

ANTI-CORRUPTION DIGEST October 2014

Welcome to Dorsey & Whitney's monthly Anti-Corruption Digest. In this digest, we draw together news of enforcement activity throughout the world and aim to reduce your information overload. Our London, Minneapolis, New York and Washington DC offices edit the digest and select the most important material so that you can use this digest as a single source of information.

The USA

Avon: Judge Dismisses FCPA-Based Securities Fraud Claims

A Manhattan federal judge has dismissed, without prejudice, a putative shareholder class action brought on behalf of purchasers of Avon stock between July 2006 and October 2011 against Avon and its former CEO, Andrea Jung, and CFO, Charles Cramb. Judge Paul Gardephe concluded that the plaintiffs failed to state a claim under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 because they failed to allege that Avon intended to deceive investors about its ability to comply with the U.S. Foreign Corrupt Practices Act (FCPA).

Judge Gardephe held that a company's general statements regarding its ethics code cannot violate the securities laws because they are not material. He also held that other statements regarding specific compliance measures and business success were material and misleading, but that the plaintiffs failed to state a claim for securities law violations because they failed to allege that Avon, Jung and Cramb acted with scienter (i.e. with knowledge of wrongdoing) when making the statements.

Interestingly, the court found that Avon's voluntary disclosure "weigh[ed] against a finding of scienter."

In May 2014, Avon announced that it had reached a $135 million settlement with the U.S. Department of Justice (DOJ) and U.S. Securities and Exchange Commission (SEC) to resolve allegations that it bribed Chinese official to become the first Western company to obtain a door-to-door sales license. The settlement has not been finalized. In addition to the settlement, Avon has spent over $300 million on its investigation into the allegations.

Second Circuit Affirms No Private Right Of Action Under FCPA

In Republic of Iraq v. ABB et al., the Second Circuit affirmed a district court's dismissal of claims brought by the Republic of Iraq against a number of purchasers in the United Nations

Oil for Food Program in which Iraq alleged that the defendants paid surcharges and kickbacks to government officials in exchange for government contracts.

In reaching its decision, the Second Circuit relied upon Supreme Court precedent recognizing that "private rights of action to enforce federal law must be created by Congress," Alexander v. Sandoval, 532 U.S. 275, 286 (2001), and noted that nothing in the FCPA indicates that it includes a private right of action. The Second Circuit also relied upon a decades-old decision by the Sixth Circuit which was the first and, until Republic of Iraq, the only court to hold that no private right of action exists under the FCPA because to allow such a right of action "would directly contravene the carefully tailored FCPA scheme presently in place," Lamb v. Phillip Morris Inc., 915 F.2d 1024 (6th Cir. 1990).

China Valves: SEC Files Injunctive Action

The SEC has filed a civil injunctive action in federal district court in Washington, D.C. against China Valves Technology, Inc. ("China Valves"), a China-based U.S. issuer formed through a 2007 reverse merger. According to the SEC announcement, the SEC alleges that China Valves and three of its executives engaged in numerous securities laws violations, including securities fraud by "intentionally misle[ading] investors about China Valves's 2010 acquisition of Watts Valve Changsha Co., Ltd. ("Changsha Valve") in an effort to mask the subsidiary's prior investigation of violations of the [FCPA] and China Valve's decision to pay sales commissions to employees that potentially violated the FCPA." According to the SEC complaint, China Valves' 8-K in which it announced the acquisition "omitted any mention of the FCPA investigation of Changsha Valve, or that the payment of unrecorded liabilities included payment of$2.2 million in sales commissions that were not recorded on Changsha Valve's books and that [the previous owner] had determined were not FCPA-compliant."

The SEC issued a temporary suspension of trading in the securities of China Valves, and instituted administrative proceedings to determine whether to revoke China Valves' registration.

The United Kingdom

Draft legislation: Reports on Payments to Governments Regulations 2014

The UK government has announced the publication of draft legislation "Reports on Payments to Governments Regulations 2014."

The Regulations implement chapter 10 of the European Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings. Chapter 10 requires certain undertakings active in the extractive and primary logging industries (such as mining, quarrying, and logging companies) to report on payments they make to governments all over the world, when such payments exceed £86,000 (c. $137,000) in a financial year.

According to the Regulations, 'payments' are broadly defined to include money or in kind contributions. A company to which the Regulations apply must file reports with the Registrar of Companies within 11 months of the end of its financial year. Failure to comply with such requirements will result in an unlimited fine for the company or imprisonment for directors who are found to have failed to take all reasonable steps to comply.

Subject to Parliament's approval, the legislation will apply to fiscal years commencing on or after 1 January 2015. Member States of the European Union are required to adopt similar measures by 20 July 2015.

Serious Fraud Office

Reports indicate that Theresa May MP, current UK Home Secretary, is advocating the closure of the UK Serious Fraud Office (SFO) and the transfer of its responsibilities to the National Crime Agency.

According to reports, a spokesperson for SFO said that: "The SFO's specialist teams of investigators, prosecutors and other experts are now vigorously pursuing the most serious suspected economic crime, including Libor and Forex rate-rigging. We know of no evidence which suggests that breaking up these teams and putting investigators and prosecutors into different organisations would be more effective."

A new corporate offence: Failure to prevent economic crime

According to reports, the UK government is considering proposals to create a new corporate offence of failing to prevent economic crime. The new offence would resemble and expand on the existing corporate offence of failing to prevent bribery under the Bribery Act 2010.

The existing standard "controlling mind" test means that to convict a corporation, the prosecution must prove, beyond reasonable doubt, that an individual at executive or board level committed the acts with the necessary intention.

The Rest of the World

Brazil

According to reports, criminal actions have been filed by Brazilian Authorities against eight Embraer SA employees for an alleged $3.5 million payoff to a retired Dominican Republic colonel, Carlos Piccini Nunez. Part of the bribe is said to have been destined for a Dominican senator, who is not named. The bribe was allegedly paid to secure a $92 million contract to provide the armed forces with attack planes.

It was reported that in 2008, around the time the contract was negotiated, the colonel was the Dominican Republic's director of special projects for the armed forces. Eduardo Munhos de Campos, Embraer's vice president for sales, allegedly promised to pay the bribe with the assistance of another vice president, Orlando Jose Ferreira Neto and six other employees whose functions ranged from managers to directors.

Payments were reported to have been made to shell companies designated by Mr. Piccini, however, in 2009, Embraer's compliance department stopped the full transfer. The balance of the bribe payments were allegedly concealed as consulting fees for selling aircrafts to Jordan, which never materialized.

Reports indicated that the employees are charged with corruption in international transactions, which carries a sentence of up to 8 years in prison upon conviction, and money laundering.

China

National Development and Reform Commission

According to reports, Liu Tienan, former deputy of the National Development and Reform Commission, confessed in court to taking bribes from various companies, including a Toyota Motor Corporation joint venture. The court said that: "The oral representation made by the defendants Liu Tienan on the allegations is: I have taken the initiative to confess to these facts of the allegations."

He and his son, Liu Decheng, were reportedly charged with taking $5.8 million in bribes. Reports indicated that Mr. Decheng collected most of the bribe money. The allegations indicate that between 2002 and 2011, Mr. Tienan took bribes to facilitate project approvals and filings for a number of companies such as Nanshan Group, Ningbo Zhongjin Petrochemical Co Ltd, Guangzhou Automobile Group, Guangzhou Toyota Motor Co Ltd and Zhejiang Hengyi Group. Mr. Tienan also reportedly aided in the approval procedures for several projects from Guangzhou Automibile Group, which in return hired his son as a special Beijing representative for one of the Group's subsidiaries.

Mr. Tienan could face life imprisonment. However, reports indicated that he is more likely to receive a lesser sentence as a result of his confession.

Reports indicate that Mr. Tienan was fired from the National Development and Reform Commission after Caijing magazine's deputy editor Luo Changping accused him of corruption, loan fraud and counterfeiting his degree.

Pharmaceutical sector

Last month, GSK was fined $489 million in China for corruption there. Further to the Changsha Intermediate People's Court in Hunan province's verdict, GSK's Chief Executive, Sir Andrew Witty, reportedly said that: "Reaching a conclusion in the investigation of our Chinese business is important, but this has been a deeply disappointing matter for GSK. We have and will continue to learn from this. GSK has been in China for close to a hundred years and we remain fully committed to the country and its people. GSK fully accepts the fact and evidence of the investigation, and the verdict of the Chinese judicial authorities. Furthermore, GSK sincerely apologizes to the Chinese patients, doctors and hospitals and to the Chinese government and the Chinese people. GSK deeply regrets the damage caused."

In the wake of the Chinese case, other major drugmakers have also been under increased review. It has been reported that Sanofi, the French drugmaker, informed US authorities that it was investigating allegations of employees paying bribes to healthcare professionals in the Middle East and East Africa to persuade them to prescribe its drugs.

Cuba

Reports indicate that 17 people, including 14 Cubans and three Canadian executives, have been convicted and sentenced to jail terms ranging from 6 to 20 years.

The charges, which include bribery, fraud, tax evasion and falsifying bank documents surrounding the Tokmakjian Group, were brought against, amongst others, Cy Tokmakjian, founder of the Tokmakjian Group, two Tokmakjian Group executives Claudio Vetere and Marco Puche, Nelson Labrada, former vice minister of the nowdefunct Sugar Ministry, and Ernesto Gomez, former director of the state nickel company Ferroniquel Minera S.A.

It has been reported that $100 million worth of the Tokmakjian Group's assets have been seized by Cuban authorities.

The company stated that the case is a "show trial" and a "travesty of justice." Reports state that numerous defence witnesses, including international tax experts, have not been permitted by the Court in Cuba to give evidence.

Cuba's relationship with Canada is reported to have been strained as a result of the conduct of the trial.

Italy

Eni SpA former chief executive Paolo Caroni and current CEO Claudio Descalzi are reported to be under investigation by Italian authorities for alleged corruption in connection with the state-owned oil and gas company's purchase, in 2011, of a 50% interest in Nigeria's OPL 245 offshore oil field. The field has, according to reports, estimated reserves of 9 billion barrels of oil.

According to reports, Eni paid $1.1 billion for the oil field. Italian prosecutors said that "at least $533 million was paid to Nigerian officials and intermediaries who helped secure the sale." Eni denies all allegations and said that all the money for the purchase went to the Nigerian government and Malabu Oil Gas. Malabu reportedly had close connections to former Nigerian oil minister, Dan Etete.

English courts, at the request of Italian law enforcement officials, froze two bank accounts belonging to Emeka Obi that contained a combined $190 million. Reports indicated that Mr. Obi is believed to have served as an intermediary for the sale.

The investigation is still ongoing.

Istanbul

The Turkish National Police detained 20 people in an investigation of bribery allegations in Istanbul's fire department, according to reports. Seven suspects were released, while the remaining 13 were arrested.

According to reports, the suspects were allegedly involved in bribery and extortion and have been involved in approximately 227 offences. They have reportedly been accused of 164 counts of forgery and bribery.

All businesses in Turkey are required to obtain a fire safety audit report in order to obtain a work permit from local municipalities. The fire department is the final authority in auditing the fire safety of buildings.

Reports indicate that the police wiretapped telephone conversations between fire department officials and business owners seeking permits. The wiretaps identified that a private nursery school paid TL 15,000 (c. £4,150) to obtain a fire-safety report despite the fact that the building was not compliant with the fire department's safety regulations.

Investigations are ongoing.

Romania

The Romanian Parliament voted, 153 to 117, to lift the immunity of former communications minister, Valerian Vreme.

Reports indicate that Mr. Vreme, who was the Romanian communications minister between 2010 and 2012, is now facing charges for abuse of power in a multi-million-euro corruption investigation involving bribes and kickbacks from re-sellers of Microsoft software.

According to reports, in 2011 Mr. Vreme signed a deal to acquire more than 179,000 Microsoft licences for Romanian schools, 73,000 more than the number of compatible computers at the time. Romanian anti-corruption authorities allege that the government paid $54 million for the licenses, out of which $20 million constituted bribes to members of successive governments and private firms.

According to reports, eight other former ministers have been involved in acts of corruption, bribery, money laundering and abuse of office in connection with contracts concluded by the Romanian government to lease Microsoft software to educational institutions between 2001 and 2012.

Reports indicate that the senate is expected to rule on lifting the immunity of two more of the former ministers.

United Arab Emirates

It has been reported that GlaxoSmithKline is inquiring into allegations of corrupt payments in the UAE.

The company has commenced investigations further to receiving a whistleblower's email, purporting to originate from a GSK sales manager in the Gulf state. In the email it was claimed that the company has made payments to healthcare professionals, hospitals, clinics and pharmacies to secure business. Customers were given bonus over-the-counter products as 'payment' for taking prescription drugs. The email also listed accusations of payments having been made for educational meetings that did not take place.

GSK is said to be investigating alleged bribery in a number of other countries, such as Lebanon, Syria, Jordan and Iraq, as well as Poland.

Corruption issues are also addressed in the Anti-Fraud Network's newsletters: see www.antifraudnetwork.com for current and archived material; see also the Computer Fraud website at http://computerfraud.us and www.secactions.com.

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