

## 4. Challenges for Compliance and Integrity Management in Latin America

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### 4.1 Introduction

In September 2018, the International Anti-Corruption Academy (IACA, a highly specialized international organization created in 2011 by an initiative of the United Nations Office of Drugs and Crimes and other stakeholders) announced the launch of a new, long-term project entitled *Corporate Compliance Program Benchmark Project* with the intention to produce „the first [public and international] database on anti-corruption corporate compliance to be set up by an academic/non-profit organiza-

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tion." Beyond the potential of the actual data generated, the IACA's project already provides a clear point of reference to a research agenda that has been steadily growing in popularity over the past decade: the role of ethics management in curbing private corruption. Thus, the IACA takes up the beacon that was first lit by the International Organization for Standardization (ISO) in October 2016 in the form of the *ISO 37001 – Anti-Bribery Management Systems*. Individually, the two initiatives might not represent a new way of understanding corruption in the private sector; but taken together, they certainly signal a breakthrough in the way the international anti-corruption community has traditionally approached the issue, and bring much welcomed attention to an area that past corruption studies have felt uncomfortable visiting.

- 1 The novelty of this international agenda also reminds us that a rather crucial dimension of corruption control continues under intense academic debate, creating a split that affects the implementation of ethics management programs (EMP) in business organizations – the preference for designs focused on legal compliance or those which emphasize moral integrity. Certainly, most contemporary programs reflect a combination of both approaches, hopefully tailoring their degree of centrality to the specific conditions faced by the organization. However, more often than not EMPs are set up without proper corruption-risk assessments and simply translate into local language the policies and guidelines adopted by their counterparts in more advanced economies.
- 2 The failure to consider local conditions poses a particularly significant source of trouble for corporations doing business in Latin America. For centuries, corruption has been a feature of this part of the world, representing, in some cases, an almost tacit norm. Very often, the issue has been justifiably portrayed as culturally accepted and tolerated, even if not necessarily welcomed in the framework of democratic rule and growing liberal values. Indeed, the phrase 'He steals but gets things done' is commonly heard in casual conversation to refer to public authorities from all levels of the state apparatus, and its popularity extends from the streets of Buenos Aires to those of Lima and Mexico City alike. More than language or religion, this acceptance of corruption as a *fact of life* is perhaps the most common Latin American trait discussed among its people.
- 3 Taking a closer look, behind this tolerance of malfeasance hides a pattern of political behavior that, historically, channeled power to elites who, abusing public funds and other resources, became ever richer and more powerful, thus enabling authoritarian regimes whenever local conditions allowed it. In these contexts, the private sector consistently played a key role in enabling the recreation of corrupt elites by conspiring with or, at the very least, accepting the preferential treatment accrued to them. Only recently has the consequent inequality affecting social groups started to generate a backlash from both business organizations and

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common citizens alike, who tired of being taxed by the myriad externalities of elite misrule, are repeatedly and forcefully expressing their rejection of corruption and demanding drastic reform and the punishment of those involved. Thus, countries in Latin America have begun to take important steps to implementing systems of integrity and pass tougher laws to fight corruption.

In this chapter, we address the general patterns of private-corruption control in Latin America, and describe the legal and cultural challenges that very often prevent compliance and integrity measures from taking root. In doing so, the chapter contrasts the theoretical progress of the field with the realities of public and private implementation in the region, aiming to present a concise but accurate depiction of the business environment and the various risks posed to local and foreign agents.

#### 4.2 Theoretical compliance and integrity approaches to corruption control

Although links between the seemingly contending approaches of compliance and integrity have recently started to take hold in debates about corporate ethics in international settings, Latin America can be said to have only recently entered the whole arena of ethics management and begun to take action in response to public fatigue with corruption. Thus, it has taken decades for the region to realize that malfeasance need not be the norm, finally prompting people in the streets as much as opinion leaders and decision makers to start talking about the future instead of merely sighing about present and past. However, notwithstanding the welcomed interest in compliance with international anti-corruption standards being introduced in several Latin American countries, the challenge invites anew warnings about the intricacies of policy diffusion and localization. For this reason, it is best to approach the topic of compliance and integrity in this part of the world by first looking at its origins and evolution elsewhere.

Looking at the historical and global origins of ethics management as academic and policy concerns, the normative split between compliance and integrity can be traced back as far as ancient China in the arguments between Confucianism and legalism, and later, in the West, through the classic works of moral philosophers and their theories of value ethics and deontological ethics. More recently (and significantly), the discussion re-emerged in the field of administrative ethics in the first half of the 20<sup>th</sup> century, and was eventually picked up by the corporate world after the emergence of compliance as a relevant issue for business organizations. As Gable et al. (2009: 457) recount, „a series of high-profile anti-trust prosecutions in the late 1950s and early 1960s brought the first expansive adoption of corporate compliance programs in the United States,” a process that would eventually reach its peak in the United States Federal

Sentencing Guidelines of 1991 and the radically new set of incentives that they produced. With this milestone we may think of EMPs as a rather recent evolution in the global corporate world, albeit one that had been in the pipeline in many forms and for many years. From the adoption of the Sentencing Guidelines onwards, compliance programs became an almost indispensable feature of international business, quickly influencing local players and spreading the spirit of the anti-corruption movement through the private sector.

- 7 Due to the form of its inception, corporate compliance was heavily influenced (one might almost say defined) by a preoccupation with criminal liability and the preventive development of an affirmative due diligence defense (Fan 2014) against prosecution. Thus, at the core of EMPs based on compliance was an emphasis on detection and punishment of rogue agents, but also the incentive to prioritize window dressing rather than the effective transformation of corporate culture.
- 8 It didn't take long for integrity to join compliance at the forefront of business ethics management. In fact, integrity concerns had been built into the structure demanded by the Sentencing Guidelines, although limited to a much smaller role. The logic was fairly straightforward: while compliance with rules and regulations is clearly a necessary aspect of organizational life, and corporations not only need to monitor the activities of their members to attain predefined business goals but also to avoid criminal and civil liabilities in order to survive, a focus on systems of control creates inefficiency and, more importantly, regularly fails to produce desired behavioral objectives. Furthermore, legalism is inherently incapable of anticipating every and all situations, thus producing a fair degree of risk that cannot be reduced without complementing it with an alternative approach. Integrity represents then the natural corrective to a condition that is inherent to organizational structures, providing them with the adaptability that business activities require.
- 9 Beyond its initial role, integrity became quickly regarded (first in academia and then by practitioners, at least in discourse) as generally superior to purely compliance models in at least one respect: it fostered a culture of individual and group self-improvement, rather than a 'race to the bottom'. In a series of interviews with CEOs conducted by Wulf (2012), respondents were of the opinion that, in the basis of compliance, „you need to understand where the line is between what you can get away with and what you cannot get away with... You can go up to this line, but we do not want you to step over it into what you cannot get away with." (p. 151) From an integrity approach, on the other hand, the organization „want[s] you to be the best you can be. And do the right thing even if the law says you do not need to do it in a certain way. You are still going to do it the right way, and you are going to do it much better than you need to." (p. 152) Indeed, Fan (2014: 366) suggests that a focus on tradi-

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tional compliance „increases the risk of ‘moral mediocrity,’ while [integrity] can encourage more self-governance.”

However, the problem with focusing purely on integrity lies in the gap 10  
between private/environmental norms and professional/organizational expectations. In other words, the discrepancy between the meanings of integrity inside and outside the organization. This situation becomes particularly acute in low-income countries, where many – if not all – major economic players in the private sector come from countries characterized by well-functioning institutions and low levels of corruption. In those cases, organizations might feel forced to (a) socialize domestic employees in line with headquarters' corporate culture, while also (b) lowering ethical standards in order to compete effectively with local insiders. Together, the contradictory movements could be called a *mutually adaptive learning strategy*. But even if the organization refuses to lower its standards, there remains the issue of employee socialization and the unrealistic expectations of having an honest employee in a ‘dishonest’ environment.

Among other important elements, business requires a shared understanding 11  
among stakeholders about the principles that are to be followed during their interactions; when this minimal condition is not met, transactions costs increase and efficiency drops. Likewise, when an individual is artificially secluded from their local normative system by imposition of compliance and integrity requirements designed for a different setting, it should not come as a surprise that the main problem becomes not one of unethical behavior, but lack of *awareness* of ethical risks. As Treviño et al. (1999: 133) indicate, „No matter how strong their values, employees cannot be expected to be naturally familiar with all of the laws and regulations that pertain to their work. Nor can they be expected to be automatically aware of the ethical ambiguities that they might face in a particular industry or position.” The risk imposed by this condition is present in all cases, but it rapidly grows in direct relation to the distance an organization travels from its cultural and economic base.

The limits of both compliance and integrity must be then considered 12  
when evaluating the performance of the elements commonly found in EMPs, such as codes of conduct; control, monitoring and auditing systems; complaint mechanisms and channels; training programs; human resources policies; and mechanisms to address potential conflicts of interests. The goal of such assessment should be the attainment of what authors have called *good corporate citizenship*: the goal of bringing organizational culture to more closely reflect the values of the larger society by focusing on integrity measures rather than compliance alone. For Gabel et al. (2009), this concept „describes the role of the corporation in administering citizenship rights for individuals and promoting socially responsible conduct... Good corporate citizens, like private individuals, are expected to obey the law.” In short, the endpoint of convergence be-

tween compliance and integrity – two approaches that have been historically at odds – is the recognition of their mutual fit in a synergetic design based on a concern for society's welfare, and not merely the increase of profits.

### **4.3 Corruption-risk factors in Latin America**

#### **4.3.1 Legal environment**

- 13 As Fernando Avelar (2012) appropriately pointed out, „Latin America is one of the primary areas where U.S. companies are most at risk from FCPA violations because of the corrupt culture of business and politics present in many Latin America countries.“ While this cultural aspect of risk assessment will be explored in the next sub-section, we need to start by considering the legal environment faced by foreign corporations in the region.
- 14 Generally speaking, regulatory frameworks related to anti-bribery systems are not as developed and stringent in Latin America as they have consistently been for the past decade in most OECD countries. While recent events such as the uncovering of a massive transnational corruption network built by the Brazilian conglomerate Odebrecht, and the production of ISO 37001 have distinctively generated an increase in efforts to control corruption in the private sector, national anti-corruption regimes are commonly characterized by their tendency towards the signaling of commitments rather than carrying out concrete implementation and enforcement activities (as suggested by data from UNDP 2012). Still, there have been important legal developments in core areas that, at the very least, affect the way business organizations address compliance and integrity in host countries. While Section IV will delve deeper into the conditions found in different countries, the rules involving corporate criminal liability and exemption/mitigation of sanctions are described below to provide a general overview of formal legal expectations.
- 15 Over a century after the Supreme Court of the United States first sanctioned the application of criminal liability against a private company (in the 1909 case *New York Central & Hudson River Railroad Co. v United States*) for making unlawful payments of rebates to another company, Latin American countries finally adopted legislation to address the responsibility of legal persons in corruption cases. Pursuing higher compliance with commitments of their own as signatory countries to the Organisation for Economic Co-Operation and Development's (OECD) Anti-Bribery Convention, Argentina, Brazil, Chile, Colombia, Costa Rica and Mexico have enacted legislation addressing various liability regimes for private enterprises, as well as conditions that may preventively be adopted to limit this type of risk exposure. In Argentina, Law No. 27401 established the criminal liability of private legal persons involved in bribery and other unlawful acts regardless of nationality of capital assets, al-

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lowing exemption from penalties if the offending company voluntarily reports the offence, returns illicit gains, and can prove to have had a properly implemented EMP prior to the occurrence of the crime. In terms of sanctions, however, the law only considers the forceful dissolution of the entity if it was created with the sole purpose of committing the criminal act, or if this represented the core of its activities. By comparison, the Chilean corporate criminal liability act embodied in Law No. 20393 established the possibility of sanctioning the offending company by ordering its dissolution if it already had been found guilty of a similar crime in the previous five years. Notwithstanding this improvement, the Chilean regime shifts the burden of proof in connection to EMPs away from the corporation and back to the prosecution, which is required to show that the crime was committed as a consequence of non-compliance with internal control duties. The unfortunate requirement is far behind the more progressive stand taken by Law No. 12846 – better known as the *Clean Company Act (CCA)* – in Brazil, which states that in applying penalties courts shall consider „the existence of internal mechanisms and procedures for integrity, auditing and incentives to report irregularities and the effective application of codes of ethics and conduct within the scope of action of the legal entity.“ But the CCA also limits its reach to the administrative sphere of law enforcement, a decision similarly adopted in Colombia through Law No. 1778 – known as the *Transnational Corruption Act* – of 2016 and this can certainly be deemed to fall short of the target set by the OECD’s Anti-Bribery Convention, which indicates that signatories must „establish the liability of legal persons for the bribery of a foreign public official“ (Article 2) and that they shall be „punishable by effective, proportionate and dissuasive criminal penalties“ (Article 3). We must unfortunately also add to this list Costa Rica (Law No. 8422, Art. 44). Mexico alone demonstrates a clear-cut approach to strong criminal liability: to create its National Anti-Corruption System (NAS) in 2016, the country enacted a General Law of Administrative Liability (GLAR), created a specialized Federal Administrative Court, and amended several acts, most relevant to our discussion the Federal Criminal Code and the National Code of Criminal Procedures, which established the criminal liability of legal persons. By following current international standards and providing integrity requirements as mitigating factors, the Mexican anti-corruption apparatus represents the most advanced approach towards EMPs with regard to legal incentives in the region, properly moving towards international standards.

Although the legal environment in Latin America has certainly changed 16  
in the second decade of the 21<sup>st</sup> century, all countries reviewed above share a similar failure in their pursuit of a better corporate compliance regime: the exclusion of concerns regarding private-to-private corporate corruption in laws addressing criminal liability. This state of affairs appropriately reflects the orthodox position which holds that corruption is an issue concerning an office, thus largely leaving anti-corruption efforts

out of the private sector. The natural consequence is that this type of unethical business practice gets mixed treatment depending on the country in which it is taking place, with victims able to claim damages in Chile under Law No. 20169 on Unfair Competition, but their Mexican counterparts having no access to redress bribery between private players unless under the much more general label of *fraud* (which requires proof of intention to mislead the other party).

#### 4.3.2 Cultural environment

- 17 As mentioned earlier, the difference between the legal environment of a transnational business organization at home and the one encountered by a branch office in a typical Latin American city is mirrored at the micro-level by the potential incompatibility between the ethical expectations faced by the individual inside the workplace and his/her social role and response to social norms more generally. For example, the traditional collectivist leaning of Latin American societies is a factor often suggested to contribute to the pervasiveness of nepotism and favoritism in public and private organizations, an argument also made by Sanchez et al. (2008). Beyond particular values, it is common knowledge that petty corruption in the form of bribery is commonplace in the region: according to a report from Transparency International (2017)<sup>1</sup> on average 29 % of people reported having paid a bribe in the previous twelve months, and 22 % stated that to complain about it would not have been socially acceptable. Thus, there seems to be a strong case for the argument connecting corruption tolerance to social norms and behavioral expectations, just as Karklins (2005) noted in the case of post-communist countries. But the ethical challenges of the cultural 'organization-environment incongruence' faced by foreign corporations is not necessarily something to be tackled through forceful compliance interventions of local agents, but rather understood as a natural feature of the business environment that is common to all other regions in one form or another.
- 18 Over fifty years ago, Strawson (1961) described such ethical concerns as „a region of diverse, certainly incompatible and possibly practically conflicting ideal images or pictures of a human life,“ a region that has traditionally been the target of law enforcement efforts that were, for the most part, unconcerned with seeing these ethical 'failures' as a problem of labeling rather than criminal pathology. Thus, the recent emphasis on ethical awareness and integrity building represents a new and welcome path to bringing organizational culture and context closer to one another and towards more successful EMP implementation.

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<sup>1</sup> People and Corruption: Latin America and the Caribbean.

## 4.4 Current regulatory trends in Latin America

### 4.4.1 Brazil: Important progress in anti-corruption compliance efforts.

Considering the resulting regulatory reforms sweeping the region, it is possible to suggest that Latin America has largely benefited from the *Car Wash* case – a criminal investigation originally focused on money laundering, but later expanded to cover a corruption network involving senior officials of Brazilian and foreign governments and construction firms. However, not all affected countries have managed to launch inquiries or international cooperation activities, therefore failing in those instances to present additional charges or provide potential evidence that may help Brazilian authorities pursue justice. Luckily for this country, progress in other areas has signaled a change of rules with potential future implications for the status quo. 19

Although having some limitations, the Clean Company Act – which received significant input from specialists from a wide variety of fields such as criminal, labor, compliance, and forensics accounting and investigation – is among the toughest anti-corruption laws in the world. Building on it, the government approved in 2015 Decree 8.420/2015, which provides criteria for evaluating a company's compliance system and adjudication of sanctions, thus promoting their adoption as potential defense and strategy for reduced administrative penalties. The inspiration behind the regulatory initiative was the mismanagement of funds related to the 2014 FIFA World Cup and the 2016 Summer Olympics held in Rio de Janeiro, and the massive backlash it generated among members of civil society and opposition forces. The level of mobilization and coordination demonstrated by Brazilian society during the ensuing protests forced the government to take effective action, and together with the imprisonment of many entrepreneurs, top executives, and even a former President, the country adopted new standards that could potentially lead it away from its traditional cycle of impunity. 20

Notwithstanding the positive outcome, the fact that the push towards systems of compliance required the presence of a vast popular mobilization capable of threatening the political establishment forces us to follow further developments with caution and necessary scepticism. As the political circumstances point to a reform previously characterized here as a pure compliance model of corruption control (regardless of the actual lexical style employed in the law), it is still too early to say whether real elements of integrity training and ethics awareness will become a regular part of doing business or will simply remain wishful thinking. 21

**4.4.2 Mexico: Struggling to implement current legislation.**

- 22 Regardless of the particular leanings of a new government, Mexicans demand real improvements in the fight against bribery and corruption.

Local market agents and investors have openly and continuously expressed concern about the level of corruption and security in the country. Naturally, these two phenomena are key risks that disrupt efficient business and deter new investors, but the government is giving positive signs that change may finally be on the way. In July 2017 the country implemented the National Anticorruption System, which now makes companies liable for acts of corruption (incurred by any employee) and able to be penalized accordingly. Although the system still lacks sufficient political will to enforce legislation systematically and across the board, it provides corporations interested in reducing their level of corruption risk with a soft incentive to self-monitor by incorporating a series of mitigating factors that may allow them to reduce potential sanctions and penalties (if and when enforcement begins).

- 23 These mitigating factors are collectively known as the 'integrity policy', and include as a minimum: (1) a manual of organization and procedures that is clear and complete, in which the roles and responsibilities of each of its areas are defined, and that clearly specifies the different chains of command and leadership throughout the structure; (2) a code of conduct duly published and disseminated among all the members of the organization, which has systems and mechanisms of real application; (3) adequate and effective control, monitoring and auditing systems that constantly and periodically examine compliance with integrity standards throughout the organization; (4) adequate complaint systems, both within the organization and towards the competent authorities, as well as disciplinary processes and specific consequences regarding those who act in a manner contrary to internal norms or Mexican legislation; (5) appropriate training and training systems and processes regarding the integrity measures contained in this article; (6) human resources policies tending to avoid the hiring of people who may constitute a risk to the integrity of the corporation. These policies will in no case authorize the discrimination of any person motivated by ethnic or national origin, gender, age, disabilities, social condition, health conditions, religion, opinions, sexual preferences, marital status or any other that threatens human dignity and have the purpose of nullifying or diminishing the rights and freedoms of persons, and; (7) mechanisms that ensure the transparency and publicity of their interests at all times.
- 24 The above mechanisms represent a truly meaningful step towards raising the level of compliance with anti-corruption laws while awarding integrity measures a proper role in corruption prevention. But with no political will to enforce them, the system may still have a long way to go before gaining the momentum it needs. Thus, to paint a clearer picture of the current status of EMPs in the country, we could say that the en-

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actment of the integrity policy is like owning a racing car in hectic Mexico City – you may take it out of the garage, and may step on the accelerator, but you will not get very far. It is up to the new administration to demonstrate the political will to foster integrity if the country wants to curb corporate and public corruption in any significant way.

##### 4.4.3 Guatemala: Setting the rules in Central America.

Despite not possessing a proper anti-corruption bill, the Guatemalan government seems determined to apply existing legislation, which is clearly significant in a country that consistently appears among the most corrupt in the region according to Transparency International's Corruption Perception Index. 25

This application of the rule of law in Guatemala has caused a great impression in the region, providing a demonstration of actual political will and a markedly new tone far from the 'culturally corrupt' label justifiably applied to it in the recent past. Not only have government officials become the target of law enforcement agencies, but, more importantly, the administration has been able to raise awareness among members of the private sector regarding their role in reducing the risks of money laundering, fraud, and corruption. In particular, the Internal Revenue Services (SAT, its Spanish acronym ) of Guatemala has become the key player in enforcing the law, focusing primarily on money laundering linked to corrupt activities. 26

Stemming from allegations from the Brazilian Car Wash investigation, one of the main industries targeted for legal action was construction. In this regard, Guatemalan leaders have demonstrated the political will to change the course of public affairs, but according to the country's private sector, there have also been many concerns regarding potential abuses of power in the administration of justice. This reaction from important economic players was certainly predictable in a system where the law had been only selectively enforced before: the sudden show of courage from specific agencies of the state to go against the status quo will most likely continue to be regarded as a source of instability until all relevant stakeholders find a new equilibrium, hopefully based on improved compliance and integrity standards. If everything goes as intended by anti-corruption advocates, Guatemala might transition from being a reactive market to one characterized by proactive initiatives, allowing a rise of awareness and implementing effective controls to mitigate the risks of money laundering, fraud and corruption in the private sector. Such a transition would, for all intentions, represent a new rule for doing business in Guatemala. 27

#### **4.4.4 Panama: Navigating reputational breaches**

- 28 For years, Panama has been a figurative paradise in many respects, but mainly due to the possibility of depositing money in its banks without revealing its actual origin or purpose. However, after the breach, popularly known as the 'Panama Papers', took place in 2016, many concerns emerged about the presence of massive funds potentially linked or related to money laundering and corruption. Yet, in 2015 Panama had adopted new controls and mechanisms applicable to the prevention of precisely those kinds of illicit activities, including the financing of terrorism and proliferation of weapons of mass destruction. Thus, the events of 2016 serve to shine a light over the (non-)application and enforcement of current legal frameworks, rightfully showing ample room for improvement regarding due diligence procedures, asset disclosure, and financial transparency. Crucially, such improvements are required first in the form of political will and engagement in collaboration with international agencies. As in other cases across the region, political will is crucial to change the culture of corruption afflicting societies and the way private individuals do business.
- 29 Anecdotally, Panama is sometimes referred to as 'the Miami of Latin America', something reflected in the way investments in the real estate sector (and others) are allegedly targeted for international monitoring. In stepping up to its geographic position and financial role, the country would greatly benefit from strengthening its practices of information disclosure in addition to putting in place a more robust system of detection of illicit funds, not only focusing on secrecy but also on more effective cooperation with other actors of the international community.

#### **4.4.5 Andean countries: Going through bumps but sending the right signals.**

- 30 As part of the Car Wash investigation, both Ecuador and Peru managed to initiate legal action against a former vice-president and president respectively. By themselves, these cases represent a positive point of inflection for anti-corruption efforts in that part of the region; however, the seeming momentum is just the proverbial 'tip of the iceberg', as markets expect to have not only a political prosecution but also to see companies and shareholders take responsibility for the damage caused. The process of raising anti-corruption standards in these countries has a deep meaning for all people involved: while private economic agents allegedly funneled public resources for their own benefit, political power was the key to deciding which companies were granted access to illicit dealings. The future is promising. However, organizations from both the public and private sectors are yet to realistically commit to investigating and punishing corrupt activities, which requires continuous enforcement of current anti-corruption frameworks and further development in line with interna-

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tional standards. Peru and Colombia have adopted appropriate legal arrangements to accomplish these tasks, but other countries such as Venezuela and Bolivia – where state ownership and interventions create a very high risk of corruption – will likely lag behind for the foreseeable future.

##### 4.4.6 Southern cone: Still pushing forward, but at a slower pace

After the Kirchner era, Argentina saw an evolution in the fight against bribery, but at a slower pace compared to other countries in the region, focusing on economic solutions rather than the effective enforcement of anti-corruption laws. To the west, the more mature Chilean market may boast lower levels of corruption in the private and public sectors, but the incidents that do take place remain difficult to uncover and prosecute. In both cases there is an understandable, albeit tacit, desire to keep prosecutorial power away from the control of corruption in the private sector. While politically sensitive, ethics management could potentially be improved there by taking advantage of the distinct cultural patterns and directly emphasizing an EMP style of good corporate citizenship rather than waiting for stronger regulatory frameworks. As the nature of integrity measures make them inherently more politically palatable, there is still much to do in both countries to reduce the risk of corporate corruption that sidesteps strong governmental action. 31

##### 4.5 Anti-corruption management in Latin America: a typical case scenario

To provide a clearer and more concise picture of some of the theoretical and empirical issues introduced above, this section recounts the actions taken by a business organization – which shall be called *Company Inc.* – to implement an EMP in Latin America. Although the players involved shall remain anonymous, the case serves to review a typical case while allowing us to reflect on the challenges faced in reducing the risk of corruption under real conditions. 32

*Company Inc.* was a relatively small but growing corporation wishing to expand internationally, ready to assume new risks that may translate into higher profits. To pursue this aim, top management was given the task of exploring potential markets suitable for investment. The main regions being considered at the time were Africa and Latin America, both representing new territory with their own operational challenges. After some consideration, top management finally decided to move forward and invest in Latin America, an overall more stable and financially promising market. 33

*Company Inc.* favored swifter entry into the unknown market by acquiring a local company instead of building up their own resources and rep- 34

utation from scratch. The chosen target, *Local Co.*, was selected by taking into consideration its market share, financial performance, tax liabilities, labor challenges, and operational costs. Since this was the first time Company Inc. had ventured outside their home country, top management considered these to be the key factors that should drive their strategy.

- 35 Corruption and security risks were not considered relevant for their assessment. Management held the strategic assumption that operating in Latin America would not be different from conducting business at home – that the rule of law, public security, and governments friendly to foreign investment could be taken for granted. They also assumed that Local Co. was not involved in any type of wrongdoing or corrupt activities, as purportedly evidenced by their sales and procurement operations, but no due diligence was conducted. In short, Company Inc. held on to its own frame of reference despite finding itself in a new environment, and so proceeded to enter Latin America without a proper assessment of the risks of corruption and related security risks which concerned the operations of Local Co.
- 36 One week after acquisition, Company Inc. dispatched an executive officer from headquarters to lead operations in Latin America. While conducting a more thorough review of Local Co.'s past activities and finances with the purpose of identifying potential areas for quick-wins or savings, a payment of approximately US\$ 100,000 was spotted which had no description. In consulting with the local group, the executive was told that the sum corresponded to a payment made monthly to secure the integrity of employees and operations of the plant. Immediately, the decision was made to stop payment – company policy indicated that it was not acceptable to allocate financial resources in such manner, and that it represented a violation of local and international compliance regulations.
- 37 Unfortunately, organized crime is embedded in many parts of Latin America. There, dealing with it is just another aspect of conducting business. The situation is certainly more prominent and ubiquitous in certain areas than others; generally speaking, however, it is only a thin line which differentiates payments to organized crime (extortion) from others related to the misappropriation of assets (fraud), bribery, or corruption, making the distinction a technicality and a source of confusion to those uninitiated.
- 38 Company Inc. discontinued the extorted payments for a few months, until the regional executive was kidnapped. The criminals had organized the attack so that he would be vulnerable, and according to his own account, the event was purposively carried out without much drama and with only the intention to provide the conditions so that he could be reasoned with regarding resumption of their previous financial arrangement. After a couple of hours, he was freed, unharmed. But the event

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prompted management to open an investigation into the affairs of their own local employees, since it was their belief that it had been coordinated from within the organization. During the investigation, two individuals were initially identified as having had access to the executive's agenda and routine movements; furthermore, they had also been directly involved in the preparation and remittance of the extortion payments. Later, conducting initial discussions and interviews, Company Inc. identified additional employees with direct access to those resources, thus triggering further investigation.

After a six-month investigation applying all available forensic investigation tools and technology (supported by outside counsel and in-house compliance team) it was identified that:

- The payment of US\$ 100,000 actually corresponded to various activities:
  - Organized crime – US\$ 50,000
  - Misappropriation of assets – US\$ 25,000
  - Bribery and corruption – US\$ 20,000
  - Other government officials for protection – US\$ 5,000
- There were at least thirty individuals involved in the illicit scheme. Some of them had direct ties to organized crime, while others had connections to different levels of local government, including the mayor's office.
- A number of individuals had undisclosed conflicts of interest, resulting in contracts with suppliers who overcharged for their goods and services.
- Allegedly, individuals connected to drug cartels had been using company trucks to transport illegal stimulants.

Thus, despite the technical resources deployed to assess market viability, top management at headquarters had missed a rather crucial dimension: the human resources available, and the environmental players present in the host economy seen from an ethical and relational position. Company Inc. had only considered traditional assets, and had not paid proper attention to the extent to which local employees honored their own commitments to informal – but significant – organizations. Thus, some of the lessons that top management learned from this experience were:

- To conduct risk assessment of fraud, bribery, and corruption, and to quantify any potential financial impact;
- To identify potential unusual transactions that may affect their reputation or make them non-compliant regarding international or local anti-bribery and anti-corruption regulations;
- To assess other operational risks that may compromise the security of their assets and personnel;

- To invest in post-acquisition compliance integration by emphasizing a culture of integrity from day one; and,
  - When applicable, to assess the compliance program and the maturity level of any international certification.
- 41 Notwithstanding the informative nature of the overall experience, the challenges presented by the business environment in Latin America were more than Company Inc. had bargained for, finally resulting in it exiting the region only a year later. Company Inc. concluded that to clear all the issues identified and make Local Co. compliant with international standards would be costlier than the estimated profits. Thus, Local Co. proved not only to be ultimately unprofitable, but most importantly, it was re-evaluated as a bigger source of risk to Company Inc.'s international reputation than it was willing to tolerate. For its investment, Company Inc. learned the valuable lesson that lack of compliance and integrity assessment invited very real threats that may not be sustainable in the medium or long term.

#### **4.6 Conclusions: How far is Latin America from Good Corporate Citizenship?**

- 42 Although the events pertaining to Company Inc. might be seen by more developed markets as a rather exceptional case, they are in fact all too common challenges for companies doing business in Latin America. While this is nothing new to local entrepreneurs and experienced investors residing in the region and/or regularly engaging in the assessment of corruption and related risks, it is important to be constantly reminded that the level of risk aversion varies from company to company and from country to country, and that newcomers must be aware of local conditions when drawing up plans and before rolling out investments.
- 43 From a theoretical perspective, economic agents should not waste further resources developing models based purely on compliance, but rather should embrace integrity measures and transition to a business style centered on good corporate citizenship. This model is expected to foster a culture of integrity inside the organization and the consequent improvement in employee behavior, resulting almost by default in not only higher compliance with local regulatory frameworks and international standards, but also in the promotion of the company as a responsible player and welcome business partner. However, when we compare this seemingly ideal model to the reality of doing business in Latin America, the challenges presented by the legal and cultural environments become painfully clear. We saw this happen in the case of Company Inc. and its unprepared incursion into unknown territory; but this was not the first instance of such a steep learning experience, and will likely not be the last. Compliance is not something that can be transplanted without proper regard for local conditions, in particular, those pertaining to law

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enforcement and common social practices. Only by improving on their typical due diligence approach and seeking to identify and mitigate the risks of fraud, bribery and corruption, can investors take the first step towards building effective EMPs and realistically pursue the enormous business potential of the region.

On top of those conditions specific to the local setting, a key aspect in realizing the challenges to policy localization involves common employee resistance to organizational change. In this regard, it is crucial for reformers to stress from the outset that compliance is not the 'enemy' of business efficiency and expediency but rather a strategic ally in pursuing solid and stable business growth. Although many areas inside an organization may perceive it akin to a meddling watchdog tasked with raising barriers, employees at all levels of the corporate ladder would be best served by recognizing it as a strategic partner entrusted with the task of protecting organizational assets and reputation by clarifying applicable rules. 44

From a practical perspective, investors wishing to conduct business in Latin America are encouraged to pursue the following goals if they wish to reduce their risk exposure: 45

- **Top management commitment.** EMPs are key components of any business strategy, and their significance only rises in environments characterized by high legal and cultural tolerance of malfeasance. Top management must lead efforts to foster a corporate culture of compliance and integrity, without which investments in higher-risk markets might quickly become a liability rather than a source of rewards.
- **Application of key contractual compliance clauses.** There are three main contractual clauses considered common practice in the compliance world: (1) the right to conduct audits, preferably by a third party; (2) termination of the contractual obligation at any time deemed necessary to preserve corporate integrity; and, (3) compliance with the company's code of conduct by all relevant business partners. Corporations are encouraged to adopt these clauses by reference to the guidelines elaborated by the International Chamber of Commerce ("ICC")<sup>2</sup>.
- **Implementation of EMPs and adoption of ISO 37001.** Summarily, these steps include the adoption and implementation of several elements such as: (1) internal financial and non-financial controls; (2) independent and effective whistleblower lines; (3) internal or external investigations, with clear sanctions and action plans; (4) an effective due diligence process; and (5) monitoring and auditing of key opera-

<sup>2</sup> Full document available at <https://iccwbo.org/publication/icc-anti-corruption-clause/>.

tions and transactions that may represent a high risk of fraud, bribery and corruption to the company. ISO 37001 is a tool that stands to become the proverbial 'keys-to-the-kingdom' at the international level.

- 46 While these goals potentially miss the mark on good corporate citizenship and even improved corporate integrity, they are crucial for the future attainment of both. The reason is simple: the undeveloped nature of corruption control in the region is directly connected to the pervasive tolerance of malfeasance affecting law and culture, and thus improving on minimalistic settings becomes a more effective approach to ethical management. In other words, rather than considering compliance and integrity as alternative approaches, we might profitably take them as evolutionary phases of an emerging EMP in Latin America.
- 47 In conclusion, the review of Latin American patterns of anti-corruption compliance and integrity awareness leads us to suggest that the region is in fact moving consistently in the direction of good corporate citizenship, not because it is explicitly aiming towards it, but precisely because it is not. Indeed, it is this sequentialism it emphasizes – from lack of regulatory frameworks to the promotion of compliance systems and the eventual possibility of integrity measures – that needs to be acknowledged by players entering the region. In this sense, Latin America might still be far from a model of good corporate citizenship, but it is definitely on the right track.

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