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The Foreign Corrupt Practices Act: Leveling the Foreign Playing Field

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From Bonds to Clemens, many of baseball's big giants climbed the ladder of success and fell back down again with the prick of a needle. What seemed like a fast way to get ahead turned into a quick way to be fined and prosecuted. Likewise, many corporate giants desiring to do work with international governments historically have used a cheap trick – bribery of foreign officials – to outscore their competitors. The Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") have started to level the playing field, however, by utilizing the Foreign Corrupt Practices Act ("FCPA" or "Act") to severely punish corporations and their employees for bribing foreign officials to gain preferential treatment. The number of FCPA prosecutions has dramatically increased in recent years, forcing corporations around the world to make conscious decisions to self-regulate their own methods of business. This article proposes to highlight recent FCPA prosecutions, to demonstrate the Act's broad enforcement and rigorous penalties, and to provide tips on complying with the FCPA.

Broad Enforcement

Simply stated, the FCPA prohibits persons from bribing foreign officials in return for business. However, the scope of enforcement of the statute is far broader than simply "persons," "foreign officials," and "bribes." Recent prosecutions under the Act demonstrate just how broadly the statutory mandates are now being enforced.

Despite a growing number of FCPA prosecutions against foreign companies, a misconception still exists that the FCPA is only a U.S. concern. Originally, the FCPA was aimed at curbing corrupt business practices by U.S. companies, including businesses that traded securities in the United States. The FCPA was enacted in 1977 after SEC investigations revealed over 400 U.S. companies had made questionable payments totaling $300 million to foreign officials to gain business. In 1998, the U.S. increased the Act's jurisdictional reach, adding penalties for any persons

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(even foreign corporations and nationals) who performed acts within the U.S. that furthered corrupt payments to foreign officials.[1] Today, the truth is, the Act applies to any company or person, including foreign ones, that issues stock in the U.S. or performs actions in the U.S. to further bribes elsewhere. Recent prosecutions emphasize these points.

Foreign Companies and Subsidiaries

In the most highly publicized and costly prosecution to date, Siemens AG paid $800 million in civil and criminal fines to the DOJ and SEC for corrupt payments occurring around the world. Siemens made 4,238 separate bribes totaling approximately $1.4 billion to numerous foreign officials to gain contract work. Siemens' bribes included payments on transactions to design and build metro transit lines in Venezuela, metro trains and signaling devices in China, power plants in Israel, high voltage transmission lines in China, traffic control systems in Russia, refineries in Mexico, and national identity cards in Argentina (to name a few). The company even had "cash desks" containing thousands of U.S. dollars which could be conveniently stuffed in a suitcase and carried to a corrupt foreign official.[2] For Siemens, "bribery was nothing less than standard operating procedure."[3]

The SEC and DOJ prosecuted Siemens AG, Siemens Argentina, Siemens Venezuela, and Siemens Bangledesh. All companies were subject to the jurisdiction of the FCPA. Siemens AG was subject to prosecution in the U.S. because it sold securities within the United States. But, the three Siemens subsidiaries are foreign companies, headquartered in other nations. The subsidiaries' only connections with the U.S. were meetings held in the States in which improper payments were discussed and U.S. bank accounts used to facilitate improper payments. The DOJ determined that these tenuous connections constituted actions within the U.S. that furthered bribes in other nations, warranting prosecution of the foreign companies. This case makes clear that if a company performs an action – even a minor one – within the U.S., that furthers corruption outside the U.S., the company is risking FCPA prosecutions.

A parent company can be prosecuted for FCPA violations committed by its foreign subsidiaries even if the foreign subsidiary is not subject to the FCPA's jurisdiction. Two cases demonstrate that the DOJ and SEC will not hesitate to prosecute a parent company for its foreign subsidiary's FCPA violations when the foreign subsidiary's books are combined with the parent company's financial reports. Siemens AG, for example, had to pay $1.5 million for its foreign subsidiaries' FCPA violations because Siemens AG failed to report its subsidiaries' violations to U.S. authorities and accounted profits from the violations in its financial reports.[4] Similarly, ITT Corporation ("ITT") paid $1.5 million in fines for its wholly-owned Chinese subsidiary's bribery of foreign officials. The Chinese subsidiary made payments both directly and indirectly through third-parties to employees of state-owned companies. In return for money, the employees recommended the subsidiary's water valves for the companies' construction projects. The profits from the illicit payments and the payments themselves were disguised by the Chinese subsidiary in financial reports that were consolidated on ITT's financial records. The DOJ prosecuted ITT for misrepresenting financial

reports and failing to regulate financial transactions within its corporation.[5]

Individual Officers and Directors

Individuals are not safe from FCPA prosecutions either. In the last year, the DOJ and SEC prosecuted executive officers, finance directors, and other bribe facilitators. For example, on May 29, 2009, Thomas Wurzel, the former President of ACL Technologies, accepted a settlement agreement with the SEC for his role in authorizing illicit payments to Egyptian Air Force officials. Wurzel consented to pay a $35,000 civil penalty.[6] The penalties can be much worse. For instance, two citizens of the United Kingdom, Jeffrey Tessler and Wojciech Chodan, were indicted on February 17, 2009, with one count of conspiracy to violate the FCPA and ten counts of violating the FCPA. The indictment alleged that two corporations, one which employed Chodan, hired Tesler to bribe lower level Nigerian government officials. The corporations entered faux contracts with Tesler, paying his company $132 million which Tesler used to bribe the Nigerian officials. If convicted on all charges, Tesler and Chodan face 55 years in prison each and more than $130 million in fines.[7] While not every convicted person faces these extreme criminal penalties, the DOJ and SEC clearly seek harsh punishments for bribing foreign officials.

Expansive Definitions

Moreover, the bribed "foreign officials" do not have to be high-ranking government officers but may be low level government employees. The FCPA broadly defines "foreign official" as including "any officer or employee of a foreign government or any department, agency, or instrumentality thereof ... or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality."[8] Thus, a person may be a foreign official if he or she wins an election, is appointed to a government agency, or is merely employed by an instrumentality of the government. "Instrumentalities," while undefined by the Act, clearly encompass state-operated enterprises. ITT, for example, was prosecuted for its subsidiary's payments to low-ranking employees of a Chinese Government run business.[9] To avoid prosecutions, it is imperative that companies recognize that "foreign officials" means much more than elected leaders. This is especially true in regions like Asia and the Middle East where the Governments' rulers often have direct influence on businesses' operations.

Additionally, "bribes" are not limited to a cash-stuffed suitcases and large monetary payments. While certainly handing a cash-stuffed suitcase to a foreign officials is an FCPA violation, the FCPA criminalizes much more. The FCPA prohibits corporations from corruptly giving foreign officials "anything of value" in return for business.[10] Enforcement actions reveal that "anything of value" has a broad interpretation, including things like vacations, airfare, perfume, gift certificates, condo time shares, and jewelry.[11] For example, in 2007 the SEC brought an enforcement action against Lucent Technologies, Inc. ("Lucent") based exclusively on excessive travel and marketing expenses.[12] The complaint alleged that Lucent, a wholly-owned subsidiary of French company Alcatel-Lucent, spent in excess of $10 million funding visits to

the U.S. for Chinese foreign officials. The officials visited U.S. destinations from Hawaii to New York City. The trips occasionally involved some opportunity to inspect Lucent's factories or receive training, but a disproportionate amount of time was spent on non-business activities like sightseeing and other entertainment and leisure activities. These facts culminated in a settlement wherein Lucent agreed to pay $1.5 million in civil penalties and $1 million to the DOJ pursuant to a non-prosecution agreement.[13] The plane tickets and entertainment passes constituted "bribes" which landed Lucent in court suffering an FCPA prosecution.

Rigorous Penalties

Violating the FCPA can result in huge civil and criminal fines, civil suits, and global embarrassment. The U.S. Government, for one, is dedicated to ending foreign corrupt business practices. SEC Chairman Mary L. Schapiro recently warned corporations around the world that "any company that seeks to put greed ahead of the law by making illegal payments to win business should beware that [law enforcement agencies] are working vigorously across borders to detect and punish such illicit conduct."[14] Their work has paid off. The past two years have been two of the biggest in FCPA enforcement history both in the number of prosecutions and strength of penalties. The SEC and DOJ are waging the war against corrupt business practices with big weapons. The last year alone has seen jaw-dropping sizes of fines. Siemens AG forked over $800 million for civil and criminal fines. Halliburton and Kellogg Brown & Root (KBR) disgorged $177 million to the SEC. KBR delivered another $402 million to the DOJ. Novo Nordisk A/S handed over $19 million for fines. The list goes on, and the message is consistent: "FCPA violations have been and will continue to be dealt with severely by the SEC and other law enforcement agencies."[15]

Civil Suits

Paying the large SEC and DOJ fines does not end the penalties. A more subtle, yet also potent penalty awaits companies after the onslaught of civil and criminal fines. Private actions by infuriated stockholders and businessmen have been filed with increasing frequency following exposure of a company's fraudulent business practices. The FCPA itself does not create a private cause of action.[16] But, the allegations underlying an FCPA prosecution can form the basis for other private causes of action. For example, in three recent cases shareholders filed actions alleging securities fraud immediately following a company's announcement of potential FCPA violations.[17] The complaints alleged that prior corporate statements on finances were materially false based on the fraudulent business practices, and the court upheld the complaints on motions to dismiss by the defendants. Thus far, two companies have settled their cases, for $6.75 million and $2.5 million, and the third is awaiting trial.[18] In addition to securities fraud, private actions have been filed alleging breach of fiduciary duty, breach of contract, and RICO violations.[19] While defendants undoubtedly have and will continue to prevail in some of these actions, the companies will still suffer the pain, expense, and negative publicity of defending a civil action, on top of paying large civil and criminal fines to the U.S. Government.

Avoiding FCPA Penalties

Practically speaking, complying with the FCPA can be difficult for businesses attempting to remain competitive in corrupt countries. But, with the growing enforcement of the FCPA, it is a necessity. Several tips can help a business avoid getting trapped in the web of corruption.

First, it is important to recognize that the FCPA outlines certain permissible payments and affirmative defenses to alleged violations. Permissible payments include "facilitating payments" which are payments to foreign officials to "expedite or to secure the performance of a routine governmental action."[20] Payments to obtain permits, licenses, or other official documents, payments to process governmental papers, provide police protection, and provide phone services are all examples of facilitating payments. The Act also lists several affirmative defenses, including: (1) payments that are lawful under the written laws of the foreign official's country; (2) reasonable and bona fide expenses incurred in the promotion or demonstration of a company's products or services; and, (3) reasonable and bona fide expenses incurred in the execution or performance of a contract with a foreign government.[21] These expenses can include travel and lodging expenditures so long as such payments do not have a corrupt purpose. When in doubt of an action's legality, a business should follow the spirit of the FCPA.

Compliance

Second, and perhaps most importantly, avoiding FCPA violations involves embracing the value of corporate consciousness. That means establishing a corporate culture of ethical business—one where employees are encouraged to do business ethically and are sharply punished for unethical behavior. A company must have more than a "paper program" of good sounding policies. Even Siemens had nicely worded policies on ethical behavior.[22] A company must establish a system of monitoring and enforcing its ethical rules. Practical tips on achieving this goal include: encouraging dissent, appointing an ethics officer, marginalizing misconduct, and rethinking goals.[23] Above all, an organization cannot ignore red flags of misconduct. For example, Siemens engaged third parties that had no expertise in the industry, used forms for payment that included no note of the services received, and paid the third parties unreasonably high fees.[24] These and other signs of corruption went undetected because Siemens refused to devise a system of internal controls adequate to catch and prevent FCPA violations.

Voluntary Disclosure

Third, a corporation should consider the voluntary disclosure of any violations. Both the DOJ and the SEC have made clear in statements and enforcements that voluntary disclosure or the lack thereof is a factor that is considered in formulating penalties. U.S. attorneys, for instance, are instructed to consider "the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate" with the DOJ's investigation when deciding a penalty.[25] The enforcement actions follow this mandate. For instance, Paradigm B.V.'s ("Paradigm") employees bribed foreign officials in multiple countries for

business. When Paradigm discovered the bribery, it voluntarily disclosed the FCPA violations, cooperated with the DOJ's investigation, and promised to create rigorous safeguards against future corruption. The DOJ citing "Paradigm's actions … including voluntary disclosure and remedial efforts" agreed not to prosecute Paradigm criminally and fined them "only" $1 million.[26] While $1 million is no small price to pay, it is a much less significant burden than the multiple millions the DOJ and SEC could have sought.

Conclusion

The DOJ and SEC are serious about leveling the playing field in foreign countries. Much like the steroid-using athletes, the bribery-fueled corporations are being caught and prosecuted with ever increasing frequency. After all, we were taught as children that "cheaters never prosper." While not too long ago in certain countries that was far from the truth, today the DOJ and SEC, armed with the FCPA, are making that child's principle a reality.

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[1] Justin Serafini, *Foreign Corrupt Practices Act*, 41 Am. Crim. L. Rev. 721, 722-27 (2004).

[2] Press Release, Cheryl J. Scarboro, Assoc. Dir. of SEC's Div. of Enforcement, U.S. Sec. and Exch. Comm'n, SEC Charges Siemens AG for Engaging in Worldwide Bribery, (Dec. 15, 2008) (on file with author).

[3] Press Release, Dep't of Justice, Transcript of Press Conference Announcing Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations, (Dec. 15, 2008) (on file with author).

[4] Mike Koehler & David Simon, *Foreign Corrupt Practices Act Compliance Lessons From the Record-Setting Siemens Enforcement Action*, BNA White Collar Crime Report, Vol. 4, No. 5 (Feb. 27, 2009).

[5] Complaint at 1, *Sec. and Exch. Comm'n v. ITT Corp.*, No. 1:09-cv-00272 (D.D.C. filed Feb. 11, 2009); *Sec. and Exch. Comm'n v. ITT Corp.*, Litigation Release No. 20896, U.S. Sec. and Exch. Comm'n (Feb. 11, 2009).

[6] *Sec. and Exch. Comm'n v. Wurzel*, Litigation Release No. 21063, U.S. Sec. and Exch. Comm'n (May 29, 2009).

[7] Press Release, Dep't of Justice, Two UK Citizens Charged by United States with Bribing Nigerian Government Officials to Obtain Lucrative Contracts as Part of KBR Joint Venture Scheme, (Mar. 5, 2009) (on file with author).

[8] 15 U.S.C. § 78dd-1(f)(1).

[9] Complaint at 1, *Sec. and Exch. Comm'n v. ITT Corp.*, No. 1:09-cv-00272 (D.D.C. filed Feb. 11, 2009); *Sec. and Exch. Comm'n v. ITT Corp.*, Litigation Release No. 20896, U.S. Sec. and Exch. Comm'n (Feb. 11, 2009).

[10] 15 U.S.C. § 78dd-1(a).

[11] See, Mike Koehler, *Compliance Lessons From an Active Year in FCPA Enforcement*, BNA White Collar Crime Report, Vol. 3, No. 4 (Feb. 15, 2008) (discussing the enforcement action against Si Chan Wooh who bribed foreign officials with money and *gifts*).

[12] *SEC v. Lucent Technologies Inc.*, No. 1:07-cv-02301 (D.C.C. Dec. 21, 2007).

[13] Press Release, Dep't of Justice, Lucent Technologies Inc. Agrees to Pay $1 Million Fine to Resolve FCPA Allegations, (Mar. 5, 2009) (on file with author).

[14] Press Release, U.S. Sec. and Exch. Comm'n, SEC Charges KBR and Halliburton for FCPA Violations (Feb. 11, 2009) (on file with author).

[15] *Id.*

[16] *Lamb v. Phillip Morris, Inc.*, 915 F.2d 1024, 1029-30 (6th Cir. 1990).

[17] *In re Faro Technologies Securities Litigation*, 534 F. Supp. 2d 1248 (M.D. Fla. 2007); *In re Nature's Sunshine Products Sec. Litig.*, 486 F. Supp. 2d 1301 (D. Utah 2007); *In re Immucor Inc. Sec. Litig.*, No. 2006 WL 3000133 (N.D. Ga. 4 Oct. 2006).

[18] Ayeh S. Portnoy & John L. Murino, *Private Actions Under the US Foreign Corrupt Practices Act: An Imminent Front?*, International Bar News, p. 31 (Apr. 2009).

[19] See, *City of Harper Woods Employees' Retirement Sys. v. Oliver*, 577 F. Supp. 2d 124 (D. D.C. 2008) (alleging breach of fiduciary duty); *Hijazi Medical Supplies v. AGA Medical Corp.*, No. 07-3419 2008 WL 4861517 *1 (10 Nov. 2008) (alleging breach of contract); *Grynberg v. BP P.L.C.*, 585 F. Supp. 2d 50 (2008) (alleging RICO violations).

[20] 15 U.S.C. §§ 78dd-1(b), 78dd-2(b), 78dd-3(b).

[21] 15 U.S.C. § 78dd-1(c)(2)(A)-(b).

[22] Mike Koehler & David Simon, *Foreign Corrupt Practices Act Compliance Lessons From the Record-Setting Siemens Enforcement Action*, BNA White Collar Crime Report, Vol. 4, No. 5 (Feb. 27, 2009).

[23] Margaret Steen, How to Prevent Cheating, Stanford Bus. Magazine (June 25, 2008) http://www.gsb.stanford.edu/news/bmag/sbsm0808/feature-preventcheating.html.

[24] Mike Koehler & David Simon, *Foreign Corrupt Practices Act Compliance Lessons From the Record-Setting Siemens Enforcement Action*, BNA White Collar Crime Report, Vol. 4, No. 5 (Feb. 27, 2009).

[25] Memorandum from Paul J. McNulty, Deputy Attorney Gen., U.S. Dep't of Justice, on Principles of Federal Prosecution of Business Organizations.

[26] Press Release, Dep't of Justice, Paradigm B.V. Agrees to Pay $1 Million Penalty to Resolve Foreign Bribery Issues in Multiple Countries, (Sept. 24, 2008) (on file with author).