	Company self-reported misconduct before PAR was initiated	2%

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<table>
<tr><td rowspan="2"></td><td>Company adopted and implemented a compliance program</td><td>1% - 4%</td></tr>
<tr><td>Company signs and complies with a leniency agreement</td><td>Reduction of applicable fine amount by up to 2/3</td></tr>
<tr><td rowspan="2">In the absence of aggravating and mitigating factors, or whenever the calculation otherwise results in an amount that equals zero or less, the fine amount will be:</td><td colspan="2">0.1% of a company's gross revenues;* or</td></tr>
<tr><td colspan="2">BRL 6,000, when not possible to utilize the company's gross revenues.</td></tr>
<tr><td colspan="3">When it is not possible to utilize the company's gross revenues;* the fine amount will be capped at a minimum of BRL 6,000 and a maximum of BRL 60,000,000.</td></tr>
</table>

* Gross revenues in the fiscal year previous to the commencement of the PAR, after taxes.

** The value of the benefit intended or obtained through the misconduct will include the value of any undue benefit promised or given to a public agent or related third parties, as the case may be. The Decree enables accused parties to deduct legitimate costs and expenses when assessing the benefit intended or obtained through the misconduct.

U.K. Financial Conduct Authority Fines and Bans Two for LIBOR-Related Misconduct

While in-house counsel and compliance professionals monitoring activities in the United Kingdom are awaiting action on a number of matters, including those related to bribery and related misconduct, other regulatory actions have hinted at new vigilance by UK regulators, particularly the United Kingdom's Financial Conduct Authority ("FCA").

On January 22, 2015, the FCA levied substantial fines on senior officers of a London-based interdealer broker relating to the firm's involvement in the wrongful manipulation of LIBOR. It is the first time that LIBOR-related fines have been levied against individuals,[1] and the action yields several lessons for managers in the financial services sector who face the risk of employee misconduct.

The former CEO of Martin Brokers (UK) Ltd, David Caplin, and the firm's former compliance officer, Jeremy Kraft, were fined £210,000 and £105,000, respectively, with a 30% discount applying in each case for early settlement.[2] Both have been prohibited from performing any "significant influence function" in the regulated sector, effectively barring them from any future senior management roles in the U.K. financial services industry.

In May 2014, the FCA had fined the broking firm £630,000 for its role in the manipulation of LIBOR.[3] Among other things, the firm was found to have minimal compliance policies and procedures in place to regulate the activities of its brokers, as well as unclear reporting lines.

The FCA's actions serve to show that individuals found to be responsible for systemic compliance failings will face sanctions in order to illustrate that relevant officers and employees, as well as their employer, will be punished. It also signals a "broken windows" enforcement ethos whereby all breaches are pursued, even those by smaller industry participants.

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1. *See* FCA Press Rel., Two Former Senior Executives of Martin Brokers Fined and Banned for Compliance Failings Related to LIBOR (Jan. 22, 2015), http://www.fca.org.uk/news/two-former-senior-executives-of-martin-brokers-fined-and-banned.
2. FCA Final Notice re: David Caplin (Jan. 22, 2015), http://www.fca.org.uk/static/documents/final-notices/david-caplin.pdf; *see also* FCA Final Notice re: Jeremy Kraft (Jan. 22, 2015), http://www.fca.org.uk/static/documents/final-notices/jeremy-kraft.pdf.
3. *See* FCA Final Notice re: Martin Brokers (UK) Ltd (Martins) (May 15, 2014), https://fca.org.uk/static/documents/final-notices/martin-brokers-uk-ltd.pdf.

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This message was echoed in the FCA's recent announcement that non-executive directors who discharge high-level functions such as Chairman or Chair of various key committees within deposit-takers and dual regulated investment firms will be subject to the new Senior Managers Regime, which aims to increase individual accountability.[4]

The FCA's Findings

David Caplin

The FCA's Final Notice identifies Caplin, the chief executive during the relevant time period, as having assumed responsibility for ensuring the firm implemented adequate compliance systems and controls. The FCA also took Caplin's direct contact with the firm's brokers to amount to the assumption of *de facto* responsibility for monitoring their conduct.[5]

In summary, the FCA found that Caplin had:

1. Presided over a firm with an "extremely weak" compliance culture;
2. Failed to implement compliance advice received from a third party consultancy which highlighted shortcomings and provided recommendations;
3. Inadequately supervised the firm's compliance function;
4. Not effectively monitored and supervised broker conduct; and
5. Failed to remedy or identify the firm's lack of controls to prevent its brokers offering or receiving corrupt inducements.[6]

Caplin was found to have contributed to a culture at the firm that placed profit ahead of regulatory compliance and which neither rewarded compliant conduct nor penalized breaches of internal controls.[7] The FCA described Caplin as considering compliance to be *"unnecessary administration."*[8]

Jeremy Kraft

Kraft was the firm's compliance officer for the period in which the FCA found Martin Brokers liable for manipulation of LIBOR. He, like Caplin, was responsible for ensuring the adequacy of the firm's compliance systems and controls. The

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4. *See* FCA Press Rel., FCA Sets Out Approach to Non-Executive Directors and the Senior Managers Regime (Feb. 23, 2015), http://www.fca.org.uk/news/fca-sets-out-approach-to-neds-and-the-smr.
5. *See* FCA Final Notice re: David Caplin, note 2, *supra*, ¶ 3.
6. *See id.* ¶ 4.
7. *See id.* ¶ 26.
8. *See id.* ¶ 23 (emphasis added).

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FCA found that Kraft failed to exercise such responsibility with due skill, care, and diligence.[9] As with Caplin, the FCA concluded that Kraft's failures and inadequate conduct helped create an environment that enabled wrongful LIBOR manipulation to occur.

The FCA concluded that Kraft had:

1. Inadequately assessed the risks arising out of the firm's broking activities;
2. Inappropriately delegated his compliance responsibilities to unqualified members of staff and inadequately trained his staff;
3. Deferred to Caplin without challenging him;

"The clear takeaway for management of all firms is that they are responsible for upholding a transparent compliance culture in which risks are identified, assessed, and addressed by way of structured compliance systems that are properly implemented."

4. Failed to seek appropriate advice and support; and
5. Not kept the FCA adequately informed of the firm's compliance issues.[10]

Conclusion

The clear takeaway for management of all firms is that they are responsible for upholding a transparent compliance culture in which risks are identified, assessed, and addressed by way of structured compliance systems that are properly implemented. Furthermore, senior compliance

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9. *See* FCA Final Notice re: Jeremy Kraft, note 4 *supra*, ¶ 4.
10. *See id.*

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officers must be prepared proactively to challenge their more senior management in the event that compliance systems are inadequate.

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