ALERTS

New FCPA Guidance Highlights Importance of Effective Compliance Procedures

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On Nov. 14, 2012, the Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") jointly issued *A Resource Guide to the U.S. Foreign Corrupt Practices Act* (the "Guide").[1] The 120-page Guide provides a detailed analysis of the FCPA from the perspective of the government agencies charged with enforcing it. The Guide was issued after complaints by U.S. business interests about certain gray areas in the statute, and an OECD recommendation to increase the transparency and consistency of enforcement under the FCPA. For the most part, the Guide recites legal interpretations previously advocated by the DOJ and SEC, although in a far more comprehensive manner. But it also contains some important new insights into how the DOJ and SEC apply and enforce what has become a critical feature of the regulatory landscape over the last decade. Additionally, the Guide includes detailed hypotheticals, scattered throughout the chapters, covering a host of important issues, such as: (1) the reach of FCPA jurisdiction; (2) the propriety of gifts, travel and entertainment ("GTE") expenses; (3) the use of so-called facilitating or "grease" payments; (4) successor liability involving acquired companies that were or were not previously subject to the FCPA and (5) vetting of agents and other third-party intermediaries via risk-based due diligence.

As summarized in the Guide, the anti-bribery provisions of the FCPA prohibit "offering to pay, paying, promising to pay, or authorizing the payment of money or anything of value to a foreign official in order to influence any act or decision of the foreign official in his or her official

capacity or to secure any other improper advantage in order to obtain or retain business."

What Does "Anything of Value" Mean?

While cash is the most obvious form of corrupt payment, "anything of value" may include GTE, charitable contributions and other expenditures. This portion of the Guide is replete with examples, delineating improper versus proper expenses. The FCPA does not prohibit gift-giving (which the Guide notes is often appropriate in business relationships) but does prohibit the payment of bribes disguised as gifts. Although the FCPA does not have a *de minimis* monetary threshold, the Guide explains that items of nominal value (e.g., cab fare, reasonable meals or entertainment, company promotional items) are unlikely to trigger liability under the FCPA absent corrupt intent to influence a foreign official. Explaining the enforcement history involving GTE expenditures, the Guide notes that the DOJ and SEC have brought such cases where there is also evidence of systemic bribery or other clear indicia of corrupt intent. The Guide recommends that companies include GTE guidelines in their compliance programs, and notes that "many larger companies have automated gift-giving clearance processes" with clear monetary thresholds and annual limitations.

Who Is a "Foreign Official"?

The term "foreign official" means any officer or employee of a foreign government or any department, agency or instrumentality thereof. Although the FCPA only prohibits bribery of public officials and not commercial bribery,[2] the phrase "foreign official" has been broadly construed by the government to include employees of state-owned entities or state-controlled entities ("SOEs"), under the theory that SOEs are "instrumentalities" of foreign governments. While defendants in recent cases have asserted (so far unsuccessfully) that the definition of foreign official under the FCPA does not extend to employees of SOEs engaged in commercial activities, the Guide makes clear that the DOJ and SEC interpret the term "instrumentality" broadly to include SOEs. In any event, the Guide provides important new insight on this issue.

According to the Guide, whether a particular entity constitutes an "instrumentality" under the FCPA requires a fact-specific analysis of an entity's ownership, control, status and function. The Guide provides a non-

dispositive and non-exclusive list of factors to consider.[3] Even more significantly (because the legal community and market participants have been pushing for guidance on this issue for years), the Guide states that "an entity is unlikely to qualify as an instrumentality if a government does not own or control a majority of its shares." The Guide then explains the limited circumstances in which DOJ or SEC enforcement actions have involved foreign officials employed by entities in which a foreign government has less than 50 percent ownership, i.e., only where the foreign government has "substantial control" over the entity at issue.

What Affirmative Defenses Are Available?

Certain business groups have been lobbying for an expansion of affirmative defenses available under the FCPA, such as a "safe harbor" defense for companies, based upon an adequate compliance program. The Guide does not endorse any such suggestion. Instead, the Guide clearly states that the FCPA's anti-bribery provisions contain only two affirmative defenses: (1) the payments are lawful under the written laws of the foreign country in question (a defense that is rarely successful as a practical matter) and (2) the payments are reasonable and bona fide expenses incurred in connection with the execution or performance of a contract or a product demonstration. The Guide also contains a non-exhaustive list of safeguards that businesses may take to ensure that an expenditure is legitimate.

What Are Facilitating or Expediting Payments?

The FCPA's anti-bribery provisions contain a narrow exception for "any facilitating or expediting payment to a foreign official … the purpose of which is to expedite or secure the performance of a routine governmental action" that involves non-discretionary acts.[4] In addition to a hypothetical scenario with real-world application, the Guide provides examples of routine governmental actions: "(a) obtaining permits, licenses or other official documents to qualify a person to do business in a foreign country; (b) processing governmental papers, such as visas and work orders; (c) providing police protection, mail pickup and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country; (d) providing phone service, power and water supply, loading and unloading cargo, or

protecting perishable products or commodities from deterioration or (e) actions of similar nature." The Guide warns that facilitation payments, although not illegal under the FCPA, may violate local laws in foreign countries or other countries' foreign bribery laws.[5]

How To Reduce FCPA Risk in Mergers and Acquisitions

The Guide provides practical advice to companies pursuing mergers and acquisitions, encouraging acquiring companies to: (1) conduct thorough risk-based due diligence on potential new business acquisitions; (2) ensure that the acquiring company's code of conduct and compliance policies/procedures apply as quickly as possible to newly acquired businesses or merged entities; (3) train the directors, officers and employees of newly acquired businesses or merged entities, and when appropriate, train agents and business partners; (4) conduct an FCPA-specific audit of all newly acquired or merged businesses as quickly as practicable and (5) disclose any corrupt payments discovered as part of its due diligence of newly acquired entities or merged entities.

The Guide summarizes predecessor versus successor liability, based upon a matrix of factors. Analyzing the factors militating against successor liability, the Guide notes that the "DOJ and SEC have declined to take action against companies that voluntarily disclosed and remediated conduct and cooperated with DOJ and SEC in the merger and acquisition context." According to the Guide, the DOJ and SEC only take action against successor companies in limited circumstances, generally in cases involving egregious and sustained violations or where the successor company directly participated in the violations or failed to stop the misconduct from continuing after the acquisition. More often, the DOJ and SEC bring enforcement actions, if any, only against the predecessor company.

The Guiding Principles of Enforcement

In what many businesses will find the most enlightening chapter, the Guide emphasizes the importance of cooperation and outlines the components of effective compliance programs. "Both DOJ and SEC place a high premium on self-reporting, along with cooperation and remedial efforts, in determining the appropriate resolution of FCPA matters." In the throes of an investigation or in the face of potential FCPA violations,

however, companies should remember that cooperation doesn't necessarily mean succumbing to all requests by the government. The Guide explicitly states: "In assessing a corporation's cooperation, prosecutors are prohibited from requesting attorney-client privileged materials with two [limited] exceptions .... Otherwise, an organization's cooperation may only be assessed on the basis of whether it disclosed the *relevantfacts* underlying an investigation — and not on the basis of whether it has waived its attorney-client privilege or work product protection."

According to the Guide, "an effective compliance program is a critical component of a company's internal controls" and may result in a downward departure under the U.S. Sentencing Guidelines in criminal cases or reduced sanctions in civil cases. The "hallmarks" of an effective corporate compliance program include:

1. Commitment from senior management and a clearly articulated policy against corruption;

2. An effective code of conduct with associated policies and procedures that are periodically updated;

3. Oversight by senior management, autonomy in decision-making, and adequate resources;

4. A risk-based approach tailored to the organization's specific needs and challenges;

5. Training for all directors, officers, relevant employees, and, where appropriate, agents and business partners;

6. Positive incentives to drive complaint behavior and clear disciplinary procedures to deter unethical/unlawful behavior;

7. Third-party due diligence;

8. Confidential reporting and internal investigations; and

9. Continuous improvement via periodic testing and review.

Companies ought to consider implementing the basic elements set forth in the Guide in order to avoid FCPA violations before they occur and, in the event they do occur, preserve the opportunity for substantial mitigation credit by the government. Citing the 2012 *Peterson* case, in

which the government declined to bring any enforcement action against Morgan Stanley, the Guide states: "DOJ and SEC may decline to pursue charges against a company based on the company's effective compliance program, or may otherwise seek to reward a company for its program, even when that program did not prevent the particular underlying FCPA violation that gave rise to the investigation."[6] As evidenced by the Guide, instituting corporate compliance programs designed to detect and prevent corruption are no longer optional measures taken by model corporate citizens; effective corporate compliance programs are the cost of doing business in today's global economy.

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If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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[1] A copy of the Guide is *available at* http://www.justice.gov/iso/opa/resources/2952012111410143819803l.pdf. *See also* Fact Sheet *available at* http://www.justice.gov/iso/opa/resources/85120121114101420662750.pdf.

[2] While the FCPA only prohibits the bribery of foreign officials, bribery in the private sector may violate other laws, such as: the Travel Act (18 U.S.C. § 1952), the U.S. mail and wire fraud statutes (18 U.S.C. §§ 1341, 1343, 1346), the anti-money laundering laws (18 U.S.C. §§ 1956-1957), the United Nations Convention Against Corruption (Dec. 11, 2003, 43 I.L.M. 37), and the U.K. Bribery Act of 2010 (applies to both public and private sector bribery).

[3] The list of factors to be considered include: "(1) the foreign state's extent of ownership of the entity; (2) the foreign state's degree of control over the entity (including whether key officers and directors of the entity are, or are appointed by, government officials); (3) the foreign state's characterization of the entity and its employees; (4) the circumstances surrounding the entity's creation; (5) the purpose of the entity's activities; (6) the entity's obligations and privileges under the foreign state's law; (7) the exclusive or controlling power vested in the entity to administer its designated functions; (8) the level of financial support by the foreign state (including subsidies, special tax treatment, government-mandated fees

and loans); (9) the entity's provision of services to the jurisdiction's residents; (10) whether the governmental end or purpose sought to be achieved is expressed in the policies of the foreign government and (11) the general perception that the entity is performing official or governmental functions."

[4] 15 U.S.C. § 78dd-1(b).

[5] E.g., Facilitating payments are illegal under the U.K. Bribery Act of 2010.

[6] *United States v. Peterson*, No. 12-cr-224 (E.D.N.Y. 2012); *SEC v. Peterson*, No. 12-cv-2033 (E.D.N.Y. 2012). *See* Press Release, DOJ, Former Morgan Stanley Managing Director Pleads Guilty for Role in Evading Internal Controls Required by FCPA (Apr. 23, 2012) (declining to bring criminal case against corporate employer that "had constructed and maintained a system of internal controls, which provided reasonable assurances that its employees were not bribing government officials"), *available at:* http://www.justice.gov/opa/pr/2012/April/12-crm-534.html; Press Release, SEC, SEC Charges Former Morgan Stanley Executive with FCPA Violations and Investment Adviser Fraud, No. 2012-78 (Apr. 25, 2012) (indicating corporate employer was not charged in the matter and had "cooperated with the SEC's inquiry and conducted a thorough internal investigation to determine the scope of the improper payments and other misconduct involved"), *available at* http://www.sec.gov/news/press/2012/2012-78.htm.

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