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The Foreign Corrupt Practices Act: Enforcement Trends in 2010 and Beyond

THE FOREIGN CORRUPT PRACTICES ACT: ENFORCEMENT TRENDS IN 2010 AND BEYOND

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Foreign bribery, once accepted as a routine cost of operating in the developing world, can now lead to significant criminal and civil penalties. The United States is investigating and prosecuting more violations of the Foreign Corrupt Practices Act ("FCPA" or "the Act") than ever before, and enforcement shows no sign of slowing down in 2010. The Securities and Exchange Commission ("SEC") recently announced the creation of a new unit devoted exclusively to enforcing the FCPA, while Department of Justice ("DOJ") officials indicated that they will be prosecuting even more individual decision makers for violations of the Act. Increased competition caused by a worldwide recession will only heighten the pressure many individuals feel to use bribery as a vehicle for obtaining and retaining business. As a result, companies must identify high-risk activities and focus compliance efforts on mitigating potential violations of the law. The question is not *whether* more investigations and prosecutions are in the offing, but *what kind* of enforcement initiatives will be forthcoming.

The best method for predicting future enforcement is to undertake a thorough analysis of past FCPA investigations, prosecutions, and settlements. A review of global enforcement activities reveals the following trends:

- The DOJ and SEC are investigating and charging individual executives, not just corporations, with violations of the FCPA. This allows the government to leverage its position against multiple parties by securing the cooperation of one against the other. It also raises the stakes for individual employees.
- Certain industries, such as the energy and medical device sectors, have proved to be particularly vulnerable to FCPA investigations.
- Penalties imposed under the FCPA have skyrocketed and now typically include hefty amounts of disgorged profits.
- The appropriate relationship between private businesses and government customers, including state-controlled companies, remains unclear in the international context. Neither the DOJ nor the SEC has provided clear guidance to companies regarding appropriate entertainment and business courtesies for government-related customers.
- Countries other than the U.S. have strengthened their own anticorruption enforcement activities, increasing the risk of enforcement and complicating compliance efforts for companies.
- FCPA enforcement continues to affect the manner in which companies enter into transactions with foreign partners or acquisition targets.
- FCPA violations have spurred a number of collateral civil actions. While these cases are rare, they present an expensive risk of additional litigation.

These trends are explored in more detail below.

TOP TRENDS FOR FCPA ENFORCEMENT

Enforcement Actions Against Individuals. As part of an ongoing effort to deter corruption, U.S. enforcement authorities are penalizing the individual decision makers implicated in bribery schemes. Two groups of individuals are now being targeted: the executives who authorize corporate bribes and the foreign government officials who receive them.

The United States prosecuted a record number of individuals under the FCPA in recent years, charging a dozen people and obtaining convictions at three separate trials in 2009 alone.[1] In late 2009, the Assistant Attorney General for the DOJ's Criminal Division, Lanny Breuer, noted that the DOJ would continue its aggressive pursuit of corporate executives.[2] This trend could have significant practical consequences. Threatened with personal exposure, more corporate executives will err on the side of caution when risks arise in a business deal or transaction. Accordingly, company leaders and counsel should be prepared to answer questions regarding the extent to which individual employees may be liable for corporate actions.

The penalties imposed on individuals for FCPA violations can be severe: lengthy prison sentences, legal fees, and steep financial penalties. Most recently, former U.S. Representative William Jefferson (D-LA) was sentenced to 13 years in prison for conspiring to violate the law.[3] Financial penalties are also serious, particularly because the FCPA prohibits "issuers" from paying for the criminal and civil fines imposed on individual officers, directors, employees, agents, or stockholders.[4] Furthermore, some executives may owe civil damages to shareholders. In 2009, several former Siemens executives paid damages ranging from €500,000 to €5 million, for a total of €19.5 million.[5]

As a result of the focus on individual criminal liability, a number of foreign citizens now face time in American prisons. A French citizen was sentenced to 30 months in prison for arranging a bogus $2.5 million "commission" payment to an official in Costa Rica in 2007.[6] Czech native and Irish citizen Viktor Kozeny unsuccessfully challenged the application of

the FCPA to foreign citizens that same year. He is fighting extradition from the Bahamas.[7]

By focusing resources on cases against individuals, the government may attract more cooperating witnesses and generate even more FCPA investigations. For example, in 2009, several executives were accused of developing an elaborate business structure designed to evade FCPA liability in connection with an energy project in West Africa. Facing 55 or more years in prison and the forfeiture of more than $130 million, those individuals assisted the government in subsequent investigations of their former employer and business partners.[8]

"The number of individual prosecutions has risen—and that's not an accident. That is quite intentional on the part of the Department. It is our view that to have a credible deterrent effect, people have to go to jail. People have to be prosecuted where appropriate. This is a federal crime. This is not fun and games."

–Deputy Chief, Fraud Section, Criminal Division, U.S. Department of Justice (Sept. 16, 2008).[9]

The focus on individuals is not limited to the DOJ. In July 2009, the SEC imposed liability on two executives under a theory of "control person" liability for the first time in an FCPA case. Under that theory, the SEC may charge an individual who manages a company absent evidence that he or she knew about or participated in a bribery scheme. In this particular case, the SEC charged two executives with violating the books-and-records provision of the FCPA after a wholly owned subsidiary made cash payments to Brazilian customs agents. The SEC alleged that the executives had overall responsibility for the international operations of the company and that the people who would know about the relevant issues were under their control. Accordingly, they had the ultimate authority and responsibility to maintain accurate internal controls as mandated by the FCPA. Significantly, the SEC did not allege that the executives had any personal knowledge of or involvement in the payments or the improper accounting entries.[10] In the future, use of the control-person theory of liability could make it easier for the government to impose liability on executives under U.S. securities laws.

Corporate executives are not the only individuals being pursued by the U.S. government for FCPA violations; the DOJ has expressed a newfound willingness to pursue foreign officials who receive corrupt payments. Thus, in January 2009, the DOJ instituted forfeiture proceedings against funds held in Singapore that purportedly contained $3 million in proceeds from bribes paid to Arafat "Koko" Rahman, son of the former prime minister of Bangladesh, relating to public works projects awarded to several companies.[11] This was the first time the DOJ had instituted such an action against the recipient of a payment prohibited by the FCPA. Consistent with this action, Assistant Attorney General Breuer noted in November 2009 that the DOJ would focus on asset forfeiture and recovery to ensure that corrupt foreign officials do not retain the illicit proceeds of their corruption.[12] According to Mr. Breuer, DOJ attorneys have been instructed to seek forfeiture in all appropriate FCPA cases.[13]

The extension of U.S. enforcement to foreign bribe recipients could have seismic implications for FCPA compliance efforts. In the past, U.S. businesses seeking to extend FCPA compliance to foreign business partners often met with resistance, with the foreign counterparts treating compliance as a problem only for the U.S. company or individual. The aggressive assertion of jurisdiction over foreign businesses under the FCPA has resulted in the adoption of compliance policies by many non-U.S. businesses, but there is no reason to believe that this policy would reduce the demand for bribes from foreign officials. The DOJ's promise to impose penalties on bribe recipients could change that equation fundamentally, putting such officials at personal risk under U.S. law for the first time.

Sectorwide Investigations. Many of the recent FCPA enforcement actions and investigations have involved up to a dozen companies from two distinct economic sectors: energy (specifically the oil and gas industry) and medical devices. This concentration can be attributed to the particular nature of those two industries and the regions in which they typically operate. These clusters of enforcement actions suggest that companies operating in certain regions or environments need to pay close attention to the activities of their partners and competitors. U.S. enforcement authorities have been quick to discover links between one corrupt agent and multiple companies, leading them to investigate entire industries.

"There must be few other countries on earth with such a glaring mismatch between their actual state and their extraordinary potential. Some call Nigeria Africa's slumbering giant. It more often behaves like the continent's suicidal maniac."

–"Mission impossible, nearly; Nigeria," *The Economist*, U.S. ed. (Aug. 4, 2007).

Oil is found, and energy companies operate, in some of the most volatile and corrupt regions of the world. It is not surprising, therefore, that many recent FCPA investigations and settlements relate to the oil industry in Africa, Central Asia, Latin America, and the Middle East. Nigeria, the largest oil producer in Africa and the eighth-largest producer in the world, is perennially singled out as one of the world's most

corrupt countries. A significant number of oil companies agreed to pay many millions of dollars in penalties for violating the FCPA in Nigeria.[14]

Medical device manufacturers also are likely to encounter foreign corruption, as they operate in an industry characterized by an unusual preponderance of state-owned customers. Almost all of the health-care providers in some countries, including hospital administrators and physicians, could be characterized under the FCPA as "government officials."

For medical device companies, these officials are the customer representatives charged with important purchasing decisions. Allegations of corrupt relationships with such individuals necessarily raise questions of FCPA compliance. It is not surprising, then, that in 2008 and 2009, a number of medical device manufacturers in the United States were sanctioned for alleged FCPA violations based on their sales activities abroad.[15]

With the success of their forays into the energy and medical device sectors, U.S. enforcement authorities are likely to look for similar patterns of illegal behavior between and among competitors in other industries. Any international business that shares key characteristics of the oil and gas or medical device industries should therefore pay careful attention to the activities of partners and competitors.

TRANSPARENCY INTERNATIONAL'S CORRUPTION PERCEPTIONS INDEX

Transparency International's Annual Corruption Perceptions Index ("CPI") ranks countries by their perceived levels of corruption, based on expert assessments and opinion surveys. In 2008, Denmark grabbed first place as the least corrupt country in the world. Somalia ranked as the most corrupt country in the world in 2007 and 2008, at No. 179 and No. 180, respectively. The following table indicates the CPI ranking for the countries in which some act of bribery has led to prosecution under the FCPA. In 2008, of the countries mentioned in this update, the United Kingdom was the least corrupt (16th out of 179), and Iraq was the most corrupt (178th out of 178).

	2002[16] (out of 102)	2005[17] (out of 158)	2007[18] (out of 179)	2008[19] (out of 180)
Angola	98	151	147	158
Azerbaijan	95	137	150	158
Bahrain	-	36	46	43
China	59	78	72	72
Costa Rica	40	51	46	47
Egypt	62	70	105	115
Ethiopia	59	137	138	126
Greece	44	47	56	57
India	71	88	72	85
Indonesia	96	137	143	126
Iran	-	88	131	141
Iraq	-	137	178	178
Italy	31	40	41	55
Kazakhstan	88	107	150	145
Kenya	96	144	150	147
Libya	-	117	131	126
Mexico	57	65	72	72
Nigeria	101	152	147	121
Oman	-	28	53	41
Qatar	-	32	32	28
Russia	71	126	143	147
Rwanda	-	83	111	102
Saudi Arabia	-	70	79	80
Senegal	66	78	71	85
Taiwan	29	32	34	39
Tanzania	71	88	94	102
Thailand	64	59	84	80
Turkey	64	65	64	58
United Arab Emirates	-	30	34	35
United Kingdom	10	11	12	16
United States	16	17	20	18
Uzbekistan	68	137	175	166
Venezuela	81	130	162	158
Vietnam	85	107	123	121
Zambia	77	107	123	115
Zimbabwe	71	107	150	166

Record Fines. Perhaps the most visible trend in FCPA enforcement has been the increase in financial penalties imposed by the DOJ and SEC. Fines hit a record $800 million in 2008, eclipsing the $44 million imposed in 2007.[20] By 2009, one penalty had exceeded $559 million.[21]

This trend has been driven in part by the growing willingness of the SEC to demand the disgorgement of profits from a corporation that violates the antibribery section of the FCPA.[22] In 2007, the SEC obtained a record $23 million in disgorged profits and prejudgment interest from a single defendant, along with a civil penalty of $10 million, for violating a 2001 cease-and-desist order prohibiting violations of the books-and-records and internal controls provisions of the FCPA.[23]

The record lasted for only one year. In 2008, the SEC ordered Siemens to disgorge $350 million in profits, in addition to the DOJ's imposition of a $450 million criminal fine. The company's internal investigation reportedly revealed €1.3 billion in questionable payments, including kickbacks to Iraqi government officials under the United Nations' Oil-for-Food Programme. The DOJ indicated that the "extraordinary" efforts Siemens made to cooperate with authorities and to improve internal compliance procedures mitigated the sentence imposed—which could have included $2.7 billion in criminal fines.[24]

DOJ OPINION PROCEDURE RELEASES

Under procedures promulgated by the DOJ, issuers and domestic concerns may seek and obtain "an opinion of the Attorney General as to whether certain specified, prospective—not hypothetical—conduct conforms with the Department's present enforcement policy regarding the antibribery provisions of the Foreign Corrupt Practices Act." 28 C.F.R. §80.1 (1992). Opinions issued by the Attorney General are published, albeit without specifically naming the companies and persons involved. While the Releases are binding only as to the requestor, the government's approach to specific fact situations can be a valuable source of guidance for companies and counsel when evaluating proposed courses of action.

The Uneasy Relationship With Government Customers. One question persists for businesses operating in markets with substantial government involvement: What kind of relationship may they cultivate with customers who are "foreign officials" for purposes of the FCPA? The FCPA permits "reasonable and bona fide" expenditures, such as travel and lodging expenses, that are "directly related to (A) the promotion, demonstration, or explanation of products or services; or (B) the execution or performance of a contract with a foreign government or agency thereof."[25] The contours of that exception remain unclear, particularly in different cultural contexts. May the company offer the employees of government entities—which are also customers—meals, entertainment, and other business courtesies? How should the company treat gift giving, if such a tradition exists in the country? Are the rules imposed by the FCPA more stringent than ethical rules that govern the recipient of the benefits?

The U.S. government has established a few outer boundaries of the "reasonable and bona fide" affirmative defense, effectively prohibiting luxury travel and entertainment with little or no business purpose. In December 2007, the DOJ and SEC settled a case with a U.S. company that spent upwards of $10 million on 315 sightseeing trips taken by approximately 1,000 Chinese government officials in 2002 and 2003. Destinations included Disneyland, Universal Studios, the Grand Canyon, and cities such as Los Angeles, San Francisco, Las Vegas, Washington, and New York. The trips, which cost between $25,000 and $55,000, typically lasted 14 days.[26] Significantly, the company is alleged to have booked the trips as "factory inspection" visits, despite the fact that it had moved all of its factories overseas.

At the other extreme, the DOJ has defined acceptable "reasonable" conduct in a fact-specific inquiry. In September 2007, the DOJ approved the payment of domestic expenses for a trip to the United States by an official six-person delegation from China for an "educational and promotional" tour of an operation site in the United States. The scheduled visit was for four days, the visitors had been selected by the foreign government, the travel was limited to domestic economy class, and the Chinese government planned to pay the cost of international airfare. The DOJ concluded that "based on the Requestor's representations . . . , the expenses contemplated are reasonable under the circumstances."[27]

Despite this guidance, many businesses are left wondering where to draw the line between "reasonable and bona fide" payments, as permitted by the Act, and entertainment that may constitute a violation of the law. The conduct proscribed in the settlements allegedly involved active deception in how the expenses were characterized. The travel allowed by the DOJ's Opinion Procedure Release is subject to so many caveats that it is of little value in planning future conduct. The undefined middle ground includes virtually all business courtesies, entertainment, travel, and other typical efforts designed to build customer relationships. Unfortunately, the government has not been forthcoming with additional guidance to fill this void.

Anticorruption Enforcement Outside the United States. While the United States continues to lead the fight against foreign bribery around the world, other countries are increasing their own anticorruption enforcement. This change is due in part to the Organisation for Economic Co-operation and Development's Anti-Bribery Convention, which sets forth standards for anticorruption legislation and enforcement in 38 signatory nations.[28] It can also be attributed to the increased resources the U.S. government has provided for anticorruption investigations worldwide. Not only has the United States bolstered the FBI and other agencies tasked with investigating FCPA violations, it has provided forensic training and technology to other countries. In many cases, FCPA-trained attorneys have been placed in foreign embassies to assist foreign governments with ongoing investigations.[29]

Many of these prosecutions stem from the United Nations' Oil-for-Food Programme scandal. In 2005, an independent inquiry committee of the United Nations chaired by former Federal Reserve chairman Paul Volcker issued two reports detailing an investigation into corrupt payments made by thousands of corporations and individuals to officials in the Iraqi government. Many of the companies implicated in the scandal now face prosecution in the United States, the United Kingdom, Italy, Ireland, Switzerland, and the Netherlands.

In June 2008, the OECD reported that 16 signatory countries had significant enforcement activities, up from 14 in 2007 and 12 in 2006.[30] By 2009, however, enforcement patterns were uneven—with active enforcement in only four of the 38 signatory nations and little or no enforcement in 21 others.[31]

Most countries have a long way to go before their anticorruption enforcement matches that of the United States. A recent operational note published by the United Kingdom's Serious Fraud Office ("SFO") suggests that the United Kingdom is taking significant steps to change the way it investigates and prosecutes cases of foreign corruption. On July 21, 2009, the SFO issued a note describing the new resources it had devoted to anticorruption enforcement and suggesting that companies would benefit from self-reporting violations and establishing effective compliance programs. Commentators called the note an "enforcement blueprint" modeled after the DOJ's enforcement of the FCPA.[32]

The SFO attributed its new approach to the anticipated adoption of an anticorruption law that Britain's Justice Secretary, Jack Straw, promised would "simplify and modernize" the United Kingdom's existing restrictions on overseas bribery. The U.K.'s current prohibition against foreign bribery represents a patchwork of common law and statutes dating back to 1889.

Country	2007 Cases	2008 Cases	Percent of World Exports 2007
Australia	1	6	1.06
Belgium*	2	3	2.90
France	17	17	4.11
Germany	>43	110	8.80
Hungary	23	24	0.58
Japan	1	2	5.15
Korea (Republic of)	9	9	2.20
Netherlands	7	7	3.69
Norway	4	5	1.04
Switzerland	16	16	1.31
United Kingdom	4	4	4.56
United States	103	125	9.84

** In 2008, Belgium brought 10 additional corruption cases on behalf of the European Union.*

Source: Transparency International

The draft bill is in a consultation period and is expected to be brought into law early in 2010, although there are some key issues still to be resolved. For example, a strict reading of the draft bill may prevent U.K. corporate entities from being held responsible and prosecuted by the SFO for bribery carried out by an overseas subsidiary. The new law would create two general bribery offenses, one concerned with giving bribes and one concerned with taking them; a new offense of bribing a foreign public official; and a new corporate offense applicable to companies and LLPs for negligently failing to prevent bribery by an employee or agent.

The SFO was formed in 1988 with the single objective of investigating and prosecuting serious and complex fraud. A decade later, its average conviction rate was 61 percent and falling (down from 85 percent), with at least three high-profile and expensive prosecutions collapsing on technicalities at the start of trial. In June 2008, the SFO endured an embarrassing and frank assessment by a former Assistant U.S. Attorney, Jessica de Grazia, who was hired by the U.K.'s Attorney General to identify how the organization could be improved. In her "private and confidential" report, de Grazia painted what *The Times* (of London) called a "graphic picture of a law enforcement agency that was manifestly unfit for purpose."[33]

The U.K. government's response was to appoint a new SFO director, Richard Alderman, with a mandate to carry out a root-and-branch review of the organization. Following sweeping internal changes, Mr. Alderman signaled that the SFO would be investigating and prosecuting cases of overseas corruption with increasing vigor. Legal commentators noted a level of irony in the SFO's announcement. Only a few years ago, the government of the United Kingdom garnered significant international criticism for ordering the SFO to discontinue an investigation into alleged corrupt payments made by a U.K. company to officials in Saudi Arabia in connection with a politically sensitive defense contract.

Additional information on the draft U.K. law is available in the *Jones Day Commentary* "Bribery and Corruption Reform: Proposed Modern UK Laws Target Companies and LLPs" (Mar. 2009), available at www.jonesday.com.

China's domestic anticorruption activities have also increased in recent years, and fighting corruption emerged as a priority for the Chinese Communist Party in January 2009.[34] Many other Asian nations are taking steps to tackle endemic corruption, creating a mosaic of disparate business environments across the continent. For example, while China ranks 132nd out of 179 in the Index of Economic Freedom created by *The Wall Street Journal* and The Heritage Foundation,[35] Hong Kong, a Chinese Special Administrative Region, is ranked No. 1.

For more in-depth information regarding the impact of FCPA compliance in China, see "The Foreign Corrupt Practices Act: Walking the Fine Line of Compliance in China," *Jones Day Commentary* (Sept. 2008), available at www.jonesday.com.

Impact on Transactions With Foreign Partners. The FCPA has had a dramatic impact on the way cross-border mergers and acquisitions are conducted. When acquiring a foreign target, American companies have an even greater need to perform thorough due diligence—a process that is often complicated by the protective legal regimes of other jurisdictions. In a 2008 FCPA Opinion Procedure Release, the DOJ indicated that where United Kingdom laws made thorough due diligence impossible, a company could evade liability under the FCPA by disclosing any and all violations committed by the target as soon as possible after the transaction. The threat of that immediate exposure to liability for the target company, and its executives, proved unpalatable and the deal ultimately crumbled.[36] In other consummated transactions, the prompt disclosure of FCPA violations appears to have mitigated the penalties imposed on the successor company.[37]

The FCPA also raises numerous concerns for American companies engaged in joint ventures with foreign partners. While an American company may exercise varying degrees of control over the venture itself or a specific transaction, it must take steps to ensure that it will not make payments towards, operate under, or benefit from any contract obtained or maintained by its foreign business partner through bribery.[38] This continues to present difficulties for businesses with overseas operations.

An Increase in the Number of Civil Actions. Civil litigation may result in additional liability for companies subject to the FCPA. So far, such cases have been rare. If they increase in number, however, they could significantly raise the defense cost of companies targeted by plaintiffs.

The FCPA does not provide a private right of action, so it remains to be seen whether civil litigation will ever become a real risk. Nevertheless, several plaintiffs have filed suits against companies purportedly engaged in bribery overseas. In some cases, companies and individuals engaged in prolonged business disputes sought to use the Racketeer Influenced and Corrupt Organizations Act ("RICO") as a means of recovery against former partners or competitors. Other groups of shareholders have filed derivative suits against U.S. corporations that settled enforcement actions with U.S. government authorities for FCPA violations.[39] In one other case, the Republic of Iraq filed a civil suit in the United States

District Court for the Southern District of New York against two individuals and nearly 100 companies implicated in the Oil-for-Food Programme scandal. Iraq alleged various RICO violations, common-law fraud, and breach of fiduciary duty.

No theory put forward thus far in civil FCPA cases shows a high probability of creating widespread litigation exposure for U.S. businesses. The growth of enforcement activity by the DOJ and SEC, however, raises the possibility that plaintiffs' attorneys will come upon a viable theory by which to start such litigation. These few cases may represent the first efforts in that direction.

CONCLUSION

The FCPA will continue to generate headlines in the coming years, as enforcement continues in the United States and abroad. As this area of the law matures, ethical businesses can better identify the practices and standards that constitute an effective compliance effort. Ideally, affirmative guidance from enforcement authorities will permit businesses to act as partners, rather than potential targets, in the fight against corruption. Either way, the risk to businesses shows no sign of receding.

ADDITIONAL INFORMATION

For further information, please contact your principal Jones Day representative, R. Christopher Cook (+1.202.879.3734; christophercook@jonesday.com), or one of the lawyers listed in this publication. General email messages may be sent using our "Contact Us" form, which may be found at www.jonesday.com.

ENDNOTES

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39 Baker Hughes has defeated three derivative suit actions based on its 2007 settlement for FCPA violations; *see* Andrew Longstreth, "Texas Judge Dismisses FCPA-Based Derivative Suit Against Baker Hughes," The AmLaw Litigation Daily (June 1, 2009), *available at* http://www.law.com/jsp/tal/digestTAL.jsp?id=1202431128281&Texas__Judge__Dismisses__FCPABased__Derivative__Suit__Against__Baker__Hughes. On May 14, 2009, a derivative class action was filed in Texas against officers and directors of Halliburton and its one-time subsidiary, KBR. The suit alleges "a laundry list of misdeeds," including a Nigerian bribery scheme that led to the companies' $579 million FCPA settlement in February. The plaintiffs allege that some of the officers and directors of Halliburton and KBR breached their fiduciary duty to provide oversight. *Policemen and Firemen Retirement System of the City of Detroit Pension Fund, Derivatively and on behalf of Halliburton Company and KBR, v. Albert O'Cornelius Jr. et al.*, In the District Court of Harris County, Texas (May 14, 2009). A derivative suit was also filed by shareholders of Pride International. *See Kyle Arnold, Derivatively on behalf of nominal defendant Pride International Inc., v. Paul A. Bragg, et al.*, In the District Court of Harris County, Texas (Oct. 14, 2009), *available at* http://www.courthousenews.com/2009/10/19/Pride.pdf.

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