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2011 EDITION

ASPATORE

First Printing, 2011
10 9 8 7 6 5 4 3 2 1

Foreign Corrupt Practices Act Compliance: Issues for Public and Private Companies

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What is the Foreign Corrupt Practices Act?

The Foreign Corrupt Practices Act (FCPA) is a US federal law enacted in 1977 to combat bribery of foreign government officials. The FCPA is divided into two parts: anti-bribery provisions and accounting provisions. Under the anti-bribery provisions, it is unlawful to make a corrupt payment to a foreign official for the purpose of obtaining or retaining business or securing an improper advantage. The Department of Justice (DOJ) is generally responsible for criminal and civil enforcement of the anti-bribery provisions.

The FCPA's accounting provisions require that "issuers" (generally, companies that trade stock on a US exchange or are required to file periodic reports with the SEC) make and keep books and records that accurately and fairly reflect the corporation's transactions and that they maintain an adequate system of internal accounting controls. The accounting provisions are generally enforced by the Securities and Exchange Commission (SEC).

Recent Trends in FCPA Enforcement

In recent years, several significant trends in enforcement of the FCPA have emerged. First, there has been a substantial increase in enforcement activity. Both the SEC and the DOJ have dedicated more internal resources to FCPA enforcement, which, in 2010 alone, has resulted in the two agencies levying over $1.8 billion in fines and penalties. *See*, "FCPA Fines Imposed on Corporations," Appendix 1.1. This heightened enforcement environment means that both public and private companies need to be ever mindful of the FCPA and how it affects their businesses.

The second significant trend is the government's increased focus on the conduct of individuals. This increased focus stems from the government's belief that criminal penalties—principally prison time—are the best deterrent to violations of the FCPA. The government's new focus on individuals is perhaps best exemplified by the first-ever large-scale FCPA sting operation executed in January of 2010, in which the Federal Bureau of Investigations (FBI) arrested twenty-two executives in the military and law enforcement products industry. The arrests resulted from an undercover operation wherein FBI agents posed as representatives of an African

country and allegedly solicited promises of bribes in exchange for the award of lucrative government contracts. *See*, *e.g.*, *U.S. v. Miskin*, Criminal Indictment No. CR-09-344 (D.D.C. Dec. 11, 2009), ¶¶ 4-5, 9-10.

This past year also saw the longest prison sentence ever handed down in an FCPA case. Charles Jumet was sentenced to serve an eighty-seven-month prison term after pleading guilty to conspiracy to violate the FCPA. U.S. Department of Justice, *Virginia Resident Sentenced to 87 Months in Prison For Bribing Foreign Government Officials*, Press Release (April 19, 2010) *available at:* http://www.justice.gov/usao/vae/Pressreleases/04AprilPDFArchive/10/20100419jumetnr.html. Jumet was the president of a company that paid over $200,000 in bribes to Panamanian officials to secure a twenty-year, no-bid contract to maintain lighthouses and buoys along Panama's waterways. His colleague was sentenced to thirty-seven months in prison for his involvement in the scheme. U.S. Department of Justice, *Virginia Resident Sentenced to 37 Months in Prison for Bribing Foreign Government Officials*, Press Release (June 25, 2010) *available at*: http://www.justice.gov/opa/pr/2010/June/10-crm-750.html.

The third major trend in FCPA enforcement is increased international cooperation and coordination. In the last few years, many countries have begun to focus on combating corruption. This has resulted in an increased willingness on the part of law enforcement agencies in other countries to work with authorities in the United States. One clear example of such coordination was in connection with the FBI sting operation mentioned above. In that case, the City of London police executed simultaneous search warrants in connection with their own investigation into the same military and law enforcement products companies targeted by the FBI sting.

The last important trend in the FCPA arena is increased civil litigation following government enforcement activity. It has become fairly common for civil suits—typically shareholder derivative suits—to be brought against a company shortly after news of an FCPA investigation becomes public. FCPA investigations also appear to have triggered class actions brought against companies and directors alleging inaccurate disclosures in violation of Sections 10(b) and 20(a) of the Exchange Act or breach of fiduciary duties under Section 502 of the Employee Retirement Income Security Act (ERISA), the latter brought on behalf of participants and beneficiaries of qualified ERISA plans.

New Developments at the DOJ and SEC

In September 2010, Mark Mendelsohn stepped down as Deputy Chief of the DOJ's Fraud Section, which houses the FCPA unit. During his term as Deputy, Mendelsohn presided over the greatest expansion of FCPA enforcement in the history of the statute. His successor, Charles Duross, is a DOJ insider who has been in the Fraud Section since 2006. While it remains to be seen exactly what influence Duross will have on the FCPA unit, there are no indications that he is likely to slow the ever-increasing pace of enforcement. It is also worth noting that the DOJ has continued to add new prosecutors to its FCPA unit, including prosecutors with expertise gathering foreign evidence and the ability to try substantial criminal cases to verdict.

At the beginning of 2010, the SEC created a specialized FCPA unit led by SEC-veteran Cheryl J. Scarboro. In the spring, the agency continued to expand its FCPA capabilities by opening a San Francisco unit solely dedicated to FCPA enforcement. The decision to open the unit in San Francisco was reportedly driven by the presence of a large number of high-tech firms in the area that regularly do business in Asia. With China's rapid ascension as a world economic powerhouse, and its reputation as a country with a high risk of corruption, the opening of the SEC's San Francisco office likely signals that companies doing business in China will be subject to increased scrutiny by the SEC.

The SEC has also recently made certain enhancements to its investigative capabilities. Most notably, the SEC delegated subpoena power to SEC officers, which enables the agency to obtain subpoenas more easily. The SEC has also developed new methods of obtaining cooperation from witnesses based on the methods already utilized with great success by the DOJ—e.g., witness letters.

Legislative Developments

The UK Bribery Act (UKBA), which was passed in the United Kingdom in April of 2010, is likely to lead to major changes in terms of the way companies approach anti-corruption compliance. The UKBA is both broader and stricter than the FCPA, and there are some significant differences between the two statutes.

Like the FCPA, the UKBA prohibits bribery of foreign officials. Unlike the FCPA, however, the UKBA also prohibits commercial bribery. Therefore, under the UKBA, a purely private transaction is prohibited if it involves a bribe. The other important distinction is that a company will be held strictly liable if it fails to prevent bribery unless it has "adequate procedures" in place to prevent the bribery. Bribery Act 2010, 2010, c. 23, § 7(2). Final implementation of the UKBA is expected this year, however, it has been delayed until the government issues final guidance as to what will constitute "adequate procedures." The British press has reported that, in all likelihood, the UKBA will not take effect until the second quarter of 2011. Nicolas Cecil, *Ken Clarke Delays Bribery Act After Protests from Business Chiefs*, London Evening Standard Online (Jan. 31, 2011), *available at* www.thisislondon.co.uk.

Another important distinction from the FCPA is the extraterritorial reach of the UKBA. The FCPA has a fairly broad extraterritorial reach—the US government has asserted that it has jurisdiction over non-US companies and non-US citizens under the FCPA on the basis of e-mails or regular mail related to the bribery being sent to recipients in the United States. The UKBA, however, goes one step further. Under the letter of the UKBA, there is no requirement that the bribery be connected to the United Kingdom. All that is required is that the *entity* involved have a close connection to the United Kingdom, or for some provisions, that the entity carry on part of a business in the United Kingdom. However, recent reports based on documents purportedly leaked by the UK Justice Ministry have indicated that the UK may curtail the broad jurisdictional reach of the UKBA prior to implementation. Simon Bowers, *Justice Minister Tries to Ease Anti-Bribery Rules*, Guardian (March 15, 2011), *available at* www.guardian.co.uk.

Among other significant differences with respect to the FCPA, the UKBA does not have an exception for so-called facilitating, speed, or grease payments—payments to speed up routine governmental functions that do not involve the discretion of a foreign official. For example, under the FCPA it would likely be permissible to pay a nominal sum of money to expedite the issuance of a visa or the connection of utility services—e.g., water and power. There is no such exception under the UKBA.

The UKBA will likely be the single most important legislative development in anti-corruption compliance in the coming years. Its broad extraterritorial reach—if these provisions remain untouched in the final version of the law—will mean that any company with operations in the United Kingdom, or that employs UK nationals, needs to be aware of the risks under this new law.

In the United States, the most significant legislative development in 2010 was the passage of the Dodd-Frank Act, which contains whistleblower provisions authorizing the government to pay rewards for "original" information related to violations of the securities laws. Under the Dodd-Frank Act, whistleblowers can receive between 10 and 30 percent of any monetary recovery over $1 million for violations of the securities laws, including the FCPA's accounting provisions, collected as a result of the information they provide. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 (H.R. 417) § 922. The Act also provides new protections for whistleblowers employed by subsidiaries of public companies and creates a private cause of action for damages in cases of retaliation. The SEC is expected to issue implementing regulations for the whistleblower provisions in the spring of 2011. The large penalties levied in FCPA cases will undoubtedly incentivize would-be whistleblowers to act upon information they encounter that could indicate an FCPA violation, and thus increasing the likelihood we will see even more high-profile FCPA investigations.

Key FCPA Cases in 2010

The year 2010 was a banner year for FCPA enforcement; eight of the top ten FCPA settlements of all time took place in 2010. *See*, "Top Ten FCPA Settlements to Date," Appendix 1.2. The fourth largest FCPA settlement to date, and one of the most significant FCPA cases of 2010, involved Snamprogetti Netherlands B.V. (Snamprogetti) and its parent company ENI S.p.A. Together, the two companies agreed to pay $365 million to resolve FCPA charges stemming from Snamprogetti's role in a joint venture (JV) in Nigeria. U.S. Department of Justice, *Snamprogetti Netherlands B.V. Resolves Foreign Corrupt Practices Act Investigation and Agrees to Pay $240 Million Criminal Penalty*, Press Release (July 7, 2010) *available at:* http://www.justice.gov/opa/pr/2010/July/10-crm-780.html. The JV

won four contracts worth more than $6 billion to build a liquefied natural gas plant in Nigeria from 1995 to 2004, all of which were awarded by a state-controlled company. Snamprogetti allegedly authorized the JV to hire two agents to pay bribes to Nigerian officials to help win the contracts. KBR and Technip—two other members of the JV—had previously resolved their FCPA-related charges independently. With Snamprogetti's settlement, the DOJ and the SEC announced that a total of $1.28 billion in penalties has been assessed in connection with the JV. *Id.* This case exemplifies the risks of partnering with JVs and other third-party agents operating in countries where corruption is common, and the need for companies to conduct due diligence on third parties with whom they conduct business, including potential JV partners.

Another key FCPA case from 2010 is the Daimler AG settlement. Daimler AG and a number of its subsidiaries resolved FCPA-related charges in April 2010. In total, Daimler AG and its subsidiaries paid approximately $185 million in disgorgements and fines to settle charges brought by the SEC and the DOJ. The companies were alleged to have made improper payments in the form of "commissions," delegation travel, and other gifts to Chinese government officials or their designees, in connection with substantial sales of commercial vehicles to Chinese government customers. U.S. Department of Justice, *Daimler AG and Three Subsidiaries Resolve Foreign Corrupt Practices Act Investigation and Agree to Pay $93.6 Million in Criminal Penalties*, Press Release (April 1, 2010) *available at:* http://www.justice.gov/opa/pr/2010/April/10-crm-360.html.

Daimler AG is significant because it illustrates the risks, from a corruption standpoint, of doing business in China. China's rapid economic growth presents tremendous opportunities for businesses, but it also presents a number of challenges. As a threshold matter, China has a well-established reputation for corruption. In 2010, China received a score of 3.5 on Transparency International's Corruption Perceptions Index (CPI). The CPI measures the degree to which public sector corruption is perceived to exist in 178 countries around the world. The CPI scores each country on a scale from 0 to 10, 0 being highly corrupt and 10 being highly clean. With a score of 3.5, China is not the lowest ranking country in the world—Somalia, Myanmar, and Afghanistan have scores between 1.1 and 1.5—but it is on the lower end of the corruption scale, indicating a high level of perceived corruption.

There are also certain structural and cultural challenges for companies doing business in China. Because many, if not most, Chinese companies are state-owned or state-controlled, even commercial transactions that are seemingly purely private affairs involve "foreign officials" under the FCPA and are thus fraught with risk. In addition, there is a culture of gift-giving in Chinese business transactions, which can lead to serious compliance challenges. While there is an exception under the FCPA for reasonable and bona fide business expenditures related to the promotion of products or services or to the execution of a contract, expenditures that are not directly related to such promotion or execution will not be viewed favorably. The Daimler AG case highlights how the structural and cultural challenges inherent in doing business in a country like China can result in significant FCPA liability for the unprepared.

Developing an FCPA Compliance Program

When developing an FCPA compliance program, it is important for a company to institute a zero tolerance policy for bribery and corruption—one that sets an appropriate tone at the top of the company, so that the company's employees are aware that it does not tolerate bribery in any form. With respect to FCPA compliance, it is difficult to overstate the government's focus on "leading by example." When the executives of a company demonstrate their commitment to and support for a compliance program, the idea is that such an example encourages rank and file employees to do the same. Conversely, "check the box" programs that exist solely on paper and are tucked away in a file cabinet are seldom effective.

Where and how to expend resources on FCPA compliance are decisions that naturally vary from one company to the next. However, most successful compliance programs share several characteristics:

Training

A company should provide mandatory anti-bribery and anti-corruption training to its employees on at least an annual basis. Training sessions should ideally be interactive and tailored (to the extent possible) to the employees' needs, and should be live for employees in high-risk areas, particularly those who have systemic contact with foreign officials. The key

is to help employees understand exactly what types of situations are likely to present FCPA issues, what the law is, and how to comply with it.

Employees should also certify that they have completed FCPA training.

Due Diligence

Just as a company may be held liable for the acts of its employees, it may also run afoul of the FCPA through the acts of third party business partners and service providers. As such, a company needs to be aware of who its business partners are—everyone from commissioned sales representatives to logistics providers, consultants, and lobbyists—and know that they are reputable. The best way to obtain this information is through rigorous due diligence, a key component of any successful FCPA compliance program.

Potential "red flags" include:

- Unusual payment patterns or financial arrangements
- History of corruption in the country where the third party operates
- Refusal by the third party to certify that he or she will not take any actions that would cause the company to violate the FCPA
- Unusually high commissions or compensation based solely on commission
- Lack of transparency in expenses and accounting records
- Apparent lack of qualifications or resources to perform the services offered
- Other ties, including personal and familial connections, between the third party and the government customer

Internal Controls

If a company trades stock or is required to file periodic reports with the SEC (an issuer), it is subject to the FCPA's accounting provisions. The statute generally requires issuers to maintain books, records, and accounts, which, in reasonable detail, accurately and fairly reflect all transactions and dispositions of the issuer's assets. Issuers may not, for example, omit improper transactions—i.e., bribes—from their books. Similarly, the FCPA

prohibits an issuer from disguising records to conceal their improper aspects or failing to identify the improper nature of an otherwise properly recorded transaction (i.e., describing an improper payment as a "consulting fee" or "special handling charge"). An issuer is therefore well advised to institute internal controls sufficient to ensure that it accurately documents its expenses for items such as petty cash disbursements, travel, and entertainment.

Auditing

A company should test its compliance program with periodic audits and best practices reviews. Not only does auditing assist a company in identifying problems within a compliance program, it also reinforces the point that a compliance program is not self-sustaining. Companies that become complacent with regard to FCPA compliance—relying on untested or outdated protocols—may find that they have no effective compliance program at all.

Self-Monitoring and Investigation

The best practice for dealing with FCPA issues when they arise is to get out in front of a problem as soon as possible. To do so, a company must continuously self-monitor for potential FCPA issues. Companies should encourage employees to report any violations internally to a hotline that is established for that purpose. Such a procedure allows a company to address potential problems sooner rather than later and investigate issues that come up as quickly as possible—an extremely worthwhile practice, particularly if the company finds itself interfacing with DOJ or the SEC on the matter at some point.

Common Misunderstandings about the FCPA

One of the biggest misconceptions about the FCPA is that it only applies to large public companies or companies in certain industries. In fact, the FCPA applies to all domestic concerns: all US nationals and companies that have their principal place of business in the United States and all companies organized under the laws of any US state. 15 U.S.C. §§ 78dd-2(a), (h)(1)

(2004). Therefore, all private and public companies in the United States that have any international connections need to be mindful of this law and its applicability to their business. Foreign nationals and businesses doing business in the United States also need to be mindful of FCPA compliance because they can be liable if they cause any act in furtherance of a bribe to occur within the United States.

Another misconception is that the FCPA only applies to government contractors, when that is not the case. Whether a company contracts with the US government is irrelevant for the purposes of the FCPA. The key issue is whether the company is doing business internationally such that payments it makes could either directly or indirectly reach the hands of a foreign official for an improper purpose.

Informing Clients of Important Changes and Developments in FCPA Compliance

Many law firms have sophisticated FCPA practice areas that offer clients a "soup to nuts" approach to FCPA compliance. Such firms are experts at designing and implementing the compliance programs described above. In addition, one of the functions outside counsel performs is keeping clients informed regarding the dynamic and ever changing FCPA landscape.

Final Thoughts

The current upward trajectory of increased FCPA enforcement is expected to continue. Every company—whether it is large, small, private, or public—needs to understand what the FCPA prohibits and how the law affects the company. If the company has any international connections, it needs to have a compliance program in place appropriate for the level of risk that is posed by the company's business model and its geographic presence.

Key Takeaways

- In the current FCPA enforcement climate, it is advisable for a company to partner with an outside law firm that has expertise in this area, and work with that outside counsel in designing, implementing, and auditing an anti-corruption compliance

program. Simply having a policy that prohibits bribery is not enough in the current environment.

- When problems are identified—i.e., through a report from a business unit, a hotline complaint, or a press report—they must be investigated thoroughly, and as quickly as possible.

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Acknowledgment: *The author wishes to thank Anthony Moshirnia and Karin Johnson for their valuable contributions to this chapter.*

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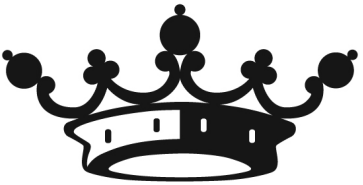

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