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The Impact of Corruption on Global Business

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I appreciate the opportunity to speak to people in the legal and business community on corruption and its impact on business. This is an area where the NFTC is increasingly turning its attention because it constitutes a major barrier to global economic growth. It is bad for the people who suffer under corrupt governments, it is bad for business, and it is bad for the development of rule of law in these countries, which is an integral part of attracting foreign investment.

For those of you not familiar with us, the National Foreign Trade Council is the premier business organization advocating an open, rules-based world economy. Founded in 1914 by American manufacturers and shippers who supported an open world trading system, the NFTC and its affiliates now serve some 300 member companies through offices in Washington and New York. Our issues include trade, investment, tax, and human resources issues affecting the ability of our members to compete effectively abroad.

The NFTC's affiliate organization, USA*ENGAGE, is a broad-based coalition representing Americans from all regions, sectors and segments of our society concerned about the proliferation of unilateral sanctions at the federal, state, and local level. Despite the fact that unilateral sanctions rarely achieve our foreign policy goals, they continue to have political appeal. USA*ENGAGE promotes responsible alternatives to sanctions that actually advance US humanitarian and foreign policy goals, such as intensified US diplomacy, corporate social responsibility and multilateral cooperation.

There is no doubt that corruption, endemic in emerging economies around the world and not unknown in more developed countries, throws economic development into chaos and discourages foreign investment. For example, Transparency International's (TI) most recent *Global Integrity Report* cites Vietnam, one of the world's fastest-growing economies, as having the second weakest overall anti-corruption framework of the group of countries assessed by TI in 2006. This should be a serious cause for concern to prospective investors, particularly since the findings suggest that governance and corruption challenges in Vietnam and similarly ranked countries are deeply rooted and systemic. And indeed, the Department of Justice announced last week the arrest and indictment of four individuals on charges that they and their company, Nexus Technologies, Inc., paid at least $150,000 in bribes to Vietnamese officials to obtain contracts to supply the Vietnamese government with technology and equipment.

Any ethical prospective investor in these countries must expend significant resources to avoid corruption with no guarantee that perfect compliance can be achieved, given the ambiguities and moving goalposts that frequently characterize enforcement today. Nor can a prospective investor that plays by the rules be assured that it can compete fairly on a level playing field for public sector projects that could benefit the populace at large and provide access

to Western technology and management. When corruption is endemic, the people, the country's infrastructure, its government institutions and companies that strive to comply with good business practices all lose out.

For many years, as you know, the U.S. stood alone, having criminalized transnational bribery in 1977 with the Foreign Corrupt Practices Act. The OECD Anti-Bribery Convention, now ratified by 37 countries, criminalized transnational bribery in 1996 for the first time for its members. The Organization of American States' Inter-American Convention against Corruption, signed by most countries in the Americas in 1996, also requires members to criminalize transnational bribery.

In 2003, the United Nations Convention against Corruption was adopted by the General Assembly. To date, 140 member nations have signed and 122 have ratified it. Interestingly, countries that have not yet ratified the Convention, include Vietnam, Saudi Arabia, India, Malaysia, Japan and Germany amongst others. The efficacy of the Convention depends upon the strength of the signatories' implementing legislation, relevant legal infrastructure of the member states and most importantly, enforcement against corrupt officials. As the Convention entered into force in December 2005, it is too early to know how effective it will be in strengthening global efforts.

The NFTC led the effort in the business community to support the UN Convention. Our efforts fostered successful government – business cooperation to ensure that US implementation appropriately addressed the treaty's requirement for a private right of action. Our suggestions were adopted by the Administration in its explanatory language submitted to the Senate along with the convention, and that enabled me to testify in support of it before the Foreign Relations Committee.

Despite these multilateral efforts, however, corruption remains endemic. In a recent article, Wharton Legal Studies professor Philip M. Nichols said, "Corruption and bribery have moved to the forefront in discussions about business. The list of countries that have been politically or economically crippled by corruption continues to grow, and businesses with long-term interests abroad will ultimately be harmed by any plans that include bribery." TRACE International, a non-profit organization that tracks anti-corruption efforts, launched a confidential bribe solicitation reporting network in 2006. According to TRACE's most recent report, more than 1,500 reports by TRACE members were made to its BRIBEline in the five months following its inauguration, documenting bribe demands in 136 countries.

Further evidence of the problem corruption poses for international trade and investment is found in the rising level of U.S. prosecutions brought by the Department of Justice (DOJ) and the Securities Exchange Commission (SEC). Over the past six years, the number of new enforcement actions has risen at least five-fold, many involving significant companies that have made major investments in compliance. According to recent press reports, Justice and SEC officials indicate that at least one hundred investigations are now in progress. Another data point: since 1990, there have been 78 SEC dispositions of FCPA cases and nearly 20 percent of them took place in 2007.

These enforcement actions involve foreign as well as U.S. firms. Although the FCPA has always applied to issuers that are neither incorporated nor headquartered in the United States,

2007 saw new efforts to enforce the law against foreign issuers, even if the activities in question occurred entirely outside the United States. Mark Mendelsohn, the Deputy Chief of the Fraud Section at Justice has stated publicly that his prosecutors are focusing on foreign issuers.

The first major prosecution was against Norway's Statoil ASA in late 2006, with the company settling charges for a fine of $10.5 million and surrendering another $10.5 million in profits. Statoil had entered into a consulting contract with an offshore intermediary entity controlled by an Iranian government official in an effort to develop portions of the South Pars oil field. Statoil agreed to pay $15 million in consulting fees over 11 years and obtained a contract to develop the field.

In June 2007, a former Alcatel executive, Christian Sapsizian, pled guilty to two counts of violating the FCPA. Sapsizian is a French citizen working for a French firm who was charged with paying bribes in Costa Rica. His sole connection to the United States was that Alcatel stock is listed on an American exchange. By the end of 2007, high-profile FCPA investigations were underway with respect to several other foreign corporations including Siemens, BAE, and Panalpina plus a host of companies implicated in the Oil for Food scandal.

2007 was also remarkable for the largest penalty levied by the U.S. government as subsidiaries of Baker Hughes received a combined penalty/fine of $44 million. In addition to financial penalties, Justice/SEC have a clear preference for requiring offending firms to retain outside compliance monitors. Half a dozen cases that concluded in 2007 included such a provision, often mandating the monitor for a period of three years.

Monitors are outside compliance experts, mostly members of the FCPA defense bar and frequently former prosecutors, who are charged with overseeing the company's compliance efforts and reporting back to the U.S. government on any new issues they might discover. As Alexandra Wrage, President of TRACE, pointed out recently in an article in *Federal Ethics Report*, as monitorships appear to be limited to a small cadre of FCPA practitioners, often an attorney is working "for" government prosecutors as a monitor in one case, while defending other clients before the same prosecutors who must approve a company's choice of monitor. With the revolving door between SEC, Justice, and the FCPA defense bar in full swing, this clearly has potential for abuse and cronyism.

Indeed, Congressional scrutiny of the selection of John Ashcroft's consulting firm at a cost of up to $52 million as a monitor resulted in DOJ "guidelines" for the selection and use of monitors being issued in March 7, 2008, four days before a hearing on the subject by the House Judiciary Subcommittee on Commercial and Administrative Law. We believe that the process remains flawed however, and support the recommendations Rep, Bill Pascrell, Jr. (D-NJ) outlined in his testimony before the Subcommittee on March 11, 2008. These include full disclosure of fees and taking the selection of monitors out of the hands of U.S. Attorneys.

Unfortunately, the scope of FCPA enforcement is such that financial burdens generated by corruption in international trade are not borne solely by the guilty. Reputable companies in the course of proposed acquisitions have uncovered problems in the company being acquired. Titan, InVision and ABB-Vetco-Gray cases are recent examples. Resolution of these problems through negotiation with the government or abandonment of the acquisition is not cheap—tens

of millions of dollars of legal fees on the part of the proposed buyer if the anecdotal evidence is correct.

Despite a plethora of multilateral and U.S. based efforts, corruption remains a serious problem. Be assured that the NFTC fully supports vigorous and even-handed enforcement of anti-corruption measures. As I said at the beginning, we view corruption as a serious trade barrier. At the same time, however, we are concerned about the ambiguous scope of some enforcement trends, the significant amounts companies must spend on compliance with no assurance that even best efforts will prevent major fines or expenditures, the chilling effect that government action can have on *bona fide* corporate social responsibility, and finger pointing at the business community as the main source of the problem

For example, the 2004 prosecution of Schering Plough in a civil action by the SEC involved corporate donations to a *bona fide* Polish charity engaged in historic preservation headed by a civil servant with whom Schering did business in another capacity. The civil nature of the prosecution meant that it focused on Schering's internal controls and accounting for the expenditure, not on whether something of value was received by the government official. Nonetheless, this settlement and other threatened prosecutions involving *bona fide* charitable contributions --with no apparent element of personal gain for the foreign official --have cast a chilling effect on corporate social responsibility.

Our members and most members of the US business community want to comply with the law, but they have to know what it is before they can do that effectively. The deliberate expansion of the FCPA by Justice and SEC through targeting new areas such as charitable contributions and foreign company operations outside US jurisdiction may be warranted by public policy, but expansion driven by prosecutions and not by amendments to the law raises questions of basic process. Companies do not have notice of the expanded scope or changed policy and an opportunity to comment before they can be penalized. Finally, emphasizing draconian enforcement against corporations as the principal means of eradicating global corruption is not enough to put a meaningful dent in the problem as some of my earlier remarks have made clear. Other, less scrupulous companies from jurisdictions with weak anti-corruption laws simply fill the gap where the playing field is skewed. If the OECD and UN Conventions do not raise the overall level of global compliance, then the United States may have to seriously consider whether a government's failure to enforce its own laws or multilateral obligations it has undertaken against endemic corruption should be actionable under either WTO rules or U.S. trade law.

The NFTC is in the process of initiating a new project to examine both U.S. enforcement issues and global compliance in greater detail, so you should expect to hear from us on this in the near future.

Thank you for the opportunity to speak to you today.