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A Client Alert from Paul Hastings

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Guidance on the U.S. Foreign Corrupt Practices Act from the Department of Justice and the Securities & Exchange Commission: The Key, as with the U.K. Bribery Act and the OECD Anti-Bribery Convention, Is a Robust Compliance Program

BY THE GLOBAL COMPLIANCE AND DISPUTES PRACTICE GROUP

Introduction

A year in the making and on the eve of a major FCPA conference, on November 14, 2012 the Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") issued a joint publication called the *Resource Guide to the U.S. Foreign Corrupt Practices Act* ("Guide") which outlines the government's interpretation of the law, provides insight into the government's enforcement priorities, and provides a tangible and concrete understanding of how the government exercises its discretion.[1] The Guide grew out of discussions with various interest groups, including large NGOs like Transparency International, industry groups such as the U.S. Chamber of Commerce, small- and mid-sized businesses, corporate compliance counsel, and investor groups. Senior DOJ officials advised that the Guide reflects the government's good faith effort to explain their interpretation of the FCPA and to reassure companies that the government will consistently enforce the FCPA.

Although the Guide does not change the way the FCPA will be enforced or add the corporate defenses businesses sought akin to those in the U.K. Bribery Act, it helpfully summarizes the current body of DOJ and SEC opinions, leading cases, and enforcement practices. Most useful, the Guide sets out hypothetical examples of what conduct is prohibited and includes multiple examples, based on real-life investigations, where the government declined to prosecute. It adds little that is new for large multinational companies or those in highly regulated industries that have been grappling with the FCPA and its nuances for decades; however, it does provide helpful insights for small- and mid-sized companies that are beginning to develop anti-corruption compliance policies and programs.

This alert highlights key aspects of the Guide, comparing it to the guidance offered by the U.K. Ministry of Justice ("MOJ") and Serious Fraud Office ("SFO") clarifying the U.K. Bribery Act and the OECD Guidelines clarifying the OECD's Convention on Combating Bribery of Foreign Public Officials ("Anti-Bribery Convention").

Definition of Foreign Officials

The Guide does not restrict the definition of foreign official, as the U.S. Chamber of Commerce and other interest groups had sought. Rather, it reinforces the interpretation that low-ranking employees and senior officials of any department, agency, or instrumentality of a foreign government are considered "government officials" under the FCPA (p. 20). The Guide reinforces that the FCPA prohibits payments to *foreign officials* rather than *foreign governments*, and is intended to prevent payments that have a corrupt purpose, such as benefiting a government official personally (p. 20). This explanation, however, may create more confusion because the enforcement actions cited in the accompanying footnote illustrate that payments to foreign governments may violate the FCPA's accounting provisions, without violating its anti-bribery provisions, and may be prohibited by other U.S. statutes, such as those addressing wire fraud or money laundering. This is similar to the government's treatment of commercial bribery which is not covered by the FCPA; commercial bribery offenses are prosecuted under other statutes (such as the Travel Act) with associated violations of the FCPA's books and records and accounting provisions.

The Guide reaffirms that employees and officials of "instrumentalities" of foreign governments, such as state-owned or state-controlled entities, are considered government officials, but explains that a "fact-specific" analysis of an entity's "ownership, status, and function" is necessary to determine whether it constitutes an instrumentality (p. 20). The Guide lists a series of factors, derived from recent case law, to be considered when assessing FCPA application, namely the foreign government's ownership percentage and degree of control; the government's own characterization of the entity; and the purpose of the entity's activities. The Guide implies that the most important factors will be whether the foreign government has majority ownership, or in the absence of a majority ownership, if the foreign government exerts practical control over the entity (p. 20). These factors do not provide the much-sought clarification for partially state-owned or controlled entities. For example, in certain markets, it may be difficult for a U.S. company to determine the ownership structure, or the practical degree of control that a foreign government might exert over a partially state-owned, or even a private company, and the difficulties are compounded when the analysis is done by sales representatives or third party agents based in the foreign country who are not lawyers.

The DOJ and SEC recognize that the level of ownership and control is not always transparent, so if a company, after a good faith analysis, determines that an entity is not a government instrumentality, it would be difficult for regulators to later prove that the company had knowledge the payment was being made to a foreign government official, a necessary element of an FCPA bribery charge. According to a senior DOJ official, the company would receive "meaningful credit" in this scenario, provided that its goal was to prevent bribery, regardless of whether the recipient is a government official or an employee of a private, commercial enterprise.

Improper & Proper Payments & Gifts, Attempting to Define "Anything of Value"

Corrupt Intent

The Guide stresses that the FCPA prevents payments and gifts that are "corruptly" offered, made, or given to induce a government official to "misuse his official position", such as improperly directing business to the payor. Accepting recent court interpretations that a defendant's conduct must be "willful", the Guide states that willful conduct is voluntary and purposeful and committed with "knowledge that [a defendant] was doing a 'bad' act under the general rules of law" (p. 14).

In contrast to other anti-bribery laws, the Guide does not establish a precise cut-off for what constitutes something of value. Rather, it reiterates that payments and gifts must be given with "corrupt intent" in order to create liability. The Guide reflects that items of nominal value are unlikely to create the requisite indicia of intent and "a small gift or token of esteem or gratitude is often an appropriate way for business people to display respect for each other" (p. 15). It also contrasts the payment of cab fare and reasonable meal and entertainment expenses with extravagant gifts such as cars, fur coats, and other expensive items (p. 15). Items of low value, however, may be improper if they are part of systematic or long-standing schemes to make improper payments. Senior DOJ and SEC officials advised at the recent ACI Conference that the government does not apply a "sliding scale" analysis to assess the propriety of a gift, in that it does not compare the value of a gift relative to the size of a bid or desired contract.

This explanation may be helpful to companies unfamiliar with FCPA compliance, but for larger companies with established anti-corruption compliance programs, the Guide does not offer any new guidance on what types of gifts and expenses a company may cover. In contrast, some countries, like the People's Republic of China, set clear dollar limits on gifts to government officials.

Travel, Lodging, and Entertainment Examples

The most practical guidance on the propriety of gifts, travel, and entertainment expenses appears in an extended hypothetical. The Guide states that if a customer's senior executives are required to inspect a selling company's facilities in Michigan over several days, the selling company may pay for business class airfare, hotel costs, ground transportation costs, a moderately-priced dinner, and entertainment expenses to attend a play and a baseball game (pp. 17-18). The Guide contrasts this example with the selling company paying for the same executives and their spouses to travel to Las Vegas, where the company has no facilities, for an all-expenses-paid, weeklong stay (p. 18). Although as described, the business travel expenses in the first example seem reasonable and tied to a clear business purpose, what if the company's facilities were located in the NYC area, and the entertainment involved balcony seats at the opera and luxury box tickets to a Yankees postseason game? What if, under the pretense of airport security measures, the customer's executives requested that the selling company wire the full cost of the business airfare in advance, or requested that individual executives be given a daily per diem fee over which they have discretion to cover their hotel and "reasonable" meal expenses? These nuanced questions still remain, despite the 130 page Guide, and companies must evaluate such expenses on a case-by-case basis and document their rationale.

At the recent ACI Conference, the government elaborated on the travel example and explained that when a company flies its own employees in business class, flying its customers of equal seniority in business class does not create the appearance of impropriety. However, if the CEO of the company is the only executive with access to a corporate jet, it would be improper to fly customers on the same corporate jet. The government will defer to a company's policies and practices, provided they reflect legitimate, reasonable business expenditures and a fair, thoughtful process, consistent with or informed by current case law and, now, this Guide.

Best Practices

There seems to be a conspicuous absence of guidance regarding the pre-approval of customer expenses. The Guide states that companies should have "clear and accessible guidelines and processes in place for gift-giving" and "larger companies have automated gift-giving clearance processes and . . . set clear monetary thresholds for gifts" (p. 16). While it is unclear what the Guide

means by "automated gift-giving" and how automated processes would weigh factual nuances and contexts, it is interesting that the Guide speaks approvingly of dollar limits set by companies, without itself setting clear gift limits applicable across industries and geographies.

Current best practices for the payment of travel, lodging, entertainment, and gift expenses require certain expenses involving government officials to be pre-approved in writing by compliance officers, with the business purpose clearly specified. At a minimum, written pre-approval should help prevent the accounting violations which have led to significant settlements in recent years. Some companies have gone to greater lengths to avoid FCPA liability and have implemented policies such as prohibiting all gifts to government officials or prohibiting the reimbursement of all entertainment expenses for government officials in light of conflicting global anti-corruption laws to which a multinational company may be bound.

Facilitating/Expediting Payments

While other global compliance laws prohibit facilitation payments entirely, and it is often considered best practice to avoid facilitation payments, the Guide reinforces the FCPA's exception for payments made "in furtherance of a routine government action." Examples of routine actions include obtaining licenses or permits, and processing government papers. The Guide makes a distinction between payments made to officials for routine actions that do not require discretion and payments made to officials to expedite acts that are within an official's discretion (p. 25). The Guide points out that, even though facilitating payments may be appropriate in some cases under the FCPA, recording a bribe as a "facilitating payment" made to further routine government actions does not absolve a company of responsibility to ensure that the payment meets the requirements of this exception (p. 25).

In practice, there may be no way for a company to know whether acts are within a foreign official's discretion or whether expediting a routine government act does not create an improper business advantage. Companies should be cautioned that the DOJ has taken a skeptical eye as to whether payments to government officials deemed routine by companies are true facilitation payments. Moreover, the U.K. Bribery Act and the OECD Anti-Bribery Convention prohibit all facilitation payments, so multinational companies are increasingly moving toward prohibiting these payments, with individual exceptions expressly approved by the Legal or Compliance Department.

Successor Liability

The Guide explains that the FCPA may create successor liability, however, it notes that if a predecessor was not previously subject to the FCPA (for example the predecessor company did not operate in the U.S., did not issue stock in the U.S., and was not otherwise subject to FCPA jurisdiction), a successor company that is subject to the FCPA cannot be liable for the predecessor's past conduct, provided the offending conduct does not continue post-closing (p. 28). The Guide stresses the need for due diligence during the merger/acquisition process because it helps companies assess their post-merger liability, reduces the likelihood that the company will pay bribes in the future, helps allocate costs of investigation and compliance before the merger is completed, and demonstrates to the DOJ and SEC that the company made a genuine effort to avoid FCPA violations. Lastly, the Guide reinforces the government's willingness to show leniency to successor companies that uncover compliance issues during a merger/acquisition and voluntarily disclose their findings (p. 28).

Liability for Acts of Foreign Subsidiaries

Senior DOJ and SEC officials at the ACI Conference reinforced the notion that a parent company can be held liable for acts of its subsidiaries, as is customary in federal law and pursuant to traditional agency principles. However, the mere fact of ownership does not automatically render the subsidiary the parent's agent, and the government will evaluate the nature of the relationship between a parent and subsidiary. Importantly, even where a parent company lacks sufficient control over the foreign subsidiary, or other circumstances prevent the DOJ from pursuing criminal violations against a parent for the actions of its subsidiary, the SEC may still be able to pursue civil enforcement of books and records violations against the parent company arising out of its subsidiary's improper conduct.

Corporate Compliance Programs

The Guide states that a proper compliance program "promotes 'an organizational culture that encourages ethical conduct and a commitment to compliance with the law.'" The DOJ and SEC do not have specific requirements, but generally ask whether: the company's compliance policy and procedure is "well-designed"; the company applies their compliance policy in "good faith"; and the policy works in practice (p. 56). However, the Guide goes on to state that good compliance policies are characterized by: commitment from senior management; clearly-articulated anti-corruption policies, codes of conduct and procedures; sufficient compliance authority and oversight assigned to one or more specific officers or executives; and sufficient resources and autonomy necessary to implement and enforce the policy. An effective compliance program includes a risk assessment tailored to a company's business and markets, ongoing training and advice, due diligence on third parties, disciplinary and other remedial measures, confidential reporting and investigation, and periodic testing and review (pp. 57-62). Again, this is nothing new but rather a restatement of best practices.

Penalties, Sanctions, Remedies, and Resolutions

In addition to the well-known criminal penalties and civil fines, the Guide describes collateral consequences where a company may be barred from doing business with the United States government and with international development banks, as well as losing the right to export products (pp. 69-71). The Guide also acknowledges a growing trend where a compliance monitor or independent consultant may be appointed to ensure future FCPA compliance. In deciding whether to appoint a monitor, the government may consider the "Seriousness of the offense; Duration of the misconduct, Pervasiveness of the misconduct, including whether the conduct cuts across geographic and/or product lines; Nature and size of the company; Quality of the company's compliance program at the time of the misconduct; [and] Subsequent remediation efforts" (p. 71).

Most helpfully, the Guide lists examples of joint DOJ/SEC declinations and describes what factors influenced their decisions not to pursue further enforcement actions. Examples of corporate conduct viewed favorably by the SEC/DOJ include: voluntary disclosure, conducting thorough internal investigations after learning of potential improper conduct, terminating or disciplining employees involved in improper conduct, taking remedial steps to improve compliance policies and other corrective measures, and severing business ties with third parties engaged in improper conduct. The Guide also implies that the government will consider whether the total amount of improper payments is relatively small (pp. 77-79).

Subsequent Corrections

At the ACI Conference, the government noted that there were two corrections to be made in the Guide: 1) on page 43, when discussing liability related to joint ventures, the Guide implies that less than 50% ownership may be sufficient to impose a responsibility to implement compliance programs; however, the FCPA requires that minority owners only use good faith efforts to maintain a joint venture's books and records and to implement other internal controls; and 2) the Guide mistakenly states that a company's responsibility for maintaining books and records extends to its joint venture *partner*; the text should simply read that a company's responsibility for maintaining accurate books and records extends to the joint venture.

Comparison with Recent U.K. Bribery Act Guidance

Although the Guide references the U.K. Bribery Act and the OECD Anti-Bribery Convention, it does not resolve any of the differences between those regulations and the FCPA. In contrast to the FCPA, the U.K. Bribery Act allows (in an effort to moderate the effect of imposing strict liability) corporate defendants to plead the existence of adequate compliance policies as a *defense*. As the Guide makes clear, in FCPA enforcement actions, the government may consider the existence of a proper compliance policy when deciding to prosecute or show leniency, but the existence of compliance policies cannot be used by a defendant as an affirmative defense. The U.S. Chamber of Commerce and other business groups had sought such a defense and modification of the FCPA following the enactment of the U.K. Bribery Act.

The U.K.'s MOJ released its own guidance on the U.K. Bribery Act, which was followed by the SFO's "revised" guidance in October 2012.[2] The initial guidance reinforced that it is a "full defence for an organisation to prove that despite a particular case of bribery, it nevertheless had adequate procedures in place to prevent persons associated with it from bribing" (¶ 1). The MOJ also restated the complete ban on facilitation payments (¶ 44). The MOJ's guidance sought to clarify a company's liability for bribes by anyone "associated" with it, and explained that this covers employees, contractors acting on behalf of the company, other entities under contract with the company, and in some cases other parties to a joint venture. Similar to the Guide, the MOJ explained that prosecutors will look to the degree of control exercised over the associated persons in determining a company's liability. Interestingly, the MOJ acknowledged that companies which may have received an "indirect" benefit from bribes made by the employees of a joint venture will not necessarily be liable under the U.K. Bribery Act (¶¶ 37-43).

The MOJ deferred for future court interpretation the issue of whether shareholders may face liability simply because their company is listed on a U.K. stock exchange, but implied that this connection does not necessarily bring the investors under the Act's jurisdiction (¶¶ 34-35). Similarly, the MOJ also deferred for court interpretation the question of whether a parent company may be held liable simply because its U.K. subsidiary, while acting independently, failed to prevent bribes (¶ 42).

The SFO's revised guidance sought to address issues regarding self-reporting and to make clear that violations of the U.K. Bribery Act would be prosecuted, because interpretations of the MOJ guidance suggested leniency. The revised guidance states that even when a company self-reports, "the SFO will prosecute if it is in the public interest to do so", or if based on the evidence, "there is a realistic prospect of conviction." Similar to FCPA enforcement, the revised guidance seems to codify the prosecution's discretion to proceed and how it may weigh a company's self-reporting, stating that "for a self-report to be taken into consideration as a public interest factor tending against prosecution, it must form part of a 'genuinely proactive approach adopted by the corporate management team when

the offending is brought to their notice.'" The revised guidance reiterates that "bona fide hospitality or other business expenditure is recognized as an established and important part of doing business" while "bribes are sometimes disguised as a legitimate business expenditure." Lastly, the revised guidance repeated that facilitation payments are considered bribes and will be prosecuted where there is a realistic chance of conviction and prosecution is in the public's interest.

Adherence to OECD Guidelines Related to the Anti-Bribery Convention

The Introduction to the Guide notes that the United States was one of the first countries to pass anti-corruption legislation, has signed the OECD's Anti-Bribery Convention, and has undergone all three phases of OECD review. The Guide further notes that the OECD has complimented the United States on being a global leader in anti-corruption efforts and attempts to incorporate much of the OECD's "Phase 3" recommendations (pp. 7-8).

Despite such attempts, the Guide does not reconcile several key differences between the OECD Anti-Bribery Convention and the FCPA.[3] Like the differences between the FCPA and the U.K. Bribery Act, the OECD Anti-Bribery Convention prohibits all facilitation payments (¶ 3). Moreover, the OECD Guidelines favor corporate "openness and dialogue with the public so as to promote its awareness of and co-operation with the fight against bribery, bribe solicitation and enforcement" (¶ 5). Public openness is not an explicit goal of the FCPA, and while companies must honor SEC reporting requirements when compliance liability might be considered material to investors, in many cases, the company and prosecutors will keep the details of FCPA investigations confidential unless the matter is prosecuted.

Conclusion

Notably, the Guide does not signal any retreat from the government's assertive enforcement of the FCPA nor provide any additional defenses. Compliance counsel will likely find the Guide's hypothetical and real-life examples helpful, although large corporations with extensive FCPA experience may be disappointed that the Guide does not resolve or eliminate the FCPA's numerous gray areas. Although the Guide also does not attempt to reconcile the key differences between the FCPA and other global anti-corruption laws, the Guide's emphasis on the need for companies to establish robust and risk-based compliance and due diligence procedures is very much in line with parallel guidance on the U.K. Bribery Act and the OECD Anti-Bribery Convention.

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[1] FCPA: A Resource Guide to the U.S. Foreign Corrupt Practices Act, available at http://www.sec.gov/spotlight/fcpa-resource-guide.pdf.

[2] The Bribery Act 2010: Guidance about procedures which relevant commercial organisations can put into place to prevent persons associated with them from bribing (section 9 of the Bribery Act 2010).

[3] Convention on Combating Bribery of Foreign Officials in International Business Transaction and Related Documents: OECD Guidelines for Multinational Enterprises – Section VII.