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Pandemic Elevates Cos.' Compliance Risks In Latin America

By **William Semins, David Peet and Megan Moore** (May 27, 2020, 7:10 PM EDT)

As European, Asian and North American governments continue to navigate how best to ease restrictions previously implemented to mitigate the effects of COVID-19, by many accounts the virus's human and economic impact in Latin America will exponentially increase.[1]

Commentators and data scientists project that Brazil may follow in the steps of Wuhan, northern Italy and New York as a global epicenter of viral spread.[2]

Latin American governments are balancing the need to respond quickly to short-term and long-term financial needs against the need to ensure that essential funds actually arrive at desired destinations without falling victim to fraud and abuse.

Case studies from the region inform multinational corporations of how both new and changing government policies might establish new points of contact with government actors or agents in the local commercial landscape, as well as the new enforcement risks that exist as a result of these programs and policy changes.

Representative National Responses

Within Latin America, responses vary greatly between countries depending on local circumstances and the government's appetite for stimulus funding. Generally, programs involve a combination of measures designed to reduce the burden of public procurement and financial programs to stimulate the economy.

The government responses in Colombia, Peru, Brazil and Mexico present a sample set which illustrates the breadth and variety of responses in Latin America.

In Colombia, the government issued an emergency decree creating the National Emergency Mitigation, or NEM, Fund program.[3] The NEM Fund provided for additional health care funding, faster direct contracting for services associated with the emergency response (e.g., procurement of medical supplies), additional credit lines for certain businesses, and delayed tax and pension contribution collection.

Peru has also robustly responded to the COVID-19 pandemic with direct payments to



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individuals, tax deferrals and government loan guarantees of up to \$2.8 million for businesses.[4]

On the other hand, Brazil and Mexico have taken less aggressive approaches in responding to the pandemic. In Brazil, the government has created additional credit lines for companies that preserve employment, lowered taxes on medical equipment and supplies, and transferred funds to state governments to support health care.[5]

Since February, Brazil has also permitted purchasers of medical equipment to bypass transparency procedures, such as public bidding, in an effort to expedite the delivery of essential materials.[6]

Similarly, in Mexico the government has enacted policies to reduce bureaucratic red tape, allowing the Ministry of Health to acquire medical supplies more easily, and accelerated the tender process for public spending.[7]

Enforcement Risks and Trends

As a result of these programs, there are elevated risks for multinationals operating in Latin America, due to increased interactions with government officials in a crisis environment. Specifically, there are risks related to (1) misappropriation of funds; (2) expedited government contracting; (3) increased transparency and monitoring; and (4) international cooperation.

Misappropriation of Funds

As the pool of discretionary funds administered by the government increases, so too does the potential that such discretion will be abused to enrich the official responsible for distribution. Misappropriation, collusion, conspiracy and other forms of undue or improper favoritism are all mechanisms through which discretion may be abused.

These risks are especially high when the funds are distributed quickly during an emergency, as is the case at present. In addition to financial penalties, companies also risk reputational damage from scandals involving inappropriate use of government funds.

In what may be a prelude of things to come, the chief prosecutor of Colombia recently asked the Colombian Supreme Court to investigate the role of the agricultural minister, as well as six other individuals and two other governmental agencies, in an alleged scheme to misappropriate emergency COVID-19 funds.[8]

The chief prosecutor alleges that these individuals were involved in a scheme to transfer funds to ghost accounts controlled by government officials, and to grant emergency credit to big companies before smaller borrowers. The ramifications of being involved in such conduct for multinational companies is significant.

Expedited Government Contracting and Commensurate Scrutiny from Regulators

In order to adequately supply public agencies, many countries in Latin America are reducing red tape and calling for expedited public procurement processes. Though this reduces the administrative burden of bidding for public contracts in Latin America, it also creates potential fraud and corruption liabilities abroad, and possibly in the U.S.

Mexican government officials have publicly stated their commitment to continuing business as usual in identifying and eliminating fraud and corruption in public procurement during the pandemic.[9] Mexico's federal attorney general also noted that business will continue as usual, despite the potential for some delays.

Peruvian President Martin Vizcarra stated on April 27 that corruption occurring during a national emergency deserves exemplary punishment, and has committed to approving increases in the budget of the Peruvian general comptroller's office to combat the threat of corruption in public contracting.[10]

Brazilian regulators at the federal and local levels are prioritizing fraud and abuse related to COVID-19.

Brazil's federal public prosecutor, or MPF, reports that it has opened 410 actions relating to overpricing or fraud, including actions relating to medical materials produced abroad, while the Office of the Prosecutor of the Department of Health, or PROSUS, is closely reviewing potential irregularities associated with six emergency contracts of the Department of Health for the Federal District.[11]

Brazil's federal police have also initiated COVID-19-related investigations, such as Operation Virus Infectio, which investigates price-gouging of masks and other personal protective equipment that was sold to the state health fund.[12]

Increased Transparency and Monitoring

As part of the varied government stimulus packages, many countries have implemented processes for increased transparency and monitoring of the funds, making it more likely that fraud will be uncovered by enforcement agencies.

For instance, Colombia's financial management information system allows for tracking of implementation and expenditure under the NEM Fund in real time.[13]

Similarly, Peru has enabled the Supreme Audit Institution, or SAI, to conduct concurrent monitoring as relief processes are being implemented rather than after the fact.[14]

Whether a company is a recipient of such relief funds or is a vendor conducting business with a company in receipt of such funds, heightened sensitivity from government regulators demands active internal monitoring efforts to ensure compliance.

To facilitate such internal monitoring, such a system should include: (1) creating general ledger accounts and/or cost centers to monitor the receipt and use of government funds; (2) increasing audit frequency and/or priority on the funds received; or (3) implementing additional layers of approval with legal and/or compliance to use funds received from such programs.

International Cooperation

Finally, although national enforcement responses to the pandemic are in their early stages, there is early evidence that enforcers around the world will work across borders to investigate alleged pandemic-related misconduct.

For instance, the DOJ recently highlighted its cooperation with state prosecutors in Brazil to identify a computer malware attack on Brazilian consumers originating from a website purporting to belong to a Brazilian brewery's giveaway of free sanitizer.[15]

In public statements, U.S. Federal Bureau of Investigation and U.S. Department of Justice officials have confirmed that COVID-19 has not delayed their ability to communicate with enforcement authorities in Latin America, and that coordination is not slowing down.[16]

In an era of ongoing cross-border collaboration between enforcement authorities in different countries, notwithstanding the differences in the way each country dispenses relief, companies may face multi-jurisdictional exposure for certain violations, including

fraud and corruption.

Key Takeaways

In order to meet the economic urgency of the moment, while operating within the region's current enforcement climate, multinationals with operations in Latin America should work with experienced counsel to identify potential pathways through which their subsidiaries or affiliates may be able to seek relief, whether acting as a vendor or fund recipient.

Specifically, multinational corporations should consider the following measures for mitigating risk in the region.

A Quick-Look Update of Risk Assessment

A multinational company should undertake an analysis to determine if there has been a change in its corruption risk profile in light of the dynamic COVID-19 market environment.

This targeted risk assessment should focus on assessing the degree to which there has been an increase in government touchpoints across three key areas of the business: (1) supply chain and distribution, (2) customer base, and (3) the capital it uses to make, market or distribute its product.

For a company that is planning to serve as a supplier of essential goods and services in Latin America, current conditions also counsel in favor of a reexamination of pricing risks.

As illustrated by Operation Virus Infectio in Brazil, price-gouging is a point of focus for enforcement authorities aiming to ensure integrity in the procurement process. As such, a supplier should ensure that pricing decision makers are familiar with any applicable federal, state, or local pricing limitations imposed by law or regulation in the target market.

In addition, pricing decisions and determinations should be substantiated and documented, accounting for relevant costs, such as production and transportation.

Finally, the pricing approval process should not allow for a rogue employee to engage in side deals outside of the limitations imposed under local law. Gatekeepers at the company should have visibility into, and the power to halt, potentially noncompliant sales.

Determining How Much Diligence Is Enough During and After the Pandemic

In a global health emergency, where relief funds are dispensed quickly to procure supplies needed to save lives, the standard of conducting commercially reasonable third-party due diligence may face extreme pressure.

As in a hospital emergency room, a triage approach to diligence may be the only recourse for some multinational compliance departments, particularly those operating in high-risk industries and markets.

Unquestionably, this crisis shortens a company's time to manage risk effectively. To the extent a purchase was made on short notice or with limited ability to complete otherwise applicable due diligence processes, companies should create and document an internal triage plan that weighs the company's need for the data, the compliance risk to the company, the exigencies of the situation and alternative means of managing any potential or identified risks.

In addition, the plan should include a requirement for a contemporaneous record of the circumstances, a documented justification for proceeding with a transaction to provide

relief materials on an expedited basis, and a plan for conducting standard diligence when the exigency of the crisis passes.

Of course, there is no pandemic defense to a violation of applicable laws, and companies should make every effort in good faith to adhere to a comprehensive, risk-based and integrated third-party diligence process that would otherwise be applicable in noncrisis situations.

U.S. enforcement officials have expressed that the circumstances surrounding a company's attempts to meet compliance obligations will be important in these extraordinary circumstances.[17]

With that in mind, in an environment where the parameters of what constitutes commercially reasonable diligence may be subject to a host of new considerations, including health-related urgency or pandemic-related roadblocks in access to information about a prospective business partner, it is important to document those considerations and pressures, as well as the steps taken under the circumstances.

For example, depending on the market and the situation, companies may reasonably focus first on obtaining clear documentary evidence of the ultimate beneficial owner of the third party, understanding the third party's role and necessity in the transaction, and insisting on robust compliance representations and warranties in purchase orders, order confirmations or other sales documentation, if no formal sales agreement is possible.

But any variance from standard procedure, however justifiable, should be carefully documented and approved in advance, with an identifiable plan for revisiting the relationship and transaction soon after the immediate crisis subsides.

While not a substitute for robust pretransaction diligence, such timely monitoring can mitigate risk by helping a company to identify and remedy potential issues within a reasonable time after the crisis has passed.

In essence, a company can demonstrate the resilience of its internal controls by showing that it planned ahead under crisis conditions and followed up on any unresolved diligence items in a timely fashion.

Managing Risk Associated with Crisis-Relief Charities

During a public health crisis, multinationals can expect greater demand for corporate philanthropic donations. Based on information collected to date, corporate donors have answered the call.

As of May 19, the philanthropy data and tracking organization Candid identified COVID-19-related charitable donations to recipients across Latin America totaling \$517.9 million.[18]

These donations can present unique challenges for a corporate compliance department due to their sheer volume and a company's natural inclination to be a good corporate citizen during difficult times. Potential recipients should be carefully vetted for personal ties to government officials and the existence of ancillary commercial benefits that the donor could receive from a government-affiliated customer through the delivery of the donation.

For example, evaluators of donation requests should be aware of pending or planned public tenders and government contracts.

Furthermore, the donor should make reasonable efforts to understand the ultimate beneficiary of the donated funds or products to ensure that a purported recipient does not serve as a pass-through for fraud and abuse.

In sum, pressures associated with considering such awards should not prevent donors from putting plans in place to address the risks of donation.

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[1] See, e.g., Uri Friedman, Brazil's Pandemic is Just Beginning, *The Atlantic* (May 10, 2020), <https://www.theatlantic.com/politics/archive/2020/05/brazil-coronavirus-hot-spot-bolsonaro/611401/>; Sergio Bitar & Daniel Zovatto, Int'l Idea (Apr. 2, 2020), <https://www.idea.int/news-media/news/impact-coronavirus-latin-america-future>; United Nations, COVID-19 to cause biggest economic contraction ever in Latin America & Caribbean (Apr. 21, 2020), <https://news.un.org/en/story/2020/04/1062292>.

[2] See, e.g., Brazil may become the global epicenter of COVID-19, *The World* (May 8, 2020), <https://www.pri.org/file/2020-05-08/brazil-may-become-global-epicenter-covid-19>.

[3] Int'l Monetary Fund, Policy Responses to COVID-19, <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#C> (last updated May 12, 2020).

[4] Int'l Monetary Fund, Policy Responses to COVID-19, <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#P> (last updated May 12, 2020).

[5] Int'l Monetary Fund, Policy Responses to COVID-19, <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#B> (last updated May 12, 2020).

[6] Compras emergenciais na pandemia são investigadas em 11 estados e no DF, *Metrópolis* (May 11, 2020), <https://www.metropoles.com/brasil/policia-br/compras-emergenciais-na-pandemia-sao-investigadas-em-11-estados-e-no-df>.

[7] Int'l Monetary Fund, Policy Responses to COVID-19, <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#M> (last updated May 12, 2020).

[8] Zdravko Ljubas, Colombian Officials Accused of Misusing COVID-19 Funds, *Organized Crime & Corruption Reporting Project* (Apr. 28, 2020), <https://www.occrp.org/en/daily/12207-colombian-officials-accused-of-misusing-covid-19-funds>.

[9] Gobierno de México, Función Pública mantiene vigilancia sobre compras públicas y recepción de denuncias durante contingencia por COVID-19 (Mar. 27, 2020), <https://www.gob.mx/sfp/articulos/funcion-publica-mantiene-vigilancia-sobre-compras-publicas-y-recepcion-de-denuncias-durante-contingencia-por-covid-19-239139?idiom=es>; Por Covid-19, suspenden audiencias, resoluciones y citatorios en FGR, *Multimedios* (Apr. 29, 2020), <https://www.multimedios.com/nacional/por-covid-19-suspenden-audiencias-resoluciones-y-citatorios-en-fgr>.

[10] Zdravko Ljubas & Nathan Jaccard, Peruvian President: Harsh Punishment for Graft During Pandemic, Organized Crime & Corruption Reporting Project (Apr. 27, 2020), <https://www.occrp.org/en/daily/12195-peruvian-president-harsh-punishment-for-graft-during-pandemic>.

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[12] Id.

[13] Claude Wendling, et al., Int'l Monetary Fund, Keeping the Receipts: Transparency, Accountability, and Legitimacy in Emergency Responses (2020), <https://www.imf.org/~media/Files/Publications/covid19-special-notes/en-special-series-on-covid-19-keeping-the-receipts.ashx?la=en>.

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[15] Press Release, Dep't of Justice, Department of Justice Announces Disruption of Hundreds of Online COVID-19 Related Scams (Apr. 22, 2020) <https://www.justice.gov/opa/pr/departament-justice-announces-disruption-hundreds-online-covid-19-related-scams>.

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