

GSK Bribery Case – End of the Matter?

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GlaxoSmithKline (GSK) has been fined £300 million and five of its employees given suspended prison sentences in China for bribery – but is this the end of the matter? What impact will the verdicts have on other multinational companies conducting business in China?

Proceedings Against GSK and its Employees in China

On September 19 the Changsha Intermediate People's Court in Hunan province found that GSK had "offered money or property to non-government personnel in order to obtain improper commercial gains"¹ by paying hundreds of millions of pounds worth of bribes, via travel agencies, to doctors, health officials and hospitals in order to use GSK's products².

At the start of the investigation last year, Gao Feng, the head of China's fraud unit, reportedly said: "We found that bribery is a core part of the activities of the company. To boost their share prices and sales, the company performed illegal actions³." It was alleged that pay/bonus packages focused too heavily on sales performance, which reportedly encouraged people to engage in bribery, and that knowledge of the bribery that was occurring was widespread across the organization (with departments beyond the sales teams having some level of involvement)⁴.

GSK employee Mark Reilly (who we understand returned to China to assist Chinese authorities with their investigation) was given a three-year suspended sentence and a deportation order⁵. Four Chinese GSK defendants - Liang Hong (Head of Operations), Zhao Hongyan (Legal Counsel), Zhang Guowei (Head of Human Resources) and Huang Hong (Head of Business Development) - were also given suspended sentences. All five individuals had entered guilty pleas.

Following the verdict, GSK's Chief Executive, Sir Andrew Witty, reportedly said that: "Reaching a conclusion in the investigation of our Chinese business is important, but this has been a deeply disappointing matter for GSK. We have and will continue to learn from this. GSK has been in China for close to a hundred years and we

remain fully committed to the country and its people. GSK fully accepts the facts and evidence of the investigation, and the verdict of the Chinese judicial authorities. Furthermore, GSK sincerely apologizes to the Chinese patients, doctors and hospitals and to the Chinese government and the Chinese people. GSK deeply regrets the damage caused⁶."

GSK has stated that it has taken steps to improve its processes and working arrangements in China. These include changes to the pay/bonus package for sales staff so that they do not encourage bribery, changing the ways in which staff engages with healthcare professionals, and implementing improved systems for monitoring and reviewing invoices and payments⁷. Despite this, GSK's management has asserted that it had "all the necessary checks and balances in place to prevent such activities" and in doing so suggested that the blame lies with rogue local executives for breaching them⁸.

Action to Follow in the UK and/or US?

The proceedings in China may not be the end of the matter. Both the UK's Serious Fraud Office (SFO) and the US Department of Justice (DOJ) have powers to bring enforcement proceedings in relation to bribery abroad. Both the SFO and DOJ are in the middle of ongoing investigations into bribery allegations involving GSK and its associated persons not only in China but also elsewhere in the world.

In May 2014, the UK SFO announced that it was investigating GSK's sales practices⁹. The SFO is likely to be focusing on whether GSK breached section 7 of the UK Bribery Act (which came into force in July 2011) by not having 'adequate procedures' in place to prevent bribery, an offence for which no prosecutions have yet been brought by the SFO against any company.

The US DOJ is also investigating GSK for bribing foreign officials, which is prohibited under the US Foreign Corrupt Practices Act. The potential for further enforcement action in the US and UK must be of concern for GSK, particularly as the company is arguably one of the first large multinational organizations to be investigated under the UK Bribery Act, and because penalties in the UK and US have historically been much higher than those imposed in China. Given the findings and evidence produced in China, it is possible that the UK and US authorities could initiate successful proceedings against GSK.

1 <http://news.sky.com/story/1338514/glaxosmithkline-fined-297m-for-china-bribes>
2 <http://www.dailymail.co.uk/wires/pa/article-2762141/Glaxo-fined-297m-Chinese-court.html>
3 <http://www.theguardian.com/business/2014/sep/19/glaxosmithkline-china-mark-reilly-deported-uk-guilty-bribery-hunan>
4 <http://www.telegraph.co.uk/finance/newsbysector/pharmaceuticalsandchemicals/11108376/China-fines-Glaxo-297m-for-bribery-Mark-Reilly-sentenced.html>
5 <http://www.dailymail.co.uk/wires/pa/article-2762141/Glaxo-fined-297m-Chinese-court.html>

6 <http://www.dailymail.co.uk/wires/pa/article-2762141/Glaxo-fined-297m-Chinese-court.html>
7 <http://www.dailymail.co.uk/wires/pa/article-2762141/Glaxo-fined-297m-Chinese-court.html>
8 <http://www.thisismoney.co.uk/money/comment/article-2762714/BEN-GRIFFITHS-Witty-hangs-GlaxoSmithKlines-woe-mounts.html>
9 <http://www.sfo.gov.uk/press-room/latest-press-releases/press-releases-2014/glaxosmithkline-plc-investigation.aspx>

Implications for Other Multinational Corporations Doing Business in China

The GSK case shows how seriously the Chinese authorities are cracking down on bribery, pursuing not just those who accept bribes but also those who offer them. Most multinational companies (MNCs) have had compliance programs in China for many years. Often such a program is substantially identical to those developed for other jurisdictions for compliance with the US Foreign Corrupt Practices Act or the UK Bribery Act. Too often what is missing is any particular tailoring to the laws and practices of China. Compliance programs rolled out in China need to be carefully adapted for this market and designed for effective implementation.

Compliance programs in China tend to be accepted more readily when they can be seen to have the full support of the local leadership team. Too often there are mixed signals, creating the impression that the compliance program was developed in the UK or US and forced on the local affiliate, whose managers and management are compensated based on sales and profit. Instead, local executives must show evidence of their commitment to a culture of compliance.

Two steps that GSK suggests an MNC may want to take are including a compliance assessment as part of each manager's performance review, and making certain that compensation arrangements do not emphasize sales volumes without due consideration for compliance. Many MNCs in China today would benefit from ensuring that compliance is part of the local compensation calculus.

If the MNC remains non-compliant notwithstanding such steps, the company needs to explore why the compliance program is ineffective and promptly take the actions necessary to remedy the situation. GSK itself does not appear to have suffered from any lack of compliance personnel, but from a failure of such personnel to effectively enforce the compliance programs they had in their computers.

Many of the companies we work with in China have graduated approval programs for entertainment expenses, such that the higher the expense or the greater the risk of apparent impropriety due to the particular person being entertained, the higher the level of internal approval required before the expense can be incurred. The GSK

case should prompt companies to consider whether such approval standards are set at high enough levels to ensure the involvement of disinterested judgment.

Not all the actions suggested by GSK are internally-focused. The GSK case may be most remembered for the dangers it reveals from reliance on intermediaries that are not subject to the same ethical or compliance standards as the MNC. Any use of intermediaries in China should be subject to a process of careful vetting and thoughtful authorization, with appropriate contractual restraints imposed on the actions of such intermediaries, and with a system for monitoring and auditing their conduct.

Lastly, local management should be trained to take the right steps in the event the authorities in China come knocking.

Compliance officers at multinational corporations have long talked about the risks posed by corrupt practices in China. The GSK case confirms in the clearest terms how serious such risks may be. GSK should not become a watchword for corrupt behavior. Rather, through its fines and the damage to reputation it has suffered, GSK may now serve as a warning to other MNCs, and, if it can be effective in implementing its new programs, a demonstration of how to respond to the challenges of doing business in China today.

Contacts

Daniel F. Roules

Partner, Shanghai

T +86 21 6103 6309

E daniel.roules@sqirepb.com

Louise Roberts

Associate, Manchester

T +44 131 830 5038

E louise.roberts@sqirepb.com

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