

## **White Collar Criminal Defense, Regulatory Compliance and Special Investigations Update**

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### **Foreign Corrupt Practices Act Update: A Rare Jury Trial, Increased Resources by the Feds and a Novel Theory to Charge Upper-Management All Reaffirm the Need for Vigilance in Policing a Company's International Practices**

#### **The Jury Trial**

Following a six-week jury trial in Manhattan federal court, a Connecticut investor was found guilty of conspiracy to violate the Foreign Corrupt Practices Act ("FCPA"). The case is noteworthy because FCPA cases rarely go to trial and the post-trial comments of the jurors provide insight into the critical "due diligence" a company or individual needs to undertake to avoid FCPA investigations by the government.

According to the evidence at trial, the Connecticut investor, Frederic Bourke, participated in a scheme to bribe senior government officials in Azerbaijan with several hundred million dollars in shares of stock, cash and other gifts to ensure that those officials would privatize the State Oil Company of the Azerbaijan Republic ("SOCAR") in a rigged (and lucrative) auction that only Bourke, his friend (a Czech investor named Viktor Kozeny), and members of their investment consortium could win (the President of Azerbaijan issued a decree directing SOCAR's privatization). According to the charges, beginning in August 1997 through fall 1998, Kozeny, Bourke and others conspired to pay millions of dollars worth of bribes to Azeri government officials to ensure that their investment consortium would gain, in secret partnership with the Azeri officials, a controlling interest in SOCAR and its substantial oil reserves.

The government did not have any evidence to show Bourke himself made any of the bribes, but they alleged he invested in the consortium "knowing" that Kozeny was making the illegal bribes to government officials and that Kozeny was giving these officials a two-thirds cut in the illegal scheme. Bourke argued, among other things, that he had only entered into the deal after his lawyers had examined it and said it was legal, and that he later had attempted to travel to Azerbaijan to alert officials of the scheme. At the end of the trial, the court instructed the jury that Bourke could be convicted if he knew directly of the bribes or if he took steps to avoid learning of the payments.

The trial lasted about a month, and the jury of seven women and five men began deliberating on July 8 and returned a verdict of guilty on July 11, 2009. The jury rejected the defense position

and found Bourke guilty of conspiring to bribe a public official. Tellingly, the foreperson of the jury said in a post-trial interview with Bloomberg news that the jury believed Bourke learned of the bribes after investing and then should have gotten out. By then, Bourke knew that Kozeny was known as the "Pirate of Prague" for allegedly stealing money from investors in his native Czech Republic. The foreperson went on to note: "It was Kozeny, it was Azerbaijan and it was a foreign country. We thought he knew and definitely could have known. He's an investor. It's his job to know."

The lesson to be drawn from the verdict and juror comments is clear: companies, investors, managers and all who deal in transactions with foreign government agencies and officials need to take proactive steps to police such conduct. Among other things, companies must make realistic risk assessments of conducting business in a particular region; must do a thorough due diligence assessment of foreign partners, employees and agents; must enact a tight and focused compliance program; must train, retrain, and certify training for all employee and agents who conduct international business; and must investigate and not ignore any "red flags" that could indicate illegal conduct.

Indeed, the jury verdict and the sentiments of the jury mirror the attitude of the Department of Justice ("DOJ") in its enforcement of the FCPA. For example, in 2004, the DOJ issued an advisory opinion that stated it would not prosecute members of an investment consortium that acquired assets in two companies that later pled guilty to paying bribes to officials of a Nigerian government agency that oversees the approval of bidders for oil exploration contracts. In an FCPA review opinion, the DOJ informed the investment group that it did not intend to take enforcement action for the pre-acquisition FCPA violations, noting the investment group's extensive due diligence and its cooperation with the government once the bribes were uncovered. Thus, continued vigilance and training are the keys to minimizing the risk of a FCPA prosecution of your company.

### **Feds Continue Aggressive Approach to Suspected FCPA Violations**

This increased diligence is all the more important as federal prosecutors have publicly stated that the trend of increased enforcement in the FCPA area will continue to increase. For example, Mark Mendelsohn, the DOJ prosecutor who heads FCPA investigations, recently stated in conjunction with a PBS documentary on bribery: "I think that companies need to be especially vigilant in this economic climate to not cut back. Our law enforcement efforts are not going to be scaled back, and so it would be, I think, a grave mistake for a company to take that path."

Mr. Mendelsohn's counterpart at the Securities and Exchange Commission ("SEC"), Enforcement Director Robert Khuzami, announced in a speech on August 5, 2009, that the SEC would create a specialized unit of attorneys and investigators to focus solely on FCPA matters and that unit would be given ample resources and expedited enforcement powers. Specifically, Mr. Khuzami has restructured the SEC's Enforcement Division into five specialized units; one of those units is "The Foreign Corrupt Practices Act Unit." As described by Mr. Khuzami, this unit "will focus on new and proactive approaches to identifying violations ... including being more proactive in investigations, working more closely with our foreign counterparts and taking a more global approach to these violations." Mr. Khuzami also announced that the investigative

process of the entire agency will be streamlined: the ability to open formal investigations and to issue subpoenas to obtain documents and testimony will no longer need approval of the SEC Commissioners; that authority will be delegated to lower level employees in the Enforcement Division; similarly, case decisions on "routine cases" will no longer need approval from the Enforcement Directors in Washington D.C., instead, senior officials in the Division offices will have that power. The SEC will also require top-level approval to agree to a tolling agreement that would draw out the length of an investigation.

Mr. Khuzami also announced that the internal memorandum prepared and sent by Enforcement Attorneys to the SEC commissioners recommending specific enforcement actions will be shorter, will be subject to fewer reviews and will require quicker turnaround times.

Finally, he announced new policies designed to increase cooperation by witnesses and potential targets of enforcement actions and announced that the Trial Units of the SEC would get more attorneys and resources. As Mr. Khuzami candidly admitted: "It is imperative that we convey to all defendants in SEC actions that we are prepared to go to trial and we will win ... Without this credible threat, we would be at a severe disadvantage. Our trial unit does an exceptional job in deploying its resources, but given the increased caseload, particularly the great increase in the number of emergency temporary restraining orders ("TROs") and asset freezes, we have committed to hiring more trial litigators to maintain the highest level of trial-readiness."

The message is clear: The government is going to "ramp up" its enforcement and trial units in all areas, including FCPA enforcement. Accordingly, companies and individuals must do the same: hire aggressive outside counsel to objectively assess that problem, but also have the experience to combat the feds if they take an unreasonable position.

### **SEC Uses Theory of Control Person Liability to Charge Individuals with FCPA Violations**

Traditionally, the SEC and DOJ have only leveled charges in the FCPA arena in those instances where the individual within the company made the bribe, authorized the bribe or was complicit in creating the inaccurate books or records that hid the bribe. Recently, however, the government has used the theory of control person liability to widen the scope of individuals who could be charged.

Specifically, last month, the SEC announced an enforcement action and settlement against Nature Sunshine Products, Inc. ("NSP"). Essentially, the allegation was that an NSP subsidiary in Brazil bribed Brazilian customs officials in 2000 and 2001 with more than \$1 million in cash to ensure importation of NSP's medical products, which were not properly registered in accord with Brazilian regulations. The SEC also charged Chief Executive Officer Douglas Faggioli, and Chief Financial Officer Craig D. Huff, alleging violations of the FCPA, 15 U.S.C. Section 78dd-1.

Significantly, these officers were not charged with direct participation in the bribery scheme; instead, the SEC charged them with "control person" liability under Section 20(a) of the Securities Exchange Act, 15 U.S.C. Section 20(a) (the "Exchange Act"). The SEC complaint alleged that Faggioli and Huff failed to supervise personnel within the company to ensure that

NSP "ma[d]e and [kept] books, records, and accounts, which in reasonable detail, accurately and fairly reflected the transactions of NSP." The complaint alleged further that Faggioli and Huff "failed to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with the generally accepted accounting principles or any other criteria applicable to such statements." Eventually, Huff and Faggioli (and the company) settled the allegations; while they neither admitted nor denied the allegations, they were forced to pay substantial fines.

The case is emblematic of the government's trend in FCPA cases to charge not only companies but individuals, too. The case also shows that the SEC is willing to take aggressive charging positions by filing complaints against company officials under the more expansive theory of control person liability.

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