REPORT

BRAZIL AND MEXICO CONSIDER ISO 37001

Alejandro Aurrecoechea
Todd Gastelum
Marcelo Sumi
Christine Vargas

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Control Risks Group, L.L.C. | 1600 K Street, NW | Suite 700 | Washington DC | 20006 | USA
T: +1 202 449 3330 | F: +1 202 223 9072

www.controlrisks.com

Brazil and Mexico represent the first and second largest economies by GDP in Latin America, and they are arguably the loudest voices calling for increased anti-corruption enforcement in the region, due to a plethora of recent public scandals. It makes perfect sense that their anti-bribery and compliance (ABC) programs, while still distinctly in development, are leading regional efforts. Which makes these two countries excellent testing grounds for the Switzerland-based International Standards Organization's newly released ISO 37001—the long awaited Anti-Bribery Management Systems standard. ISO 37001 dropped on October 14 and immediately prompted questions: what organizations are authorized to certify companies; which public offices are responsible for enforcement and will they be effective; and most importantly is the economic and political upside to embracing and supporting the standard worth the costs to do so? As Latin America's tolerance for corruption evaporates, Brazil and Mexico will continue to improve their long-term ABC legislation; it remains to be seen whether ISO 37001 will influence their efforts.

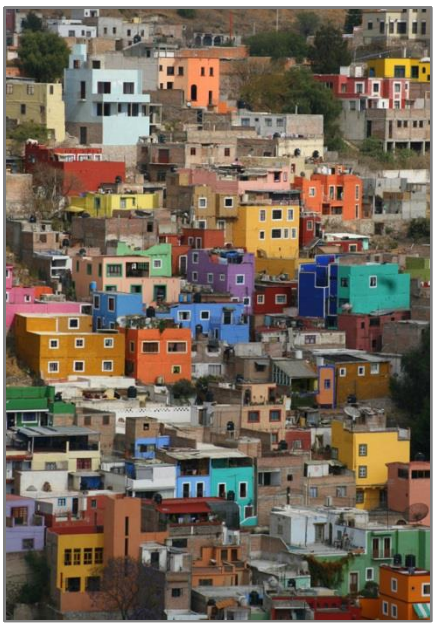
Brazil has in recent years been shaken by corruption scandals; investigations into national oil company Petrobras revealed a multibillion-dollar kickback scheme implicating company directors, private executives and senior political figures. The resulting crisis helped sink the government's approval ratings, fuel large-scale protests and boost support for the impeachment of President Dilma Rousseff, who was removed last August for allegedly breaking fiscal laws. Mexican president Enrique Peña Nieto has also watched his approval ratings plummet over this past year, prompting his public apology in July over a luxury real estate scandal involving his wife and the Ministry of Finance. As a result, both countries are working to strengthen and enforce anti-corruption laws to enhance compliance and public sector accountability. Incorporating ISO 37001 into their efforts could offer a credibility boost for legislation, given that it hews closely to the Foreign Corrupt Practices Act (FCPA) and the UK Bribery Act (UKBA).

Brazil's compliance market has come of age over the past two years with the Petrobras investigation (known as Operation Car Wash) and the 2013 passage of the Brazilian Clean Company Act, which established companies' legal responsibility for corruption. Since the demise of the bureaucratic Comptroller General of Brazil (*Controladoria Geral da União,* CGU) at the hands of Michel Temer (then Brazil's interim President), a new Ministry of Transparency, Monitoring and Control (MTMC) was established in May 2016 to support the implementation of the Act—although, ironically, its inaugural leadership was removed shortly after following corruption-related accusations.

Any public office in Brazil with access to federal, state or municipal funds can trigger an investigation under the Clean Company Act. This partially decentralized system, overseen by the MTMC, has increased incentives for companies to take a proactive approach in building and/or improving their compliance programs by seeking external support and hiring full-time compliance personnel. The cascading effects of this include the recasting of compliance as the hot new field, which in turn is broadening the talent pool of compliance professionals and boosting the number of educational programs designed to train them. Talent, from old hands to millennials, now feels that compliance can offer a promising, successful career.

This broadening compliance market could trigger a cottage industry of ISO 37001 certifiers, but only if the certification offers tangible benefits. These benefits could include leniency from prosecutors when certified companies are indicted for compliance violations. Certification could also mean increased reputational appeal to foreign investors and partners. It will take at least two years for any first adopters to demonstrate this return on investment through more favorable outcomes during brushes with the MTMC, and increased revenue from global partnerships. In the meantime, the majority of Brazilian companies may take a wait-and-see approach.

In contrast, Mexico's ABC regime and compliance market are less mature and hampered by a current lack of enforcement. That responsibility will fall to the centralized National Anticorruption System (NAS), which is responsible for enforcing seven primary laws enacted in July 2016. These include the General Law of Administrative Responsibilities (*Ley General de Responsabilidades Administrativas)* commonly known as the "Ley 3-de-3," which refers to its requiring public officials to disclose their a) personal assets, b) tax returns and c) potential conflicts of interest. Additionally, for the first time, the law means corporations can be sanctioned and penalized for acts of corruption, including significant fines and prison time for those found guilty.



Unlike Brazil, not all public offices across the government will have the authority to launch an investigation into corrupt activities. Instead, a centralized, slow-to-coalesce coordinating committee of four to five as-yet-unnamed federal regulators will have that responsibility. Those federal regulators will be presided over by a representative of a civilian participation committee, all of whose five members will be proposed by a nine-member board consisting of academics and civil society representatives. Meanwhile, each Mexican state and municipality is now legally required to build its own anti-corruption system to police itself and its public officials, using the federal example as a blueprint. This process, however, is far from complete as states have an entire year to change their legal framework to come in line with federal NAS legislation.

It also remains unclear which federal, state or municipal regulating bodies will enforce what portion of the seven laws—not to mention set standards for fines and punishments and determine the form in which these will be levied. There is also concern that the federal budget submitted to Congress on September 8 does not earmark sufficient resources for the prompt implementation of the NAS. It's unclear whether Mexico is in a position to dedicate resources to considering ISO 37001 as a certification alongside some twenty ABC laws still to be produced. Which means, in the short term at least, getting certified under ISO 37001 may only be worth dedicating the time and money—not to mention undergoing a process involving intense scrutiny—if it yields increased appeal and credibility across global markets, particularly the United States. At present the US supplies the majority of Mexico's FDI. Mexico's politicians are likely more concerned with completing and enforcing the laws the public is currently demanding.

Corruption is a disease that has long plagued Brazil, negatively affecting the country's political culture, business environment and society more broadly. Recent investigations, particularly Operation Car Wash, helped put the problem back into the public debate and at the top of people's minds. And while the motivations behind Rousseff's impeachment are complex to say the least, the Petrobras corruption scandal played a decisive role in sealing her political fate. However, despite major improvements brought about by investigations and legislative initiatives, the corruption phenomenon remains embedded in Brazilian politics, with some politicians remaining eager to once again sweep the subject under the rug. As such, adopting an ISO standard and further strengthening ABC practices may not be seen as a political priority in the context of continuous political tensions.

Brazilian businesses, however, can take a more proactive approach. The recent sentencing of executives from the energy and construction sectors already indicates that Brazilian compliance enforcement is becoming increasingly effective. It's simply a question of which Brazilian industry is next in line for a reckoning. While the energy and construction industries remain the main focus of

attention, further probes, often with evidence emerging from Car Wash, have already expanded into sectors as diverse as pharmaceutical, healthcare, food processing, electricity, entertainment and financial services. In the face of increasing integrity risks across the business environment, the ISO 37001 certification could provide a key differentiator for companies operating in Brazil that want to differentiate themselves from their peers to become preferred global partners in their sector.

Mexico has not had a wide-ranging corruption probe such as the Car Wash scandal in Brazil. But current public discontent in response to corruption scandals overall is not without its consequences. It certainly helps explain the loss of President Peña Nieto's party, the PRI, in seven of the twelve governorships at play in the June 7 elections—although the PRI, which has a majority in the lower house of Congress, is likely to maintain loyalty to Peña Nieto until the end of his term in 2018.

Meanwhile, civil society scored a win in pressuring Congress and state legislatures to validate the constitutional reform of May 2015 that included the citizen-regulated NAS. Subsequently, it was civil society that participated actively in the negotiation of the corresponding laws and secured the president's support for this new legislation through protests. Public discontent has been channeled into this fight and, at the moment, is somewhat satisfied by this victory. Touting ISO 37001 as a standard to be valued, implemented and enforced could help Mexico's politicians further placate their constituents, especially as civil society organizations are expected to continue pushing for the implementation of the NAS over the next two years, in light of the continued reticence shown by the Peña Nieto administration to do so. Public outcry against corruption is not so vociferous that Mexican politicians are out conducting witch hunts against one another with evidence of scandal or promising draconian sentences for those guilty of graft to cheering crowds. Touting the Standard could still win political points, albeit short-lived ones, unless their speeches are backed by the NAS taking ISO 37001 seriously when it finally gets up and running.

But Mexico's private sector deals largely with US partners and distributors, and the US Department of Justice has yet to mention the certification as a credible enhancement to a company's internal compliance program. Key Energy was fined $5 million just this year for FCPA violations after an employee at its Mexican subsidiary was caught paying bribes to a representative of PEMEX, Mexico's state-owned oil and gas monopoly. Meanwhile, public bids for public infrastructure projects remain opaque at the state and municipal levels. At the federal level, this process has improved somewhat due to transparency laws, but the federal Public Works Law needs to be amended to foster more competitive bidding processes (i.e., reduce the direct granting of contracts without competition). When it is, federal anti-corruption efforts will be poised, as is their purpose, to set the tone for the country—not the ISO 37001. The other side of this argument is that Mexican companies could use the certification as an outward signal that they are seeking to adhere to a standard comparable to the FCPA and UK Anti-Bribery Act while the Mexican government gets its laws and the NAS stood up and in working order.

Both Brazil and Mexico have work to do in bolstering the confidence of foreign investors. The most compelling argument for certification under ISO 37001 seems to be FDI. According to Control Risks' and Oxford Economics' Economic and Political Risk Evaluator (EPRE), Brazil's GDP is forecast to remain flat in 2017 (0.1% expansion). According to EPRE analysts: "Growth will likely return in 2018, albeit at a modest 1.8% but rising to around 3% over the medium term as a newly elected, more business-friendly government pushes through important structural reforms. Meanwhile, Mexico's GDP growth will likely average 2.7% per year in 2017-20, with growth potential benefitting from structural reforms and increased FDI" …which has to come from investors who are reasonably confident they're making decisions with the right risk ratio.

With flat growth in Brazil, and only modest growth in Mexico, it behooves politicians and businesses in both countries to seek ways in which to render their offerings more attractive. Meanwhile, in the short term, expectations of facilitation payments unfortunately remain entrenched within both countries' business cultures. Often, the view is that business cannot progress without bribery. Each country's new anti-corruption laws have loopholes that businesses and government officials will continue to exploit to procure licenses, permits and other benefits. And both countries' private sectors are increasingly seen as encouraging corruption as much as the public sectors.

ISO 37001 could serve as a compliance booster in Brazil and a driver of change in Mexico. The standard provides clear guidelines that Brazilian corporations of all sizes can use to underscore their ABC efforts, and Mexican corporations can use it to build and expand their corporate compliance programs in advance of truly effective, nationwide NAS enforcement. This could create a more secure business environment in both countries for international partners and investors, but only if the return on investment in the next two years proves significant in both revenue generation and political capital for those willing to take the plunge and adopt the Standard before the majority of their peers.