An FCPA Primer

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The Foreign Corrupt Practices Act[1] ("FCPA" or "the Act") had been steadily, albeit infrequently, enforced since its enactment in 1977. In the last few years, however, a flood of enforcement actions has been pursued by both the Department of Justice (the "DOJ") and the Securities and Exchange Commission (the "SEC"). As a result of this new enforcement imperative, the scope of the Act has changed without the usual judicial review — and those changes have rocked the business world.

In this essay, I provide a brief review of the history, background and operative provisions of the FCPA. I discuss the broad interpretation of key terms of the anti-bribery provisions, and identify recent prosecution trends, which together with the dearth of judicial interpretation, have contributed to ambiguity in the FCPA. I conclude by analyzing elements for corporate "best practices" gleaned from recently resolved FCPA enforcement matters.

History and Background

About ten years after FCPA was passed, Congress and American corporations perceived a competitive disadvantage from FCPA regulations in comparison to other countries that were not burdened by similar anti-corruption laws. In fact, at that time, the law in many countries provided tax breaks and incentives to companies that resorted to paying bribes when conducting business outside their borders. To alleviate the perceived competitive disadvantage, Congress added certain affirmative defenses to FCPA liability, and more importantly, the United States began urging other countries to adopt comparable anti-corruption legislation.

After nearly ten years, and with significant lobbying efforts from the U.S., the Organization for Economic Co-operation and Development (the "OECD") adopted a comprehensive anti-corruption regime. The OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (the "OECD Convention"), enacted in 1997, required signatory countries to enact measures that are substantively similar to the prohibitions in the FCPA, such as the prohibition against bribing foreign officials, the establishment of criminal and civil penalties for violations, and the requirement to implement books and records and compliance controls to support anti-bribery efforts. The OECD Convention was a turning point in international anti-corruption efforts.

By the mid-2000s, many countries enacted national anti-corruption legislation aimed at transnational business activity. Germany, for example, actively enforces its OECD Convention-inspired anti-bribery legislation, notably in its initiation of the Siemens AG prosecution, which was later a joint prosecution effort with the DOJ that was settled for a record fee and penalty in December 2008. The United Kingdom enacted the Bribery Act, which criminalizes both offering and accepting a bride (the FCPA only regulates offering a bribe) and provides for strict liability against companies whose compliance systems fail to prevent a bribe.[2]

In the United States, FCPA prosecutions were steady, but sparse, with a couple of actions a year. As late as 2004, the slow acceleration of prosecutions did not change — with combined prosecutions by the DOJ and the SEC at a mere five FCPA cases. More recently, however, FCPA enforcement has exploded. Between 2007 and 2009, the DOJ and the SEC brought

[1] Title 15, United States Code, Sections 78dd-1, *et seq.*

[2] Bribery Act, 2010, c. 23, §§ 1, 2 (Eng.), available at http://www.justice.gov.uk/publications/bribery-bill.htm. Implementation of the Bribery Act 2010, which had been due to come into effect in April 2011, is to be delayed.

sixty-four and forty-seven FCPA enforcement actions, respectively, almost twice as many actions as the total number of cases brought in the first twenty-eight years of the Act's existence.

The Sarbanes-Oxley Act of 2002 ("SOX") and the United Nation's Oil-For-Food Program are widely accepted as two reasons for the onset of increased FCPA enforcement. The comprehensive reporting requirements of SOX expanded the amount of information that the government was able to access. In addition, SOX provided enhanced protection of whistleblowers. The Oil-For-Food Program was beset with corruption, and in 2005, the UN-commissioned internal investigation connected with the program released a scathing report of the corruption that named 2,253 companies that reportedly made corrupt kickback payments to the Iraqi government totaling more than $1.8 billion. For regulators, the report was a ready-made list of FCPA investigations.

The volume of FCPA actions in 2010 again broke the record and DOJ officials have stated that enforcement of the FCPA will continue to trend higher. In addition, the number of FCPA prosecutions is expected to continue to increase as a result of the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank") in July 2010. Particularly because of the whistleblower provisions, which provide enhanced monetary incentives and protections for whistleblowers who report securities law violations to the SEC. One report suggests that the SEC has already been receiving more than one FCPA tip a day since the Dodd Frank whistleblower bounty program became law.

Two Main Provisions of the FCPA

The FCPA has two main provisions: the anti-bribery provisions,[3] and the books and records / internal control provisions.[4] The anti-bribery provisions apply to a wide range of entities, including U.S. persons and U.S. companies, "issuers" (corporations whose securities are publicly traded in the United States), and anyone within the territory of the United States. The anti-bribery provisions have three core elements, which prohibit giving: (1) "anything of value" to a; (2) "foreign official" (3) "to obtain or retain business." The DOJ's interpretations of the core elements have been the subject of intense discussion, as further described below.

The books and records / internal control provisions are narrower than the anti-bribery provisions in that they only apply to publicly-held companies with shares traded on a U.S. exchange. This category, however, can include numerous foreign companies whose shares trade on a U.S. exchange. The books and records provisions require companies to (1) "make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions" of the company's assets; and (2) "devise and maintain a system of internal accounting controls."

Broad Interpretation of Key Terms of the Anti-Bribery Provisions

Considering that the FCPA has been in force for over thirty years, one would expect a rich repository of case law that provides a sense of clarity on how to comply with it. However, there are very few court opinions that provide interpretive guidance on the key terms of the Act.

The FCPA has been the subject of almost no formal rule making and is seldom litigated — almost all actions settle before trial. As a result, the DOJ's interpretations of core elements of the FCPA rule without challenge. In addition, the DOJ's interpretations are not uniform among the various agencies and districts, rendering determinations of which factual situations potentially violate the FCPA are unclear and unpredictable.

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[3] *See* 15 U.S.C. §§ 78dd-1, 78dd-2 (2006).
[4] 15 U.S.C. § 78m(b)(2)(A).

The ambiguity of the anti-bribery provisions' three core elements demonstrates how unpredictable FCPA enforcement can be.

1. **Anything of Value.** The Act does not define, and no FCPA decision has addressed the scope of "anything of value." The only guidance provided is the outer limits, for example, "anything of value" is not restricted to actual payments of money nor is it subject to a *de minimis* exception.

   The incongruity of two factual scenarios that were alleged to demonstrate "anything of value" in two recent FCPA actions illustrates how unclear the element is. In the action against Kellogg Brown & Root LLC (a Halliburton affiliate) filed by the DOJ in January 2009, "anything of value" included a "briefcase containing one million dollars in one hundred dollar bills" and "a vehicle containing Nigerian Currency valued at approximately $500,000 [left] in the hotel parking" until the money was removed by Nigerian foreign officials.[5]

   By contrast, in the action against UTStarcom Inc., filed by the SEC in December 2009, "anything of value" had a more nuanced factual basis. The accoutrements deemed to violate the FCPA, included "overseas trips by [foreign] employees … to attend executive training programs at U.S. universities."[6]

2. **Foreign Official.** Elected foreign government officials, other foreign heads of state, and employees of foreign government agencies are indisputably "foreign officials" under the FCPA.[7] However, the majority of FCPA enforcement actions do not implicate indisputable government officials, instead, the "foreign officials" often named are agents of foreign state-owned or state-controlled enterprises or companies. The definition of foreign official does not explicitly include agents of state-owned or state-controlled companies, but the DOJ broadly interprets the term "instrumentality thereof" in the definition of "foreign official" to include employees of agents of state-owned or state-controlled companies.

   Many practitioners resist this broad interpretation and argue that the DOJ has read the phrase "instrumentality thereof" as allowing investigation and prosecution of companies for FCPA violations despite a limited connection between companies' foreign business partners and the foreign government. Despite these concerns, enforcement agencies continue to aggressively interpret the "foreign official" element and have steadfastly refused to provide guidance on the issue.[8]

3. **To Obtain or Retain Business.** The third element of an FCPA anti-bribery violation is "to obtain or retain business." Unlike the "foreign official" and "anything of value" elements, the "to obtain or retain business" element has been subject to judicial scrutiny.

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[5] *See* Criminal Information ¶¶ 17-20, United States v. Kellogg Brown & Root LLC, No. H-09-071 (S.D. Tex. Feb. 6, 2009), *available at* http://fcpaenforcement.com/FILES/tbl_s31Publications/FileUpload137/5714/KBRCriminalInformation.pdf.

[6] Complaint ¶ 16, SEC v. UTStarcom, Inc., Case No. CV 09-6094 (N.D. Cal., Dec. 31, (2009), *available at* http://www.sec.gov/litigation/complaints/2009/comp21357.pdf.

[7] The FCPA defines "foreign official" as: any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization. 15 U.S.C. §§ 78dd-1(f)(1)(A), -2(h)(2)(A), -3(f)(2)(A) (2006).

[8] *See e.g.,* Lanny A. Breuer, Assistant Att'y Gen., DOJ, Criminal Division, Keynote Address to the Tenth Annual Pharmaceutical Regulatory and Compliance Congress and Best Practices Forum (Nov. 12, 2009), *available at* http://www.ehcca.com/presentations/pharmacongress10/breuer_2.pdf. ("But who exactly qualifies as a 'foreign official' … and what constitutes a corrupt offer or payment that violates the FCPA? Of course, the answers to those questions depend on the facts and circumstances of every case, and I can't give you binding guidance from the podium today.")

However, the case law is not helpful in determining the parameters of the element. In *United States v. Kay*,[9] the Fifth Circuit considered "whether payments made to foreign officials to obtain unlawfully reduced customs duties or sales tax liabilities can ever fall within the scope of the FCPA." The appellate court answered in the affirmative, thereby overturning the district court's opinion. The appellate court agreed with the district court that the "to obtain or retain business" element was ambiguous, but based on the legislative history, could be interpreted to include more than just payments to acquire or retain government contracts. The Fifth Circuit held that "Congress intended for the FCPA to apply broadly to payments intended to assist the payor, either directly or indirectly, in obtaining or retaining business … , and that bribes paid to foreign tax officials to secure illegally reduced customs and tax liability constitute a type of payment that can fall within this broad coverage."

The decision did not analyze the parameters of the "to obtain or retain business" element, except to find that the specific factual scenario presented in *United States v. Kay*, could be the basis for the "to obtain or retain business" element, consequently, the one element that has been scrutinized by the judiciary is not much clearer than it was before the Fifth Circuit decision.

After more than thirty years of FCPA enforcement, the Act remains lacking in judicial analyses. Companies will not take the time, expense and risk the consequences of losing a trial to set legal precedent by challenging an expansive interpretation by the government. In addition, most FCPA matters are not prosecuted in the traditional sense, which is another reason for the lack of judicial analyses of the Act.

Pretrial Diversion Agreements

In an effort to balance holding corporations responsible for unlawful conduct against the risk of collateral consequences, the government has shifted prosecutions to the pre-indictment stage of corporate criminal proceedings. The fall of Arthur Anderson, after being indicted during the Enron debacle, taught the DOJ to be more cautious of the harmful consequences to innocent third parties when investigating viable businesses for possible criminal conduct. The concern over destroying businesses and the resulting collateral damage to stakeholders prompted the DOJ's increased use of deferred prosecution agreements ("DPAs") and non-prosecution agreements ("NPAs") (also known as "pretrial diversion agreements"),[10] including in the FCPA context.

With NPAs and DPAs, the government either defers or omits formal criminal charges.[11] Pursuant to many pretrial diversion agreements, a company voluntarily enters a probationary period and agrees to: (1) enact substantial internal reforms, and (2) cooperate with the government, thereby avoiding collateral consequences of an indictment. The company also pays a penalty and often may be required to submit to federal monitoring. Each pretrial diversion agreement is tailored to the specific company and alleged factual situation, and the corporation is required to comply with the specific terms designed by the government. The shift

[9] *United States v. Kay*, 359 F. 3d 738 (5th Cir. 2004),

[10] Although DPAs and NPAs have previously only been used by the DOJ, the SEC has recently started to use them too. On January 13, 2010, the SEC announced a new "Cooperation Initiative", which includes the potential for using pretrial diversion agreements. Press Release, SEC Announces Initiative to Encourage Individuals and Companies to Cooperate and Assist in Investigations, *available at* http://www.sec.gov/news/press/2010/2010-6.htm.

[11] "[A] deferred prosecution agreement is typically predicated upon the filing of a formal charging document by the government, and the agreement is filed with the appropriate court. In the non-prosecution agreement context, formal charges are not filed and the agreement is maintained by the parties rather than being filed with a court." Craig S. Morford, Memorandum for Heads of Department Components and United States Attorneys, n.2 (March 7, 2008), *available at* http://www.justice.gov/dag/morford-useofmonitorsmemo-03072008.pdf

from formal prosecution to pre-trial NPAs and DPAs reflects a shift in DOJ policy that is becoming a "rather routine way of resolving investigations of corporate crime as to companies."[12]

There are benefits and drawbacks to the use of pretrial diversion agreements. The benefits include, *inter alia*, less disruption to the business and minimizing collateral consequences. The drawbacks arise from the fact that the agreements are not scrutinized and companies acquiesce to them without argument. As a result of the governments' broad interpretations of the Act and zealous enforcement through the use of NPAs and DPAs, the scope of FCPA has broadened and the prospects for predictability are minimized.

Expanded Scope and Unpredictability in FCPA Enforcement

In recent enforcement matters, the DOJ and the SEC have expanded the scope of the FCPA by, *inter alia*, prosecuting non-U.S. subsidiaries, foreign agents, "control persons" and when no foreign official is involved in a matter.

Non-U.S. Subsidiaries. Since the 1998 amendments to the FCPA, jurisdiction can be asserted over both U.S. and non-U.S. persons who committed violations while in U.S. territory, however, today, the DOJ has used the FCPA to prosecute non U.S. persons who are neither U.S. residents nor doing business in the United States. As currently applied, the FCPA is being increasingly used to hold U.S. entities and issuers liable for improper payments of their non-U.S. subsidiaries. Both the Siemens AG and Kellogg Brown & Root matters were triggered by actions of non-U.S. subsidiaries. Siemens AG and three subsidiaries plead guilty to violating the anti-bribery and books and records provisions of the FCPA, and agreed to pay $450 million in combined criminal fines;[13] the Kellogg, Brown & Root, LLC / Halliburton joint enforcement action involving massive bribery schemes in Nigeria that was settled for $579 million in combined criminal and civil proceedings.[14]

Foreign Agents. Many companies doing business abroad hire the services of foreign agents who are knowledgeable in the customs and business practices of the local country. But the attractive features of a foreign agent, such as, knowledge of the local business environment and relationships with key local business entities also present the most troublesome FCPA risks.

In *United States v. Kozeny,*[15] Frederic Bourke was convicted of conspiring to violate the FCPA even though he had no direct knowledge of the bribes made by Viktor Kozeny, a foreign agent. In *Kozeny*, the jury found that the investment scheme's involvement with the oil industry, the common perception of corruption in Azeri business transactions, and Viktor Kozeny's questionable history meant that Bourke knew or should have known that bribery was taking place. Thus, Bourke was convicted based on conscious avoidance of knowledge to a substantial probability that his investment funds would be used to make bribes.

Control Person Liability. The SEC has been expanding the scope of liability in civil cases too. In *SEC v. Nature's Sunshine Products Inc.*,[16] the SEC used a novel theory for individual liability

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[12] Mary Jo White, Corporate Criminal Liability: What Has Gone Wrong?, in 37th Annual Institute on Securities Regulation 815, 824 (PLI Corp. Law & Practice, Course Handbook Ser. No. B-1517, 2005).

[13] Press Release, Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations and Agree to Pay $450 Million in Combined Criminal Fines, *available at* http://www.justice.gov/opa/pr/2008/December/08-crm-1105.html

[14] Press Release, Kellogg Brown & Root LLC Pleads Guilty to Foreign Bribery Charges and Agrees to Pay $402 Million Criminal Fine, Enforcement Actions by DOJ and SEC Result in Penalties of $579 Million for KBR's Participation in a Scheme to Bribe Nigerian Government Officials to Obtain Contracts, *available at* http://www.justice.gov/opa/pr/2009/February/09-crm-112.html

[15] *United States v. Kozeny,* 664 F. Supp. 2d 369 (S.D.N.Y 2009).

[16] *SEC v. Nature's Sunshine Products Inc.*, No. 09-CV-0672 (D. Utah July 31, 2009).

by relying on defendants' status as control persons of the company. The SEC charged CEO Douglas Faggioli and CFO Craig Huff with violating the books and records and internal control provisions in connection with payments allegedly made by the company's Brazilian subsidiary to customs officers in Brazil. The SEC did not allege that the two executives participated in or had personal knowledge of the underlying bribes, or the way the bribes were booked in the company's consolidated financial statements. Faggioli and Huff merely had supervisory responsibility for maintaining the company's books to reflect its dealings with Brazil accurately. The case settled with the executives paying a fine to the SEC.

No "Foreign Official" Element. In what may prove to be a controversial approach to the "foreign official" element, the January 2010 arrests of twenty-one executives in Las Vegas during a Shooting, Hunting and Outdoor Trade Show were based on an FBI sting labeled "Catch-22" in which no foreign government official participated. FBI agents posed as representatives of a government minister from an African country, and proposed a scheme in which the executives or employees would pay a 20% commission to win government business.

As demonstrated by examples above, FCPA enforcement trend includes, (1) a focus on non-U.S. subsidiaries; (2) greater scrutiny of business executives, including responsibility for foreign agents and a greater expectation that executives play a meaningful role in ensuring FCPA compliance; and (3) novel prosecution tactics.

Creating an Effective Compliance Program

As the number of FCPA matters increase and the scope of the Act broadens, further legal interpretation from the bench, and greater clarity from the DOJ and SEC specifying the boundaries of acceptable conduct would enable companies and executives to avoid risking FCPA violations as they operate through myriad associations in complex environments. Although traditional modes of guidance do not appear forthcoming, much can be gleaned from the proliferation of recently entered and published DPAs and NPAs. In many agreements, the DOJ attached a document entitled "Corporate Compliance Program."[17] The Corporate Compliance Program details the DOJ's assessment of best practices to conduct business while complying with the FCPA. In the section below, I have paraphrased the thirteen "internal controls, policies, and procedures" outlined by the DOJ as the minimum standards that companies must maintain.

1. Corporate Compliance Code. Companies must have "a clearly articulated and visible corporate policy" against FCPA and applicable foreign law violations, "which policy shall be memorialized in a written compliance code."

2. Management Support. Senior management must provide "strong explicit, and visible support and commitment to its corporate policy against violations …."

3. Compliance Standards for Every Level of Employee. "[D]evelop and promulgate compliance standards and procedures to reduce the prospect of violations … and encourage and support the observance of ethics and compliance standards and procedures … at all levels of the company [including,] directors, officers, and employees … and outside parties …."

   All employees must be notified that compliance with "standards and procedures" is the "duty of individuals at all levels of the company." Standards and procedures "shall include policies governing: gifts; hospitality, entertainment, and expenses; customer travel; political contributions; charitable donations and sponsorships; facilitation payments; and solicitation and extortion."

[17] Corporate Compliance Program at Attachment C of the DPA for Panalpina World Transport (Holding) LTD, issued on October 27, 2010, *available at* http://www.justice.gov/opa/documents/panalpina-world-transport-dpa.pdf.

4. Risk Assessment Addressing Individual Circumstances. Develop compliance standards and procedures "on the basis of a risk assessment addressing the individual circumstances of the company" including, *inter alia*, "geographical location"; "industrial sectors of operation"; "involvement in joint venture arrangements"; and "degree of governmental oversight and inspection."

5. Regular Review and Update. Compliance standards and procedures must be reviewed at least "annually, and update them as appropriate" taking into account "developments in the field" and "industry standards, and update and adapt them as necessary to ensure their continued effectiveness."

6. Responsible Senior Corporate Executive(s). One or more "senior corporate executives must be responsible for the implementation and oversight" "of a company's corruption policies, standards, and procedures" and shall have "direct reporting obligations to independent monitoring bodies," "an adequate level of autonomy" and "sufficient resources."

7. Financial and Accounting Procedures. A system of financial and accounting procedures must be maintained to ensure "the maintenance of fair and accurate books, records, and accounts to ensure that they cannot be used for the purpose of foreign bribery or concealing such bribery."

8. Training and Certifications. Mechanisms designed to ensure that "anti-corruption policies, standards, and procedures are communicated effectively" must be implemented and shall include: "periodic training" and "annual certifications."

9. Internal Reporting. "[M]aintain, or where necessary establish, an effective system for: (a) "Providing guidance and advice … on complying with [company] anti-corruption compliance policies … including when they need advice on an urgent basis or in any foreign jurisdiction"; (b) "Internal and, where possible confidential reporting … to report breaches of the law or professional standards or ethics concerning … violations of the compliance policies"; (c) Responding to such requests and undertaking appropriate action in response to such reports."

10. Procedures to Address Violations. "Institute appropriate disciplinary procedures to address" violations of, *inter alia*, "the anti-corruption laws and [company] anti-corruption compliance code … [I]mplement procedures to ensure that where misconduct is discovered reasonable steps are taken to remedy the harm … and to ensure that appropriate steps are taken to prevent further similar misconduct…."

11. Procedures Concerning Foreign Agents. "[I]nstitute appropriate due diligence and compliance requirements pertaining to the retention and oversight" of foreign agents, including: (a) "documented risk-based due diligence"; (b) "informing agents of [company's] commitment to abiding by laws on the prohibitions against foreign bribery and [company] ethics and compliance standards"; (c) seek "reciprocal commitment" from foreign agents.

12. Provisions in Agreements. "[I]nclude standard provisions in agreements … to prevent violations of the anti-corruption laws with all agents and business partners" including, (a) "representations … relating to compliance"; (b) "rights to conduct audits of the books and records"; (c) "rights to terminate … as a result of any breach of anti-corruption laws ...."

13. Periodic Review and Testing. "Conduct periodic review and testing of its anti-corruption code … to evaluate and improve their effectiveness … taking into account relevant developments in the field and evolving international and industry standards."

The increase in FCPA enforcement over the last few years demonstrates that companies and executives, in all industries, doing business in all countries face FCPA risk and exposure. It is important to understand the unique way the Act is being enforced and where — beyond usual sources, such as case law — to find useful guidance.

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