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The International Comparative Legal Guide to:

Business Crime 2014

4th Edition

A practical cross-border insight into business crime

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An Overview of Business Crime in Latin America

Diaz Reus

Michael Diaz, Jr.

Carlos F. Gonzalez

The Scourge of Corruption

On May 24, 2013, former President of Guatemala Alfonso Portillo boarded a plane to Teterboro Airport in New Jersey. Surrounded by police officers, Portillo claimed he was being "kidnapped" and assured reporters he would return to Guatemala soon, once the case against him collapsed. The scene followed an extradition order against Portillo, who served as President from 2000 to 2004 and faced charges in a New York federal court of conspiring to launder some $70 million of Guatemalan funds through foreign bank accounts, including several located in the United States. The U.S. filed charges against Portillo in 2010 for what prosecutor Preet Bharara called "converting the office of the Guatemalan presidency into his personal ATM". The indictment specifically charged Portillo with violating 18 U.S.C. § 1956, an anti-money laundering statute. He faces up to 20 years in prison on these allegations, as well as monetary penalties. While Portillo awaited trial in the U.S., the Guatemalan government proceeded to freeze almost $4 million held by Portillo and his family members in various European bank accounts.

On August 28, 2013, the head of the anti-corruption unit of the Bolivian National Police, Mario Fabricio Ormachea Aliaga, travelled to Miami, Florida, with the intent to extort a Bolivian businessman. The businessman had fled Bolivia two years earlier seeking political asylum in the U.S. after enduring political persecution and the expropriation of his airline business and assets by the Bolivian government. After the FBI filmed the extortion attempt, wherein Ormachea openly stated that he was acting on the authority of Bolivian President Evo Morales and Vice-President Alvaro Garcia Linera, the FBI arrested Ormachea in Miami on charges of extortion. Ormachea is currently in federal custody without bond and is facing a maximum of twenty-five years' imprisonment.

These cases, like the many before them as well as those currently being investigated, illustrate the sad fact that business crime in Latin America is not limited to low-level public employees. Rather, crimes such as corruption reach even the highest levels of government and are sadly on the rise. While several Latin American countries have vowed to combat corrupt practices and have enacted legislation to formalise their intentions, meaningful change requires active enforcement as well as the political will and sacrifice to exact it. In the meantime, as Latin American countries begin working to strengthen their enforcement regimes, the greater threat to corrupt practices and their participants is coming from the jurisdiction asserted by courts abroad – specifically in the United States and in the United Kingdom. Both the U.S. Foreign Corrupt Practices Act (FCPA) and the U.K. Bribery Act (UKBA) have had extraterritorial reach.

Latin America's "Culture of Corruption"

The notion that there is a "culture of corruption" in Latin America has led some writers to note that decades of unstable economies and turbulent politics in the region have undermined the rule of law and given birth to a view that corruption, or rather that acts deemed to be corrupt from an outsider's perspective, are merely a part of quotidian life and an additional cost of conducting business in the region. Such a view of corruption brings to mind the much-criticised (non-Latin) Chinese cultural practice of *guan-xi*, which literally means "relationships" or "connections" and translates in business to exchanging gifts or favours – a traditionally gracious practice that nonetheless often steps into the realm of what is popularly perceived as unlawful corruption.

The argument that corruption is merely part of the Latin American culture, and an unavoidable part of doing business in the area, however, holds little sway in advocating that nothing should be done to punish and deter the practice. As Latin American economies increasingly mesh with the rest of the world, important transactions are now rarely conducted exclusively within the confines of any one country. The costs of corrupt practices are thus increasingly borne by a diverse set of interest groups, including widely dispersed foreign investors as well as the international financial institutions involved in cross-border transactions. A common business practice of "gifting" can quickly turn into a complex scheme of international money laundering involving misappropriated public funds, at least from the perspective of regulators and law enforcement.

Corruption's Negative Impact

Official corruption carries with it heavy economic and social costs. Some estimates show that the cost of corruption amounts to more than five percent of global GDP (US$2.6 trillion) with more than US$1 trillion paid in bribes each year. [See Endnote.] In Latin America, actual corruption is pegged at five to 10 percent of overall government spending and 15 to 30 percent of infrastructure spending.

These figures indicate that corruption cannot be so readily dismissed as an inescapable regional cultural practice, but that it must instead be actively combated and deterred by a real threat of significant criminal and financial liability. Aggressive domestic legislation and political initiatives, such as President Maduro's in Venezuela, are certainly a first step in the combat. However, these measures must be followed up with a consistent campaign of criminal prosecution of high profile cases, including the imposition of severe penalties that can serve to deter similar future unlawful

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conduct. Until Latin American countries catch up with the pace of corrupt practices through adequate legislation and unyielding enforcement, the extraterritorial reach of foreign statutes, including U.S. anti-money laundering laws, the FCPA, and the UKBA, will have to fill in the regulatory void left by deficient local programmes.

How Different Countries Deal With Corruption

In drawing generalisations about the region, it is often easy to overlook the specific steps that individual countries are taking to deal with, or respond to, allegations of official corruption. Every country follows a different approach. Their responses to claims of corruption or lax enforcement of anti-corruption law are as varied as each country's unique leadership. Consider the cases of Venezuela and Mexico.

Venezuela

One of the most forceful recent government initiatives to combat corruption is taking place in Venezuela. President Maduro is calling the rampant corruption in his country a "national emergency". Since taking office in March 2013, President Maduro has led an anti-corruption crusade that has already resulted in the arrests of dozens of officials at state owned companies and government ministries. To further his initiative, Maduro is now seeking fast-track legislative powers that would allow him to enact laws by decree without parliament's approval.

Mexico

In 2012, the *New York Times* unleashed a scandal when it reported allegations of an extensive practice of bribery by Walmart's Mexican subsidiary, Walmex. The allegations were based on statements made by a Walmex official who supposedly had alerted company executives in 2005 about the bribes, to no avail. Internal Walmart e-mails since released have further indicated that Walmart's CEO, Mike Duke, may indeed have been on notice of the bribery allegations as early as 2005, contradicting earlier statements that the company knew nothing of the bribery practice. The world's largest retailer now finds itself subject to numerous lawsuits by stockholders contending the company may have violated the FCPA as well as other anti-bribery statutes. By some accounts, at least $24 million in "suspect payments" were made as part of Walmex's scheme to ensure desirable locations for new stores by paying Mexican officials bribes related to zoning laws and environmental regulations. Walmart has thus far expended $300 million on its internal investigation into these allegations and has budgeted an additional $150 million in related expenses for the remainder of 2013.

More recently, a joint venture formed by German corporation Siemens AG and SK Engineering of South Korea was accused of bribing officials at Mexico's state-owned oil company, Petróleos Mexicanos (Pemex), one of the largest companies in the world. The venture's executives allegedly paid bribes to Pemex officials in order to secure a lucrative oil refinery contract. These allegations were nothing new for Siemens, however. In 2008, the company agreed to a $450 million criminal fine from the Department of Justice and disgorgement of $350 million in wrongful profits to the SEC in order to resolve the numerous charges it faced for violations of the FCPA. The $800 million combined penalty was nearly twenty times the previous record fine for FCPA violations. A few years later, in 2011, the SEC brought suit against seven Siemens executives, including a former member of Siemens' managing board. The SEC's lawsuit alleged the executives had participated in a bribery scheme paying nearly $100 million in bribes to top Argentine officials in order to land a $1 billion contract to make national identity cards.

International Perspective

Executives at multinational corporations in the United States and other countries are increasingly taking anti-corruption statutes seriously and implementing corporate programmes to ensure compliance with the various applicable regulations. On one front, there is the U.S. Foreign Corrupt Practices Act of 1977, which granted the U.S. Department of Justice and U.S. Securities and Exchange Commission broad jurisdiction to enforce the statute's prohibition against the bribery of foreign officials. The statute is often deemed to have extraterritorial reach on the basis of an only minimal U.S. nexus, potentially imposing serious penalties on foreign entities and individuals engaging in bribery conducted entirely abroad.

On another front, the U.K. enacted its own Bribery Act of 2010, which went into effect in mid-2011, in order to update and enhance its foreign anti-bribery measures. Intended to better address the requirements of the OECD's 1997 Anti-Bribery Convention, the UKBA is now among the strictest legislation internationally on bribery. In particular, the law introduced a strict liability offence under Section 7 of the Act for a corporation's failure to prevent bribery on its behalf. Because the only defence against an allegation of a Section 7 violation is a showing of adequate preventative procedures in place, companies are now required to establish extensive internal programmes, including conducting bribery risk assessments and consistently monitoring their business practices.

Like the FCPA, the UKBA has extraterritorial reach for both U.K. companies operating abroad as well as for overseas companies with a presence in the U.K. The Act's broad territorial scope means that a foreign company that carries on any part of its business in the U.K. could be prosecuted for its failure to prevent bribery, even where the bribery allegedly takes place entirely outside the territory of the U.K. Companies with a U.K. presence thus find themselves playing a significant regulatory role. Such quasi-governmental responsibility, however, is hardly surprising given that many multinational corporations have access to financial and informational resources beyond those of some governments. These private entities are indeed in the best position to regulate business crimes, especially in light of the sad reality that a government itself plagued by corruption can hardly be expected to adequately control the corrupt practices taking place within its borders. This dilemma is illustrated by the above case of Bolivia, whose top anti-corruption cop is currently locked up in a Miami jail cell on charges of extortion.

Because multi-national corporations must now ensure that their internal anti-bribery programmes comply with a series of applicable regulations, they are having to expand, rather expensively, their compliance procedures to cover a broader range of possible infractions, recognising that even compliance with the FCPA does not ensure that their internal programme constitutes adequate procedures as required under the distinct UKBA. They must additionally be cognizant of domestic regulations in the specific countries where they conduct business. Companies are thus best positioned to minimise their risk exposure to civil and criminal liability for allegations of bribery schemes when they can prove rigorous internal compliance programmes and proper due diligence, including procedures for inquiry, investigation, and personnel training.

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Tax Evasion

Of the common business crimes in Latin America, tax evasion is the least policed, punished, and regulated. It is also the most widespread and directly linked to the region's continuing underdevelopment. The distributional consequences of tax evasion undermine governmental efforts to improve citizens' quality of life and to fuel the healthy expansion of a consuming middle class with economic power. Tax evasion drains billions of dollars annually from governmental projects in Latin America, thereby depriving countries of the resources necessary to provide the infrastructure and the education base crucial for further development.

What leads so many Latin American companies and individuals to evade taxes? While tax evasion is by no means a business crime unique to Latin America, or to developing regions generally, violators are certainly more likely to get away with the crime when local tax laws are inadequately enforced and government agencies lack the sophisticated tools with which to actively monitor money transfers. A deeper inquiry into the social motivations behind tax evasion in Latin America, however, would likely reveal that much of the justification for this common unlawful practice stems from negative perceptions of governmental use of tax proceeds. In a region plagued by corruption, the expectation that hard-earned profits will go directly into the pockets of dishonest government officials by way of bureaucratic misappropriation leads many to actively seek methods by which to avoid or minimise their tax obligations. Local and international financial firms play a critical role in facilitating tax evasion by catering to their clients' desire to conceal funds and direct them abroad, often to tax havens in Europe or in the Caribbean.

A potentially powerful weapon in combating tax evasion is the adoption of international agreements on cooperation of reporting obligations and on disclosure of account holder identities. In the U.S., the Internal Revenue Service has made strong progress in recent years in its fight against international tax evasion. By piercing international bank secrecy laws and entering groundbreaking international tax agreements with foreign countries, the U.S. has collected billions of dollars in penalties from tax evaders. Its Offshore Voluntary Disclosure Program has also proven a success by encouraging evaders to voluntarily disclose and pay applicable fines rather than risk detection by the IRS and possible criminal prosecution. These steps, and similar ones taken by major European countries, have paved the way for Latin American countries to follow suit.

By adopting tax treaties and establishing similar mechanisms for cracking down on tax evasion, Latin American countries can benefit from the momentum that the U.S. has initiated with measures such as the U.S. Foreign Account Tax Compliance Act of 2010 (FATCA). The Act could provide a model for Latin American countries seeking to participate in what has now become a global assault on tax evasion. Mexico has certainly followed in the U.S.'s footsteps. In just the five months spanning March-August 2013, Mexico signed tax treaties with Hong Kong, Qatar, Kuwait, and Colombia. It now relies on a tax treaty network comprising 56 countries. By harmonising fiscal systems, tax treaties can provide greater legal certainty to investors. They can also be designed to prevent tax evasion through exchanges of information by tax authorities. Their implementation is an important step in addressing the rampant tax evasion throughout Latin America, especially because tax evasion so heavily relies on the international transfer of money into secretive foreign accounts. Without secrecy, the risks and costs of evading taxes increase significantly.

Tax Evasion: Colombia's Other War

In late 2012, the failure and subsequent liquidation of Interbolsa, Colombia's largest stock-broker, became one of the largest financial scandals in the nation's history. Among Interbolsa's suspect practices was what Colombia's Comptroller General's Office characterised as "substantial tax evasion". Interbolsa allegedly offered customers what it called "financial optimization services"– apparently code for tax evasion. Specifically, Interbolsa and its related companies offered clients the opportunity to take advantage of a well-known tax loophole, whereby the firm would allegedly transfer clients' portfolios to different "third party" accounts for a duration of a few days, thereby escaping the tax regularly imposed on such financial transactions.

This scenario, however, leaves unclear where the fault really lies. While the Comptroller General's Office reprimanded Interbolsa's shortcoming in controlling the taxes on its banking transactions, the government's faulty oversight and its failure to remedy this existing loophole were arguably what allowed this practice to proceed for so many years. The fact that the red flags of tax evasion took so long to be noticed begs the question: *where were the regulators?*

Money Laundering

Money laundering is the direct by-product of other business crimes and is independently criminalised in the U.S. under 18 U.S.C. § 1956. Money laundering garners the greatest attention when it is linked to terrorism or, as in the context of Mexico and Colombia, to the illicit drug market. However, it is also a critical component of corrupt practices, as in the case of Alfonso Portillo and others. Because money laundering takes place in many disguises and because few governments have the adequate financial or informational resources to effectively regulate the crime, responsibility has been increasingly shifted onto the shoulders of private parties. Specifically, global financial institutions, which are arguably in the best position to monitor financial transactions and detect suspect laundering schemes, have been burdened, at great expense, with the sort of regulatory responsibility traditionally assumed by government agencies.

In July 2013, a federal judge in New York approved HSBC's $1.9 billion agreement with the U.S. to resolve charges that the bank had enabled Latin American drug cartels to launder billions of dollars. Europe's largest bank was accused of failing to monitor more than $670 billion in wire transfers and more than $9.4 billion in purchases of U.S. currency from HSBC Mexico. In addition, because of a lack of proper controls, drug cartels in Mexico and Colombia were allegedly allowed to move more than $800 million through HSBC's U.S. unit from 2006 to 2010. The bank, according to the U.S. and cooperating ex-bank officials, had cut resources for its anti-money laundering programmes in order to increase its profits.

The agreement between the U.S. and HSBC has drawn extensive criticism for allowing the bank and its management to avoid further criminal proceedings over the serious charges. HSBC, however, was not proven to have actually laundered anything. Rather, its internal documentation and reporting processes were simply deemed inadequate to prove that it had not done so. The $1.9 billion fine, therefore, was not for money laundering but, rather, for failing to strictly abide by regulations demanding active monitoring and prevention of money laundering operations.

Money laundering schemes are certainly harmful to Latin American countries, as they permit billions of dollars of public funds to be channeled abroad and fund terrorist and drug operations in the

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region. However, legal battles with financial institutions and the imposition of fines could also prove problematic. As a result of the increasingly stringent money laundering rules, and in the wake of HSBC's recent fine, international financial institutions have begun pulling away from otherwise profitable operations in emerging markets. While these moves have thus far been mainly in Africa and the Middle East, Latin America risks losing important financial market players and their critical provision of capital and banking services. Access to the global financial system and to its instruments and institutions is essential for the continuing development of Latin America and for the financial security of its citizenry. Striking a balance between allocating the responsibility of preventing money laundering onto financial institutions and not scaring these companies away with excessive risk of liability will prove a worthwhile challenge in order to satisfy the region's interest in rooting out business crimes while simultaneously cultivating a thriving financial market.

HSBC found itself in the spotlight once again in March 2013, when Argentina charged the bank with facilitating money laundering and tax evasion in the country. The government accused HSBC of conspiring with private companies to hide bank accounts so as to evade taxes and launder money. HSBC, however, is hardly alone in these scandals. JP Morgan and BNP Paribas have recently faced similar charges for failing to adequately monitor wire transfers and, consequently, enabling money laundering. In July 2013, former JP Morgan executive, Hernan Arbizu, who has been under investigation since 2008 for his own fraudulent schemes, provided testimony before an Argentine court admitting he helped Argentine clients move billions of dollars into offshore accounts as part of a massive tax evasion scheme. Argentina's national financial investigations unit, which has been criticised for conducting lax investigations, has announced plans to formally accuse JP Morgan of money laundering.

Argentina is among several Latin American countries that have developed their own specialised investigative and prosecutorial units to pursue charges of business crimes. The effectiveness of these recently implemented national measures, however, is questionable. Meanwhile, foreign regulators such as the Financial Action Task Force, the intergovernmental body responsible for developing and promoting policies to combat money laundering, are often seen as having a stronger hand in this battle.

Conclusion

Business crimes take place in countries around the world. However, they thrive in less developed regions where the legislative and regulatory environment is lax and prosecution unlikely. In Latin America, where decades of political instability and economic setbacks have undermined the rule of law, bribery and corruption can reach even the highest levels of government.

The costs of these business crimes are enormous, imposing significant burdens on developing states by draining billions of dollars in public funds and creating an environment conducive to tax evasion. These unlawful practices will no longer be tolerated and present far more risk to business crime participants than they have ever faced before. Foreign nations, such as the U.S. and the U.K., are no longer turning a blind eye on business crimes occurring abroad. Whether for the sake of business integrity, for the protection of their own domestic investors, or to combat terrorism and drug dealing, these powerful nations lack no incentive to actively participate in the effort to curb these criminal practices.

Merely enacting laws, however, is not enough – real reform requires enforcement through aggressive high-profile prosecutions. The requisite enforcement measures, however, can be costly and require investments in the training of competent investigators and prosecutors. The penalties imposed on guilty parties can allow governments to recover some of these costs, but so far there continues to be a noticeable lack of penalties in Latin America in general. One theory is that corrupt practices reach so deeply into governmental institutions that the public officers responsible for combating business crimes are themselves active participants, perhaps receiving bribes in exchange for silence and inaction.

Until enforcement by Latin American governments catches up with the rapid pace of ingenuity and innovation characteristic of business crimes, improved cooperation among the countries in the region and, more importantly, mutual legal assistance treaties with better-equipped nations, especially the U.S., would be wise. Foreign investors doing business in Latin America are well advised to review their compliance measures, ensuring that their operations meet the requirements of the FCPA, the UKBA, and the local laws where they conduct business. Companies or their individual officers may otherwise find themselves under investigation for criminal activities and face the risk of indictment, extradition, and the potential payment of hefty fines, as well as possible jail time.

Endnote

Global Agenda Council on Anti-Corruption and Transparency 2013, WORLD ECONOMIC FORUM, available at:

http://www.weforum.org/content/global-agenda-council-anti-corruption-transparency-2013 (last visited Sept. 16, 2013).

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