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A legal update from Dechert LLP

DOJ and SEC Issue Foreign Corrupt Practices Act Guidance

On November 14, 2012, the U.S. Department of Justice ("DOJ") and Securities and Exchange Commission ("SEC") released a rare and comprehensive publication entitled "A Resource Guide to the FCPA," which sets forth guidance regarding the U.S. Foreign Corrupt Practices Act ("FCPA").[1]

As is well-known, the FCPA prohibits bribery – more specifically, it prohibits ***giving, offering, or promising anything of value to foreign officials for the purpose of inducing or influencing the foreign official to misuse his or her official position to obtain or retain business***. The FCPA applies (1) to all U.S. persons and issuers of securities regardless of where the bribe is paid, and (2) to any person or entity (i.e., even non-U.S. persons or issuers) if any act in furtherance of the bribe took place in the United States. The Act also requires U.S. issuers to record accurately all payments in their books and records.

While the much-anticipated guidance breaks little new legal ground and is non-binding, it is an essential consolidation of the government's positions on many issues that frequently arise under the FCPA, including the definition of a foreign official, the propriety of travel and entertainment expenses, successor liability following mergers for FCPA violations, the characteristics of an appropriate corporate compliance program, and potential outcomes and penalties for FCPA violations. The guidance also provides numerous case studies and examples of conduct that would or would not likely lead to enforcement action.

The reality remains that many issues that arise in the context of potential FCPA violations are very much fact-specific and still require difficult judgment calls to assess the extent of potential law enforcement interest. While the following is by no means a comprehensive description of the contents of the 120-page guidance, highlights include:

Definition of a Foreign Official:

- The DOJ and SEC reiterate their previously stated position that the definition of a foreign official is very broad and includes anyone employed by or acting on behalf of a foreign government, regardless of seniority.
- The definition also includes employees of state-owned enterprises. Such enterprises include, for instance, hospitals in countries where the healthcare system is state-run, utility companies, and any company that is an "instrumentality" of a foreign government.
- The guidance provides a list of factors, culled from actual jury instructions, to consider in determining of whether a given entity is an "instrumentality" of a foreign government.[2] These factors include, but are not limited to:
  - The extent of government ownership
  - The extent of government control (an entity is unlikely to be considered a government instrumentality if the government neither owns nor controls a majority of the shares)
  - How local law characterizes the entity and its employees
  - The purpose of the entity's activities
  - The level of financial support from the government

Third Parties:

- The guidance reiterates the existing policy: Actions through a third party are covered by the FCPA and therefore a company must take care to examine potential "red flags" associated with third-party agents or intermediaries. Such red flags may include:
  - Excessive commissions or unreasonably large discounts
  - Agreements that only vaguely describe the services to be provided
  - The agent is not in the line of business for which it is hired
  - The agent is affiliated with a foreign official or was suggested by a foreign official
  - The payment is to an offshore account

Gifts, Travel, and Entertainment:

- Clients frequently express concerns about whether payments for gifts, travel and entertainment for business partners who may be deemed foreign officials are permissible. The text of the FCPA does not explicitly exclude amounts under a certain dollar threshold or carve out a "de minimis" exception.
- However, the guidance provides more color than the government had previously provided on what sorts of hospitality are acceptable, reiterating what seasoned practitioners have often advised clients:
  - Items of nominal value such as cab fare, reasonable hospitality expenses, and company promotional materials are unlikely to be deemed to evidence any corrupt intent and therefore are unlikely to lead to an enforcement action
  - Extravagant gifts (for instance, sports cars or other luxury items, trips lasting two weeks and costing $25,000 to $55,000) may well violate the Act
  - Frequent smaller gifts or travel for which there is no legitimate business purpose (for instance, expenses for frequent "training" trips when training did not occur during many of the trips) or expenses paid for family members may also violate the Act
- All expenses – small or large – must be accurately described in the company's books and records.

Corporate Liability, Including Successor Liability:

- A parent may be liable for a subsidiary's actions: (1) directly, if the parent is itself sufficiently involved in the corrupt activity, or (2) under traditional agency principles.
- Successor liability: An acquiring company generally acquires its target's liabilities, including liability for violations of the FCPA. If an entity that is subject to the FCPA acquires an entity that was not previously subject to the FCPA, however, any actions taken by the acquired entity before the acquisition are not subject to the Act. Plainly, if the acquired company's wrongful conduct continues after the acquisition, such post-acquisition conduct would be subject to the Act, though the government would take into account the acquiring company's efforts to detect and eliminate the corrupt activity. Acquirers should take steps such as:
  - Conducting thorough risk-based anti-corruption due diligence
  - Ensuring that their code of conduct and compliance policies and procedures apply to the target company as soon as possible
  - Training officers, directors, and employees of the target company
  - Conducting an FCPA-specific audit
  - Promptly reporting any corrupt payment detected

Adequate Corporate Compliance Program:

- The guide explains that, as the agencies have previously noted, the adequacy of a company's compliance program is a factor considered by the DOJ and SEC when deciding what, if any, action to take against a company, but an adequate compliance program does not provide an absolute defense (unlike the U.K. Bribery Act).
- In evaluating a company's compliance program, the agencies focus on how well the compliance program is designed, whether it is being applied in good faith, and how well the program works.
- The guidance does not provide any strict requirements for compliance programs, nor do any particular features guarantee non-prosecution.

- Instead of a “check-the-box” list, the resource guide explains certain hallmarks of an effective compliance program, including:
  - Commitment from senior management
  - A clearly articulated policy against corruption
  - A code of conduct
  - Compliance policies and procedures detailing internal controls, auditing practices, and document policies
  - Senior executives are responsible for the oversight and implementation of the compliance program and have the appropriate autonomy and resources from management
  - The degree to which a company analyzes the particular risks it faces
  - Training throughout the company
  - Enforcement through incentives and disciplinary measures
  - Monitoring of third parties (including agents, consultants, and distributors) through due diligence
  - The availability of a mechanism for employees to report potential violations in a confidential manner
  - An internal investigation process for investigating complaints
  - Continuous improvement through periodic testing and review
  - In the context of mergers and acquisitions, pre-acquisition due diligence and post-acquisition integration

Accounting Provisions:

- The Act requires issuers to “make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer” and to have adequate internal controls.
- The accounting section of the FCPA carries potentially higher penalties than the anti-bribery section and is likely to be implicated almost any time a bribe has been paid, as well as in instances when not all the elements for a bribery offense are present, but a payment has been mischaracterized in some way.
- The guidance explains that bribes are often mischaracterized as:
  - Commissions
  - Consulting fees
  - Travel and entertainment fees
  - Petty cash withdrawals
  - Supplier/vendor payments
- FCPA accounting provision violations may lead to certain anti-fraud and reporting violations under the Exchange Act or Sarbanes-Oxley Act.
- Companies and individuals can be held criminally liable for willful accounting violations.

Resolutions and Penalties:

- The guidance describes various possible resolutions of criminal FCPA cases (DOJ), including declinations, plea agreements, deferred prosecution agreements, non-prosecution agreements, and trial.
- The guidance describes various possible resolutions of civil FCPA cases (SEC), including civil injunctive actions and remedies, civil administrative actions and remedies, deferred prosecution agreements, non-prosecution agreements, termination letters, and declinations.

When Do the Agencies Decline To Prosecute?

- The guidance provides a rare window into cases in which the agencies declined to prosecute or institute enforcement actions (declination) despite the presence of bribes or attempted bribes. While these six examples cannot be taken as any promise of future action by the government, certain patterns among the cases emerge:
  - All six companies voluntarily self-disclosed
  - All companies had robust compliance programs and/or undertook substantial remedial actions to improve their programs when the problems came to light

- In at least some of the cases, the companies terminated the relationship with the offending party, whether a third-party agent or an employee
- At least three of the cases concerned “small” or “relatively small” bribes

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While this unusual release by the DOJ and SEC is a welcome development, it is not a panacea. Difficult judgment calls about potential exposure will remain, and unique fact patterns, not clearly addressed by the guidance, will arise on a regular basis. Indeed, the guidance itself emphasizes that many areas of FCPA enforcement are subject to multi-factor tests – not bright-line rules.

Dechert is available to investigate potential violations, assist in responding to government inquiries, draft FCPA compliance policies and procedures, provide training, or discuss any other questions or concerns you may have about the FCPA or its U.K. analog, the U.K. Bribery Act.

Footnotes

1 The Criminal Division of the U.S. Dep’t of Justice & the Enforcement Division of the U.S. Securities and Exchange Commission, *FCPA: A Resource Guide to the U.S. Foreign Corrupt Practices Act* (Nov. 2012).

2 The U.S. Court of Appeals for the Eleventh Circuit will soon hear a case that challenges the expansiveness of the government’s position on what constitutes a government instrumentality. *See United States v. Esquenazi*, No. 11-15331 (11th Cir.).

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