Mergers & Acquisitions and Anti-Corruption Compliance

Tuesday, February 14, 2012

As the economy improves and merger activity increases, it is important to remember the risks of FCPA liability when acquiring a company or entering into a joint venture. Simply put, you don't want to acquire an FCPA violation.

Companies will sometimes rush to close a deal without conducting any due diligence — that is a recipe for disaster. On the other hand, companies alert to the risks have been able to avoid successor liability altogether or, more frequently, to obtain assurance about the scope of potential FCPA liability before the transaction is complete.

Since an acquiring company may be held criminally liable for FCPA violations committed by the target company both before and after closing, pre-closing due diligence is critical to assessing risks and avoiding liability. Additionally, the party should request measures for good governance, accurate recordkeeping and anti-bribery efforts, seek audit rights, anti-corruption representations and written commitments to abide by anti-corruption laws; even if these requests aren't honored, a record of such requests could help protect against or minimize FCPA exposure for the company. For joint ventures, the company can be held liable for the future conduct of the joint venture, but it depends on the governance proportion of the JV or majority company (e.g. board members, voting rights).

FCPA enforcement actions have centered on failures to identify or correct bribery schemes after an acquisition. In 2004, the proposed merger between Lockheed Martin Corporation and Titan Corporation, a military intelligence and communications company, collapsed following the discovery of FCPA violations during pre-acquisition due diligence. After Lockheed Martin discovered the potential FCPA concerns at Titan during its due diligence, the parties jointly disclosed the matter to the DOJ. Lockheed and Titan pushed back the closing date of the merger two times in order to allow Titan time to settle the matter, but the merger collapsed in June 2004 after Titan was unable to resolve the DOJ's investigation. Later, on March 1, 2005, both the DOJ and SEC announced settlement of FCPA enforcement actions filed against Titan. Titan pleaded guilty to violating the anti-bribery and books and records provisions of the FCPA, as well as a criminal tax violation, arising out of Titan's decision to employ a third-party agent to assist on a project to build a wireless telephone network in Benin, and agreed to a criminal fine of $13 million, and a civil disgorgement penalty of $15.4 million to the SEC.

More recently, Snamprogetti, a subsidiary of ENI, engaged in a bribery scheme for 10 years ending in 2004. In 2006, ENI sold Snamprogetti to another company, Saipem. And yet, four years later, in 2010, Snamprogetti was charged with FCPA criminal violations and agreed to a $240 million fine (ENI and Saipem were jointly liable for the fine).

In 2005, Dimon Inc. and Standard Commercial Corporation merged to form Alliance One. Five years later, DOJ brought a criminal case against Alliance One for FCPA violations committed by foreign subsidiaries of Dimon and SCC before the merger. The foreign subsidiaries entered guilty pleas and

Alliance One was required to cooperate and retain an independent compliance monitor for three years.

The scope and depth of FCPA due diligence, which must include an assessment of bribery, books and records, and internal controls risks, will depend on factors such as the nature and location of the company's business. For example, a business model that involves frequent interaction with government regulators or customers may require more scrutiny than one that does not.

In addition, the nature of the business may require scrutiny of specific areas, including, inter alia, political contributions, lobbying activities, and payments to customs agents. The FCPA due diligence inquiry is ultimately a risk-based assessment – an assessment of financial controls, business locations, use of third-party agents, prior internal investigations, FCPA compliance culture (e.g. existence of training/employee discipline or hotline reporting system), and the company's overall compliance structure, including corporate policies, training and audit practices, and scrutiny to determine whether certain expenses—such as travel, gifts, and entertainment—have been used to benefit government officials.

In addition, there are basic purchase agreement protections against FCPA liability. Specifically, the agreement may include provisions such as warranties and indemnifications against possible FCPA violations, participation in transactions permitted under local law, absence of government owners in company, no corrupt payments were made to foreign officials, and that the books and records are complete and accurate.