

# ***Implications of the Foreign Corrupt Practices Act for the Construction of Compliance Systems in Chinese Multinational Enterprises***

**Xiaohan Zhang<sup>1,a,\*</sup>**

*<sup>1</sup>Shandong University of Political Science and Law, Jinan, Shandong, China*

*a. xiaohanzhang@sdupsl.edu.cn*

*\*corresponding author*

**Abstract:** While multinational enterprises venture abroad in pursuit of high profits, but this also exposes them to increasing risks. Among them, corruption risks and compliance problems in the process of overseas operations have become one of the main obstacles to the development of multinational enterprises. Especially in recent years, the U.S. has utilized the Foreign Corrupt Practices Act (FCPA) to step up enforcement efforts against Chinese enterprises, which has made Chinese multinational enterprises face an even more severe overseas situation. How to improve the compliance system construction of Chinese multinational enterprises has become a hot topic of concern in the theoretical and practical circles. The FCPA serves as a model for the global anti-bribery compliance system, and its specific anti-corruption provisions and enforcement mechanisms are relevant to the current situation of Chinese MNEs' extraterritorial operations and compliance management. Therefore, it is imperative to improve the anti-corruption compliance system of Chinese multinational enterprises based on the FCPA framework.

**Keywords:** Foreign Corrupt Practices Act, Commercial Bribery, Corporate Compliance, Multinational Enterprises

## **1. Introduction**

In 1977, the U.S. enacted the Foreign Corrupt Practices Act (FCPA), which is the first law in the world to combat bribery. At the same time, some of the enforcement rules covered by the Act also provide a model for reference by enterprises in other countries in anti-bribery compliance. As far as the current judicial practice is concerned, the risks of Chinese MNEs' extraterritorial operations being subjected to FCPA enforcement mainly include the risks of differences in laws and regulations, the risks of loopholes in internal management, the risks brought about by cultural differences, and the risks brought about by regulatory pressures. In 2018, after the FCPA launched the "China Action", the enforcement attention to the corruption enforcement of Chinese companies' extraterritorial operations was further strengthened. In 2018, after the FCPA launched "Operation China", the focus on enforcement of corruption in Chinese MNEs' extraterritorial operations was further strengthened. However, the attention of academics on anti-corruption laws and institutions still needs to be strengthened, and theoretical research lags behind anti-corruption practices to a certain extent [1]. Based on the fact that Chinese MNEs' extraterritorial operations are constantly subject to legal

sanctions in different jurisdictions, there is an urgent need for China's anti-foreign corruption legislation to shift from symbolic to practical legislation, which should play a guiding role in constructing an anti-corruption compliance system as well as give full play to the effectiveness of China's anti-foreign corruption system [2]. Therefore, this paper will start from the anti-corruption compliance problems of Chinese MNEs' overseas operations, combine the useful contents of the Foreign Corrupt Practices Act, and offer advice and suggestions for Chinese MNEs to reasonably avoid corruption risks in international trade and build an anti-corruption compliance system.

## **2. Compliance of corruption in Chinese MNEs**

### **2.1. Current Status of the Development of Anti-corruption Compliance Systems in Chinese MNEs**

At present, the status quo of the anti-corruption compliance system for MNEs can be categorized into two aspects: the external environment and the internal system. First, the current situation of the external environment generally shows a significant increase in foreign compliance risks. Against the backdrop of trade friction, the U.S. government put forward the "Preventing China Initiative" in November 2018, which makes it clear that it is the goal to thoroughly investigate the overseas non-compliance cases of Chinese MNEs that are in competition with U.S.. This means that Chinese MNEs will face more frequent compliance investigations and prosecutions in Africa, Europe, and regions along the "Belt and Road" in Asia. As a result, the constraints on Chinese MNEs in the changing international situation will further increase.

Secondly, from the internal system point of view, foreign-related compliance laws not only have strict requirements on the specific behavior of enterprises, but also have specific technical specifications on the internal control system and its implementation. However, the current status of Chinese MNEs' internal compliance management presents a lack of awareness of the detailed provisions of anti-corruption compliance, leading some enterprises to believe that their own internal compliance systems are relatively perfect. Since anti-corruption compliance overseas is a very broad concept, it includes enterprises' compliance with a series of important laws and regulations of other countries or international organizations, such as international anti-corruption conventions and laws, export control, and overseas labor regulations, etc. This paper will focus on Chinese MNEs' repeated violations of anti-corruption laws and regulations. This paper will take the example of Chinese MNEs that have been repeatedly investigated and prosecuted by the FCPA, and examine how they should build an internal control system that complies with international standards from the perspective of preventing major compliance risks.

### **2.2. Characteristics and Shortcomings of Chinese MNEs' Anti-corruption Compliance System**

As mentioned earlier, the current situation of the anti-corruption compliance system of Chinese MNEs operating overseas is characterized by high pressure from external sanctions and insufficient internal compliance awareness and compliance management experience.

Firstly, the pressure of external sanctions on Chinese MNEs' anti-corruption compliance mainly comes from the "long arm jurisdiction" of the FCPA. The U.S. export control and unilateral sanctions have caused a series of damages to Chinese MNEs, the most typical of which is the blocking of Huawei's 5G technology, resulting in Huawei's 5G communication equipment being refused to be used by many countries. The United States has set up the so-called "Entity List", the scope of which includes Chinese MNEs, universities and scientific research institutions. Enterprises on the list have, on the one hand, lost the opportunity to import or use U.S. high-tech products and services and to engage in business with the United States. On the other hand, third countries, third parties, and even

Chinese MNEs or individuals, fearing the impact of the United States' "long arm jurisdiction", have taken the initiative to cut off business contacts with the United States, resulting in the loss of business opportunities [3]. It is evident that the heightened compliance risk resulting from the international situation requires Chinese MNEs to promptly enhance their anti-corruption compliance measures.

Secondly, Chinese MNEs exhibit insufficient awareness and experience in overseas anti-corruption compliance and management. This is primarily manifested in their limited understanding of regional laws and regulations, inadequate compliance awareness due to cultural differences, and disorganized internal management. For example, a case occurred in Zambia in 2019, where the World Bank issued a 20-month ban on a company and its distributor for alleged "fraud" in a project aiming to improve power facilities. As a result, the company was disqualified from participating in World Bank-funded projects for the mentioned duration [4]. As evident from the statement issued by the World Bank, Chinese MNEs demonstrate deficiencies in both substantive and procedural compliance within their anti-corruption compliance systems. The World Bank highlighted that the China Electrical Design and Research Institute (CEDRI) engaged in fraudulent practices, failed to disclose elements of conflict of interest, and submitted false documents bearing the name of China Electrical Engineering Co., Ltd. (CNEEC) to fulfill the requirements of the contract under the project. As a controlled subsidiary of CNEEC, CNEEC failed to monitor the misconduct of China Electrical Engineering Design Institute."

These findings indicate shortcomings in both the implementation and monitoring aspects of anti-corruption compliance among Chinese MNEs [5]. Chinese MNEs exhibit two main deficiencies in their anti-corruption compliance systems: procedural and ethical. Procedurally, some Chinese MNEs lack the motivation to participate in the sanctions process and take sanctions relief measures. They respond passively to sanction notifications, offering no defense or explanation, and fail to act promptly to mitigate improper conduct, resulting in missed opportunities to reduce or waive penalties. Secondly, ethically, Chinese MNEs lack a sense of integrity and hold strong traditional beliefs about human trade. They often disregard the anti-corruption laws and regulations of the countries where they operate and have a limited understanding of the criteria for defining corruption under the law. In practice, they engage in non-compliant transactions as "agents" or "third parties," and resort to bribing overseas government officials and staff to achieve their business goals. To address these shortcomings, Chinese MNEs urgently need to supplement and improve their foreign-related anti-corruption compliance system based on current characteristics and measures.

### **3. Compliance strategies**

#### **3.1. Law review**

##### **3.1.1. Background of FCPA**

The FCPA was introduced in the context of the Watergate scandal of the 1970s and the subsequent series of investigations. After the Watergate scandal, the U.S. Securities and Exchange Commission (SEC) found that more than 400 U.S. companies admitted that they had bribed foreign officials, totaling as much as \$3 billion. Foreign officials, totaling up to 3 billion U.S. dollars. Based on the fundamental purpose of curbing corporate bribery overseas, the U.S. Congress passed the FCPA in 1977 [6].

##### **3.1.2. Legal provisions of FCPA**

The FCPA contains of two main provisions: the anti-bribery provision and the accounting provision. The anti-bribery provision explicitly states that any individual or business organization that bribes a foreign official to obtain or retain business is subject to the FCPA. It prohibits the use of U.S.

communication systems, payment methods, or other tools to offer money or any other valuable item to a foreign government or government official, or to use the influence of the bribe recipient to gain business advantages. The accounting provisions are a crucial component of the FCPA. They focus on strengthening the internal anti-corruption compliance system of enterprises and targeting practices where corruption is concealed through third-party payments or other deceptive means. The accounting provisions aim to ensure that companies maintain accurate accounting records, promoting proactive measures to prevent corruption within organizations. Overall, the FCPA aims to combat overseas bribery and corruption by both penalizing those who engage in bribery and encouraging companies to establish robust internal compliance systems.

### **3.1.3. Legal Enforcement of FCPA**

In the United States, the enforcement of the FCPA is carried out by two main authorities: the United States Department of Justice (DOJ) and the United States Securities and Exchange Commission (SEC). The DOJ is responsible for all criminal charges, as well as civil suits brought by non-issuers for violations of the corruption provisions. The SEC is responsible for civil actions brought by issuers and their directors, officers, shareholders, agents or employees. The SEC has overlapping jurisdiction with the DOJ over matters under the FCPA. However, the DOJ has exclusive jurisdiction over criminal accounting violations, and both the DOJ and the SEC have authority to pursue civil liability for accounting violations. In addition, the U.S. Department of Commerce has jurisdiction over exporters with respect to the underlying FCPA issues [7]. Notably, an important enforcement aid to the FCPA is the doctrine of long-arm jurisdiction, which means that a defendant who is not domiciled in the state where the court is located may be served with a subpoena as long as the defendant has "minimum contacts" with the legislative court. Minimum contacts, anyone in the world who has a connection with the United States satisfies the minimum contacts, such as using a United States operating system, a United States e-mail address, trading in United States dollars, all of which satisfy the minimum contacts and give the United States long-arm jurisdiction [8].

## **3.2. Case Brief**

### **3.2.1. Case 1: A Bribery Case Involving a Former Employee of A Multinational Bank**

On June 23, 2021, the SEC found Asante K. Berko, a former employee of a multinational bank, guilty of violations of the FCPA [9]. Berko was convicted of paying bribes to Ghanaian government officials through an intermediary company to help a Turkish energy company secure a project to build and operate a power plant in Ghana. Notably, although Belko was a senior executive in the UK division of the multinational bank at the time he used the intermediary to pay the bribe, and the Turkish energy company was a client of the UK division. However, as the bank's head office and UK division were not involved in the bribery and the bribe was discovered during internal compliance monitoring, Belko's bribe was promptly suspended from the Turkish company. In the end, the bank did not become a defendant in the case.

### **3.2.2. Case 2: A Bribery Case Rejected by The DOJ**

Between late 2016 and early 2020, some employees of Corsa Coal Corporation (Corsa) were involved in a scheme to bribe Egyptian government officials. The purpose of this scheme was to secure and maintain contracts for the supply of coal to Al Nasr Company for Coke and Chemicals, which is a state-owned and controlled coke company in Egyptian [10]. According to the 2023 Update of the U.S. Department of Justice's Criminal Division Corporate Enforcement and Voluntary Self-Disclosure Policy, on March 8, 2023, the Fraud Section and the U.S. Attorney's Office for the Western District

of Pennsylvania Office found that Corsa's conduct did not violate the FCPA. This was because the company voluntarily disclosed its misconduct, cooperated with the government's investigation, and implemented appropriate remedial measures in a timely manner. As part of the resolution, the company agreed to disgorge profits obtained from the illegal scheme, taking into account its financial capabilities. This case demonstrates that establishing a robust and effective anti-corruption compliance system and promptly addressing compliance issues can effectively mitigate legal penalties and public scrutiny.

### **3.3. Anti-corruption Compliance Insights from Two Cases**

As mentioned, the two cases provide insight into the establishment of anti-corruption compliance systems for Chinese MNEs. This involves conducting compliance review and due diligence during the early stages, as well as self-reporting and self-disclosure after corruption investigations. To begin with, in terms of preliminary compliance management and due diligence, enterprises can assess the level of risk associated with third-party relationships based on various factors such as their location, industry, services provided, business needs, nature of the third party, and types of transactions involved. Based on this assessment, enterprises can categorize these risks as high, medium, or low. If necessary, they can conduct further enhanced or supplementary due diligence which may involve detailed review of qualification documents, sample projects and past cooperation, retrieval of public information, in-depth back-testing, interviews.

Secondly, regarding self-disclosure in late-stage corruption investigations, companies should proactively and promptly disclose any misconduct. This self-disclosure should encompass providing comprehensive cooperation, including disclosing all relevant facts about the misconduct and individuals involved in the violation. MNEs should also commit to continuing their cooperation with ongoing governmental investigations and future prosecutions, if any. Additionally, companies should willingly agree to disgorge any illegally obtained funds that their financial capabilities.

In summary, Chinese MNEs should establish an anti-corruption compliance system that covers the entire process from the pre-event stage to post-event actions. They can draw valuable lessons from the experiences of multinational enterprises in other countries regarding anti-corruption compliance. In addition to the cases mentioned earlier, they can also learn from Wal-Mart's internal investigations and evidence collection in anti-corruption efforts [11].

## **4. Suggestions for Improving the Compliance System of Chinese MNE**

With the increasing overseas investment by Chinese MNEs, it is crucial for them to establish a comprehensive anti-corruption compliance system that covers the entire process in relation to the FCPA. Here are five key areas that Chinese MNEs should focus on.

### **4.1. Improve the Internal Compliance Risk Assessment Mechanism of The Enterprise**

Chinese MNEs face both external and internal risks when operating overseas. It is essential for these enterprises need to conduct a thorough assessment of the external investment environment. This includes investigating whether operating region poses a high risk of bribery, examining the legal policies related to bribery in the investment location, and establishing compliance standards. Moreover, due diligence should be conducted on business partners to ensure that suppliers and manufacturers share and adhere to the same compliance standards. Internal risk assessments should also be given significant importance, along with implementing checks and balances on power dynamics between departments to prevent departmental abuse of authority. Additionally, it is imperative to have anti-corruption agreements for employees. It's important to note that the



assessment process is not a one-time exercise but an ongoing review to promptly identify and address emerging issues.

#### **4.2. Establishment of Authentic and Effective Accounting Books**

The accounting provisions of the FCPA require companies to accurately record all overseas expenditures in their accounting books. Failure to make detailed entries is considered a violation of the FCPA. This provision aims to restrict the sources of bribery funds and reduce instances of bribery. Unfortunately, some Chinese MNEs are still engaged in "false accounting", where improper expenditures are justified or hidden through third-party accounting firms. To address this issue, it is crucial for Chinese MNEs to establish genuine accounting books that accurately reflect their financial transactions. By doing so, illegal transactions can be exposed, and companies can effectively defend themselves against allegations of bribery. This not only helps protect Chinese MNEs from FCPA penalties but also enables them to build a robust anti-bribery compliance system.

#### **4.3. Separation of Corporate Audit from Compliance**

This measure primarily applies to state-owned MNEs operating outside of China. According to the Guidelines for Overseas Business Compliance Management [12], it is mandated that the corporate compliance management function be separate from the internal audit function during compliance reviews. This requirement ensures that the audit department of the enterprise conducts independent audits to assess the implementation of compliance management and the effectiveness of the enterprise's compliance management system. The purpose of this measure is to prevent mutual interference between these two functions within state-owned enterprises, which can exacerbate internal corruption. By implementing this separation, Chinese MNEs can effectively strengthen their internal anti-corruption system and promote a culture of compliance.

#### **4.4. Emphasizing Due Diligence Before Cross-border M&A**

Due diligence refers to a comprehensive investigation of various aspects of the target company, including its legal relationships, financial status, tax details, and more. It involves analyzing the strengths and weaknesses of the enterprise, understanding the risks associated with the M&A transaction, and developing strategies to mitigate those risks. This process is crucial because under the FCPA, there is strict "successor liability" meaning that if the acquired company has violated the FCPA prior to the merger, the legal risk will be transferred to the acquiring party. Conducting thorough due diligence is necessary to avoid the potential risks associated with an M&A transaction. A comprehensive assessment should include evaluating the business model and scope of the target company, determining if it engages in government-related business activities, assessing the primary location of its operations and the business environment in that region, and examining whether it has subsidiary companies or branches under its control. It is also important to assess whether the target company has a robust compliance system in place and whether it has previously violated the FCPA. By conducting timely due diligence, the acquiring party can not only have the necessary discretion under the FCPA in case any compliance issues arise, but also identify potential problems early on and protect its business reputation [13].

#### **4.5. Circumvention of Long-arm Jurisdiction**

The exercise of jurisdiction over enterprises and individuals under the anti-bribery provisions of the FCPA based on the principle reflects the extraterritorial reach of the United States. Chinese MNEs that have been subject to sanctions under this principle can potentially optimize their approach to

circumvent the long-arm jurisdiction by severing the "minimum connection" and opting for locally developed communication, payment, and transaction platforms. Considering China's current capabilities in communication technology, payment systems, and transaction platforms, and barring any objective limitations such as foreign exchange restrictions, choosing domestic service providers can effectively evade U.S. long-arm jurisdiction and reduce the risk of being implicated. However, it is essential for enterprises to conduct a comprehensive assessment of their specific case to determine the likelihood of being subjected to "over-enforcement" before attempting to circumvent the long-arm jurisdiction. If there is no basis for enforcement actions based on the facts of the case, enterprises should exhaust the legal process to uphold justice and protect their rights.

## 5. Conclusion

Currently, the anti-corruption compliance system of Chinese MNEs operating abroad faces challenges and lacks attention. While many Chinese MNEs gradually establish their anti-corruption compliance systems after being sanctioned for corruption in overseas operations, this often comes at a high cost. Furthermore, there is a lack of sufficient understanding among academics regarding relevant laws and regulations, particularly in analyzing specific provisions and cases under the U.S. FCPA and summarizing anti-corruption compliance measures suitable for Chinese MNEs. Considering the increased enforcement efforts by the U.S. utilizing the FCPA against Chinese enterprises, it has become even more urgent for Chinese MNEs to establish effective anti-corruption compliance systems. To address this, it is recommended that Chinese MNEs implement an internal compliance assessment mechanism, maintain accurate and reliable accounting records, separate corporate compliance management from the audit function, prioritize due diligence in cross-border mergers and acquisitions, and optimize strategies to avoid long-arm jurisdiction. By adopting these measures, Chinese MNEs can identify potential issues early on, mitigate the risk of penalties under the FCPA, and avoid significant financial losses. It is also crucial that experts and scholars pay more attention to the development of anti-corruption compliance systems for Chinese MNEs, supporting their international expansion and ensuring long-term success.

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