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FCPA: Regulators' Expansive "Foreign Official" Definition Under Attack

By Paul T. Friedman and Ruti Smithline

For the last several years, federal regulators have enforced the Foreign Corrupt Practices Act (the "FCPA") with an unprecedented, aggressive approach. And, for the most part—rather than litigate—companies and individuals alike have negotiated resolutions behind closed doors, leaving the regulators' expansive interpretation of the FCPA unchallenged and untested in the courts. That is, until very recently.

A necessary element to prove a violation of the FCPA is that the intended recipient of the corrupt payment be a "foreign official." There is little doubt that a person with an official position and corresponding title (*i.e.* Senator or Minister) fits within the statute. In enforcing the FCPA, however, federal regulators look beyond titles and take a nearly boundless view of who qualifies as a "foreign official." The statute defines the term "foreign official" as:

[A]ny officer or employee of a foreign government or any department, agency or instrumentality thereof . . . or any person acting in an official capacity for or on behalf of any such government or department, agency or instrumentality. . . .¹

Relying on the phrase "department, agency or instrumentality thereof," both the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) treat employees of state-owned or state-controlled entities (SOE) as "officials." The DOJ and SEC do not look at the SOE's function—whether it provides a traditional government service.² Rather, regulators focus on the degree to which the entity is controlled by a foreign government. Moreover, because the DOJ and SEC take the position that the FCPA applies to "any public official regardless of rank or position,"³ any employee of an SOE—from an entry-level clerk to the CEO—will be considered a "foreign official" for purposes of the FCPA.

Although commentators have criticized—with increasing vigor—the DOJ and SEC's expansive interpretation of "foreign official,"⁴ most would-be-defendants generally accepted the regulators' view without challenge. That is why, in 2009, when the individual defendants in the Nexus Technologies case filed a motion to dismiss the criminal complaint against them on the basis that the recipients of the bribes were not foreign officials,⁵ the FCPA-world awaited judicial guidance with bated breath, hoping that the federal regulators would be reined in. But, the court denied defendants' motion to

¹ 15 U.S.C. § 78dd-2(h)(2).

² See *United States v. SSI Int'l Far East Ltd.*, No. 06-cr-398 (D. Or. 2006) (steel mill); *SEC v. York Int'l Corp.*, 07-cv-01750 (D.D.C. 2007) (construction company).

³ See <http://www.usdoj.gov/criminal/fraud/docs/dojdocb.html>.

⁴ Prepared Statement of Professor Mike Koehler Before the Subcommittee on Crime and Drugs of the United States Senate Committee on the Judiciary (Nov. 30, 2010), available at <http://judiciary.senate.gov/pdf/10-11-30.%20Koehler%20Testimony.pdf>.

⁵ *United States v. Nam Quoc Nguyen*, No. 08-cr-522, Defendant's Motion to Dismiss Indictment (E.D. Pa. Oct. 16, 2009) (Docket No. 99).

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dismiss without opinion.⁶ Likewise, in 2010, the court in *U.S. v. Esquenazi* denied a similar motion with a cursory opinion.⁷

The first quarter of 2011 saw an uptick in defendants litigating FCPA cases. In three separate cases, defendants filed motions to dismiss challenging the DOJ's interpretation of "foreign official" under the FCPA.⁸

Of these three cases, only the *Lindsey* case has been litigated through a jury verdict—a big win thus far for the DOJ. The defendants in the *Lindsey* case, including two senior executives and the company itself, were accused of violating the FCPA by giving bribes to two high-ranking employees of the Comisión Federal de Electricidad ("CFE"), an electric utility company wholly-owned by the Mexican government.⁹ Defendants did not dispute that CFE was owned by the Mexican government.¹⁰ Rather, defendants argued that a state-owned corporation—of any kind—was "disqualifie[d] as an entity properly addressed by an FCPA indictment."¹¹ According to defendants, "[i]t [was] plain from the definition of 'foreign official' that Congress did not intend for FCPA liability to be based on payments made to employees of state-owned corporations like CFE."¹²

But the Judge denied defendants' motion "because a state-owned corporation having the attributes of CFE may be an 'instrumentality' of a foreign government within the meaning of the FCPA."¹³ Rejecting the defendants' argument, the court reasoned that an "instrumentality" need not share "all of its characteristics with both a department and an agency" because then "the term 'instrumentality' would be robbed of independent meaning."¹⁴ Rather, the court found that CFE had "various characteristics of government agencies and departments," such as: (1) it exclusively provides a service, the supply of energy, which the Mexican government recognized as an exclusive government function; (2) the key officers and directors are or are appointed by government officials; (3) it is financed largely through governmental appropriations; and (4) it was created by statute as a "decentralized public entity." Recognizing that the "legislative history of the FCPA is inconclusive," the court determined that while Congress may not have intended "to include all state-owned corporations within the ambit of the FCPA, neither does it provide support for Defendants' insistence that Congress intended to exclude all such corporations from the ambit of the FCPA."¹⁵ The *Lindsey* case proceeded to trial, and on May 10, 2011, the jury handed down guilty verdicts on all counts against the defendants—including the first-ever verdict against a company.¹⁶

⁶ See *id.*, Order Denying Motion to Dismiss (E.D. Pa. Dec. 30, 2009) (Docket No. 108).

⁷ See Order Denying Motion to Dismiss, *U.S. v. Esquenazi*, No. 09-cr-21010, at 2 (S.D. Fla. Nov. 19, 2010) (Docket No. 309).

⁸ See *United States v. Noriega*, 2:10-cr-01031 (C.D. Cal.) (the "*Lindsey*" case); *United States v. O'Shea*, 4:09-cr-00629 (S.D. Tex.); and *United States v. Carson*, 8:09-cr-00077 (C.D. Cal.).

⁹ See First Superseding Indictment, *United States v. Noriega*, No. 2:10-cr-01031-AHM (C.D. Cal. Oct. 21, 2010) (Docket No. 48).

¹⁰ See *id.*, Criminal Minutes - General Denying Motion to Dismiss (April 20, 2011) (Docket No. 474).

¹¹ *Id.* at 6 (quoting Defendants' Reply Brief at 2).

¹² *Id.* at 2 (quoting Defendants' Opening Motion at 6).

¹³ *Id.*

¹⁴ *Id.* at 8 (emphasis added).

¹⁵ *Id.* at 14.

¹⁶ See DOJ Press Release, California Company, Its Two Executives and Intermediary Convicted by Federal Jury in Los Angeles on All Counts for Their Involvement in Scheme to Bribe Officials in State-Owned Electrical Utility in Mexico (May 10, 2011), available at: <http://www.justice.gov/opa/pr/2011/May/11-crm-596.html>.

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It is too early to tell how broadly or narrowly other courts will read the *Lindsey* decision, which is quite fact-specific and will almost certainly be part of the anticipated appeal to the Ninth Circuit. Nevertheless, it is likely that at least the pending motion to dismiss in *U.S. v. O'Shea* will be affected by the *Lindsey* decision. John Joseph O'Shea, the former general manager of ABB Network Management, filed a motion to dismiss in March 2011, challenging the DOJ's interpretation that employees of state-owned enterprises are foreign officials under the FCPA.¹⁷ Undoubtedly, the major hurdle for O'Shea is that the foreign officials he is charged with allegedly bribing are employees of CFE—the exact same entity involved in the *Lindsey* case. Oral arguments on O'Shea's motion are scheduled for May 24, 2011.¹⁸

The third pending challenge is in the *Carson* case—a potentially stronger challenge to the DOJ's broad interpretation of foreign official. In that case, the CEO and five executives of Control Components Inc., a California-based valve manufacturing company, were charged with allegedly paying bribes to employees of state-owned customers (SOEs) in China, Korea, Malaysia and the United Arab Emirates.¹⁹ The indictment alleges no government contacts for each of the SOEs other than the fact of state ownership. Defendants moved to dismiss on the basis that, among other grounds, employees of SOEs are not foreign officials under the FCPA.²⁰ Defendants contend that Congress “knew about SOEs when it enacted the FCPA” and “knew how to include SOEs in the definition of ‘foreign official’ if it had wanted to do so. Clearly, Congress did not do so.”²¹ The DOJ, on the other hand, argues that SOEs may be considered instrumentalities of a foreign government in “appropriate circumstances.”²² Defendants challenge the DOJ's position on the grounds that the “lack of any meaningful or discernable standards for deciding” whether an SOE falls within or outside the FCPA renders the FCPA “unconstitutionally vague.”²³ The court heard oral arguments on the motion on May 9, 2011, and the judge took the motion under submission. A decision is pending.

How the decision in the *Lindsey* case, and possibly the *O'Shea* and *Carson* cases as well, on the pivotal “foreign official” issue will affect the scope of FCPA enforcement for individual and corporate defendants remains to be seen. Judicial challenges are likely to escalate, given the regulators' unrelenting approach to FCPA enforcement.

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¹⁷ See Opposed Motion to Dismiss Counts One Through Seventeen of the Indictment, *United States v. O'Shea*, No. 4:09-cr-00629 (S.D. Tex. Mar. 7, 2011) (Docket No. 47).

¹⁸ See *id.*, Order Setting Hearing (May 17, 2011) (Docket No. 71). It is worth pointing out that the same prosecutor who tried the *Lindsey* case will try the *O'Shea* case. See *id.*, Notice of Availability for Trial (May 9, 2011) (Docket No. 70).

¹⁹ See Indictment, *United States v. Carson*, No. 8:09-cr-00077 (C.D. Cal. Apr. 8, 2009) (Docket No. 1).

²⁰ See *id.*, Defendants' Reply Brief (May 2, 2011) (Docket No. 354).

²¹ *Id.* at 1.

²² *Id.*, Opposition to Defendants' Amended Motion to Dismiss, (April 18, 2011) (Docket No. 332).

²³ See *id.*, Defendants' Reply Brief (May 2, 2011) (Docket No. 354).

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