

Localization of MNCs' Anti-bribery Compliance Policy in China – Through the Dual Lens of the FCPA and Chinese Law

By David Pan and Kenneth Kong

Chinese subsidiaries and branches of MNCs headquartered in foreign countries, as well as Chinese companies which have invested overseas, may be subject to multiple jurisdictions, including the law of the parent country, the host country and even third party countries. Facing regulatory oversight in different countries, MNCs are inclined to adopt a globally uniform Anti-Bribery Compliance Program (“ABCP”) and implement such ABCP in a “top-down” manner to its subsidiaries and branches worldwide. The ABCP aims to satisfy all the legal and regulatory requirements in different countries by meeting the best practices worldwide. To assist implementation in various places of business, generally the ABCP is written clearly and concisely, with translated versions in local languages. Nevertheless, due to cultural and legal differences, a simple transplantation of an ABCP into China may encounter obstacles, with a certain fine-tuning required for smooth implementation. Among others, two examples are chosen in this article to analyze the rationale and method of such required fine-tuning: (i) gift and entertainment policy; and (ii) the local written law rule.

1. Business Entertainment and Gifting

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U.S. or European based MNCs are governed by the FCPA, British Bribery Act or similar foreign laws and regulations, which prohibit or strictly restrict MNCs from entertaining or giving gifts to foreign government officials in their business activities. For compliance purposes, an MNC usually follows this rule in its ABCP. However, compared with Europe and the U.S., Asian countries including China have a more ingrained business culture of entertainment and gift-giving. In this “die-hard” culture, Chinese subsidiary companies of U.S. or European MNCs might be concerned that an absolute observance of the prohibition or restriction on gifts and entertainment as required by ABCP would put them in a disadvantageous position when competing with less scrupulous rivals. Hence,

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such Chinese subsidiary companies might request their headquarter offices to allow certain tweaks to such a policy. Depending on the balance of interests and the extent of the headquarters' trust in the Chinese management team, MNCs vary in their attitudes towards whether tweaks are necessary, and if so the extent of such tweaks. Based on the prevailing practice of leading companies across industries, Llinks' regulatory compliance team has summarized the following best practices on this issue:

- (1) MNCs shall unequivocally establish the universal application of ABCP as the basic rule, while only limited exceptions should be permitted in a limited time period to a safe extent based on a thorough risk assessment. Meanwhile, the Chinese management team of MNCs shall be required to phase out the practice of business entertainment and gift-giving to government officials, until the practice is fully eliminated. With respect to the limited exceptions, the legal department, compliance department and audit department of MNCs must jointly conduct a thorough and complete risk assessment to determine the safety of such exceptions. It is advisable that the legal and compliance departments should review and approve the reasonable amount to be spent on each permitted business entertainment and gift-giving in advance.
- (2) Whether the recipients of the business entertainment or gifts are government officials or not, the permitted business entertainment and gift-giving must not be made *quid pro quo* or have the same effect.
- (3) According to the FCPA, any gifts given to government officials must not be cash or cash equivalent. The *Interpretation of the PRC Supreme People's Court and the PRC Supreme People's Procuratorate on Issues Concerning the Application of Law in Handling Criminal Cases of Corruption and Bribery* (***“Interpretation on Issues Concerning Application of Law in Handling Criminal Cases of Corruption and Bribery”***) expands the scope of “cash and goods” used in bribery to include any proprietary interests like benefits convertible into cash or other benefits which can only be obtained with payment of cash. For compliance purpose, any fine-tuning of an ABCP must not permit cash or proprietary interests to be granted to governmental officials in any business entertainment or gift-giving context. Taking the custom of gifting moon cakes as an example, some MNCs subsidiaries in China give moon cake coupons to governmental officials during the Chinese Mid-Autumn Festival as a gesture of gratitude. Nevertheless, the moon cake coupons in essence constitute a bill with cash value with certain geographical and time period restrictions, since such coupons can not only be used for redeeming moon cakes but also can be exchanged for certain amounts of cash. Therefore, even if the ABCP was altered to permit moon cake gifting to governmental officials as a limited exception, such gifts must be given in the form of moon cakes rather than as coupons.
- (4) With limited exceptions made available through the fine-tuning, ABCPs shall, based on reasonable business needs, strictly control the number of times, spending amount, and reasons for business entertainment and gifting. According to the *Interpretation on Issues Concerning Application of Law in Handling Criminal Cases of Corruption and Bribery*, if the bribes are accepted repeatedly and

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remain unpunished, the amount of all such bribes shall be taken into account cumulatively in any sentencing or punishment. Although entertainment or gifts with small values to government officials do not normally constitute bribes, the risk of a “cumulative amount” should not be ignored. In practice, leading MNCs in China set the frequency of entertainment or gift-giving to the same recipient (government officials or non- government officials) to no more than twice a year with a spending limit of US\$ 50 per occasion.

2. Rule of Local Written Laws

The FCPA incorporates the provisions of “local written laws”. Such provisions provide U.S. companies with a defense against legal liabilities for paying foreign government officials any expenses, such as travelling expenses, if the payments are mandated by local written laws. The premise of such exemption is that the payment must be lawful under the local written laws and regulations, while any payments made pursuant to the local industrial practice, the local custom or unilateral requirements by any governmental authorities are not eligible for the local written law defense.

In an ABCP, MNCs might include the rule of local written laws cautiously. However, the application of the rule in China is far more complicated because of the ambiguity of certain Chinese laws and regulations.

[Case Study]

Company A, a Chinese subsidiary of a U.S. company, engages in the business of material manufacturing. In 2015, Company A needed to import a large number of special equipment for a new plant project. Company A was instructed by the local Municipal Bureau of Quality and Technical Supervision of X City (the “**Bureau**”) that the Bureau would delegate a special equipment supervision and inspection team, led by a department director, to conduct onsite examinations of certain vendors of pressure vessels overseas, with the relevant expenses to be borne by Company A. After researching relevant laws and regulations, Company A found that according to D3 under the *Special Requirements of Imported Pressure Vessels' Supervision and Inspection* of the *Supervision and Inspection Rules of Pressure Vessels* (TSG R7004-2013) (the “**TSG R7004-2013 Rules**”) issued by the General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China (“**AQSIQ**”), “the inspection of imported pressure vessels can be conducted through overseas supervision and inspection of the vessels' manufacturing process...For overseas supervision and inspection, the supervision and inspection institution shall establish the time schedule with users or manufacturers of the imported pressure vessels, and shall send inspectors overseas, and shall complete the work record such as the supervision and inspection report. ” Nevertheless, the TSG R7004-2013 Rules are silent as to which party shall bear the relevant expenses for supervision and inspection.

The Bureau required the supervision and inspection team (consisting of four inspectors) to conduct the overseas inspection multiple times. The total traveling expenses would be a significant amount. Company A was caught in a dilemma: On the one hand, if it chose to refuse the payment, the plant project would not be completed for operation without the special equipment. On the other hand, if it chose to pay such travelling expenses, it might run the risk of being deemed as making a payment (offering a bribe) to

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foreign government officials under the FCPA. Could Company A invoke the rule of local written laws as a defense?

Company A's legal counsel first considered a solution that the abovementioned expenses would be borne by the overseas manufacturers of the equipment. The plan was rejected for the following reasons: (i) according to the FCPA, since Company A had knowledge that the governmental authority required it to bear the expenses, Company A shall be liable for the misconduct of its vendors whom it requested to pay; and (2) if its vendors directly pay the travelling expenses of the governmental officials, it would be more difficult for Company A to oversee the reasonableness of such expenses. Payment of any expenses unrelated to the mandatory inspection would increase Company A's risk of breaching the FCPA.

When analyzing the applicability of the local written law defense, Company A was confronted with three obstacles: first, according to Article 1 of the *Regulations on Strict Restrictions of Leading Cadres' Overseas Visits* ("**Regulation on Cadres' Visits**"), which was issued by the General Office of the Communist Party of China and the General Office of the State Council in 1989, leading government officials at the associate, provincial or ministerial level shall not accept any invitation of visit from foreign invested companies or overseas Chinese corporations, nor shall they request such invitations from any aforesaid entities. According to Article 4 of the *Supplementary Provisions of Regulations on Strict Restrictions of Leading Cadres' Overseas Visit* issued in 1991 ("**Supplementary Provisions**"), "temporary business trips made by leading cadres and other governmental officials at the prefectural or departmental level (or below) shall also be subject to strict approval and control pursuant to the aforesaid principles. " If the aforesaid policies were mandatorily applicable to the visits made by the Bureau's supervision and inspection team, the payment by Company A would obviously violate the "local law". Secondly, could the TSG R7004-2013 Rules on technical specifications fall within the category of local written laws? Thirdly, even if the TSG R7004-2013 Rules was affirmed as a local written law, it did not expressly require Company A to pay such expenses.

Company A's in-house counsel and their external legal counsel conducted extensive and thorough research. In the end, Company A agreed to pay the travelling expenses for the supervision and inspection team, while the following measures were implemented to comply with the FCPA:

- (1) Company A held a meeting with the foreign affairs office of City X and the Bureau. In the meeting, these two governmental departments clarified that the purpose of the *Regulation on Cadres' Visit* and *Supplementary Provisions* was to scrutinize leading officials' overseas visits without any specific purpose. In this case, the supervision and inspection team would make the overseas visits to carry out its administrative duties. Therefore, such visits would not violate the *Regulations on Cadres' Visit*. Company A made the meeting minutes accordingly, which recorded the opinions of the two governmental departments;
- (2) Upon Company A's request, its external legal counsel issued a legal opinion which affirmed that the *Supervision and Inspection Rules of Pressure Vessels* was a departmental rule on technical specifications enacted by AQSIQ pursuant to the *Law of the People's Republic of China on Special Equipment Safety* and the *Supervision Regulations on Special Equipment Safety*;

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- (3) The Bureau expressly stated in the minutes of the meeting in relation to the overseas supervision and inspection of the equipment of Company A that: (a) the supervision and inspection work would be organized and carried out by the Special Equipment Inspection and Research Institute of City X (the “**Research Institute**”); and (b) the supervision and inspection team would include officials of the special equipment department of the Bureau, as well as the specialists from the Research Institute. After the meeting, Company A negotiated with the Research Institute about the travelling expenses and entered into a supervision and inspection service contract accordingly. Pursuant to the contract, Company A would pay the agreed expenses to the Research Institute rather than the Bureau;
- (4) The copy of the Approval on Visit to Foreign Countries and Hong Kong and Macau, which was issued by the foreign affairs office of City X, was kept by Company A; and
- (5) Company A designed the itineraries of all overseas visits of the supervision and inspection team and kept a record of the itineraries. It ensured that all visits were for the purposes of official duties only, while irrelevant activities were not included. The expenses were reasonable and appropriate commensurate with the purpose of the visits.

The above case demonstrates that the ambiguity of certain laws and regulations, combined with a government department conflating its supervision power with its public service duty, may cause uncertainty in the application of the FCPA's rules in China. It is advisable that the legal counsel of MNCs deal with these uncertainties in the course of formulating and implementing an ABCP cautiously.

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