

Chapter 7

Is foreign bribery an attractive investment in some countries?

One of the most basic legal principles is that crime should not pay. Yet this chapter will show that, in many jurisdictions with weak sanctions, foreign bribery may be an attractive investment. In others, foreign bribery is subject to strong penalties, although some of these penalties exist only on paper because they are not backed up by effective enforcement. Only a few countries combine strong sanctions with active enforcement of anti-bribery laws. Thus, this chapter paints a picture of fragmented deterrence across the 41 Parties to the Anti-Bribery Convention. This patchwork of incentives and disincentives for foreign bribery is explored using simulations of “net present value” for “investments in foreign bribery” under assumptions of both certainty and uncertainty. The simulations draw on sanctions data produced by the OECD Working Group on Bribery for each of the 41 Parties to the Anti-Bribery Convention and on the cash flows – including both bribes and benefits – associated with a real-world bribery scenario. They show, in particular, that in many countries having low fines for paying bribery, a company would still be willing to “invest” in a foreign bribery scheme even if it knew in advance that it would be caught and fined at the end of the bribery scenario. This implies that fines for bribery are set too low in many jurisdictions.

Main findings

- Fragmentation across jurisdictions of fines and enforcement effectiveness create both strong incentives and disincentives for foreign bribery across the Parties to the Anti-Bribery Convention. This fragmentation is documented by simulations of returns on investments in foreign bribery for Parties to the Convention.
- The simulations are based on the cash flows from a real-world bribery scheme. For each Party that has a maximum sanction for foreign bribery, this maximum sanction is applied to the cash flow analysis to calculate a net present value for the investment in the bribery scheme.
- The results show that, because of low sanctions in many jurisdictions, companies would still have an interest in investing in the bribery scheme, even if they knew with certainty that they would be caught at the end of the scheme.
- Simulations under an uncertainty scenario where a firm faces at least some probability of getting caught and sanctioned for bribery in each year of the scheme also show a strong fragmentation of incentives. This implies that an appropriate balance between enforcement effort and levels of sanctions needs to be found in order to establish an effective system of deterrence.
- The simulations also show that the availability of effective systems of confiscation – that is, the deprivation of property by a competent authority, such as a court – has the potential to significantly reduce the fragmentation of incentives, but in many cases the Parties to the Convention lack the necessary expertise and legal infrastructure to establish such systems.

Introduction

Foreign bribery is subject to severe penalties in a handful of jurisdictions – and these penalties are enforced in even fewer. However, in other jurisdictions, foreign bribery can still be a good “investment” because of low sanctions and/or weak enforcement. The varying types and levels of sanctions across jurisdictions, combined with varying detection and punishment probabilities, create financial and economic fragmentation by making foreign bribery a viable option in some jurisdictions and an unattractive one in others.

This chapter explores the widely divergent incentive systems that companies face when it comes to foreign bribery. It focuses on sanctions, which are a crucial aspect of any legal regime. As legal incentives have important effects on economic activity, the extraordinary variability in sanctions for foreign bribery are an important source of fragmentation in the global economy. This is because diverging sanctions regimes around the world create an uneven playing field for companies in different jurisdictions and widen the scope for cross-border legal engineering designed to lower companies’ exposure to sanctions for foreign bribery. The next section briefly describes the existing comparative data for the 41 Parties to the OECD Anti-Bribery Convention, which shows wide variability in sanctions policies.

This chapter then presents two simulation scenarios designed to facilitate comparison across sanctions regimes, including the regimes' rules for imposing corporate fines and confiscating the bribe and/or the proceeds from bribery from convicted companies. The two scenarios convert the cash flows from a bribery scheme and the maximum available sanctions for bribery in each jurisdiction into comparable values across jurisdictions by calculating the net present value of the investment in the bribe scheme. This net present value of bribery may be positive or negative. These simulations – which are based on the cash flows associated with an actual foreign bribery scheme uncovered by real world enforcement actions – document the extent to which foreign bribery remains a highly profitable activity in some jurisdictions but is potentially heavily sanctioned in others. In other words, it quantifies fragmentation in incentives and disincentives for foreign bribery. Because the chapter only considers two types of sanctions – fines and confiscation – it does not capture the full set of incentives facing companies.¹ Nevertheless, it provides a vivid illustration of the why enforcement and adequate fines and confiscation matter.

Dissuasive sanctions regimes and foreign bribery as an investment opportunity

One of the most basic objectives of law enforcement is to ensure that crime does not pay. For foreign bribery, this means that paying bribes to foreign public officials is (or should be), on average, a money-losing proposition. The Anti-Bribery Convention states that penalties for foreign bribery should be, among other things, “dissuasive” (see Box 7.1).

Box 7.1. The OECD Anti-Bribery Convention and sanctions for foreign bribery

The Preamble to the OECD Anti-Bribery Convention states *inter alia* that the purpose of the Convention is to prevent foreign bribery from distorting “international competitive conditions”. It recognises that “achieving equivalence among the measures to be taken by the Parties is an essential object and purpose of the Convention”.

Article 3 of the Convention requires each Party to ensure that legal persons (essentially, companies) are subjected to penalties – which may be criminal or non-criminal – that are “effective, proportionate and dissuasive”. Under Article 3(3), each Party must ensure that they can confiscate “the bribe” plus “the proceeds of the bribery of a foreign public official” (or property whose value is equivalent to such proceeds), unless the Party would apply “monetary sanctions of comparable effect”.

Significantly, however, the Convention does not require complete uniformity. In numerous places, the Convention expressly limits the Parties' obligations concerning foreign bribery to measures that are “in accordance” with their national legal principles.¹ Indeed, the *Commentaries*, which were adopted along with the Anti-Bribery Convention, clarify that the Convention merely “seeks to assure a functional equivalence among the measures taken by the Parties”.² Article 3 is no exception, as Article 3(1) provides that the “range of penalties” for foreign bribery “shall be comparable to that applicable to the bribery of the Party's own public officials”.

Fifteen years after the Convention went into force, 40 of the 41 Parties to the Convention can now impose sanctions on legal persons (for example, companies) for foreign bribery. While the WGB has not concluded that all of these regimes for legal persons satisfy the obligations under Articles 2 and 3 of the Convention, it has collected data on the Parties' types and levels of sanctions through the first three phases of monitoring.³

1. See, e.g. OECD Anti-Bribery Convention, art. 2 (“Each Party shall take such measures ..., in accordance with its legal principles, to establish the liability of legal persons...”); see *id.* at art. 4(2) (“Each Party which has jurisdiction to prosecute its nationals for offences committed abroad shall take such measures ... to establish its jurisdiction [over foreign bribery] according to the same principles”).
2. *Commentaries on the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions* (21 Nov. 1997) (hereinafter the *Commentaries*), comment 2.
3. As of December 2015, the WGB has finished the third phase of monitoring for all but two of the Parties to the Convention. The fourth phase of monitoring began in 2016.

At a minimum, the concept of “dissuasive” means that companies’ expected gains from bribes, after accounting for legal sanctions, should be negative. Foreign bribery is not supposed to be an attractive investment.

Seen from the perspective of a company engaged in international business transactions, the expected gains or losses from foreign bribery (or other economic crimes) will depend on, first, the probability that a crime will be detected and successfully prosecuted and, second, the sanctions imposed as a result of a successful prosecution. Higher probabilities of being sanctioned for a crime and higher sanctions both produce lower expected net present values for crime. Thus, making sure that “crime doesn’t pay” implies that effective law enforcement and sanctions regimes should, at a minimum, create conditions which make the expected net present value of the crime negative for most bribe scenarios. The simulation scenarios presented in this chapter show that this is not always the case.

Comparative data on sanctions for foreign bribery

OECD data published in the monitoring reports of the OECD Working Group on Bribery in International Business Transactions (WGB) show that sanctions on companies for foreign bribery take a variety of forms: fines; confiscation; and debarment, which is the exclusion (often temporary) from public procurement processes or obtaining public advantages.

Fines are monetary penalties. Depending on the jurisdiction, they can result from judicial or administrative proceedings or from settlement agreements with prosecutors. The WGB monitoring reports show that:

- Many countries establish maximum fines, which place an upper limit on the size of the fine that a company can be forced to pay. These limits are established in various ways:
 - ❖ Some countries impose simple maximum thresholds for monetary fines. These vary greatly in size from about USD 580 000 in the country with the lowest threshold to over USD 10 million in the highest threshold.²
 - ❖ Other countries have more complex rules for maximum fines. For example, fines may be set at multiples of bribe amounts (e.g. one country sets the maximum at 100 times the bribe amount for very large bribes). Other rules (of which there are many) include: setting the maximum as a multiple of the benefit (or “proceeds”) received; as a function of the gravity of the bribery offence or as a combination of the considerations just listed.
- Eight countries do not set “maximum” thresholds for fines.

Confiscation is “the permanent deprivation of property by order of a court or other competent authority”.³ In practice, confiscation regimes are highly fragmented across the 41 Parties to the Anti-Bribery Convention. In addition, the WGB has found that confiscation regimes are rarely or only occasionally used in most jurisdictions. In contrast, a few jurisdictions have active confiscation regimes.⁴ Other features of these regimes include:

- The rules for confiscation vary in important ways. Some allow confiscation only of assets directly involved in illegal acts, whereas others allow confiscation of indirectly related assets or of equivalent values.
- Experience with confiscation in the context of bribery cases involving companies is uneven. Some countries lack legislation and jurisprudence. In most jurisdictions, little is known about how courts would handle confiscation in complex foreign bribery cases.

This is especially true because such cases often involve assets held in several jurisdictions and multi-tiered company groups.

- The different ways that countries determine how much and what should be confiscated further reinforces the theme of fragmented jurisdictions. The Anti-Bribery Convention obliges Parties to provide that the bribe and the “proceeds” of a bribe or “property the value of which corresponds to that of such proceeds, are subject to seizure and confiscation or that monetary sanctions of comparable effect are applicable.” However, countries have different rules for determining what constitutes the “proceeds” of the bribe.⁵
- In addition, some countries appear to be hampered by lack of expertise or legislation. In effect, they do not have an operative mechanism for confiscation. Such situations leave “many corporate wrongdoers unpunished, walking away with their ill-gotten proceeds”.⁶
- In some countries, monetary sanctions (fines) are mutually exclusive with confiscation.

The simulations discussed below will focus only on the monetary fines and confiscation.

The net present value of foreign bribery: description of simulation scenarios

The simulation results presented in this chapter show that the large variation in sanctions regimes across the Parties to the Convention translates into analogous variations in the profitability of foreign bribery for companies operating in different jurisdictions. The overall picture painted by these simulations is one of widely diverging incentive systems for foreign bribery and myriad opportunities for escaping sanctions by judicious corporate structuring across jurisdictions.

To explore the dissuasiveness of the sanctions that Parties to the Convention can impose on legal persons for foreign bribery, this chapter applies the sanctions available in each Party to the facts arising out of an actual foreign bribery case. The bribery scenario draws on the facts of a bribery scheme involving a major multinational enterprise operating in the electrical power field. This scheme involved USD 1.9 million in improper payments (including cash and in-kind gifts) made over the period 1997-2004 in order to obtain tainted contracts with two electrical power companies in the host country. The contracts yielded a profit for the bribing company of some USD 13 million. For the criminal part of this case the company pleaded guilty to violating anti-bribery laws and was ordered to pay a USD 17.1 million criminal fine in September 2010. Thus, from the initiation of bribe payments to the settlement of the criminal enforcement action, this bribery episode covered the 1997 to 2010 period.

The simulations produce estimates of the net present value (NPV) of the “investment” in foreign bribery: i.e. the value – positive or negative – of the decision to bribe. While the amount and timing of the cash flows relating to both the bribe payments and the benefits received are held constant for each simulation of NPV, the sanctions vary by jurisdiction. Specifically, the simulated sanctions for the different jurisdictions are calculated under the assumption that the country will impose the maximum fine available given the nature of the offence. Thus the simulations are only calculated for the 33 countries that have maximum sanctions.⁷ (Eight of the 41 Parties can impose sanctions on companies but do not set maximum sanctions). The simulations assume that the simulated sanction is paid on the date that it was actually paid in the bribe scheme under consideration (e.g. at the end of September 2010).

- *Perfect certainty.* This scenario presents a hypothetical company with certain knowledge of the cash flows associated with a bribery scheme – that is, with the actual sequence of

bribe payments, the actual sequence of benefits and the simulated amount of sanctions to be paid at the date the case is resolved (e.g. September 2010 in the case used for the simulations). The scenario then asks whether or not the company would be willing to “purchase” this series of cash flows for a positive price. If the answer to this valuation question is “yes, the company would pay a positive price for this series of cash flows”, then the sanctions regime is not dissuasive enough – it creates positive economic incentives for foreign bribery. Subsequent sections will show that in many jurisdictions the answer to this question is indeed “yes”, while in others the NPV of the investment is highly negative.

- *Uncertainty.* The second scenario incorporates the idea of imperfect enforcement – that is, not all acts of foreign bribery are detected and sanctioned. For a given sequence of cash flows (here, the bribes and benefits of the bribery scheme), lower detection and punishment probabilities result in higher expected NPVs for foreign bribery. These simulations assume that each year, the company faces a fixed probability, α , of getting caught and having to pay the sanction and $(1-\alpha)$ of not getting caught. A programme is used to calculate the expected NPV of this investment in foreign bribery for a range of α values. The simulations show that high probabilities of being caught and punished (that is, high α) can, in effect, make up for low sanctions because they lower the net present value of investment in foreign bribery. Since it is widely assumed that α is, in fact, very low in most jurisdictions, a reasonable law enforcement strategy might be to set high fines in order to compensate for consistently low probabilities of getting caught.

Further details on the simulation methodology can be found in Annex 7.A1.

The NPV of the bribery scheme under perfect certainty

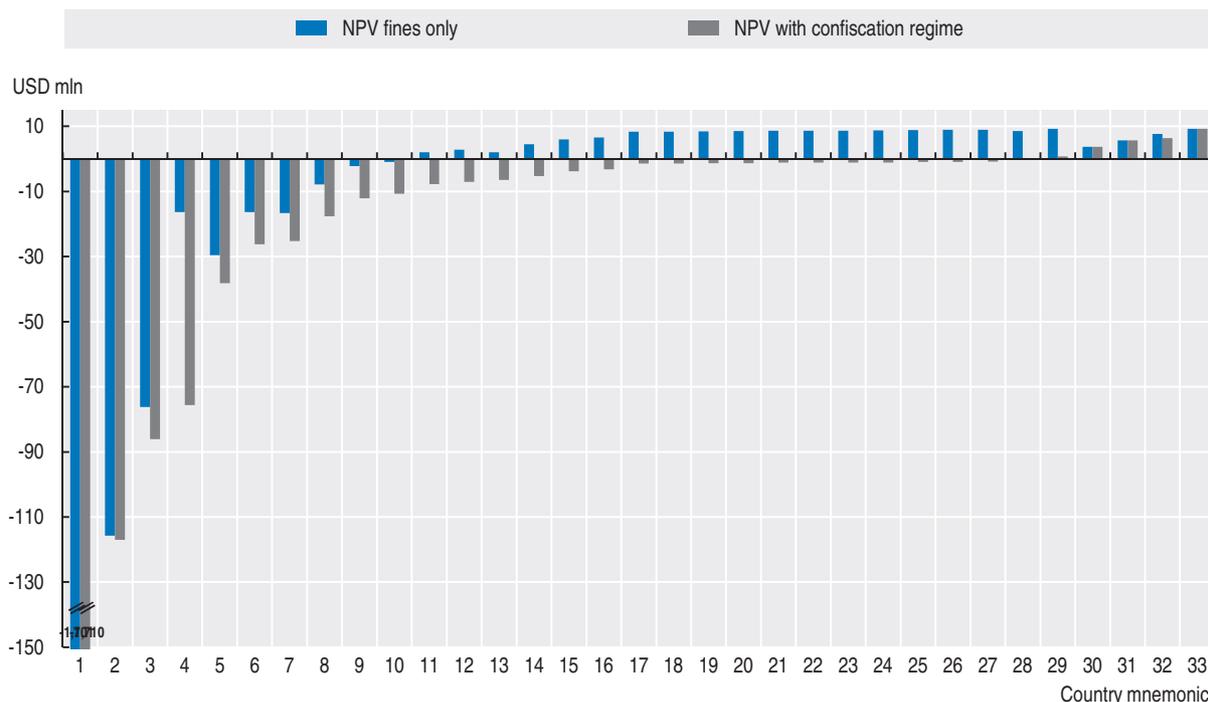
The perfect certainty scenario described above can be used to benchmark sanctions regimes using the chronology of benefits and bribes associated with the actual electrical power bribe scheme. As a benchmark, it is possible to calculate the NPV of the scheme,⁸ evaluated in 1997, when the scheme was initiated; that is, using the actual bribe amounts, benefits and the USD 17.1 million criminal sanction. Using these “cash flows” (including the actual monetary sanction paid at the end of the scheme) and the risk free discount rate prevailing during the bribe period (3.6%) yields a NPV for the actual bribe scheme of USD -1.6 million – thus negative and therefore somewhat punitive.⁹ The simulated NPV of the bribe scheme under other sanctions regimes is shown in Figure 7.1.

The simulation results underscore the fragmented nature of jurisdictions’ regimes for sanctioning foreign bribery. This fragmentation in turn creates large variations in the economic incentives (or disincentives) for engaging in foreign bribery – the range between highest and lowest NPV among the 33 countries is USD 1.7 billion if only fines are considered and about the same range if confiscation is also allowed.

Further key points about the simulation results are:

- *Scenario involving only the maximum fine.* Under this scenario, 23 countries’ maximum fines would produce positive NPVs for this bribery scheme. The median NPV for all 33 countries under this scenario is positive, at almost USD 6 million. Furthermore, in one jurisdiction, which cannot sanction companies for foreign bribery, the NPV of the bribe scheme would be USD 9.6 million. This contrasts with the very large negative NPVs that are produced by other countries’ fines. The largest negative NPV would have been

Figure 7.1. **Net Present Value (NPV) of the foreign bribery scheme under different sanctions regimes**



Note: One of the simulated NPVs is such a large negative that it exceeds the largest negative value on the vertical axis. Countries that have corporate fines for foreign bribery but that do not establish maximum thresholds are not included in the simulation.

Source: OECD calculations using sanctions data taken from OECD Working Group on Bribery monitoring reports (OECD, n.d.).

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negative USD 1.7 billion if the maximum allowable fine were to be imposed (which is off the vertical axis in Figure 7.1). It should be noted, however, that the three countries with the most punitive fines (on paper) have never successfully prosecuted a company for foreign bribery.

- *Scenario involving a fine and/or confiscation.* Adding the possibility of confiscation along with the fine pushes many more jurisdictions into the negative NPV range. The median simulated value for the NPV with fines and confiscation falls to a negative USD 1.5 million. Whereas 23 countries had positive NPVs for the bribery scheme when only fines are involved, only six countries still have positive NPVs for the bribery scheme under the confiscation scenario. However, it should be reiterated that recourse to confiscation is rare and likely to pose major procedural hurdles in many jurisdictions.

The NPV of the bribery scheme when detection and punishment is uncertain

The second simulation explores how a company might evaluate a bribe opportunity when faced with uncertainty over whether the bribery scheme will be detected, successfully prosecuted and sanctioned. That is, unlike under simulation one, where the timing and level of the cash flows associated with the bribe (bribe payments plus benefits accrued) and the fines were assumed to be known with certainty in advance, simulation two examines the financial logic underpinning the decision to bribe when there is a non-zero probability of getting caught and punished.

In other words, this second simulation scenario combines monetary sanctions and non-zero probabilities of punishment. Both sanctions and enforcement influence the financial logic of bribery. The two variables – sanctions levels and probabilities of getting caught and sanctioned – constitute separate but related variables in any deterrence strategy. Governments can influence probabilities of detection and punishment by, for example, investing in enforcement capacity or by improving the effectiveness of prosecution and court procedures. This simulation seeks to assess whether or not these two variables combine to create a dissuasive environment for foreign bribery in various jurisdictions.

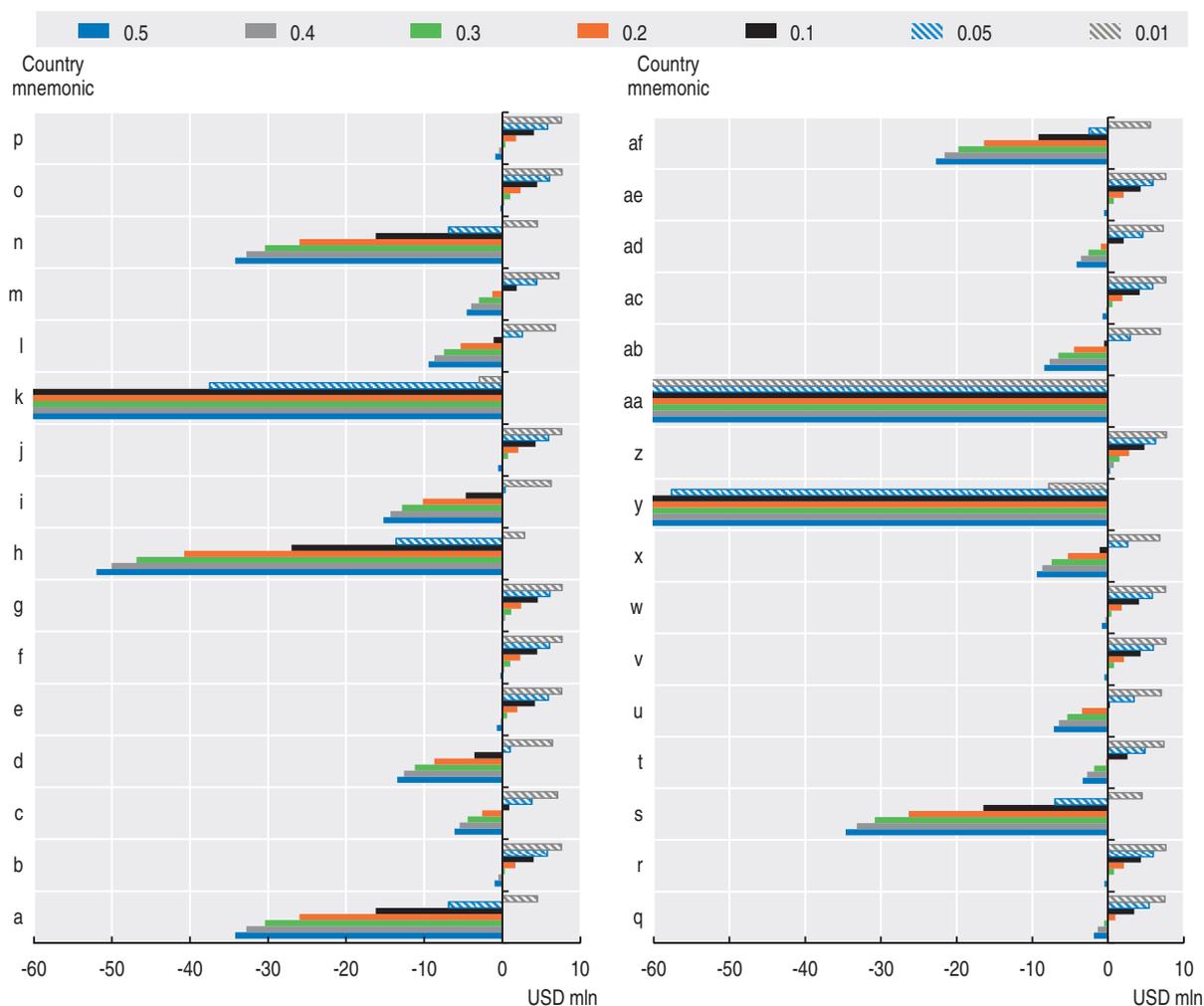
This assessment involves the calculation of the expected NPV of the bribery scheme using the cash flows of the electrical power bribery scheme (bribes and benefits) and a simulated sanction, again under the assumption that the maximum sanction available in each of the Parties to the Convention is applied. As in the first simulation discussed above, the bribe amounts are the actual bribe amounts paid in order to obtain the tainted electrical power contracts and the benefits are what the company earned from contracts.

What differs in this second simulation is the introduction of a single parameter to account for uncertain detection and punishment. The detection/punishment probabilities are assumed to be constant every year until the statute of limitations runs out. Thus, the company is assumed to face the same risk every year of getting caught. In this scenario, the statute of limitations is assumed to be the same for each country (that is, six years since the time of the last illegal act).¹⁰ The discount rate used in this uncertainty simulation is higher than under the perfect certainty scenario in order to account for the uncertainty of detection. Specifically, the rate used is 6.5%, which was the bribing company's actual return on total assets over the period.

The results from this simulation are again presented in two scenarios: fines only (Figure 7.2) and figures plus confiscation (Figure 7.3). The figures show the expected NPV from the electrical utilities bribe scheme under the maximum sanctions assumptions and under alternative simulated probabilities of punishment.

The simulations under uncertain detection/punishment largely reinforce those of the perfect certainty scenario. That is, as in the first simulation, the finding of “fragmented” jurisdictions is very much in evidence, with some countries showing highly negative expected NPVs for bribery and others positive NPVs for investments in foreign bribery even at fairly high detection/punishment probabilities. More specific findings are described below.

- *Some countries have high de jure maximum sanctions for foreign bribery.* A few countries have very negative NPVs in Figure 7.2 (for fines only), even at low detection probabilities (in other words, their de jure maxima are so high that the associated expected NPV is negative even if the probability of getting caught is very low). Their high, de jure maximum fines produce high negative values for investments in bribery, even at the lowest detection probability (e.g. at 1% per year) and even when only fines are taken into account. When the possibility of confiscation is taken into account (Figure 7.3), then four countries have regimes which impose losses on companies even at very low detection probabilities (the lowest probability in the simulation being a 1% probability per year of getting caught and prosecuted). In other words, under these countries' sanctions rules, bribery is a bad investment (assuming the rules are enforced), even when the probability of getting caught is extremely low.
- *Many countries show positive NPVs for investments in bribery, even when detection probabilities are high.* At a 50% annual detection rate, no country has a positive NPV for this bribery scheme. On the other hand, at a 40% detection rate, five countries show positive NPVs.

Figure 7.2. **Expected Net Present Value (NPV) of bribe scheme with fines only**

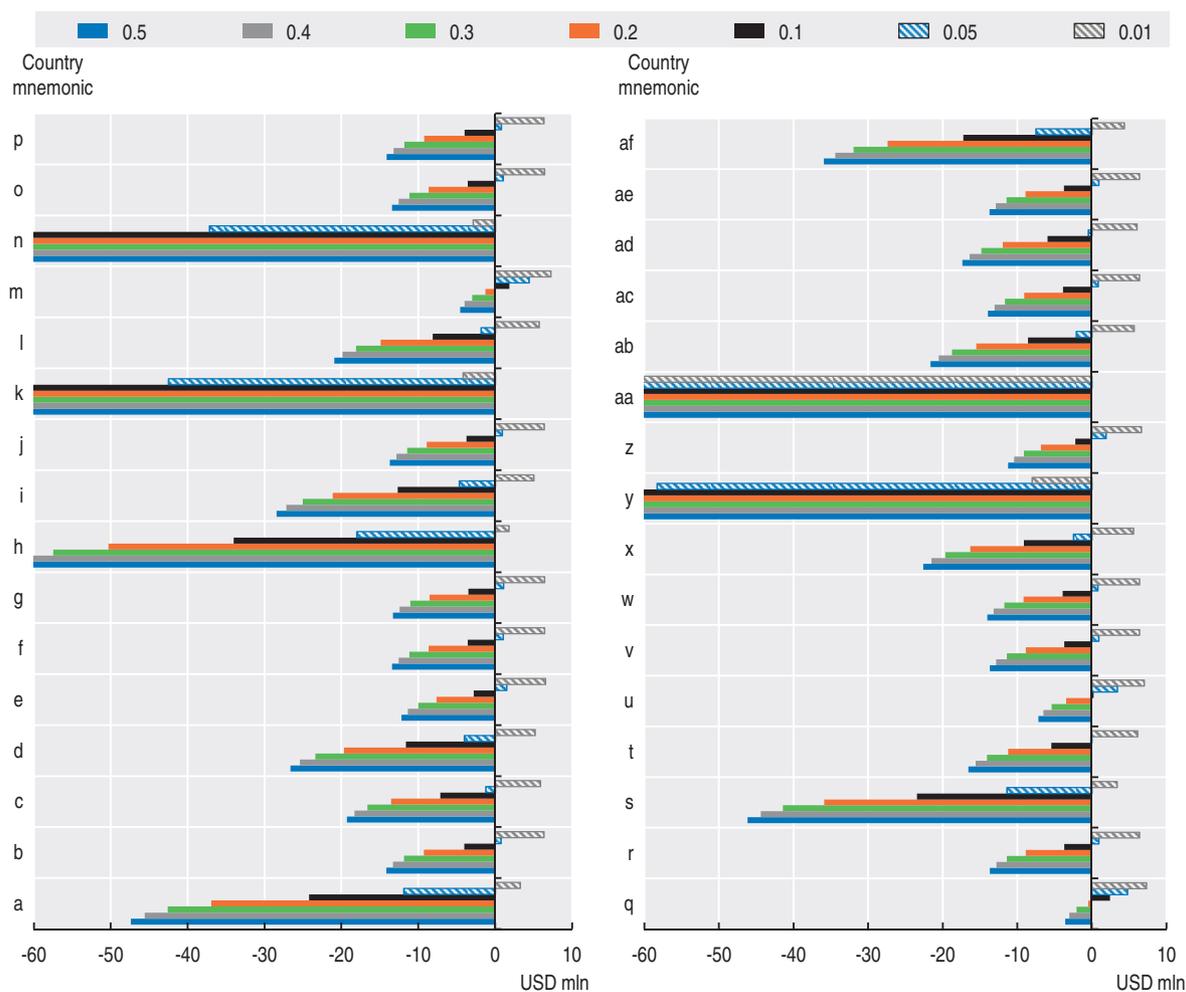
Note: Bars correspond to 7 different detection/successful prosecution probabilities, from 1% to 50% per year.

Source: OECD calculations using sanctions data taken from OECD Working Group on Bribery monitoring reports (OECD, n.d.).

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The median NPV for the 33 countries turns negative (that is, the deterrence regime becomes somewhat dissuasive) at somewhere between 20% and 10% detection rates. Thus, in the absence of credible confiscation threats, many legal environments do not appear to be strongly dissuasive of foreign bribery, even with detection rates that may be quite a bit higher than those prevailing in the real world.

- *The availability of confiscation – if this tool is in fact used – weakens the finding of fragmentation.* As can be seen in Figure 7.3, the availability of confiscation weakens the finding of fragmentation in sanctions regimes for foreign bribery. Thus, putting in place credible confiscation policies would go a long way towards eliminating positive incentives for foreign bribery. This finding mirrors that of the perfect certainty simulations and, as already noted, most countries (including many of those whose rules for fines are shown to be not dissuasive) do not have operative confiscation systems. Thus, while, in theory, confiscation could help to harmonise sanctions regimes across the Parties to the Convention, in practice it does not yet play this role.

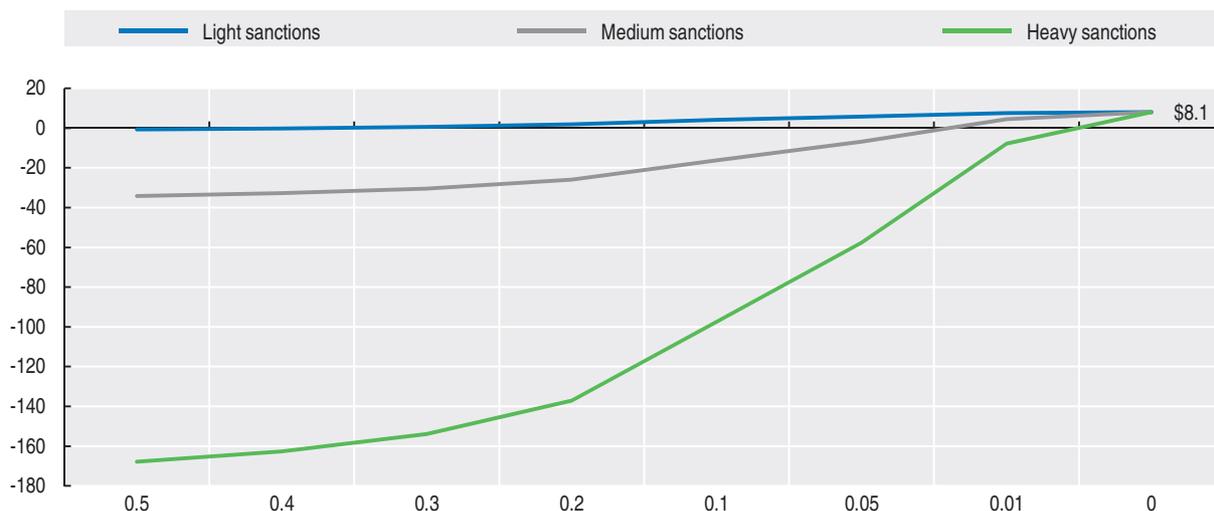
Figure 7.3. **Expected Net Present Value (NPV) of bribe scheme with fines and confiscation**

Note: Bars correspond to seven different detection/successful prosecution probabilities, from 1% to 50% per year.

Source: OECD calculations using sanctions data taken from OECD Working Group on Bribery monitoring reports (OECD, n.d.).

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- *Sanctions and detection probabilities need to combine to create effective deterrence.* The uncertainty simulations clearly show that countries wishing to increase deterrence can act on two policy instruments – detection/punishment (which can be raised inter alia by investing in enforcement capacity) and on the level of sanctions. The two act as complements in determining the dissuasiveness of the enforcement system. This can be seen in Figure 7.4, which maps detection probabilities against the expected NPV of the scheme for three countries selected to illustrate different policy mixes. Figure 7.4 shows that the first country’s very high nominal fines produce a positive expected NPV for the bribe scheme only at very low probabilities of punishment (between 0 and 1% per year). At the other extreme is the permissive country (which represents the many countries that have low nominal fines). Under this permissive regime, the expected NPV is positive even at quite high detection probabilities – it enters the negative expected NPV zone at an annual probability of punishment of about 36-37%. Between these two extremes is the “middle sanctions” country, where the expected NPV for the bribe scenario becomes negative at an annual detection rate in the 2-3% range.

Figure 7.4. **Expected Net Present Value (NPV) of bribe as a function of detection probabilities**

Note: Vertical axis is expected net present value in USD millions; horizontal axis is annual detection probability and is not to scale.

Source: OECD calculations using sanctions data taken from OECD Working Group on Bribery monitoring reports (OECD, n.d.).

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Conclusions

At the present time, the playing field established by foreign bribery laws is highly uneven for companies operating out of different jurisdictions. Rules on sanctions create environments of heavy sanctions in some jurisdictions, while other sanctions regimes are quite permissive of foreign bribery.

These findings are subject to a number of caveats. This analysis, like all simulations, presents a simplified version of reality. Several particular simplifications should be noted. First, the analysis assumes that companies' bribery is only potentially detected and prosecuted by the authorities of that company's country. In reality, companies' malfeasance may end up being prosecuted by the authorities of another country. Indeed, this is the situation in many non-United States foreign bribery cases. Also, the model does not capture the value of intangibles, such as reputational damage, and for other forms of punishment, such as incarceration.

The evolution of foreign bribery law in the 41 Parties to the Convention is marked by processes of both convergence and divergence.

Convergence. Prior to the signing of the Anti-Bribery Convention in 1997, foreign bribery was legal in nearly all Parties to the Convention and was tax deductible in most. In addition, many of the 41 countries could not sanction companies (as opposed to individuals) for foreign bribery. In less than two decades, the vast majority of Parties have built sanctions regimes for foreign bribery by companies where none existed before. Thus, under the Convention, there has been considerable harmonisation and convergence of law and practice in three crucial areas of law: making foreign bribery a criminal offence; making companies (not just individuals) liable for foreign bribery and eliminating the tax deductibility of bribes.

Divergence. But, as shown by these simulations, major differences persist in the sanctions regimes of the 41 Parties. Without further reforms to raise sanctions for companies or increase punishment probabilities, foreign bribery will remain an attractive investment

opportunity in many jurisdictions. An additional element of divergence is introduced by large differences in enforcement efforts among the 41 Parties as well as the uneven application of confiscation provisions. According to OECD enforcement data,¹¹ 24 of the 41 Parties to the Convention have never successfully sanctioned an individual or a company for foreign bribery since the Convention entered into force in 1999. Thus, most of these sanctions regimes exist more on paper than in practice. For example, three of the countries with the heaviest *de jure* sanctions under these simulations have never successfully concluded a foreign bribery enforcement action – thus, while their regimes look dissuasive on paper, they are not used in practice. In contrast, a few countries are active enforcers of foreign bribery law, including several countries that have stepped up enforcement activity in recent years.

Sanctions and detection probabilities jointly influence incentives to bribe. For foreign bribery – where detection probabilities are thought to be low – it is important to maintain sanctions at high enough levels to compensate for low detection probabilities. In this way, the two policy variables combine to create an environment of effective deterrence. Since it is probably easier in the short run to raise sanctions levels than to increase detection rates, countries that wish to enhance anti-bribery deterrence may wish to raise sanctions levels as a rapid way of enhancing disincentives for foreign bribery.

Sanctions need to account for lengthy investigation and resolution of cases. Another point highlighted by the NPV simulations is that, investigations and resolution (via court proceedings or negotiated settlements or both) can take a long time. The electrical power bribery scheme used in the simulations took place over a period of 14 years, starting from the first bribe payments in 1997 to the final settlement in September 2010. At a discount rate of 6.5%, one dollar of fine paid in 2010 had a present value of 41 cents at the beginning of 1997. Thus, when investigations and resolutions take many years, sanctions will be heavily discounted by companies simply because of the time value of money. Sanctions regimes need to account for this if they are to succeed in lowering incentives to bribe.

Sanctions need to be set at higher levels in many countries. Some countries' sanctions rules appear to be permissive of foreign bribery by companies – they encourage foreign bribery by helping to make it a profitable activity. Policy makers should be aware of the economic implications of sanctioning practices. Many will no doubt be surprised at how high sanctions must be if they are to be genuinely dissuasive for foreign bribery. This is especially true in situations where the probability of getting caught and sanctioned is low, where investigations and resolutions take a long time and where the business advantages obtained are important.

Higher sanctions are not always better sanctions. Appropriate sanctions regimes have a floor, the level of which is determined by not systematically letting bribery be an attractive investment opportunity. This floor can be established through a judicious combination of sanctions, detection probabilities and reliability in resolution/prosecution. However, this does not imply that higher sanctions are always better.

In a real world of deterrence, a portfolio of tools is needed to address the myriad considerations raised by sanctioning companies. For example, very high levels of sanctions could create the possibility of “liquidating sanctions” – that is, a company might be forced into bankruptcy by monetary sanctions. Although such an outcome may be acceptable (indeed, some Parties provide for dissolution of companies as a sanction), societies may wish to retain the possibility of applying sanctions that are both dissuasive and that avoid bankruptcies.

In addition, there is the difference between incentives facing companies and incentives facing their employees and business partners. It may well be the case that the various individuals within the company (e.g. officers, employees) may not see monetary sanctions paid by the company as a whole as a deterrent for their own individual decisions to bribe. Their individual incentive systems might be quite detached from the incentive systems created by law enforcement for the company as a whole. Much depends on whether and how the company's governance framework translates company interests into incentives for individual units and employees.

This highlights the importance of designing sanctions regimes with a portfolio of tools – including monetary fines for companies, but also sanctions for individuals such as possible jail terms – in order to obtain an effective overall framework of deterrence. It also suggests that countries may wish to integrate incentives for implementing effective compliance programmes into company sanctions regimes. The issue of what policy mixes create effective sanctions for foreign bribery is one of ongoing experimentation among the 41 Parties to the Convention. Possibilities include civil and criminal actions against individuals, restitution of victims, imposing interest payments on monetary sanctions in order to account for the time value of money and disqualification from government programmes such as public procurement and export credits. The WGB provides a platform in which Parties can learn from each other's experiences and improve their policies in these areas.

Notes

1. The purpose of this chapter is to explore, using standard financial analysis techniques, how fines and confiscation policies influence financial incentives and disincentives for foreign bribery. For this reason, other behavioural influences affecting the decision to bribe are not accounted for. This analysis does not include other types of sanctions than fines and confiscation (e.g. bars to companies' eligibility to participate in public procurement processes or from export credit programmes). It also abstracts from other sanctions such as reputation effects, prison sentences, executive liability and disqualifications to engage in certain types of businesses.
2. Foreign currency amounts are converted into USD using exchange rates prevailing in early November 2015.
3. *Commentaries on the Convention on Combating Bribery* (adopted by the Negotiating Conference on 21 November 1997), comment 22.
4. OECD (2012).
5. See Chapter 2.A.1 of OECD (2012).
6. See Page 12 of OECD (2012). This monograph states: "Some countries still lack legislation to address the confiscation of the proceeds of bribery, considering such calculations too complicated. Other countries may have legislation in place but have never tested it in practice."
7. One of the Parties to the Convention cannot hold companies responsible in any way for the crime of foreign bribery. The simulations therefore assume that this country's maximum fine is zero.
8. Since the would-be briber under this scenario knows with certainty the future cash flows associated with the bribe, a risk free discount rate is used. This is calculated as the average over the bribe period (1997-2010) of annual interest rate on 6-month T-bills as published by the US Federal Reserve Board. For the company involved in the electrical power bribe scheme, this discount rate is 3.55%.
9. This amount does not include books and records violations imposed for this bribe scheme and others undertaken by the same multinational enterprises under a separate proceeding.
10. The assumption that the statute of limitations is the same for all countries influences the results. In particular, it means that countries that have a relatively short statute of limitations would have a "real" expected NPV for the bribery scheme that is more than the simulated value (because, in reality under such a statute of limitations, the company is at risk of getting caught for a shorter period of

time). Analogously, countries that have a relatively long statute of limitations would have a “real” expected NPV for the bribe scheme that is less than the simulated value because the company would be at risk of detection/prosecution for a longer period of time. The reason that the simulations make this limiting assumption is that, in practice, rules of statutes of limitations are exceedingly complex. For example, the events that “start the clock ticking” are defined differently in different countries (e.g. last illegal act, the start of an investigation). Moreover, in some countries, the “count” can be restarted once the procedures reach particular milestones.

11. OECD (2014).

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ANNEX 7.A1

Methodology for simulation scenarios

Using information taken from the WGB's Phase 1-Phase 3 reports, this chapter examines the type and level monetary sanctions (fines) and other property-based sanctions (confiscation) adopted by the 41 Parties to the Anti-Bribery Convention on Combating Bribery. The simulation methodology uses readily available information in order to establish internationally comparable metrics that support the contention that fines are too low in many of the 41 Parties and to shed light on the meaning of the term “dissuasive” in the reference in Article 3 of the Anti-Bribery Convention to “effective, dissuasive and proportionate” sanctions

Key characteristics of the simulation scenarios are:

- *Scenario 1. Perfect certainty:* Assume that the company deciding whether to engage in foreign bribery knows in advance and with certainty all of the cash flows associated with the bribe. The question explored in the first simulation is whether the Parties' sanction regimes for companies make it economically rational to engage in bribery if one knows in advance what the cash flows from the bribery scheme will be. That is, will the present value of the total benefits from the bribe minus the present value of the bribe amounts paid (both of which are known with certainty under this scenario) exceed the present value of the sanctions imposed (also known with certainty)?
 - ❖ For timing of benefits from the bribe and costs of the bribe (that is, the amount of bribe paid) assume that “best case” for company: receive profits (as of Day 1) and sanctions (day of settlement – here 29 September 2010).
 - ❖ For type and level of sanctions: the simulations incorporate the “worst case” scenario for the company. That is, they assume that each country imposes the highest possible amount of fines and confiscation available.
 - ❖ The discount rate is the average yearly return on 6-month T-bills published by the Federal Reserve Bank for the period over which the bribe scheme occurred.
- *Scenario 2. Uncertain detection and punishment:* This scenario incorporates the possibility that the firm will not get caught and punished for its act of bribery. The scenario uses the same cash flow assumptions as for the perfect certainty scenario (on the cost and chronology of the bribe and of the cash flows associated as well as the “simulated” maximum sanctions for each jurisdiction). It also assumes that each year, the company faces a fixed probability, α , of getting caught and having to pay the sanction (the same simulated maximum sanction as in scenario 1) and $(1-\alpha)$ of not getting caught. A programme is used to calculate the value of this real option for a range of α values. The

discount rate used is the average total return on assets for the company for the period over which the bribery scheme occurred. The model will show that high deterrence (that is, α is high) can, as a means of ensuring that crime does not pay, make up for low sanctions because high probabilities of getting caught lower the net present value of the investment in foreign bribery.

The model further assumes:

- *Statute of limitations.* The statute of limitation creates time limits for enforcement procedures. Once this time limit has expired, the court lacks jurisdiction to try or punish a defendant. For the perfect certainty scenario, this statute of limitations is assumed to not come into play before the final year of the net present value calculation (that is, when the sanction/confiscation amount is paid). For the uncertainty scenarios, the statute of limitation determines when the simulation scenario ends (that is, the company no longer has legal risks because the statute of limitations has expired).
- *Discount rates.* The discount rate used to calculate present values under the two simulation scenarios are: 1) the 6 month T-bill annual yield for the risk-free scenario and the company's actual return on total assets over the bribe period for the non-zero enforcement risk scenario (3.55%); 2) the return on total assets for the company over the bribe scheme period (6.5% for the 1997-2010 period.)
- *No procedural hurdles or uncertainties regarding assets to be confiscated.* All property subject to confiscation will in fact be found and confiscated.



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