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Brazil's Much Anticipated Decree to Further Combat Corruption Takes Effect

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Anti-Corruption

Brazil is living what local prosecutors refer to as "the largest known corruption scheme in Brazil's modern history." The ongoing corruption investigation has gained notoriety not only for its alleged size, but also because at its center lies Petrobras--Brazil's state-controlled oil behemoth. Amidst this scandal, which has spurred an increasing number of nationwide protests against the federal government, Brazil has continued to reinforce its anti-corruption laws.

Brazil's Clean Companies Act (Law No. 12,846),[1] which took effect on January 29, 2014, has now been followed by Decree No. 8,420,[2] which Brazil's President Dilma Rousseff signed into law on March 18, 2015 and became effective the following day. The Decree fleshes out aspects of the Act that had not been fully developed previously. The Decree establishes (1) the process for imposing administrative liability on legal entities for corrupt acts; (2) the guidelines for calculating fines; (3) the rules governing leniency agreements; and (4) the criteria that Brazilian regulators will use to assess anti-corruption compliance programs.

Brazil's Clean Companies Act

The Act subjects Brazilian companies and other Brazilian entities, plus foreign entities having a registered office, branch or other representation in Brazil to civil and administrative sanctions for bribing a Brazilian or foreign public official. The Act also applies to fraud in relation to public tenders. Such legal entities are held strictly liable for the harmful acts set forth in the Act that are performed in their interest or benefit. Violations of the Act can be sanctioned with administrative fines of as much as 20% of gross revenue in the year preceding the beginning of the investigations.

The Act contains potentially powerful incentives for voluntary disclosure, including up to a two-third reduction in the fine that otherwise could have been imposed. Entities with developed and implemented compliance programs can also qualify for reduced sanctions.

While a step in the right direction, the Act lacked critical details about the administrative process for adjudicating liability and left many open questions relating to sanctions. The Decree serves to fill in some of these gaps.

[1] Law No. 12846/13
[2] Decree No. 8420/15

The Decree's Key Provisions

A. Administrative Proceedings

The Decree sets forth that violations of the Act shall be investigated and decided by means of an administrative liability proceeding (*Processo Administrativo de Responsabilização*, or "PAR proceeding").

Jurisdiction. Generally, the highest authority of the entity against which the wrongful act was committed shall have jurisdiction to conduct the PAR proceedings. In certain situations, however, the Office of the Comptroller-General of the Union ("CGU"), has concurrent jurisdiction to initiate and conduct PAR proceedings. For example, when the entity with jurisdiction lacks objective conditions to conduct the PAR proceedings, the issues are highly complex, the contracts with the affected governmental entity involve a high amount, or when more than one public entity is involved.

The CGU also has jurisdiction to investigate and prosecute misconduct involving a foreign (*i.e.*, non-Brazilian) government.

Procedure. Upon learning of potential misconduct, the competent authority shall decide whether to:

- open a preliminary confidential investigation;
- initiate confidential PAR proceedings; or
- close the matter.

If the competent authority decides to initiate PAR proceedings, it will appoint a commission of two or more tenured public employees to conduct the proceedings. During the PAR proceeding, the Company under investigation will have the opportunity to present evidence and a defense. The Decree also grants the commission broad powers, including the power to request courts to order the search and seizure of assets of companies under investigation.

The PAR proceedings shall be concluded within 180 days, at which time the commission will render a report to the competent authority. The report must address the facts identified and the Company's liability, and recommend sanctions or the termination of the proceeding. The competent authority will then decide the matter, based on the evidence produced in the PAR proceedings. Any administrative decision imposing a penalty may be appealed to the authority rendering the initial decision.

B. Sanctions

The Decree details the criteria for imposing the sanctions set forth in the Act. Companies engaging in corrupt practices may be subject to:

- administrative fines or penalties;
- publication of the administrative decision imposing penalties, including in a media outlet in the area in which the violation occurred or in a nationally distributed publication, at the company's headquarters, and on the company's website; and
- debarment, if the violation involves government bidding and procurement.

Calculation. Under the Decree, the amount of any fine is determined based on a comprehensive calculation that takes into account certain aggravating and mitigating factors. Which factors apply to a given case must be determined during the administrative proceedings.

In essence, certain aggravating factors will increase the total percentage of gross revenue used to determine the amount of the fine. Likewise, certain mitigating factors will reduce the applicable percentage of gross revenue used to calculate the fine.

To begin, the percentage of a company's gross revenue that will be applied to determine the fine amount shall reflect the following factors:

- If harmful acts persisted over time, add 1-2.5%;
- If management tolerated or was aware of the misconduct, add 1-2.5%;
- If public services or a contracted project were interrupted, add 1-4%;
- If the transgressor had a poor rating in the insolvency database and had net profits in the fiscal year prior to the harmful acts, add 1%;
- If the transgressor is a repeat offender within five years from the publication of the judgment of the preceding violation, add 5%; and
- Depending on the value of the contract sought or awarded, add 1-5%.

Next, the total percentage may then be decreased as follows:

- If the violation was not consummated, subtract 1%;
- If there is evidence that the damage caused has been repaid, subtract 1.5%;
- If the entity cooperates with the investigation (regardless of any leniency agreement), subtract 1-1.5%;
- If the company voluntarily discloses the misconduct to the authorities prior to the initiation of the PAR proceedings, subtract 2%; and
- If there is evidence that the company has adopted and implemented a compliance program, subtract 1-4%.

Fine Limits. While the Act established that companies would be liable for fines between 0.1% and 20% of a company's annual gross revenue, the Decree clarifies the minimum and maximum limits of any such fine:

- At a minimum, fines shall be the greater value between:
  - the benefit sought or obtained by the company;
  - 0.1% of the company's gross revenue; or
  - R$ 6,000, only if annual revenue is impossible to determine.
- At a maximum, the fine shall be the lesser value between:
  - 20% of the company's gross revenue; or
  - three times the value of the benefit sought or obtained by the company.

The value of any benefit sought or obtained is equal to any gain sought or obtained which would not have occurred without the misconduct, plus the value of any improper benefit offered or given to a public agent or related third parties.

Similar to the approach used in the U.S. to calculate "gross gain" under the federal sentencing guidelines, 18 U.S.C. § 3571, the Decree allows companies to deduct legitimate costs and expenses from the value of the benefit sought or obtained.

C. Leniency Agreements

The Clean Companies Act authorizes regulators to enter into leniency agreements with companies accused of misconduct to reduce or eliminate any possible sanctions. The Act and the Decree establish the conditions, form, and content of such leniency agreements.

To qualify for a leniency agreement, however, a company must cooperate and collaborate "effectively" with the investigation and any administrative proceeding. This means that the cooperation must result in (1) the identification of all other persons involved in the violation, if any; and (2) the expeditious retrieval of information and documents corroborating the violation under investigation.

In addition, to enter into a leniency agreement, a company must:

- be the first to express an interest in cooperating with the investigation;
- have completely ceased its involvement in the misconduct;
- admit its participation in the misconduct;
- cooperate fully and permanently with the investigations and the administrative proceedings, appearing whenever summoned by the regulators at the company's own expense; and
- provide evidence of the misconduct.

Once the company has performed under the terms of the leniency agreement, it may be entitled to any or all of the following benefits:

- exemption from publication of the sanctioning administrative decision;
- exemption from the prohibition of receiving incentives, subsidies, subventions, donations or loans from state or state controlled entities;
- reduction in the fine imposed by up to 2/3; or
- exemption from the administrative sanctions set forth in other statutes governing public tenders and government contracts.

The effects of a leniency agreement may extend to legal entities belonging to the same "economic group" provided that they have ***jointly*** signed the agreement and performed under the leniency agreement.

D. Compliance Programs

The most notable aspect of the Decree is its emphasis on the implementation of effective compliance programs. The Decree dedicates an entire chapter to compliance programs-- *i.e.,* exactly how much the existence of a compliance program will mitigate any fine imposed and,

more importantly, mandates the adoption of or enhancements to an existing compliance program.

The Decree defines a compliance program as:

> a set of mechanisms and internal procedures on integrity, auditability, and incentivized reporting of irregularities, as well as the effective application of codes of ethics and conduct, policies and directives aimed at detecting and correcting deviations, fraudulent acts, irregularities and illicit acts performed against the national government or a foreign government.[3]

Further, the Decree recognizes that no two companies are the same and so there is no "one size fits all" compliance program. Instead, an effective compliance program must be risk-based, and take into account the characteristics and risk factors of each company, including its size, internal structure, industry sector, the countries in which it operates, and the extent of the company's interactions with government entities.

Additionally, the Decree sets out the following aspects of a compliance program that will be weighed to determine its effectiveness:

- Tone at the top, including the commitment to compliance of the board and senior management;
- The standards of conduct, code of ethics, integrity policies, and procedures, applicable to all employees, managers and third-party providers;
- Periodic training;
- Periodic risk analysis to make adjustments to the compliance program;
- Accounting records that comprehensively and accurately reflect transactions;
- Internal controls that ensure the timely preparation and reliability of the company's reports and financial statements;
- Specific procedures to prevent fraud and illegal conduct in interactions with the public administration (*i.e.*, public bidding and contracting, obtaining licenses, paying taxes);
- Independence, structure, and authority of the internal body responsible for enforcing and monitoring the compliance program;
- Channels for reporting irregularities that are open and widely publicized to employees and third parties;
- Mechanisms for the protection of good faith whistleblowers;
- Disciplinary measures in case of violations of the compliance program;
- Procedures for prompt interruption and remediation of irregularities;
- Appropriate third party due diligence and supervision;
- Verification of any irregularities or illicit acts of any legal entities acquired;

[3] *Id*. Article 41.

- Continuous monitoring of the compliance program; and
- Transparency concerning donations to political candidates and parties.

Conclusion

The Decree, while a much anticipated follow-up to the Clean Companies Act, is only one of a series of anti-bribery measures expected to be implemented in Brazil to address the perceived problem of corruption. Specifically, the Decree notes that additional regulations and guidelines relating to the governance and assessment of compliance programs shall be issued by the Comptroller-General of the Union.

Companies operating in Brazil now have a more robust local law with which they must comply. Nevertheless, the parameters set forth in the Decree are consistent with best practices for creating an effective compliance program to minimize the risk of running afoul of other anti-bribery laws, such as the Foreign Corrupt Practices Act and the U.K. Bribery Act. Entities operating in Brazil should consider developing or re-examining their compliance policies, and procedures to ensure that they meet the parameters for an effective compliance program set forth in the Decree.

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