Reuters Legal News

Russia's invasion of Ukraine: effects on regional FCPA enforcement

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MARCH 22, 2022

For companies doing business in Russia, the invasion of Ukraine will have broad implications that go beyond compliance with economic sanctions. One of the key compliance risks in the region has always been the Foreign Corrupt Practices Act (FCPA). The FCPA aims to tackle foreign corruption by prohibiting the bribery of foreign government officials and requiring companies to maintain an adequate system of internal controls.

The combined effect of these provisions is that companies engaged in foreign bribery, or who turn a blind eye to such conduct, can face an FCPA enforcement action from the Department of Justice (DOJ) or the Securities and Exchange Commission (SEC), and sometimes both. FCPA fines are some of the biggest collected by the DOJ and SEC, and the average fine (https://stanford.io/3qmOWjF) over the last 10 years is well over $100 million.

While there may be a decrease in overall FCPA enforcement due to companies exiting Russia, there will be a much higher risk of FCPA liability for those that remain operating in the country. In addition, we can expect to see an increase in enforcement for companies operating in Eastern Europe and the Commonwealth of Independent States (CIS), particularly in jurisdictions where Russian President Vladimir Putin has cultivated close ties with Moscow.

Current state of FCPA enforcement in Russia

Before looking at how the invasion of Ukraine will affect FCPA enforcement in Russia, it's important to understand the dynamics that have shaped the current state of FCPA enforcement in the country. To do this, it's useful to use enforcement activity in China as a tool for comparison. Both countries are ranked poorly on Transparency International's Corruption Perception Index (https://bit.ly/3L1KRct) (Russia is ranked worse for corruption than China) and both have frosty relationships with the U.S.

In addition, FCPA enforcement actions in both countries have broadly similar fact patterns. Typically, the conduct involves a company using agents or consultants to pay bribes or kickbacks to win business for the company. In most cases, the bribery does not involve high-ranking politicians; rather, it involves relatively obscure government officials who work at state-owned companies. This is a key issue in both China and Russia as many large companies in both countries have some element of state ownership.

While almost 40% of all FCPA settlements in the last five years have involved conduct in China, only about 7% have involved conduct in Russia, but there is good reason for this divergence. FCPA enforcement activity is heavily focused on companies that have a security traded on a U.S. exchange. This is because companies that have a security traded on a U.S. exchange are subject to both the FCPA's 'anti-bribery' and 'internal controls' provisions. (Companies that do not have a security traded on a U.S. exchange are only subject to the FCPA when the violation involves conduct within the U.S.).

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While there are 150 Chinese-based companies with a security traded on a U.S. exchange, there are only eight Russian-based companies. This means that U.S. regulators have had far fewer Russian-based companies that could be the target of an FCPA enforcement action. Even though regulators can target U.S.-based companies with operations in Russia, Russia's lower level of economic activity also contributes to its comparatively low level of FCPA enforcement.

The more business being done in a region, the more opportunities there are for FCPA violations. This is why the countries with the highest levels of FCPA activity are countries with large economies (China, Brazil, India and Indonesia). Russia has a significantly smaller economy than those countries and understandably sees fewer FCPA enforcement actions. The key takeaway here is that FCPA enforcement activity is not a function of how 'corrupt' a country is perceived to be, but has more to do with the level of economic activity and the number of potential targets available for FCPA enforcement actions.

New dynamics introduced by the conflict

Russia's invasion of Ukraine has introduced two new dynamics that will shape future FCPA enforcement activity in the region. The first dynamic is that Russia has now been elevated to priority-number-one for U.S. enforcement authorities. In addition to strong rhetoric regarding tackling Russian corruption, President Joe Biden has created a unique task force with the specific goal of enforcing sanctions, export restrictions and economic countermeasures designed to freeze Russia out of global markets.

While the task force is focused on sanctions violations, these rarely occur in a compliance vacuum. The work of the task force is likely to turn up a variety of corrupt foreign officials in Russia, and this could lead to FCPA referrals to the DOJ or SEC for companies with close ties or working relationships with those officials.

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While this new political dynamic will favor more FCPA enforcement, the economic effects of the invasion may outweigh this. The sanctions imposed by the U.S. and its allies have already crippled the Russian economy, and there is likely to be a cutback on government spending and infrastructure projects in Russia. This drop in economic activity will provide fewer opportunities for FCPA violations. More presciently, the sanctions have also led to hundreds of companies withdrawing from Russia, meaning that the already-small pool of companies that could be the target of an FCPA investigation is shrinking quickly.

Even for companies that may have violated the FCPA prior to their exit, leaving Russia will still help them reduce FCPA liability. Abandoning operations in Russia provides the companies with a remediation story that defense counsel dream of: The business unit in question no longer exists, the company no longer operates in the jurisdiction and, most likely, any employees involved in the misconduct no longer work for the company. These are the kind of facts that could lead to a significant reduction in an FCPA fine, or a declination if the company self-discloses the conduct.

The upshot of these two dynamics is that while the pool of potential FCPA violators is going to shrink significantly, for those remaining in Russia, there will be a much higher risk of becoming the target of an FCPA investigation.

Eastern Europe and CIS

In addition to the increased risk of operating in Russia, companies should expect to see more compliance risks in Eastern Europe and the CIS. Many countries and political leaders in these jurisdictions have strong ties to the Kremlin which will make them a visible target for FCPA enforcers. Companies with operations in these regions should be proactive in strengthening local compliance programs and investigating possible compliance weaknesses.

In addition, there may also be a rise in FCPA enforcement for businesses linked to Russian 'oligarchs,' a group that appears to be growing by the day. For example, Alexei Mordashov, who was recently put on the sanctions list, is alleged to own a substantial part of German travel group TUI. (TUI may be able to avoid FCPA enforcement given that its stock is traded over-the-counter rather than on a U.S. exchange).

As countries around the world collaborate to identify individuals with ties to the Kremlin, the press coverage may become an advertisement to the DOJ and SEC that those companies are ripe for an FCPA audit. In addition to the increased regional risk in Russia, Eastern Europe and the CIS, compliance professionals in those regions will have their work cut out for them.

About the author

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This article was first published on Reuters Legal News and Westlaw Today on March 22, 2022.