Anti-corruption efforts in Latin America: A CHANGING LANDSCAPE

By Recaredo Romero

Latin America's long-awaited broad-scale mobilization against corruption has started to materialize, and is expected to continue. Due to popular demands from a growing middle class as well as pressure from international development organizations, countries such as Brazil, Colombia and Mexico have recently enacted anti-corruption frameworks that place strict penalties on individuals and corporations found guilty of acts of bribery, fraud in public procurement and bid rigging.

The passage of these regional laws coincides with increased scrutiny on business transactions in Latin America by the US DOJ and the US SEC. In recent months, actions concerning Foreign Corrupt Practices Act (FCPA) violations have been brought against companies and individuals doing business in Argentina, Brazil, Mexico, Panama, and Venezuela. Moreover, an increase in future Latin American-focused FCPA cases is likely, as the risk and prevalence of corruption remains high, and the new local anti-bribery laws set the expectation for more effective judicial cooperation between the US and Latin America.

Brazil

After millions took to the streets in more than 100 Brazilian cities in June-July 2013 to express discontent over their government's massive public spending and lack of institutional transparency, Brazilian politicians were spurred into passing a landmark anti-corruption bill that had previously stalled in Congress for over three years.

Known as the "Clean Company Law (*Lei Anticorrupção Empresarial*)," the legislation establishes direct civil and administrative liability for companies found guilty of foreign and domestic bribery and takes effect in January 2014. The new law includes harsh penalties for violations, and gives the government authority, among several remedies, to seize a company's assets or blacklist it from future contracts.

Colombia

Colombia, the Andean region's most populous country, has undertaken significant efforts to fight corruption. The new Anti-Corruption Statute (Law No. 1474 of 2011) criminalizes the bribery of both local and foreign public officials, includes imprisonment penalties of up to 15 years and, like the UK Bribery Act, specifically addresses commercial bribery.

A significant development is the launch by President Juan Manuel Santos of the world's first "High Level Reporting Mechanism" (HLRM) in April 2013. The HLRM is a preventive mechanism designed to address corruption in public procurement and the public sector, to issue early warnings and allow the government to take necessary corrective measures but, at the same time and to the extent possible, ensure that the bidding procedure is successfully carried out.

Mexico

Mexico has also seen corruption move to the forefront of public concern. Shortly after becoming President-Elect in late 2012, Enrique Peña Nieto announced a bill to create a National Anti-corruption Commission that would have the powers to investigate both private and public corruption cases at federal, state, and municipal levels.

A few months earlier, the Federal Law against Corruption for Public Procurement (*Ley Federal Anticorrupción en Contrataciones Públicas – LFACP*) went into effect in June 2012. The LFACP could play an important role in developing the necessary institutional reform to handle President Peña Nieto's plans to allow private investment in Mexico's oil and gas sector for the first time since 1960, which could usher in a wave of new foreign direct investment.

Enforcement challenges

Policy experts have identified a significant correlation between corruption and the strength of a nation's regulatory and enforcement mechanisms. Countries such as Haiti and Venezuela, which have among the lowest international rankings of public governance, correspondingly have the highest rates of perceived corruption. Conversely, Chile, which has the strongest institutional controls according to the 2013 World Bank "Doing Business Report," also maintains the Latin America's lowest rate in fraud, bribery, and graft.

As Chile's success in combating corruption has demonstrated, the challenge for Latin America has less to do with enacting policy and more to do with implementing and enforcing it. Countries that recently implemented reforms, such as Brazil, Colombia, and Mexico, will need to enhance their internal capacities to effectively track complex money trails. Meanwhile, the delicate nature of prosecution cases involving public officials will require substantial determination and political will.

Prevention better than response

Given recent developments throughout the region and increased scrutiny of business in Latin America by regulators such as the US DOJ and SEC, companies should redouble efforts to enhance their anti-corruption compliance programs. The following four recommendations are worth noting:

» **Proper risk assessment:** Risks vary from country to country, within different industries or by company depending on the level of government interaction. Adequate identification of the risks and related exposure is key to tailoring effective procedures and controls.

» **Third party due diligence:** Companies should look into the details of transactions and their related third parties (e.g., agents, suppliers, joint venture partners) to identify and avoid the risk that third parties could offer bribes on their behalf. The due diligence should provide a good understanding of the third party's track record, business practices, and reputation. A higher level of due diligence should be conducted on high-risk third parties.

» **Due diligence on local investment targets:** Investors should undertake in-depth due diligence reviews of the target's anti-corruption policies and procedures, the target's culture and leadership stance toward integrity and ethics, and market reputation. A multi-tiered due diligence approach depending on the level of government exposure is recommended.

» **Training:** Many Latin American companies have little to no awareness regarding the requirements of local (and international) anti-bribery laws. A robust training program should be designed and implemented, and their related activities properly documented. Training should ideally include employees of relevant third parties as well.

While it is too early to predict whether government agencies will aggressively enforce recent anti-corruption laws, companies should certainly expect a higher number of corruption-related prosecutions in Latin America than those observed in the past. Companies that do their homework will be better prepared to prevent incidents, or seek more lenient treatment from the authorities and other stakeholders, should an incident occur.

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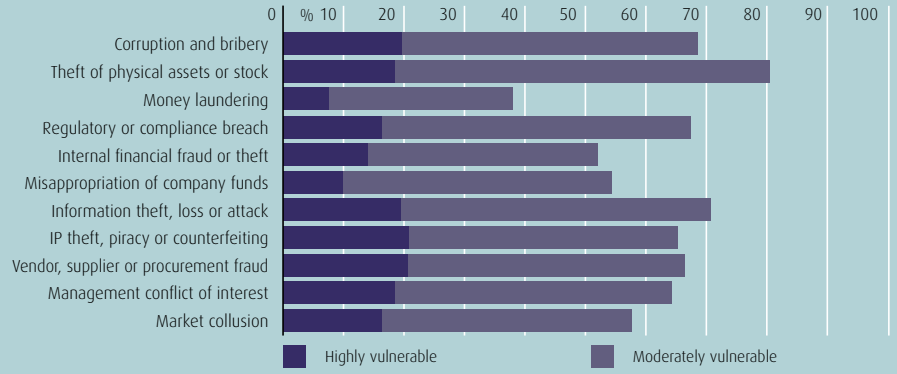
NATURAL RESOURCES — ECONOMIST INTELLIGENCE UNIT REPORT CARD

The natural resources sector has mixed news this year. On the one hand, overall fraud incidence (72%) is above average, as is the number of respondents reporting an increase in exposure to fraud at their firms (85%). Similarly, these companies saw the highest incidence of corruption and bribery (19%) of any industry. On the other hand, the average proportion of revenue lost to fraud (1.5%) is only slightly above the survey norm. Although corruption is a well-known issue for extractive industries, the survey suggests that vendor or procurement fraud requires greater attention. The sectoral incidence of this crime (25%) is markedly above the survey norm (19%). Moreover, vendors and suppliers played leading roles in fraud at 29% of all natural resources companies last year, or 42% of firms that experienced fraud and where the perpetrator was known – also above the norm. Nevertheless, a below-average number of natural resource company respondents believed that their company is at least moderately vulnerable to vendor fraud (67%, compared with 70% for the overall survey), while only 44% said that their firms were planning to invest in vendor or partner due diligence (compared with an average of 43%). Looking ahead, efforts against this type of fraud deserve a higher profile.



Loss: Average percentage of revenue lost to fraud: 1.5%

Prevalence: Companies affected by fraud: 72%

Areas of Frequent Loss: Percentage of firms reporting loss to this type of fraud:
Information theft, loss or attack (27%) • Theft of physical assets or stock (26%) • Vendor, supplier or procurement fraud (25%) • Corruption and bribery (19%) • Management conflict of interest (17%)
Regulatory or compliance breach (16%) • Internal financial fraud or theft (16%)

Increase in Exposure: Companies where exposure to fraud has increased: 85%

Biggest Drivers of Increased Exposure: Most widespread factor leading to greater fraud exposure and percentage of firms affected: IT complexity (38%)