Wining and Dining Foreign Officials

What's OK and What's a Crime

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In December 2007, Lucent Technologies Inc. secured a non-prosecution agreement from the Department of Justice (DOJ) and settled an enforcement action with the SEC for conduct related to travel and entertainment expenses incurred on behalf of Chinese government officials and for the manner in which these expenses were booked. The Lucent settlement adds to a number of existing guideposts regarding permissible interactions with foreign officials under the Foreign Corrupt Practices Act (FCPA). This article examines the Lucent settlement together with prior FCPA enforcement activity related to travel and lodging, and offers some practical advice for compliance counsel.

REASONABLE AND BONA FIDE EXPENSES

The FCPA prohibits the bribery of foreign officials and efforts to obscure that conduct on the books and records of public companies. Specifically, the FCPA's anti-bribery provisions prohibit offers, payments, promises or authorizations to pay, any money or thing of value to any foreign official for purposes of influencing any act or decision in order to obtain or retain business. The accounting provisions require that public companies make and keep accurate books and records, and maintain internal controls sufficient, for example, to ensure that transactions are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles.

While prohibiting payment of any money or thing of value to foreign officials, the FCPA contains an affirmative defense arguably permitting certain expenses to be incurred on behalf of these same officials. "It shall be an affirmative defense [that] the payment, gift, offer, or promise of anything of value that was made, was a reasonable and bona fide expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign official, party, party official, or candidate and was directly related to … the promotion, demonstration, or explanation of products or services; or … the execution or performance of a contract with a foreign government or agency thereof." Thus, "travel and lodging expenses" may be permissible under certain circumstances.

LUCENT: WHAT NOT TO DO

Although it is fair to say that the Lucent settlement outlines the types of travel and lodging expenses that the DOJ will consider impermissible, it is perhaps better to say that it confirms what many practitioners have counseled clients for years: stick closely to the statute, the public resolutions, and the DOJ guidance.

As Lucent acknowledged in the Statement of Facts attached to the DOJ's non-prosecution letter, and as alleged in the SEC Complaint, it paid expenses for approximately 1,000 Chinese officials to take approximately 315 trips to the United States over a period of at least three years. Done correctly, the mere fact of the trips might not have presented problems. Indeed, it is notable that none of the settlement papers included a charge or acknowledgment that Lucent violated the anti-bribery portion

of the statute. Despite this, the language of the resolution clearly indicates that the conduct pressed the bounds of the affirmative
defense.

In relation to the business purposes of the trips, there was a "disproportionate amount" of sightseeing and leisure time, the SEC alleged. For example, although Lucent paid for officers and engineers of a subsidiary of a government majority-owned company to travel to the United States, only five days were spent at Lucent facilities, whereas nine were spent on activities at locations other than the Lucent facilities. On another trip, Lucent paid for employees of a government-owned company and family members to visit Niagara Falls and the Grand Canyon.

In addition to the disproportionate amount of non-business activity, Lucent "improperly recorded expenses for these trips," according to the DOJ's Statement of Facts accepted by Lucent. The SEC Complaint elaborated that Lucent booked visits as factory inspection tours "knowing that only sightseeing, entertainment and leisure activities would be taking place." In another instance, the Complaint alleged, expenses incurred for a government official were booked as employees' lodging expenses.

Lucent got in trouble with the Feds because it wined and dined its Chinese customers the way Lucent and its competitors routinely do with engineers and purchasing agents of private overseas companies — which may be perfectly legal. For the Feds, however, the Chinese businessmen were "foreign officials" subject to the FCPA because they worked for "a subsidiary of a government majority-owned company." The SEC alleged that Lucent conducted little or no inquiry whether the trip recipients were government officials and had no process for reviewing the trips for FCPA compliance. Thus, the Lucent case highlights the risks posed when there is no affirmative inquiry into whether the customer or counterparty qualifies as a foreign official.

WHAT CAN YOU DO?

Lucent's predicament is of course not the first time a company has found itself in an enforcement mess due to travel and lodging provided on behalf of a foreign official. Past FCPA enforcement activity confirms that this is an area of recurring risk. While there are few bright lines, the settled enforcement actions offer directions regarding the affirmative defense and what may be permissible.

In another recent enforcement action, the SEC charged Ingersoll-Rand Co. with violations of the FCPA's accounting provisions stemming primarily from the Oil-for-Food investigation. However, the SEC also alleged that Ingersoll-Rand incurred travel and lodging expenses on behalf of Iraqi officials. According to the Complaint, an Italian "factory tour had a legitimate business purpose," but a two-day side trip to Florence, including pocket money for the officials, violated the company's policies. As with Lucent, Ingersoll-Rand was not charged with a bribe. Rather, the matter was settled as an accounting violation because, as the Complaint alleged, the company inaccurately recorded the expenditures as "cost of goods sold." Provision of pocket money in contravention of the company's internal FCPA policy was charged as an internal controls violation.

Another settled case, *U.S. v. Metcalf & Eddy* (an unusual civil enforcement action brought by the DOJ in 1999), makes clear that first-class airline tickets for a government

official and his family may draw an enforcement action, as might cash advances on per-diem expenses when those expenses are otherwise covered. Provision of lavish travel was not "reasonable," and the cash advances were not "bona fide" expenditures. Unlike Lucent, Metcalf & Eddy settled the matter as an anti-bribery enforcement action rather than as an accounting violation.

Side trips to places such as the Grand Canyon or Niagara Falls should be viewed as barred, as the Lucent resolution teaches. Such side trips are not "directly related to … the promotion, demonstration, or explanation of products or services."

The FCPA sets forth a procedure, similar to the SEC's better-known "noaction letters," to advise companies whether the DOJ would pursue an enforcement action on a given set of facts. 15 U.S.C. §§ 78dd-1(e), 78dd-2(e) When combined with prior FCPA Opinions, these FCPA Opinion Procedure Releases offer clear guidelines to a company considering whether and, if so, how to incur travel and lodging expenses for a government official. Two Releases from 2007 address the "promotional expense affirmative defense." While not the complete list, here are the most important lessons:

- The DOJ clearly prefers that the company not select the officials who will travel. The 2007 Releases make the point that no enforcement was warranted in part because the foreign government selected the officials whose travel would be covered by the company. Having the foreign government nominate the officials demonstrates transparency between the company and the foreign government.
- The travel must directly relate to "promotion, demonstration, or explanation of products or services." The permissible "Study Tour" and "educational and promotional tour" addressed in the Releases conformed to this requirement. Side trips to the Grand Canyon or Florence in the Lucent case did not.
- The Opinions stress moderation, mentioning that travel should be economy airfare and any per diem should be modest ($35/day). One FCPA Opinion indicated that the total cost of a permissible nine-day trip for five people was $16,875. The cost thus broke down to $375 per person per day, including airfare, hotel, and local transportation. Of course, when the company is an issuer, the expenses must be accurately recorded in the books and records.
- Finally, the DOJ FCPA Opinions approved of the proposed travel in part because the traveler did not have authority to award business or a license to the company, nor were there any contracts or licenses pending before the officials' agencies.

CONCLUSION

While the FCPA does not prohibit the provision of travel and lodging to foreign officials, the scope of the affirmative defense is narrowly drawn. By reviewing past enforcement actions and DOJ Opinions regarding the "promotional expense affirmative defense," compliance counsel can piece together a picture of how to structure a study or promotional tour for foreign officials and record the tour's expenses without running afoul of the FCPA. It is equally important to establish a clear set of benchmarks that are

communicated to business operations in the field to assure the effectiveness of the company's internal controls.