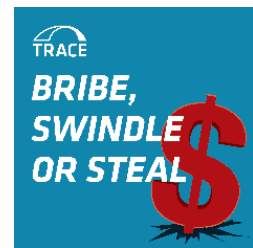


BRIBE, SWINDLE OR STEAL



Spotlight on Brazil – Rafael Gomes

[00:00:06] Welcome back to the TRACE podcast, Bribe, Swindle or Steal. I'm Alexandra Wrage, and today, we're talking about Brazil with my guest, Rafael Gomes. Rafael has been the chief governance and compliance officer at Petrobras for about six months. He has extensive experience in senior roles in the legal department of Sun Microsystems and then later as general counsel, legal VP and chief ethics and compliance officer for Wal-Mart Brazil. Between in-house positions, he's also worked at law firms where he focused on a broad range of issues for his clients. Rafael, thank you for joining me.

[00:00:39] Thank you for the opportunity.

[00:00:41] It's really a pleasure to talk to an expert in Brazil because there is so much going on there right now. A few years ago, with its hosting of the World Cup and the Summer Olympics still on the horizon, Brazil seemed to be positioning itself to get really tough on corruption. But since then, we've seen Lava Jato, Petrobras, Odebrecht scandals and the impeachment and imprisonment of some political officials at the highest levels in Brazil. Should we see everything that's happened in these last couple of years as a positive sign, or does the volume of cases there mean that the problem is somehow intractable?

[00:01:20] First of all, I think those were interesting times because we were expecting two of the major world sporting events to happen in Brazil. It was supposed to be a fun time, exciting times. All those were expected to fuel development, economic development, investments and so on. The problem is that, in 2013, one year before the World Cup, things turned really bad. The crisis was clearly on the horizon - the economic crisis. And then the incumbent president's popularity and approval rates were going down. People are unhappy with many things, and there were many protests, ugly protests on the streets and so on and leading to uncertainty even as to how was the safety going to be around the World Cup. Really, really, let's say, contrasting with what you expect to see happen in the country before such big events, especially the World Cup where every Brazilian loves soccer and all of that. The interesting thing is that in 2013, the Brazilian Anti-bribery Act or Clean Company Act is enacted in August 2013, and it has a six-month period before entering into force in January 2014. I think the next day, also, there was a change. There a new law that changes rules about the plea bargaining and cooperation with authorities for individuals, and then those rules are within a law that deals with organized crime and racketeering. That is actually what has fueled the success of the carwash operations. Then we turn to 2014, and in March, the first time we hear the carwash operation surfaces as a serious operation that is going on by the federal police, and later that year, we lose the worker and all of that. That's not directly related here. Then we have the director of Petrobras, Paulo Roberto Costa, that goes on record, cooperates with the authorities

and gives a lot of information that hits the company directly, and then comes the perfect storm. The bread and the oil prices were down, were really low. Then we had a political crisis where very tight presidential elections and a lot of demonstrations that the people were not happy at all with the scenario. Then we had the devaluation of the Brazilian real, and Carwash hits Petrobras, so for Petrobras, this was the perfect storm. From then on, we have a series of events that have to do with the subpoena from the SEC and the creation of a special independent investigation committee to investigate and retaining a U.S. law firm, a Brazilian law firm and a big-four to start one of the probably one of the biggest internal investigations around FCPA-related matters. In one case, it's interesting because if you think Petrobras is a government instrumentality on the one hand, and then the people who were bribed were actually Petrobras' employees and executives, certain Petrobras employees and executives, so it's an investigation where you're even curious as to, "How is it that this is going to end up?" Because we're not talking about a company that was going out paying bribes to win government business. It's kind of the other way around, and then investigation goes on. Because it's a very different case, the root cause analysis brought- and I think that's an interesting, different view from what you would see somewhere else. Petrobras was a highly hierarchical company. It was, in its origins - it had a quazi-military structure and functioning in the old days. Much of that was, too, in terms of culture. It was very hierarchical, so if you were told to do something, you would just do what you're told. The second is, there was a stove-piped company. It was very decentralized, and each and every executive director or officer responsible for one of these areas, he was pretty much the president of that division. That caused things to happen within certain divisions of the company where there was not a strong central function that was controlling and that was managing, that was overseeing and that could challenge decisions and audit and everything else that we know that should happen in a corporation and a company as big as Petrobras. Another part of it were the reverse incentives. Given that Petrobras is a public company - not a public company in the way we consider a publicly listed company, but rather it's a state-owned enterprise or at least a state-controlled enterprise - and as a result, the employees are considered public officials, so all employees of Petrobras, but I am a public official as of today. The structure that was built, the career plan and the compensation plans, they created certain reverse incentives that were not necessarily based on merit and created the possibility of, first, people getting higher positions and staying in higher positions in view of their loyalty not to the company, necessarily, but to the person who put them in that position, so to their bosses. That's also something that created an environment that was not favorable to transparency, not favorable to keeping to the policies and procedures and following and abiding by the internal policies, procedures and the law. I sometimes called those, rather than only reversed, I sometimes talk about perverse incentives that we were able to identify. The promotions and also the advancements in salary were also not, let's say, necessary built in a way that would favor more independence and that those who are top performers would necessarily be the ones being recognized, promoted and advancing in their careers. One of the major things that were also a part of the problem that was identified and was in Petrobras' 20-F in 2015 relating to 2014 is a material witness in controls that is the

management override. Even though there were written rules and procedures that, in principle, would cause transactions to have to follow a certain procedure and be approved by certain internal departments or be subject to specific controls, there was a lot of transactions. There were a lot of transactions that were simply, "Okay. Even though we have not followed everything, the higher-up is telling us to make this payment. Just go ahead, make the payment. Even though the controls would tell you otherwise, and you have not followed the rules of the procedures." This environment also, taking into account that you're talking of a company that was controlled by the government but that was supposed to be acting somewhat independently and autonomously from the government, that was that was not the case. The way people were chosen to be in key positions and the way that the key positions were distributed were clearly used in a way to return favors or to give favors. That's a big part of the problem, there was a lot of political interference with the company's management and with the company's business. Even the business agenda was pretty closed and controlled directly by the government. Lots of conflict of interests in all this mess and what we would say is the cherry on the cake, but it's pretty much more like throwing a watermelon on the cake because it's not only the icing on the cake. It's really what really made it hurtful to the company, is that the company's - the biggest vendors and contractors - they organized in the form of a cartel to then move against the company and just destroy, let's say, put the company on a corner and ripping the company off with overcharged contracts, unnecessary amendments to contracts and continued extensions of contracts that wouldn't make sense and so on. I think that was the final shot of mercy, if you would say.

[00:11:40] That's a great insider overview, Rafael, but backing up a little bit to broader picture in Brazil: Lula's in jail, Dilma was removed from office, Temer is weighed down by his own set of corruption allegations. A series of corruption revelations can make people really cynical, or it can spur them on to significant action. How would you describe the current mood in Brazil in this respect? Are people optimistic?

[00:12:14] I'll give you my personal take because I am optimistic. I see all of this as an evidence. The fact that we have the former head of our House of Representatives in jail, we have many politicians that were in high, strategic and important positions in government in jail - some of them have taken pleas, and as a result of those changes that I alluded to earlier, those changes to the law that brought the possibility and enhanced the possibility of the law enforcement in Brazil, using plea agreements and giving credit to corporations to individuals. This has fueled the investigations, and we have a scenario where the former president is in jail, and he's in jail because there was significant independence, in my view, from the federal prosecutors and the federal police being able to move against politicians from different parties. It's not only from this or that party. You cannot say this was targeted on party A, B or C. You have a whole array of politicians that are subject to significant enforcement action and criminal prosecution. In my view, that's a very good sign that Brazil is actually being able to attack and fight corruption and put people in jail and have people being removed from office and so on. But then, of course that the amount of people, the number of deals and scandals and investigations and

ramifications, is somewhat scary to the point where they say, "Wow. Is there a way out? Is there light at the end of the tunnel?" I think that there is light at the end of the tunnel because at least our current political presidential and campaign for many other state governors and for the House of Representatives, senators, etc. - many of the politicians that were tainted in all of this, many of them were not able, even in their home states, to get reelected. We look at that, as people who work with compliance and fighting corruption and anti-bribery, we look at some of the names that were not elected, and we see that as a good sign. People are actually holding them responsible for everything that they saw in the midst of these investigations and the prosecutions and so on. In general, I think that the Brazilian people have first, learned a lot more about how our politics were working and how things were being done, and they don't like it, the ballots were showing that people are not happy with any of this.

[00:15:31] It's interesting. You have a very far-right presidential candidate in Bolsonaro, who is doing very well and may well be that we learn globally - not just in Brazil - that authoritarian leaders are a response to the electorate's concerns about widespread corruption. I'm curious: You have worked, of course, in senior in-house positions and also at a law firm. If you were speaking to a group that was entering the Brazilian market for the first time right now, given some political volatility, this recent series of cases - what advice do you have for them?

[00:16:13] As with other new market you're entering, you need to try to understand as best as you can what's the status of that country in terms of its politics. At this very moment, first of all, I'd say, wait for the second runoff and see who is going to be the president because I think that we have to, as you mentioned - the country is divided, and there is a lot of polarization. Two very opposite candidates: I think that one may be trying to use all this resentment of the Brazilians with the status quo and how politics was done that was a result of Car Wash and everything else, and on the other hand, you have somebody saying, "Yeah, but we don't want a far-right party in office either." Right now, Brazil is facing really challenging times in terms of, it's not to say that the people see either/or as the solution for corruption. Maybe one is try and say, "I am the answer," but we look at it and say, "I am not sure what the right answer is." The problem is because their government programs, their views of the economy, their views of the place that the government has in the economy and in some other key areas of society are very different. The first thing I would see, at least you try to understand who's going to win. That would be a first step. A second step would be to understand the changes that we've seen in the past four or five years in the business environment, very positive changes in the business environment in Brazil. That I am absolutely certain of, and it's not very difficult for one to make that diagnosis. You go to companies today, and you talk about compliance. Five years ago, it was something that companies subject to subsidiaries of U.S.-based companies and maybe if you, for some reason, think or believe you are subject to the FCPA, are one of the companies that would be actually engaged in putting together the compliance programs and trying to understand whether or not what you're doing makes sense, if they are abiding by the major laws or regulations, if they are aligned to all the convergence that's going on around the world in terms of what a compliance program should look like - like all the different guidelines and all

the different best practices that are believed to be important to have to be followed. Today, you see thousands of companies having understood that compliance is positive, that compliance is a must in this new business environment, that this global business environment is requiring that of them. Petrobras is strongly requiring that from its supply chain. I see that if a company is now entering into Brazil, they will find a much more transparent and a much more compliant business environment and a different business culture. There's much more room for you to sit with a company that you're about to partner with or that you were considering to obtain for a strategic part of your business as a key or strategic supplier and have an open conversation about what is it that you do to try to prevent, detect and remediate instances of bribery, fraud and related issues in your company. We are, today, in a totally different, better scenario and environment.

[00:20:34] That all sounds very optimistic, so that's good news. I really appreciate your insight into this. You are a recognized expert on the Brazilian compliance landscape. It's very helpful to have your perspective. Thank you so much for joining me today, Rafael.

[00:20:49] Well, I thank you, and we're here and open. We're talking a lot about this. A lot of benchmarking is going on, and we are really engaging with the oil and gas sector in Brazil. I am very happy that, at this moment, we're able to take advantage of everything bad that happened to use it as a fuel to make sure that we make all progress in Brazil in compliance and anti-bribery.

[00:21:19] Excellent. We'll watch the outcome of some of this benchmarking. Thank you again for joining us.

[00:21:26] Thank you.