

IKEA and the Graft Factor

By Brook Horowitz

A decision of Swedish furniture retailer IKEA to suspend further investment in Russia because of corruption is a sign that business here is still fraught with risks for international investors. While President Dmitry Medvedev has taken a clear position on anti-corruption and introduced legislation to curb official bribery, the reality is that corruption continues on a massive scale in the economy and society. However, IKEA's response to the corruption challenge — to reduce further investment rather than pull out altogether — suggests that the risks can be managed. International companies and governments have an important role to play in helping Russia clean up its act by engaging their Russian counterparts in the fight against corruption.

Amid the financial crisis, governance has been at the center of attention of international regulators. Earlier this year, the G20 meeting showed a new resolve of governments to clamp down on corruption in all its forms. Leaders at the Group of Eight summit in Italy this month renewed their commitment to enforcing the OECD Convention on Combating Bribery of Foreign Officials. In the United States, the Foreign Corrupt Practices Act and its more rigorous application has generated an increasing number of successful cases.

Russia is neither a signatory of the convention nor a member of OECD, but the Foreign Corrupt Practices Act still applies to any company with business in the United States. According to a Deloitte survey, multinational companies are most concerned about the potential for contraventions of the act in Russia — above China, Africa and the

Middle East. In the past, multinationals took a flexible attitude toward doing business in Russia, citing local customs and culture to justify using distributors and agents to make "facilitating payments," or lavishing entertainment or gifts on decision-makers. But this will no longer fly in the new era of tough regulation. For companies that are subject to the long arm of U.S. legislation, these are all red flags. The consequences of getting it wrong are huge fines, extensive reputational damage and, in some cases, personal liability. Never has the gap between the responsibilities of top

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executives of multinational corporations and the practical risks on the ground in Russia been so great.

Many companies have introduced ingenious management systems to raise the alarm in high-risk countries, such as internal audits and spot checks, due diligence of all third-party contractors and detailed monitoring of financial flows. These are all very well, but they are not sufficient in countries such as Russia where corruption is the norm. For example, Russian employees — under pressure from their bosses to achieve sales figures and from their clients to pay to achieve them — find it difficult to judge the limits to which they can go to get business. Asking for advice about the rules is not customary. Neither is

taking personal responsibility for decisions. Whistle-blowing is almost inconceivable in a society that was rent asunder by the denunciations of the Stalinist era. Many of these practical ways of ensuring compliance, employed elsewhere quite successfully, are still met with incredulity and smirks by employees.

In order to turn themselves into "corruption-free zones," companies need to create a culture of value-based behavior rather than rule-based compliance. But ultimately, as IKEA's recent example showed, they should be prepared to walk away from new business if the risks are too high or the compromises too extensive.

One thing that is needed is the political will and participation of governments to dispense with corruption. U.S. President Barack Obama could use his newly minted presidential commission with Medvedev to reinforce the importance of the Russian government and business engaging in the international fight against corruption. He could offer government exchanges and expertise and help speed up negotiations for Russia's accession to the OECD. In exchange Russia could sign the OECD Anti-Bribery Convention and reopen negotiations for accession to the WTO.

With this kind of positive engagement, Russian government and business will join with their international counterparts in the long fight against corruption and at the same time begin to rebuild their own international credibility.

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