# The FCPA in Investment Transactions

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# THE FCPA IN INVESTMENT TRANSACTIONS*

*Lucinda A. Low and John E. Davis* **

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## I. Introduction: The Expanding Reach of the FCPA

Since its enactment in 1977, the Foreign Corrupt Practices Act (FCPA or the Act) has been an important consideration for U.S. companies doing business abroad. The FCPA grew out of abuses that came to light in the early to mid-1970s, in which large U.S. companies used bribes to government officials to obtain business in both developed and developing countries. The FCPA criminalized the bribery by U.S. persons and companies of foreign government officials, political party officials, and candidates for political office in order to obtain business./1/ It also mandated that companies with publicly traded securities in the United States adhere to prescribed standards of record keeping, maintain internal controls, and take other steps to ensure that investors could obtain a true and complete financial picture of those companies' activities./2/ Coupled with a prior amendment to U.S. tax laws denying any tax deduction for bribes,/3/ and the normal panoply of criminal laws addressing fraud (such as mail and wire fraud prohibitions and conspiracy provisions), the FCPA provided the U.S. government with a range of tools for combating improper payments in the overseas business activities of U.S. companies.

The increase in U.S. direct foreign investment abroad over the last fifteen years has brought to the fore FCPA issues in a wide variety of investment transactions. Spawned by the increasing access to at least portions of the economies of the Soviet successor states and emerging markets in the People's Republic of China, South and Southeast Asia, Latin America, and the general trend toward privatization of state-run enterprises, U.S. companies and their counsel engaged in international projects are facing a multitude of FCPA issues, some of them perennial and familiar, and others more subtle and uncharted.

These issues have arisen in a legal landscape that has been substantially altered in just the last five years. Despite controversy engendered almost from its enactment by the FCPA's unilateral application and aggressive vicarious liability provisions, the law has endured despite efforts to abolish or weaken it. The 1998 amendments to the FCPA, adopted in anticipation of U.S. accession to the Organization for Economic Cooperation and Development (OECD Convention) discussed below, significantly expanded the law in certain respects./4/ Dozens of prosecutions under the antibribery provisions, and many more enforcement actions under the books and records provisions, have been brought in the twenty-six years of the Act's existence. Many of the most significant cases date from the last few years, reflecting recently heightened enforcement efforts. Prosecutors are increasingly taking advantage of the potent tools provided by antimoney laundering laws.

The last decade also has found U.S. companies in a "second generation" compliance effort, responding to higher compliance standards recently articulated by courts, the Federal Sentencing Guidelines, enforcement

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officials, and the challenges of doing business in new and, in some cases, difficult foreign markets./5/ Companies have focused on ethics and compliance programs with new urgency since the enactment of the Sarbanes-Oxley legislation in 2002/6/ and in anticipation of amendments to the Federal Sentencing Guidelines for Corporations (which took effect in November 2004) that provide substantial new detail regarding the U.S. government's view of an "effective compliance program."/7/ At the same time, foreign companies, especially those with publicly traded stock in the United States, have begun to grapple with FCPA compliance in the wake of the first enforcement actions against them./8/

At the same time U.S. compliance standards have been strengthened, dramatic changes have occurred in the international landscape. Developed and developing countries alike, as well as international institutions, have become far less tolerant of corrupt activity by and toward government officials. Among the most significant recent developments in the international arena are several international conventions that have been adopted or have entered into force with substantial participation in a relatively short period of time. These include the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, sponsored by the OECD Convention;/9/ the Inter-American Convention against Corruption, adopted by the Organization of American States (OAS Convention);/10/ the Criminal Law Convention against Corruption of the Council of Europe (COE Convention);/11/ the African Union's anticorruption convention;/12/ and the recently signed United Nations (U.N.) Convention against Corruption./13/ In addition to establishing new international standards for countries that participate in these conventions, each of the conventions includes provisions to facilitate cross-border investigations and enforcement. Other countries are beginning to bring enforcement actions under their OECD counterparts.

Also significant for international investment are the recent amendments to the rules applied by the World Bank and other international financial institutions (IFIs) to outside contractors and consultants, barring corrupt practices in bank-financed projects and authorizing sanctions for noncompliance./14/ These rules are being applied and enforced, resulting in debarment and significant losses of business opportunities./15/

Despite the proliferation of enforcement activity and guidance on compliance standards in the United States and around the world, it is still rare for situations arising under the FCPA to be clear-cut. Most of them require difficult judgments to resolve and the balancing of business objectives against risks that can often only be imprecisely quantified in the face of murky facts. The statute is written in broad terms. Despite the FCPA's age, very little regulatory guidance exists on how to comply with it. Nor is the case law extensive, since companies prosecuted for violations tend to settle the case rather than litigate the allegations.

The difficulties of risk assessment are especially acute in the investment arena. Issues such as those a company may face in structuring, for example, a joint venture with a parastatal entity in a foreign country have only been touched on in the FCPA jurisprudence. Issues with foreign partners, mergers and acquisitions, the responsibility of a parent for a wholly owned foreign subsidiary, and the duties of a minority investor are but some of the other contexts in which issues can arise.

This chapter begins with a brief overview of the Act, highlighting its application in the foreign investment context. It then reviews what little regulatory and judicial guidance exists for companies operating in the foreign investment arena, through a series of what the authors consider to be fairly common scenarios in investment transactions. The chapter will also briefly address, in more detail, the efforts by the various international institutions noted above to address corruption and their potential effect in the international investment area. Finally, the chapter provides some practical steps to assist in the avoidance of potential FCPA issues in investment contexts.

## II. The FCPA in Investment Transactions: An Overview

The FCPA contains two types of rules — the antibribery provisions and the accounting provisions. The antibribery provisions were designed to address what were perceived as corrupt practices used by U.S. companies in obtaining business in foreign countries. Paradigm examples included large bribes to foreign government officials to secure government contracts and the payments of large fees to "consultants" who performed no services, but passed money through to



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government officials. These payments were often masked by slush funds, off-book accounts, and other financial practices, both in the United States and abroad, which led to the enactment of the accounting provisions.

## A. Antibribery Provisions

### 1. Elements of a Violation

The antibribery provisions of the Act — which consist of three distinct but largely parallel provisions reaching different but overlapping universes of persons/16/ — criminalize bribery of a foreign official to secure business./17/ A violation of the antibribery provisions consists of the following elements:

- a covered person, with a nexus to U.S. commerce (when required);
- takes an action in furtherance of
- a payment of — or an offer, authorization, or promise to pay money or the giving of anything of value — to any
  - "foreign official";
  - foreign political party or party official;
  - candidate for foreign political office;
  - official of a public international organization;
  - other person while "knowing"/18/ that the payment or promise to pay will be passed on to one of the above
- "corruptly" for the purpose of
  - influencing an official act or decision of that person;
  - inducing that person to do or omit to do any act in violation of his or her lawful duty;
  - securing any improper advantage; or
  - inducing that person to use his or her influence with a foreign government to affect or influence any government act or decision
- in order to obtain, retain, or direct business to any person.

15 U.S.C. §§ 78dd-1(a), 78dd-2(a), and 78dd-3(a).

While the "classic" FCPA cases involve a money payment to a government official having decision-making authority over the award of a contract, even a quick perusal of the foregoing elements of a violation reveals their potential application to a much wider set of circumstances. "Anything of value" can, for instance, include a stock interest in a joint venture company, a contractual right or interest, real estate, personal property, or other interests arising from business relationships. As a result, the mere formation of a joint venture or establishment of an investment relationship with certain parties — for example, a foreign government official or someone closely connected to such an official — can raise FCPA issues.

Moreover, even in the context of a purely private joint venture (*i.e.,* a joint venture between companies with no government ownership), the ability of the joint venture to operate in the host country may turn on discretionary government decisions, including foreign investment approvals; the obtaining of concessions (as in the natural resources sector), franchises, or licenses (as in the telecommunications sector in many countries or in other "sensitive" sectors); tax or customs concessions; and other regulatory actions or benefits. As a condition to investment approval, the government may require the foreign investor to partner with a local firm, subcontract certain work to local firms, meet specified local employment standards, build infrastructure, or satisfy other performance conditions. The process of positioning oneself to do business in a foreign country thus typically offers a variety of opportunities for government approvals that fall under the broad rubric of "obtaining business" as that element of the FCPA has been developed./19/

In the context of a joint venture with a state-owned entity (parastatal) or a company owned or controlled by a foreign government official, the issues are magnified. Because the FCPA does not distinguish between government officials acting in a sovereign capacity on behalf of the government or a government "agency" and those acting in a commercial capacity for a state "instrumentality," virtually any transaction between a person subject to the FCPA and the employees of a state-owned entity, from the simple payment of directors' fees to employment contracts to stock options, can raise FCPA issues. These transactions may not ultimately be violations of the Act, but the issues they raise must be addressed and risk mitigation steps may need to be taken.

Finally, FCPA issues can arise in post-formation operational decisions, in the context of a joint investment with either a private partner or a government official/entity that has passed FCPA muster in its



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formation. Joint venture partners not themselves subject to the FCPA can, by their actions, trigger FCPA liability in the same way an agent or consultant might if they take actions within the United States or if there is "knowledge" or authorization by the U.S. partner. The risk of "knowledge" or authorization, as illustrated below, may be even greater in a shared enterprise than in the agency context.

Thus, if all the requisite elements are present, and the transactions involve or implicate persons subject to their coverage, the antibribery provisions clearly can apply to both the formation and operational stages of investment relationships.

**2. Persons Subject to the Antibribery Provisions**

The FCPA's antibribery provisions apply to "domestic concerns," "issuers," and "any person" acting in U.S. territory. 15 U.S.C. §§ 78dd-1(a), 78dd-1(g), 78dd-2(a), 78dd-2(i), 78dd-3(a), and 78dd-3(f)(1). In the wake of the 1998 amendments to the FCPA, proof of a U.S. territorial nexus for "U.S. persons" and companies is no longer required./20/ Thus, a violation by these "U.S. persons" can occur even if the prohibited activity takes place entirely outside of the United States and does not involve the use of any instrument of U.S. interstate commerce. Non-U.S. persons covered as foreign "issuers" or under the new "any person" prohibition must still act with the necessary territorial nexus to the United States for there to be U.S. jurisdiction. *Id.*

The definition of "domestic concern" covers a large universe of persons and entities, including individual U.S. citizens (wherever located), U.S. resident aliens,/21/ corporations, and other business entities (including partnerships) organized under the laws of a state of the United States or having their principal place of business in the United States, and officers, directors, employees, and agents of any of these entities, regardless of their nationality./22/ 15 U.S.C. § 78dd-2(h)(1).

"Issuers" constitute a more narrow range, being defined as companies that register securities in accordance with 15 U.S.C. § 78l or are required to file reports under 15 U.S.C. § 78o(d), or any officer, director, employee, or agent of such company. This definition captures those selected foreign companies that issue stock on a U.S. securities exchange and their personnel, in addition to certain U.S. companies (which are already subject to the statute as "domestic concerns"). This would include, for example, foreign companies that list American Depository Receipts (ADRs) on a U.S. stock exchange. The individuals caught by the "issuer" provisions can include non-U.S. citizens and residents as well as U.S. citizens./23/

"U.S. persons" includes the same business entities as "domestic concerns," but covers only U.S. nationals, and not foreign nationals who reside in the United States. 15 U.S.C. §§ 78dd-1(g)(2), 78dd-2(i)(2).

Finally, any "person" (no matter what nationality) acting within U.S. territory is covered by the FCPA. 15 U.S.C. § 78dd-3(a). Although the statute is ambiguous, the legislative history of the Act and case law confirm that foreign subsidiaries of U.S. companies acting on their own behalf and not as agents of covered persons generally are not covered by the antibribery provisions. *See* H.R. Conf. Rep. No. 95-831, at 14 (1977), *reprinted in* 1977 U.S.C.C.A.N. 4098, 4126; *Dooley v. United Techs. Corp.*, 803 F. Supp. 428, 439 (D.D.C. 1992) (legislative history excludes foreign subsidiaries from FCPA coverage). Furthermore, foreign individuals who are not officers, directors, employees, or agents of a U.S. company or a foreign issuer generally are not covered by these provisions. However, as noted above, if either a foreign subsidiary or a foreign person not otherwise covered performs any acts in furtherance of a prohibited payment within the United States, they could be directly liable under the FCPA's territoriality jurisdictional prong.

In addition, due to the potential for liability for acts of a third party under the third FCPA element cited above (the "knowledge" or "vicarious liability" provisions), reliance on foreign incorporation where there is U.S. management and control can be a weak shield. Indeed, the legislative history affirms that U.S. parent corporations may remain indirectly liable for FCPA violations by a foreign subsidiary. H.R. Conf. Rep. No. 95-831, at 14 (1977) ("the conferees intend to make clear that any issuer or domestic concern which engages in bribery of foreign officials indirectly through any other person or entity would itself be liable under the [FCPA]"). The U.S. Congress enacted these provisions to prevent companies from adopting a "head-in-the-sand" approach



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to the activities and identities of their foreign agents and business partners. *See* H.R. Conf. Rep. No. 100-576, at 920 (1988). This problem has also been characterized as "willful blindness"or "unwarranted obliviousness" to any action or fact, including applicable "red flags" (discussed in more detail below) that should reasonably alert a company's management to a "high probability" of an FCPA violation. *Id.* In such cases, "knowledge" may be inferred even if a company does not have actual knowledge of a payment.

### 3. Exceptions and Affirmative Defenses

#### a. Exceptions

The sole statutory exception in the FCPA is for gratuities to government officials who perform "routine governmental action." 15 U.S.C. §§ 78dd-1(b), 78dd-2(b), 78dd-3(b). The statutorily enumerated examples of such action are

- — obtaining business permits;
- — processing governmental papers such as visas;
- — providing police protection, mail delivery, or scheduling inspections associated with contract performance or the shipment of goods;
- — providing phone, power, or water service, loading and unloading cargo, or protecting perishable products from deterioration; or
- — other similar activities which are ordinarily and commonly performed by an official.

These so-called facilitating or grease payments — which are used to expedite the processing of permits, licenses, or other routine documentation — are not prohibited by the FCPA.

This exception may be more useful to U.S. companies in the investment context than in the trading context, since investors could easily encounter the full range of examples of "routine governmental action" enumerated in the statute in the course of establishing and operating a business abroad. Nonetheless, it remains an exception of very limited scope and raises an interesting question of whose law applies in determining whether the action of a government is or is not "routine"; is it routine by U.S. standards or by foreign standards?/24/

#### b. Affirmative Defenses

The 1988 amendments to the FCPA added two affirmative defenses for certain types of payments. First, the statute provides for an affirmative defense where the payment at issue "was lawful under the ***written*** laws and regulations of the foreign official's ... country." 15 U.S.C. §§ 78dd-1(c)(1), 78dd-2(c)(1), 78dd-3(c)(1) (emphasis added)./25/ The second affirmative defense is for certain payments made to reimburse foreign officials for expenses directly associated with visits to product demonstrations or tours of company facilities or in connection with the execution or performance of contracts. 15 U.S.C. §§ 78dd-1(c)(2), 78dd-2(c)(2), 78dd-(c)(2).

Both defenses can apply to investments, although the facts of most cases rarely support the conventional application of the first defense. Nevertheless, it may be applied — at least by analogy — to transactions or activities which are legally compelled by host country's written laws and authorities — for example, the requirement that a parastatal entity participate in a project, or that the investor satisfy other terms or conditions mandated by the government./26/

### 4. Official Guidance

Very little regulatory guidance exists on how to comply with the FCPA in the trade context; even less exists on investment issues. Except for the Opinion Procedure regulations (described below), which provide limited substantive guidance and only a trickle of review and opinion procedure releases, there are no implementing regulations and no guidelines issued by the Department of Justice (DOJ)./27/ There are a handful of review releases involving investment transactions; these are referred to in more detail in later in § II.

Until recently, of the enforcement actions that have occurred over the years, only a few have implicated an investment transaction, and two of them were ancillary to schemes to procure a government contract./28/ Recent years, however, have seen a dramatic increase in investment-related cases. A series of cases in 2001 against individuals associated with Owl Securities and Investment Ltd. (OSI) involved a conspiracy to make various payments for various government actions related to a planned investment./29/ 2003 brought the first enforcement actions centered on investment issues, and to date neither has been completed. *See United States v. Bodmer,* No. 03-Crim. 947, 2004 U.S. Dist. LEXIS 959



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(S.D.N.Y. Jan. 28, 2004); *United States v. Giffen,* No. 1:03-cr-00404-WHP, 2004 U.S. Dist. LEXIS 24132 (S.D.N.Y. Dec. 2, 2004). Other recent actions, *United States v. Syncor Taiwan, Inc.,* Cr. No. 02-1244 (C.D. Cal. Dec. 2002), *SEC v. ABB Ltd.,* 1:04CV1141 (RBW) (D.D.C.), Lit. Rel. No. 18775, July 6, 2004, and *InVision Technologies* (DOJ, "InVision Technologies Enters into Agreement with United States," Dec. 6, 2004) all involved payments related to sales of products and services to state-owned entities, but arose through due diligence in a merger and acquisition context.

Many of the cases involving investments have involved liability of U.S. parent companies and U.S. individuals under either the antibribery or accounting provisions for payments on behalf of affiliates operating in foreign countries to obtain favorable treatment of the company's operations by local customs, tax, or project management authorities./30/ Thus, the courts have only recently begun to grapple with the extent to which investment transactions may pose different issues and require different responses from trade transactions.

**B. Accounting Provisions**

In addition to the antibribery provisions, the FCPA requires publicly held companies to maintain certain record-keeping standards and internal accounting controls. These are designed to fight accounting devices — which include off-book accounts and slush funds — designed to hide the existence of bribery payments. The accounting controls are intended to ensure that shareholders receive an accurate picture of the company's expenditures.

**1. Requirements of the Record-Keeping and Internal Control Provisions**

The record-keeping provision of the statute requires companies to make and keep books and records "which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer." 15 U.S.C. § 78m(b)(2)(A). All the transactions of issuers are covered, not just their foreign transactions. The internal accounting controls require companies to "devise and maintain a system" that, among other things, "provide[s] reasonable assurances that ... transactions are executed in accordance with the management's general or specific authorization." 15 U.S.C. § 78m(b)(2)(B)(i). Unlike the antibribery provisions, which by definition can only apply to transactions involving payments by foreign officials, the accounting provisions apply without regard to the existence or extent of a company's foreign operations (although several enforcement actions, such as *Triton Energy*/31/ and *IBM,*/32/ involved operations of a foreign subsidiary).

The FCPA requires "reasonable" rather than absolute assurance that accounting controls are adequate. *Id.* The records must be sufficient to "satisfy prudent officials [as in] the conduct of their own affairs." *Id.* § 78m(b)(7). The Senate Report accompanying the original Act recognizes that "standards of reasonableness must apply" and that "management must necessarily estimate and evaluate the cost/benefit relationship" in establishing a system of controls. S. Rep. No. 95-114, at 8, *reprinted in* 1978 U.S.C.C.A.N. 4106.

**2. Persons Subject to Accounting Provisions**

Unlike the antibribery provisions, the accounting provisions apply only to "issuers." 15 U.S.C. § 78m(b). Foreign subsidiaries that are majority owned by an issuer are also subject to the accounting controls. Where an issuer holds 50 percent or less of the voting power of a foreign subsidiary, however, a 1988 amendment to the accounting provisions requires only that the issuer make a "good faith" attempt to cause the affiliated company to maintain the internal accounting controls. *See* 15 U.S.C. § 78m(b)(6).

Thus, the application of the accounting provisions to foreign subsidiaries turns strictly on equity ownership and not a broader concept of control. Although issuers with minority status in foreign affiliates still need to take steps to satisfy the "good faith" attempt requirement, having satisfied that, the affiliates themselves will not be caught.

**C. Other Relevant Laws**

The preceding sections have detailed the core provisions of the FCPA. The reach of the FCPA is effectively extended by other statutes that can be used in place of, or in addition to, the FCPA in cases involving allegedly corrupt conduct. These include conspiracy laws, the federal law prohibition on interstate travel in aid of racketeering, mail and wire fraud laws, and, especially in recent years, antimoney laundering laws.

Federal money laundering laws now include in the list



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of "specified unlawful activities" (SUAs) that serve as predicate offenses several corruption-related offenses: felony violations of the FCPA and foreign bribery, whether or not a violation of the FCPA. Moreover, the money laundering laws can be used to prosecute the funding of an investment transaction, through 18 U.S.C. § 1956(a)(2), which criminalizes the interstate or foreign transfer of funds to ***further*** an SUA. This provision may capture many investment transactions that would not otherwise be caught because they do not involve proceeds of crime — no proceeds are required under this section.

That these laws are a potent weapon when the FCPA itself may be unavailing — for example, because of lack of the necessary jurisdictional nexus over a foreign person — is illustrated by the recent decision in the *Bodmer* case. Bodmer, a Swiss citizen, acted as an agent on behalf of a group of investors formed to attempt to acquire interests in SOCAR, the Azerbaijan national oil company, which was due to be privatized. Several of the members of the consortium were U.S. corporations. The U.S. government alleged that Bodmer facilitated the payment of millions of dollars in cash and wire transfers, to acquire privatization instruments issued by the government of Azerbaijan, as well as to fund payments to senior officials of Azerbaijan, the oil company, and the State Property Committee. For this conduct, Bodmer was charged with one count of conspiracy to violate the FCPA's antibribery prohibition and one count of conspiracy to launder money./33/ (The indictment also sought $150 million in restitution, among other claims.) *See United States v. Bodmer,* No. 03-Crim. 947, 2004 U.S. Dist. LEXIS 959 (S.D.N.Y. Jan. 28, 2004).

In July 2004, a New York federal district court dismissed the conspiracy to violate the FCPA charge against Bodmer, based on its finding that, as a foreign national, he lacked fair notice that the criminal sanctions of the FCPA applied to him after the 1998 amendments. His motion to dismiss the money laundering conspiracy charge, however, was denied. The court held that the case could go forward, even though the alleged corrupt practices were entirely extraterritorial, and even though the FCPA conspiracy count was dismissed on jurisdictional grounds. *See United States v. Bodmer,* 342 F. Supp. 2d 176 (S.D.N.Y. 2004).

## III. The Developing Web of International Anticorruption Conventions

Since the passage of the FCPA more than twenty-five years ago, U.S. companies have complained about the competitive disadvantage it creates for them *vis-à-vis* their foreign competitors. The possibility of vicarious liability created by the Act's definition of "knowledge" (as discussed above) requires a level of precontractual due diligence, education of a foreign partner, monitoring, and in some cases a forgoing of business opportunities for U.S. companies. Until recently, these obligations were not faced by their foreign competitors. For that reason, the U.S. government's agenda has long included a "leveling of the playing field" by multilateralizing anticorruption rules. Until a few years ago, such an effort yielded principally derision. But in the last decade, particularly since 1996, dramatic changes have occurred in the international landscape. Driven in part by economists' reevaluation of corruption's effects on development and by high-profile corruption in various countries, both the developed and the developing world's attitudes toward corruption have changed. This opened the way for initiatives to develop international standards to combat corrupt practices, resulting in a myriad of new international anticorruption treaties and regimes. These treaties are designed to facilitate cross-border enforcement of anticorruption laws, and their impact can already be seen in recent prosecutions.

This section briefly summarizes each multilateral initiative, highlighting key areas related to the investment context. How these conventions impact particular scenarios will be discussed in those sections.

### A. OAS Convention

In 1996, the OAS countries signed the Inter-American Convention against Corruption, which became effective on March 20, 1997, the first of a series of international treaties addressing transnational corruption. *See* Inter-American Convention against Corruption, Mar. 29, 1996, *reprinted in* 35 I.L.M. 724 (1996). With the deposit of Brazil's instrument of ratification on July 24, 2002, the OAS Convention covered the United States, Canada, and all major economies in Latin America. The OAS Convention obliges states, among other things, to criminalize the bribery of both domestic and foreign



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officials as well as the solicitation or receipt of a bribe. The OAS Convention also requires criminalization of "illicit enrichment" of or by a public official./34/ It also provides for extradition and asset seizure of offending parties. In addition to emphasizing heightened government ethics, improved financial disclosures, and transparent bookkeeping through nonmandatory provisions, the OAS Convention facilitates international cooperation in the gathering of evidence and asset seizure and forfeiture actions./35/ The addition of a monitoring mechanism subsequent to the OAS Convention's entry into force has served to strengthen accountability of countries for implementation./36/

**B. OECD Convention**

The OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions was ratified by the requisite number of parties and entered into force on February 15, 1999. By the end of 2004, thirty-six countries, including most of the major capital exporting countries, had ratified the OECD Convention./37/

The OECD Convention is short and focused — it consists of only seventeen Articles covering the offense of transnational bribery, ancillary or related offenses, jurisdiction and penalties, international cooperation in the investigation and prosecution of transnational bribery (including, uniquely, standards for addressing jurisdictional conflicts), a process for monitoring implementation, and entry into force, reservations, and implementation. It is accompanied by official commentaries that expand on the text./38/ The main purpose of the OECD Convention is to require countries to proscribe the bribery of foreign public officials in the same way that countries prohibit the bribery of their domestic officials. To this end, the OECD Convention requires that parties enact national laws criminalizing the bribery of foreign public officials with the focus on the supply of funds — the person who promises or gives the bribe, in contrast to the offense committed by the official who receives the bribe./39/

The key provisions of the OECD Convention are mirrored in most ways by the FCPA, with a few exceptions, such as the OECD Convention's lack of an exception for "facilitating" payments./40/ In the investment context, the OECD Convention's requirements for penalties are relevant. The OECD Convention requires parties to institute "effective, proportionate, and dissuasive criminal penalties" comparable to those applicable to bribery of the party's own domestic officials./41/ Where a party's domestic law does not subject nonnatural persons (*e.g.*, corporations) to criminal responsibility (*e.g.*, Japan), the OECD Convention requires the party to ensure that legal persons are "subject to effective, proportionate, and dissuasive noncriminal sanctions, including monetary sanctions."/42/ In all cases, the OECD Convention requires each party to take such measures as are necessary to ensure that the bribe and the proceeds of the bribery of the foreign public official are subject to seizure and confiscation or that monetary sanctions of "comparable effect" are applicable./43/ The Commentaries define the "proceeds" of bribery as "the profits or other benefits derived by the briber from the transaction or other improper advantage."/44/ Finally, the OECD Convention requires each party to consider the imposition of additional civil or administrative sanctions, including exclusion from public benefits or aid; temporary or permanent disqualification from participation in public procurement; judicial supervision; and judicial "winding-up."/45/

**C. Council of Europe Conventions**

The Council of Europe, in which the United States has observer status, has adopted two conventions related to transnational corruption. The Criminal Law Convention on Corruption entered into force on July 1, 2002; the United States signed the Convention at the end of September 2000, but has not ratified it./46/ A more ambitious Civil Law Convention on Corruption (which the United States has not signed at this date) entered into force January 11, 2003./47/ On May 4, 1998, the Council's Committee of Ministers adopted a resolution that authorized the establishment of the Group of States against Corruption (GRECO), whose purpose is to improve the capacity of its members to fight corruption by following up on compliance with their undertakings./48/

The Criminal Law Convention requires the criminalization of both active and passive (*i.e.*, receipt) domestic bribery. It then goes beyond both the OAS and OECD Conventions to require criminalization of both active



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and passive bribery in the ***private*** sector./49/ The Convention also requires criminalization of transnational bribery of officials./50/ Article 12 of the Criminal Law Convention criminalizes "trading in influence," and record-keeping issues are addressed using criminal law provisions, a unique approach among the international conventions./51/

In the investment context, a key distinction of the Criminal Law Convention from other treaties in this area is its articulation of grounds for corporate liability. Parties are required to adopt measures necessary to ensure that nonnatural persons can be held responsible for the offenses of active bribery, trading in influence, and money laundering, when the offenses are committed ***for their benefit*** by a natural person, "who has a leading position within the legal person — based on a power of representation, or decision making or control authority."/52/ Where such natural persons are accessories or instigators, corporate liability should accrue as well. In addition, parties are required to take measures

> to ensure that a legal person can be held liable where the lack of supervision or control by a natural person referred to in ¶ 1 has made possible the commission of the criminal offenses mentioned in ¶ 1 for the benefit of that legal person by a natural person under its authority./53/

Such corporate liability does not exclude the possibility of individual liability for the perpetrators, instigators, or accessories./54/

Criminal liability based on a lack of supervision and control arguably represents an extension of corporate criminal liability beyond that provided in the FCPA, although recent cases have begun to push in that direction. It is apparently, however, a recognized standard of liability in the laws of some European countries. Investors in Criminal Law Convention signatory countries would be advised to review their compliance and controls systems with this standard in mind.

**D. Other Regional Conventions**

The European Union (EU) and the African Union have also adopted broad anticorruption conventions./55/ The EU Convention is in force, while the African Union Convention, adopted only in 2003, is not yet in force. These regional instruments make Asia the only region not to have embraced the convention approach./56/ However, the U.N.'s pursuit of a global convention, described in the next section, may make the absence of an Asian regional convention less significant.

**E. U.N. Convention**

The most recent, and conceptually most ambitious, international convention addressing transnational corruption is the U.N. International Convention against Corruption, which was opened for signature on December 9, 2003. The U.N. Convention addresses six principal topics:

(1) mandatory and permissive preventive measures applicable to both the public and private sectors, including accounting standards and the promotion of codes of conduct and compliance programs for private companies;
(2) mandatory and permissive criminalization obligations, including obligations with respect to public and private sector bribery, trading in influence, and illicit enrichment;
(3) the availability of private rights of action for the victims of corrupt practices;
(4) extensive antimoney laundering measures;
(5) cooperation in the investigation and prosecution of cases, including collection actions, through mutual legal assistance and extradition; and
(6) asset recovery./57/

It is too early to determine whether the U.N. Convention will attract wide adherence, and how effective it will be in prompting enforcement against transnational bribery by countries that have not done so through the present; entry into force is not expected until at least late 2005. At least as interpreted by the U.S. government, U.S. law already includes most if not all of the provisions that the U.N. Convention would make mandatory once it takes effect, and, thus, it should not drastically affect U.S. enforcement of the FCPA and related statutes.

With regard to investment issues, the asset recovery provisions primarily focus on strengthening intergovernmental mechanisms for the recovery of assets



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plundered by corrupt governments (such as efforts by Nigeria to recover assets deposited by members of the former Abacha regime in banks in various countries, including the United Kingdom and United States)./58/ However, two other provisions, both of which have already attracted controversy, could have potentially significant effects on investment transactions if implemented by ratifying states when the U.N. Convention takes effect.

The first is Article 34, which obliges states to take measures to address the consequences of corruption, including through the annulment or rescission of contracts, withdrawal of concessions, or other similar instruments that may have been tainted by corrupt practices. Although written in mandatory terms, the provisions direct states to give due regard to the rights of third parties acquired in good faith — an important qualification, albeit one that may not go far enough to give business comfort — and to fundamental principles of the host state's domestic law. However, the Article is not limited by its terms to offenders — that is, those convicted of violations of the offenses prescribed by the U.N. Convention. The absence of such a limitation may enable this article to be applied in a wider variety of situations than has traditionally been the case in enforcement actions, potentially even to third-party investors. Thus, companies that do business abroad or at home through government contracts, concessions, licenses, and permits (upon which substantial investments are often predicated) should be aware that this provision may prompt more widespread revocation of rights than has historically been the case./59/

How the "good faith" provision is interpreted is also critical. The presumably easy cases are where there is collusion between the third party and the prior corruptor, or the third party and the corruptor are related. But these may be the rare cases. A more difficult case would be the acquiror who identifies evidence of past corruption in a transaction but nonetheless proceeds with the acquisition. Would this acquiror be acting in good faith if it proceeds with, in effect, actual knowledge of such past corruption? And what of the acquiror who may identify "red flags" in the course of due diligence, but ultimately does not reach any conclusive determination regarding the past corruption? (A situation which may be very common.) Is proceeding with knowledge of such red flags a "good faith" action? Or does the acquiror have to be blissfully ignorant of the past corruption? If so, does that not create incentives for acquirors to put their heads in the sand, contrary to the intent of the FCPA and international standards?

And what of the "due regard" obligation, a rather vague and even circular concept, since what is due may depend on the third-party's good faith? Presumably the lapse of time will be relevant to whether revocation is appropriate, as well as subsequent investments made by acquirors in reliance on good faith.

Finally, what remedies would a third party have in the event of rescission or annulment of a concession? If the third party were a foreign investor in a country having a bilateral investment treaty (BIT) with the investor's home country, the protections of the BIT, for example, against expropriation and unfair and inequitable treatment would apply. So would concepts of non-discrimination (national treatment and most-favored-nation treatment). Although corruption might be asserted as a defense to claim under these provisions, the host government would, therefore, presumably want to proceed with great caution before revoking previously granted rights.

This brief discussion highlights the difficult issues the revocation remedy envisioned by Article 34 implicates.

A second provision of concern is Article 35 of the U.N. Convention, which requires states to take such measures as may be necessary, in accordance with their domestic law principles, "to ensure that entities or persons who have suffered damage as a result of an act of corruption have the right to initiate legal proceedings against those responsible for that damage in order to obtain compensation." The mandatory language of this article appears to require states to establish private rights of action in civil proceedings for damages. Although corruption issues have represented increasingly fertile ground for private civil litigation in recent years, recognizing private rights of action from criminal anti-corruption statutes such as the FCPA/60/ would almost certainly expand the scope of such actions.

Despite the mandatory language of Article 35, the *travaux préparatoires* to the U.N. Convention state as follows:



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> [T]his article is intended to establish the principle that States Parties should ensure that they have mechanisms permitting persons or entities suffering damage to initiate legal proceedings, in appropriate circumstances, against those who commit acts of corruption (for example, where the acts have a legitimate relationship to the State Party where the proceedings are to be brought). While Article 35 does not restrict the right of each State Party to determine the circumstances under which it will make its courts available in such cases, it is also not intended to require or endorse the particular choice made by a State Party in doing so./61/

The U.S. government apparently interprets this note as not requiring it to adopt new federal legislation establishing a cause of action for damages suffered from corruption, and indeed, the article is written in non-self-executing terms. However, questions have been raised whether this language, even if the absence of specific implementation, will influence courts asked to decide whether the FCPA or other existing anti-corruption laws implicitly create private rights of action against investors based on corrupt activities. It has also raised the question as to whether the U.N. Convention as a whole, and this provision in particular, may provide a basis for action under the treaty prong of the Alien Tort Claims Act./62/ Properly handled by the United States in the ratification process, Article 35 would, in fact, appear to raise little risk of this./63/ However this issue plays out in U.S. ratification of the U.N. Convention with respect to the ability of plaintiffs to access U.S. courts seeking damages, it seems clear such damage actions will become more common in other countries.

Whether these new remedies created by the U.N. Convention are good or bad depends very much on whether one expects them to be used offensively against one, and whether one thinks about the importance of private actions in relation to public enforcement. Although it is much too early to have a sense of how these provisions are likely to be implemented at the national level, there is no doubt they could have significant implications for investment transactions.

**F. International Financial Institutions**

Finally, as noted above, international financial institutions also have taken new initiatives to avoid financing corrupt activity. These initiatives, if enforced and supported by various civil service reform efforts encouraged by the banks in borrower countries, may have a substantial long-term impact on corruption. Within the World Bank Group, the International Development Association (IDA) and the International Bank for Reconstruction and Development (IBRD) have issued revised guidelines for procurement under IBRD loans and IDA credits and for the use of consultants by borrowers that included anticorruption provisions. World Bank, Guidelines: Procurement under IBRD Loans and IDA Credits, §§ 1.14, 1.15 (May 2004) <siteresources.worldbank.org/intprocurement/resources/procurement-may-2004.pdf> Guidelines: Selection and Employment of Consultants by World Bank Borrowers, §§ 1.22, 1.23 (May 2004), <siteresources.worldbank.org/intprocurement/resources/consultant-may-2004.pdf>. The procurement guidelines delineate immediate and specific consequences for violations. Upon discovery of fraudulent or corrupt conduct by a bidder or, once financing has been granted, by a borrower, the guidelines state that the Bank will reject the bidder's proposals for awards, cancel the remaining portions of loans already granted to the borrower, and debar the borrower from future World Bank financing, either for a specified time period or indefinitely. To help World Bank officials in policing possible corrupt activities, the guidelines give the World Bank the right to inspect the books and records of any suppliers and contractors involved in the performance of a bank-financed contract, and to submit the records to outside auditors appointed by the World Bank. Similar requirements are created by the consultant guidelines, which include provisions for canceling financing to borrowers if it is determined that their consultants engaged in corrupt or fraudulent behavior. The International Finance Corporation and other IFIs involved in project lending have also adopted, or are adopting in this area, new rules and contractual standards to enforce these rules. In early 2004, the World Bank determined to require that bidders on World Bank-financed projects certify that they have a compliance program in place.

As noted in the introduction to this chapter, these rules are being enforced, even as the World Bank is subject to continuing criticism about not doing enough to stem corruption in donee countries. In July 2004, the World Bank debarred for three years a Canadian company,



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Acres International Limited, finding that Acres had made payments to its representative in Lesotho knowing that they would be used to bribe the government official responsible for a World Bank-financed project./64/ The debarment followed an August 2003 affirmation on appeal of Acres's conviction in Lesotho for bribery. Other major companies have been sanctioned by the World Bank as well. *See, e.g.,* "List of Debarred Firms: Fraud and Corruption," <web.worldbank.org/wbsite/external/projects/procurement/debarred.html>. To the extent investments involve IFI financing or funding, the risks of running afoul of the IFIs' new anticorruption standards must be taken into account.

With the above summaries of the relevant U.S. law and international standards in mind, this chapter will now discuss specific scenarios in the investment context that can create the potential for FCPA liability.

## IV. Specific Investment Scenarios and Issues

The application of the FCPA to investment transactions is best explained through examination of different investment scenarios. In this section, we examine issues as they arise under three basic investment models: a private joint venture/private merger or acquisition, a joint venture with a company owned by a "foreign official," and a joint venture with a government or parastatal organization.

### A. Private Joint Ventures or Mergers/Acquisitions

A U.S. company investing in a foreign country may

- — acquire 100 percent of the stock or assets of an existing business;
- — acquire only a portion of the stock or assets of an existing business;
- — merge an existing in-country operation with one owned and operated by another in-country investor; or
- — make a "greenfield" (new) investment alone or in conjunction with other partners.

The structure of any of these investments will be dictated by business, tax, and other considerations in the United States and in the host country.

The primary FCPA concern in this context is vicarious liability for the U.S. investor. Such liability concerns can arise either from actions taken by a foreign partner or acquiree either in the past or, even more acutely, from ongoing operations that are related to the business being entered into or acquired by the U.S. investor, or from the fact that the foreign partner is actually owned or controlled by a foreign government official.

The risks can derive not only from direct investments in foreign countries, but also through mergers or acquisitions with other U.S. companies with multinational investments and operations. As discussed below, several recent cases (*Syncor, Baker Hughes,* and *ABB,* as well as reports related to the recently abandoned proposed acquisition of Titan by Lockheed) have involved U.S. companies that were considering acquiring or had recently acquired other U.S.-based businesses with foreign operations as to whose activities FCPA issues were raised. In some cases, these issues were uncovered during due diligence related to the proposed merger or acquisition. In others, the issues arose after the transaction was completed (thus transferring responsibility and liability to the acquiror), but prior to the complete implementation of compliance controls by new management. Further, enforcement officials in the FCPA, as well as the customs, export controls, and sanctions areas, have echoed a theme of successor liability through enforcement actions and other forums. While these positions have yet to be tested in court, they raise substantially the potential risks in merger and acquisition transactions.

#### 1. Threshold Issues

Whatever the structure, there are several potential FCPA issues that face a U.S. company contemplating a joint venture, acquisition, or investment in a foreign host country or a merger/acquisition involving international operations.

#### a. Identity of Partner or Acquiree

At the outset, the U.S. company should establish the identity and credentials of its prospective partner or acquiree. This is an extension of the "know your customer" concept prevalent in other regulatory areas, such as export controls and antimoney laundering. In the anticorruption compliance context, the questions focus on whether the partner or acquiree is really a private company, or whether there is some type of indirect owner-



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ship or control by the government or a government official — for example, a "silent partner" relationship. The U.S. company should conduct the appropriate due diligence — in the same fashion as it would perform due diligence on a prospective agent — to make this determination.

The true ownership circumstances of the foreign partner may not always be easy to determine, particularly if there are bearer shares or the ultimate beneficial owner (UBO) is several levels up from the shareholder entity. The UBO may have deliberately created a non-transparent structure to hide its ownership interests. If due diligence (discussed below) reveals that the company is truly private, the mere formation of a joint venture or the transfer of funds related to a merger/acquisition (*e.g.,* the mere issuance of shares in the venture to a foreign partner or the entering into of the investment agreement) does not meet the second element of the FCPA: Nothing "of value" has been given or promised to a government official through the operation of the investment transaction. Pre- or post-formation transactions of the foreign partner or the merged or acquired entity may raise issues for the U.S. investor, however.

**b. Potential Preformation/Premerger Payments**

The activities of even a purely private foreign partner prior to the formation of the joint venture or the acquisition may raise FCPA issues for the U.S. partner or acquiror. The most obvious example is if the foreign partner or acquiree has made a bribe, offer, or promise of payment to a government official to get, for example, permission to transfer part of an existing interest, a business license, or a natural resource concession to the joint venture or the foreign partner.

Under the vicarious liability provisions, the U.S. company's potential liability in this instance will turn on whether it had "knowledge" of or "authorized" the payment. While at the preformation stage of a transaction there may be no contractual relationship binding the two parties, the U.S. company, nonetheless, could be held vicariously liable for an illegal payment if the intent is to secure a benefit in which the U.S. company, as a coventurer or acquiror, will share, and if (because of the existence of "red flags" or other facts) it authorizes, or is aware of and consciously disregards the probability of such a payment occurring./65/

Enforcement officials have stated that, in their view, the U.S. company has an obligation to avoid compensating the foreign partner/acquiree for any past improper payments. Reimbursement of the foreign partner for any such prior payments is viewed by the DOJ as equivalent to participating in the original payment, since the economic effect is the same as the case where a U.S. party merely uses the foreign partner as a conduit for the payment. As discussed in more detail below, this view has shaped DOJ requirements on safeguards required for proposed transactions to pass muster in the Opinion Procedure process. *See* FCPA Opinion Procedure Rel. 01-01 (May 24, 2001) (some safeguards included measures to relieve the joint venture of liability for past payments to agents of acquiree).

In many cases, however, a U.S. company should not be liable for the activities of a foreign partner or related company prior to entering the relationship. A number of factors determine the relative risk of liability. The structure of a transaction often has legal effects. For example, a joint venture may involve only a foreign subsidiary of a company otherwise covered by the FCPA; indeed, there are often several intervening subsidiaries between the venture partner and the ultimate parent that are designed to limit the liability of the parent for the acts of its affiliate. In a merger/acquisition context, legal responsibility for the actions of an acquired or merged entity can depend, in part, on whether the transaction involved an equity or an asset purchase. Generally, purchases of assets do not convey the potential legal liabilities of the entity from which the assets were purchased./66/ Conversely, a transaction involving the transfer of equity generally conveys both the assets and liabilities of the acquired or merged entity to the successor in interest. Successor liability in the context of the FCPA thus may depend in part upon the structure of the transaction. It may also depend on the knowledge and intentions of the buyer. Even an asset transaction could be a vehicle for improper payments. However, one advantage of an asset transaction is that it may allow for risky assets to be excluded from the transaction.

Successor liability has not been squarely addressed in enforcement actions over the last few years; avoiding such liability, however, has been a key driver of corporate behavior. The relevant cases and review releases identify two significant factors that enforcement officials



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have signaled are important in determining possible successor liability for past actions:

(1) the extent of due diligence conducted (or lack thereof) to identify and address potential issues; and
(2) the extent and effectiveness of safeguards adopted to prevent reimbursement by the acquiror/U.S. partner of improper actions and to prevent them in the future.

**(1) *The Importance of Due Diligence.*** A basic step often cited by enforcement officials to address potential liability for the actions of business partners or other "intermediaries" (such as agents or consultants) is due diligence. As noted by the DOJ, "[t]o avoid being held liable for corrupt third-party payments, U.S. companies are encouraged to exercise due diligence and to take all necessary precautions to ensure that they have formed a business relationship with reputable and qualified partners and representatives." U.S. Dep't of Justice and U.S. Dep't of Commerce, "Foreign Corrupt Practices Act: Antibribery Provisions," Mar. 15, 2002, <www.usdoj.gov/criminal/fraud/fcpa/dojdocb.htm>.

In our view, the test for whether a due diligence effort has been sufficient should be thoroughness within the standards of reasonableness. This is not a "one size fits all" test: the necessary scope and depth of such due diligence will be driven by the facts and circumstances of each case, particularly the "red flags" present. A transaction involving only minimal or no red flags will likely require a very different level of effort than a transaction involving multiple or serious ones. If the U.S. investor has conducted reasonable inquiries under the circumstances and has not become aware of a foreign official's interest or of past improper payments by the venture partner or possible acquiree as a result — and does not otherwise have "knowledge" of that interest (through potential red flags that are discovered but not examined and addressed) — payments to the joint venture partner or for the acquisition should not be considered to be made with the knowledge of an impermissible pass-through./67/ Obviously, the investor covered by the FCPA must be able to document the nature and results of the search to establish its reasonableness.

The question of what steps are reasonable has been a focus of several opinion releases and cases related to investment transactions, mostly in cases where pre-acquisition due diligence has uncovered payments by the potential acquiree. The most recent release, FCPA Opinion Procedure Release 04-02 (July 12, 2004), is related to the *ABB* enforcement action (discussed below). While the release is the most direct indication yet by the DOJ on what measures it might consider necessary to avoid successor liability in the FCPA context, many may question how appropriate the extraordinary measures taken in that case are for a more general standard. According to the Opinion, after execution of a preliminary acquisition agreement in October 2003, the investor group acquiring certain ABB affiliates and ABB agreed to jointly conduct an "FCPA compliance review," as part of the preacquisition due diligence using separately engaged outside counsel and forensic auditors, of the relevant entities for a five-year period. ABB provided the investors with access to relevant witnesses and records. The Opinion notes that this review entailed

— over 44,700 "man-hours" of work by more than 115 attorneys;
— manual review of over 1,600 boxes and 4 million pages of documents and electronic files;
— over 165 interviews of current and former employees and agents of the entities;
— review by over 100 forensic accountants of details of hundreds of thousands of transactions in twenty-one countries; and
— twenty-two separate reports by investors' counsel on the entities' operations.

In keeping with the enforcement agencies' recent emphasis on "real-time enforcement," all documents and witness interview memoranda were provided to the DOJ and SEC as they were produced.

The extent and evident cost of the extensive measures cited in the Opinion are such that many would consider this to be wholly impractical in many circumstances and thus of limited value as a template for other merger/acquisition situations. Over 44,700 man-hours of work by more than 115 attorneys — which could entail costs of $10 to 20 million, or even more — do not represent, in our view, a plausible minimum standard for avoiding



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successor liability, even if the costs were shared between the acquiring and acquired companies. Thus, we turn to other releases to assess this issue.

In another recent release, FCPA Opinion Procedure Release 03-01 (Jan. 15, 2003), a U.S. issuer requested clarification of how the DOJ would view the purchase of the stock of an unnamed company where due diligence revealed that officers of a foreign subsidiary of the acquiree had authorized and made payments to individuals employed by foreign state-owned entities to obtain and retain business. Both the requesting issuer and the acquiree had disclosed results of investigations into the payments to the DOJ and the SEC. The requestor expressed concern that by acquiring the company it would also acquire potential criminal and civil liability under the FCPA for the past acts of the acquiree.

The DOJ indicated that it would take no enforcement action against the issuer for the preacquisition conduct of its future subsidiary. Among the relevant facts cited in the release supporting this determination were the remedial actions taken by the acquiree, including disclosure to the public and suspension of senior officers and employees implicated in the payments pending the conclusion of acquiree's internal investigation. The acquiring issuer also represented that it would perform the following actions once the sale were completed: continued cooperation with the DOJ, SEC, and foreign law enforcement;/68/ appropriate discipline of employees found to have made the improper payments; disclosure of any additional preacquisition payments made by the acquiree; extension of requesting issuer's compliance program to the acquiree; implementation of a system of internal controls at the acquiree; and maintenance of accurate books and records.

A similar factual pattern was at the heart of the *Syncor* case (indeed, there are indications that Release 03-01 is related to this case). Syncor International Corporation voluntarily disclosed, in November 2002, that its planned merger partner, Cardinal Health Inc., had, in the course of its merger due diligence, discovered evidence of possible improper payments to officials of state-owned health care facilities abroad. According to public papers in the case, Syncor Taiwan, a foreign subsidiary of the acquiree, paid physicians employed by state-owned hospitals in Taiwan in order to secure sales of pharmaceuticals and to obtain referrals of patients to medical imaging centers owned and operated by the company. The improper payments, which totaled $457,117, were made with the authorization of the chairman of the board of Syncor Taiwan. The payments were recorded as "promotional and advertising expenses." The investigation by Syncor and Cardinal also uncovered smaller payments by subsidiaries in Mexico, Belgium, Luxembourg, and France. *SEC v. Syncor Int'l Corp.*, 1:02CV02421 (D.D.C. Dec. 10, 2002), Lit. Rel. No. 17887. As a result, Syncor International paid a $500,000 fine, at the time the largest fine ever in an SEC FCPA enforcement action. *Id.* At the same time, Syncor Taiwan paid a $2 million fine to settle a single criminal FCPA charge. *United States v. Syncor Taiwan, Inc.*, No. 02-CR-1244-ALL (C.D. Cal. 2002).

Another recent case, the *ABB* case, arose out of a voluntary disclosure by ABB in late 2003 reportedly derived from internal due diligence performed in advance of an agreement between ABB and a consortium of private equity investors to sell two ABB subsidiaries to the consortium. *United States v. ABB Vetco Gray, Inc. and ABB Vetco Gray U.K., Ltd.,* Case No. 04-CR-279-01 (S.D. Tex. July 6, 2004)./69/ To resolve allegations of over $1.1 million in payments to government officials in Angola, Kazakhstan, and Nigeria through cash, gifts, entertainment, and sham consulting contracts, ABB, Ltd., a Swiss-based foreign issuer, agreed to a settlement requiring it to disgorge $5.9 million in allegedly ill-gotten earnings and pay a $10.5 million civil penalty to the SEC. At the same time, the two ABB subsidiaries that engaged in the illicit transactions, ABB Vetco Gray, Inc. and ABB Vetco Gray U.K., Ltd., each agreed to plead guilty to a related two-count felony information in a plea agreement with the DOJ, and each were assessed $5.25 million in criminal fines. The SEC's $10.5 million civil fine against the parent was deemed satisfied by the subsidiaries' payment of the criminal fines. Resolution of the potential liability and completion of internal due diligence were reportedly conditions of the Purchase and Sale Agreement, announced in January 2004, and these requirements were expressly acknowledged in the plea agreements entered into by ABB's subsidiaries.

Failure to conduct appropriate due diligence prior to closing an acquisition or making particular payments can



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have consequences. At least one case suggests that the failure to perform due diligence prior to a payment was itself a partial basis for liability. The *Baker Hughes* case primarily involved payments in Indonesia to tax authorities authorized by senior officers of the company. However, the SEC's order in the case noted that in investigating the Indonesian payments, Baker Hughes discovered that an acquired entity, Western Geophysical, had previously made payments through subsidiaries to agents in India and Brazil "without determining to whom the money ultimately would be paid or the specific purpose of the payment." *In the Matter of Baker Hughes Inc.,* SEC Accounting and Auditing Enforcement Rel. No. 1444 (Sept. 12, 2001) at 13. In India, an agent of the Indian subsidiary paid $15,000 to obtain shipping permits in India and later sought reimbursement from the company. The subsidiary paid the agent and recorded the payment without determining to whom the money ultimately would be paid, thereby inaccurately describing it in its records. In Brazil, the company approved a $10,000 payment made by its Brazilian agent to obtain an approval for the restructuring of Baker Hughes entities in Brazil. The company recorded this payment without determining to whom the money ultimately would be paid and inaccurately described it.

The public documents in *Baker Hughes* do not explicitly state that the payments in India and Brazil were actual bribes. The violation noted by the SEC seems to be based on the acquiring parent's responsibility for the subsidiary's failure to perform due diligence sufficient to ensure that the payments, whatever their size, were not bribes. In public statements, SEC officials have suggested that the payments may not have been accompanied by back-up documentation sufficient under generally accepted accounting principles. The consent decree includes a specific requirement that due diligence be conducted in the future.

Thus, in recent years, due diligence has emerged as the most fundamental FCPA safeguard to be taken by covered entities and persons in preparation for all transactions, whether they be agency retainers or investment deals. As is evident in the above discussion, the absence of appropriate and thorough due diligence may result in successor company liability for past FCPA violations. What diligence is due continues to be a case-by-case determination, though it can be costly. A set of established steps and types of inquiries can be adduced from the relevant authority, and § V.B.1. below discusses these steps.

However, the conduct of due diligence itself is not sufficient; failure to respond to issues raised by due diligence can have serious consequences later. For example, the *Triton Energy* case materials from the SEC show that management "ignored danger signals and took no precautions" in response to various pieces of information, including reports collected by a controller during due diligence prior to Triton's assumption of operator responsibilities from a predecessor venture partner regarding cash payments to Indonesian officials. *See In the Matter of Gore, Puetz, McClure and Murphy,* SEC Accounting and Auditing Enforcement Rel. No. 889 (Feb. 27, 1997) at 12. The parent company ultimately consented to an order for a $300,000 fine. *SEC v. Triton Energy Corp.,* 1:97CV00401 (D.D.C. Feb. 27, 1997), Lit. Rel. No. 15266. Addressing issues raised by due diligence is the focus of the next section.

**(2) *Designing Appropriate Safeguards.*** As shown by the outcomes of the cases discussed above, acquirors can better manage potential FCPA risks by conducting pre-transaction due diligence. Indeed, failure to conduct due diligence can lead to successor liability that can adversely affect the anticipated economic benefit of a transaction. Identifying potential issues is not sufficient, however, since discovery of the past action represents a "red flag" regarding the activities of the foreign partner that may give the U.S. company the "knowledge" requisite for future vicarious liability for any similar acts the foreign parties might take post-closing. To reduce liability risks, an acquiror or venturer should design and implement safeguards that respond directly to the red flags identified.

In the acquisition context, both the DOJ and the SEC have made it clear they are looking to acquirors that uncover FCPA issuers in pretransaction due diligence to commit to implement "rigorous" anticorruption compliance programs that cover the acquired entity. *See* FCPA Opinion Procedure Rel. 04-02 (July 12, 2004). Section V.A. below covers most of the nonremedial elements of such programs./70/



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The need for implementing these compliance programs and any transaction-specific safeguards as soon as possible after the acquisition or merger is highlighted by the *Baker Hughes* case. As discussed above, the company found that an affiliate had made payments through subsidiaries to agents in India and Brazil without appropriate levels of due diligence. The payment in India related to the activities of a wholly owned subsidiary of a company, Western Geophysical Corporation, which Baker Hughes acquired in August 1998 as part of its acquisition of Western Atlas Corporation. The payment occurred only two months after Baker Hughes acquired Western Geophysical and was not discovered until much later. Even so, the SEC order stated that Baker Hughes had violated the accounting provisions of the FCPA, as it was responsible for its newly acquired subsidiary's actions.

The DOJ has most recently addressed safeguards relevant to potential past payments by a foreign joint venture partner in FCPA Opinion Procedure Release 01-01 (May 24, 2001). In this release, a U.S. company requested clarification of how DOJ would view a 50/50 joint venture with a French company and, in particular, how the DOJ would view certain provisions of the joint venture that addressed contracts entered into by the French company prior to the enactment of French Law No. 2000-595 against Corrupt Practices (FLAC), implementing French obligations under the OECD Convention.

The U.S. company's representations to the DOJ included assurances by the French company that none of the contracts were originally procured in violation of any applicable antibribery laws. In addition, all agency agreements entered into prior to January 1, 2000 (the FLAC's effective date), had been terminated, and any outstanding payment obligations under those agreements liquidated, such that none of those obligations would be contributed or retained by the joint venture. For agreements entered after January 1, 2000, neither the U.S. company nor the venture would expend funds to pay any obligations going forward. The joint venture also developed a "rigorous" compliance program for all future agency relationships. Finally, the U.S. company retained the right to terminate the joint venture if the French company was convicted of, or admitted, violating the FLAC or if, in the opinion of the U.S. company, the French company had violated antibribery laws in such a manner as to have a "materially adverse effect" on the joint venture. Although the DOJ agreed not to pursue enforcement action based on those safeguards, it qualified its decision in a number of respects.

The DOJ first noted that, even if the French company did not violate the FLAC or previous French antibribery laws but did contribute contracts that were in violation of another antibribery law (such as the domestic law of the country of a foreign official who may have received a bribe), the U.S. company could face FCPA liability for any continuing payments to foreign officials pursuant to or in connection with those contracts. The DOJ also specifically declined to endorse the "materially adverse effect" standard as the trigger for termination, apparently because it was viewed as potentially too narrow to ensure that the U.S. company could remove itself from the joint venture in the case of continuing bribes, which would expose it to FCPA liability. This statement illustrates the DOJ's aggressive views regarding withdrawal obligations in transactions where corruption issues have arisen. Finally, the DOJ commented favorably on the U.S. company's compliance program; however, it refused to endorse any specific parts of the program, and, in fact, the release did not discuss any of the program's details.

In an earlier Review Release, the DOJ decided not to pursue enforcement action in a case where an agent of the foreign company in which the U.S. company wished to invest offered to pay a gratuity to low-level government employees to facilitate approval of the transaction. *See* FCPA Review Procedure Rel. 84-02 (Aug. 20, 1984). The DOJ's position apparently was based on several facts:

(1) no payment was actually made;
(2) the U.S. firm had no knowledge that a payment was made and had discouraged the payment when the agent made the offer;
(3) the U.S. firm would have a minority interest in the foreign concern after the transfer of assets;
(4) the U.S. firm agreed to notify the DOJ and the host country government of any future FCPA violations by the foreign company; and
(5) the U.S. firm retained the right (but not the obligation) to sever the relationship if it learned of an FCPA violation. *Id.*/71/



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*See also* FCPA Opinion Procedure Rel. 97-01 (Feb. 27, 1997) (when it learned of possible involvement of representative in past illegal payments, requestor was allowed to pursue the relationship after obtaining direct FCPA certification by representative to DOJ and promising to monitor future performance closely).

Of course, appropriate safeguards that address potential past payments often provide a baseline for safeguards needed going forward, as future activities of an investment venture are equally likely to create sources of potential liability for companies covered by the FCPA. Section V.B.2. below discusses a sample of standard transaction-specific safeguards.

**(3)** ***Combating the Use of the FCPA as an Offensive Weapon in Merger and Acquisition Transactions.*** The potential for the FCPA to be used as an offensive weapon in mergers and acquisitions or other transactions has not gone unnoticed by both U.S. and foreign parties. Although few of these instances are reflected in published cases or review releases, the possibility of such actions are real in the authors' experience, and can raise significant issues and risks in transactions. Specifically, because no specific level of evidence is required for U.S. enforcement authorities to initiate an FCPA investigation, a party hoping to deter an acquiror through allegations of corruption may find a receptive audience in enforcement officials (both in the United States and, potentially, in the host country). The fact that such "whistleblowing" (the term is used most advisedly) may come from one with a commercial axe to grind (*e.g.*, a competitor for the assets) or even one with unclean hands (due to a role in past management of the asset) does not appear to prevent or deter an investigation. Such an action may, therefore, have the result of giving the DOJ and/or the SEC a seat at the negotiating table. That enforcement authorities' presence in the transaction will in many cases have a chilling effect on the appetite of the parties for proceeding is predictable. While this result may be appropriate for genuinely corrupt transactions, those may be the extreme, and less prevalent, victims of such a practice. More often, the merger and acquisition process will be characterized by some degree of uncertainty, ongoing factual development, the development of transactional safeguards that are responsive to the risks presented, and the ultimate evolution of a more settled picture in which the risks of going forward may be evaluated before a decision to proceed to closing is taken.

Acquirors anticipating the possibility of a whistleblower attempt to use the FCPA or host country anticorruption laws as a commercial weapon are faced with difficult choices:

- — to approach the relevant authorities preemptively;
- — to ignore the risk and hope nothing comes to pass and proceed with the transaction;
- — to halt the transaction; or
- — to proceed, with heightened vigilance and attention to safeguards.

Of course, if evidence of unclean hands on the part of the whistleblower can be developed, that evidence could be read in a countercomplaint against the whistleblower if a jurisdiction with effective enforcement and links to the whistleblower may be found. Civil litigation options may also be relevant. Even though more countries are applying domestic anticorruption laws to at least their own nationals, until active U.S. enforcement is matched by efforts of other countries, companies subject to the FCPA will likely face disparate risks of victimization through use of the FCPA as an offensive weapon.

**2. Ongoing Activities of a Foreign Joint Venture or Affiliate**

Ongoing activities of a joint venture may raise classic FCPA issues relating to payments. The joint venture or foreign company may not be a "domestic concern" or an "issuer" under the statute; if so, it would not be directly covered by the FCPA unless it took actions in furtherance of an illicit payment inside the territory of the United States or acted as the agent of a domestic concern or issuer. *See* 15 U.S.C. §§ 78dd-1(a), 78dd-2(a), and 78dd-3(a). However, the venture's or affiliate's U.S. directors and officers would be subject to the FCPA. *See* 15 U.S.C. § 78dd-2(h)(1). Also, Congress apparently intended that the covered U.S. shareholder remain vicariously liable for any illegal activities of which it has knowledge or authorizes, or if the joint venture is acting as its agent. Even if this responsibility does not arise under the FCPA's antibribery provisions, parents have been held responsible for their affiliates' or ventures' actions under the accounting provisions. Difficult questions can thus arise in the operation of a joint venture.



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Formal management or informal control of the venture by the U.S. shareholder or affiliate results in various ways for FCPA risks to arise. In its managing role, the U.S. company or its officers may have direct responsibility for actions taken or a greater chance to authorize or acquire (or be imputed with) "knowledge" of illegal activities. The *Monsanto* and *Triton Energy* cases illustrate this risk with regard to a wholly owned subsidiary. The complaint in *Triton* alleged that the parent company violated the FCPA because it failed to exercise sufficient control over its subsidiary's activities, including failing to remove employees suspected of making illegal payments and ignoring a whistleblowing report by an internal auditor, while the complaint in *Monsanto* suggested the parent was responsible for payments of its foreign subsidiary./72/

Is it better, then, for the U.S. partner not to manage the venture or affiliate business, or to have only a minority stake? These decisions are transaction-specific, and investors must weigh the possibility of reduced liability against the disadvantages that may come with a reduced interest. In any event, level of ownership, or even lack of active management by a parent, is not likely to be dispositive./73/ Even without it, a U.S. partner with knowledge of the activity or an ability to veto the action at the board or shareholder level could be held responsible for an FCPA violation.

For example, what if shareholders are requested to infuse the venture with more capital, and the shareholders are made aware that such capital is intended to fund or reimburse an illegal payment? FCPA Opinion Procedure Release 01-01 (May 24, 2001), discussed above, makes clear that the DOJ would consider any such request to create FCPA liability for the shareholder if granted. While the venture itself may be beyond the reach of the FCPA's jurisdiction in this case (though not if it or its personnel takes any action in furtherance of the payment in the United States), the U.S. shareholder or U.S. officers, directors, or employees of the venture could be held indirectly liable if they had "knowledge" of the illegal payment. The SEC actions against former Triton Energy managers make clear that "knowledge" could be imputed if such personnel ignored red flags or engaged in other "head-in-the-sand" behavior.

Or what if the U.S. directors become aware that foreign management has made or committed to make questionable payments in the course of operations? While there are no cases directly on this issue, U.S. enforcement officials have made it clear that such directors are still covered by the Act and must, therefore, take all actions possible within the scope of their effective powers to prevent such a payment by the venture, including voting against it repeatedly.

The basic question becomes: To what extent does a U.S. shareholder in a foreign-managed entity have a duty of inquiry with regard to the affiliate's ongoing conduct, to protect itself against an allegation that it put its head in the sand? Could the "good faith" obligation in the books and records context with regard to minority-owned foreign affiliates be applied by analogy in the antibribery context? As these questions suggest, even with a minority stake, a U.S. investor in a foreign enterprise is not insulated from risk./74/

**3. Subsequent Changes in Ownership**

FCPA risks may arise if the foreign partner is a private company at the time of the initial investment, but its ownership subsequently changes. The potential risk is determined by the identity and role, and the U.S. company's knowledge of, the new owners of the business partner.

Issues can be triggered if the new owner is a government official (*see* § III.B. below), a government body (*see* § III.C. below), or is otherwise in a position to influence official decisions (*e.g.*, a member of the royal family or a close relative of the president of the host country). However, the more important considerations are the owner's role (were they brought in to influence the government or "to obtain or retain business"?) and the U.S. partner's knowledge of and participation in the ownership change (did the U.S. company, for example, exercise knowledgeable shareholder consent in the new ownership arrangement?). If all of the answers to these questions are affirmative, there could be an FCPA problem.

Again, the broad knowledge standard of the statute does not allow U.S. companies to bury their heads in the sand regarding these issues. FCPA liability can arise even if the U.S. company had no actual knowledge of all the details of the new ownership structure. The best way



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to prevent risks is to be forewarned about changes in ownership. When structuring the initial venture agreement, U.S. companies should insist — as they often do in the trade context — on including obligations to disclose any change in the foreign partner's ownership status. Termination rights and indemnification rights linked to any such changes, both discussed below in § V.B.2.e. and f., may also be desirable.

### B. Joint Venture with a Company Owned or Controlled by a Government Official

A joint venture with an entity owned or controlled by a government official raises issues of both vicarious and direct liability under the FCPA. In many countries, including several key emerging markets,/75/ it can be very difficult to tell who is a government official. In some cases, a U.S. company can encounter people at every level of the host country's government, each with an interest in, or a claim of authority over, a proposed transaction. Sorting out these officials' portfolios and the general scope of officialdom in the host country is a key threshold issue for FCPA compliance./76/

#### 1. Official Position

The FCPA defines a "foreign official" as "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." 15 U.S.C. §§ 78dd-1(f)(1) and 78dd-2(h)(2).

This definition has broad coverage and can apply to individuals whose "official" status may not be readily apparent. Someone who is not a full-time government employee may, nevertheless, have a special appointment to perform a specific task that may render him or her a foreign official under the "acting in an official capacity" prong of the definition. *See United States v. Young & Rubicam, Inc.*, 741 F. Supp. 334 (D. Conn. 1990) (indictment for conspiracy to violate FCPA based on payments of kickbacks to the Jamaican Minister of Tourism and an individual who acted on behalf of the Minister and the Tourism Board and served as chairman of a government instrumentality involved in tourism); *SEC v. Ashland Oil, Inc. and Orin E. Atkins* (Complaint for Permanent Injunction), 2 FCPA Rep. 696.95, 696.97 (July 8, 1986) (enforcement action involving bribery of a British national holding several official positions, including "special adviser" to the Sultan of Oman on intelligence and security issues, a position not listed in the official *Oman Gazette*). In FCPA Review Procedure Release 80-1 (Oct. 29, 1980), the DOJ indicated that even an honorary government official with only ceremonial duties and no substantive decision-making responsibilities was, nonetheless, a "foreign official" under the Act. Thus, the standard for being designated a "foreign official" is relatively low.

U.S. enforcement authorities have treated payments to spouses and dependent family members of foreign officials as payments that directly benefit the officials themselves. In the *Metcalf & Eddy* case, the complaint explicitly alleged that paying for the first class travel of the chairman's immediate family members (his wife and two dependent children) was "a payment of a thing of value to the chairman." *United States v. Metcalf & Eddy, Inc.*, 1:99cv12566 (Complaint) (Dec. 9, 1999). In the *BellSouth* case, the company settled without admitting liability and paid a fine in a case in which the SEC alleged that its Nicaraguan subsidiary had improperly recorded payments to the wife of a Nicaraguan legislator who was the chairman of the legislative committee with oversight over telecommunications issues. *SEC v. BellSouth Corp.*, 1:02-CV-0113, Lit. Rel. No. 17310 (N.D. Ga. Jan. 15, 2002). *See also* FCPA Review Procedure Rel. 83-02 (July 26, 1983) (addressing travel and entertainment expenses for the wife of a foreign official).

An additional issue arises when dealing with officials and employees of "instrumentalities," who fall within the definition of "foreign official." Employees of wholly state-owned companies are clearly covered. *See, e.g., SEC v. ABB Ltd.*, 1:04CV1141 (RBN), Lit. Rel. No. 18775 (D.D.C. July 6, 2004) (payments to engineers at Angolan state-owned oil company and to consultant also employed by Kazakhstan state oil company). However, especially in the mid- to late 1990s, many state enterprises that had been wholly owned by foreign governments were partially privatized to raise capital for the company's operations or to raise general revenues for the country's treasury. This raises the question of what level of government ownership or control is required for an entity to be deemed an "instrumentality" under the FCPA.



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The Act itself provides no definition of "instrumentality." The OECD Convention, which the FCPA was designed to implement when amended in 1998, in its official Commentaries defines state ownership to include those "public enterprise[s]," regardless of legal form, over which a government may, directly or indirectly, "exercise a dominant influence." Commentaries on the Convention on Combating Bribery of Officials in International Business Transactions ¶ 14 (Nov. 21, 1997), *reprinted in* 37 I.L.M. 8 (1998) (Commentaries). The Commentaries provide further, "This is deemed to be the case, *inter alia,* when the government or governments hold the majority of the enterprise's subscribed capital, control the majority of votes attaching to shares issued by the enterprise or can appoint a majority of the members of the enterprise's administrative or managerial body or supervisory board." *Id.*

The Commentaries thus look not only to ownership, but to functional control. Applying their definition to the privatization scenario, they appear to treat an entity as a public enterprise until the moment when the government gives up control. Although the Commentaries do not address explicitly the issue of negative control — veto power — the "dominant influence" language appears to suggest affirmative rather than negative control. If correct, this interpretation would mean, for example, that 50/50 joint ventures, or "golden share" arrangements, would not confer public enterprise status under the OECD Convention, and thus under the FCPA./77/

The OECD Commentaries also look to another factor to determine whether officials or employees of "public enterprises" fall within the scope of the OECD Convention's prohibitions: whether officials of such enterprises should be deemed to perform a "public function." This analysis reflects the commonsense notion that, when governments enter into private enterprise, not all of the enterprise's actions should be deemed to be "public functions." Sometimes these state-owned enterprises are just commercial actors and the prohibitions on corruption of public officials should not extend to such actors just because some countries choose, unlike the United States, to be commercial actors. The OECD Commentaries state that "[a]n official of a public enterprise shall be deemed to perform a public function unless the enterprise operates on a normal commercial basis in the relevant market, *i.e.,* on a basis which is substantially equivalent to that of a private enterprise, without preferential subsidies or other privileges." Commentaries, ¶ 15.

Whether courts will look to the OECD Convention for guidance on this topic in interpreting the FCPA remains to be seen. The fact that the Commentaries focus on facts regarding the enterprise at issue that may not be easily ascertained (for example, whether an entity operates on a regular commercial basis) may discourage reliance on the Commentaries's standard in compliance practice.

Returning to the FCPA's text, the FCPA's definition of "foreign official," although broad, does not cover the entire potential universe. A former government official does not remain a "foreign official" under the FCPA. *See* FCPA Review Procedure Rel. 85-03 (Jan. 20, 1987)./78/ Also, as opposed to dependents, nondependent relatives of government officials are not themselves "foreign officials" for FCPA purposes merely because of their family relationships (*see* FCPA Review Procedure Rel. 84-01 (Aug. 16, 1984)), although there have been cases in which the DOJ has focused on family ties between nondependents when specific facts suggest influence. *See United States v. Liebo,* 923 F.2d 1308 (8th Cir. 1991) (in investigating gift of airline tickets to an official and his fiancée, part of focus was on facts showing the gift's effect on influencing the official's cousin, the key decision maker for contract at issue). However, blood ties plainly increase the risk of improper third-party payments, especially in countries where extended families tend to operate as economic units. In such situations, the DOJ has at times sought contractual commitments by such family members not to pass on improper payments to their relatives. *See* FCPA Opinion Procedure Rel. 95-03 (Sept. 14, 1995).

All this is true in the trade as well as the investment context. To the extent investment transactions tend to be longer-term, or tend to involve companies rather than individuals as partners, the risk that one's partner could be — or at least include — someone who would qualify as a foreign official is increased in the investment context.

### 2. Degree of Control by or Benefit to a Government Official

The DOJ generally assumes a pass-through in any



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relationship where a foreign partner is owned by the government or a foreign official. *See* FCPA Opinion Procedure Rel. 93-01 (Apr. 20, 1993) (payments by U.S. joint venture partner to venture assumed to benefit foreign partner directors, who were government officials). Thus, payments to companies that are wholly owned by a foreign official would likely be viewed by the DOJ as payments to that official.

Payments to companies which are controlled, but not wholly owned, by one individual raise more complex issues. If the controlling shareholder of such a company is a foreign government official, then the FCPA issue as to that individual is the same as in the case of the wholly owned and controlled company. If other shareholders are — although noncontrolling and "passive" — government officials, then a potential FCPA issue arises as to those shareholders as well. *See United States v. Rothrock*, Cr. No. 343 (W.D. Tex. June 13, 2001) (director of Russian instrumentality purchasing equipment was also director and shareholder of entity owned by the instrumentality and a Swiss company; payment of a sales commission to joint Russian/Swiss company was deemed to be payment to director); FCPA Opinion Procedure Rel. 95-02 (Sept. 14, 1995) (passive investment by some foreign officials in joint venture company presumed to benefit such officials).

Since 1995, the DOJ has taken aggressive steps that, as a practical matter, extend the effective reach of the FCPA to foreign persons, including potential investment partners, who are not otherwise covered. This has occurred both in cases in which the partners are foreign officials, and in cases where the partners are private individuals.

FCPA Opinion Procedure Release 95-03 (Sept. 14, 1995) stated that foreign parties, including a government official, represented directly to the DOJ that they would adhere to the FCPA as if they were subject to the Act. Similar direct certifications, using much the same boilerplate language, were made in FCPA Opinion Procedure Releases 96-02 (Nov. 25, 1996) (representative agreement with state-owned enterprise), 97-01 (Feb. 27, 1997) (representative agreement with private company), 98-02 (Aug. 5, 1998) (representative agreement with private company), 00-01 (Mar. 29, 2000) (new government official seeking to retain certain benefits from his former private employer), and 01-02 (July 18, 2001) (foreign official signed representations to DOJ related to joint venture). In FCPA Opinion Procedure Release 95-02 (Sept. 14, 1995), foreign officials certified directly to the DOJ that they would not undertake certain activities, and U.S. and foreign parties agreed to give the DOJ an effective veto power over the transaction should certain changes occur. This pattern indicates that the DOJ often insists on such direct certifications from foreign parties as a condition for issuing a favorable FCPA opinion.

Certifications to the DOJ may subject foreign parties to investigation and liability under U.S. laws forbidding false statements to the U.S. government. Requiring certifications from foreign parties suggests an attempt to use the false statements law as a bridge for extending the substance of the FCPA to foreign parties who are not generally subject to the Act itself./79/ While the requirements for such certifications raise issues of comity and appropriate extension of extraterritorial jurisdiction, it is clear, based on recent FCPA Opinion Procedure Releases, that the DOJ would likely request that any investor contemplating an investment with an entity owned or controlled by a foreign official obtain such a direct certification before issuing an opinion under the Opinion Release procedure.

### 3. Legitimate Business Motives and the Use of Influence

As has been recently noted by the courts, "[n]one contend that the FCPA criminalizes every payment to a foreign official." *United States v. Kay*, 359 F.3d 738, 743 (5th Cir. 2004). Thus, business relationships with government officials are permitted in certain circumstances, and with appropriate safeguards, under the Act. The DOJ has approved such relationships in its FCPA Opinion Procedure Releases. *See* FCPA Opinion Procedure Rel. 01-02 (July 18, 2001) (DOJ approved venture with foreign company to bid on government contracts whose chairman and shareholder was adviser to senior government officials and who was himself a public education official); FCPA Opinion Procedure Rel. 95-03 (Sept. 14, 1995) (DOJ approved a joint venture between U.S. company and family investment company of foreign government official that contemplated securing at least some business from the foreign government).



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However, a key question is motive. When a company proposes a joint venture or other investment transaction with an entity in which a government official is involved, a key question is why that entity or official has been selected as a partner. Is it for business expertise and knowledge of the local market, or is it for prestige and influence? If he or she has been selected for his or her influence, does that make any relationship a per se violation? What if the partner's official position is wholly unrelated to the activities of the joint venture?

Before even considering the FCPA in this context, local law implications must be considered. If the proposed partner is a government official, then his or her "outside" activities may be subject to conflict of interest rules, approval requirements, or other restrictions under local law. These need to be thoroughly investigated and addressed. Local law may also be informed by the recent spate of international conventions. For example, countries that have adopted the Council of Europe's Criminal Law Convention could ban any activities considered to be "trading in influence." If possible, however, a determination that such a transaction is allowed under local law can provide a response to any allegation of corrupt intent and may allow the investor to consider pursuing the first affirmative defense under the FCPA.

Whether the FCPA itself prohibits the selection of this type of person for his or her influence is a difficult question. The purpose of the FCPA is to stem the ***corrupt*** use of influence; it does not prohibit the use of influence per se. The legislative history of the FCPA provides that "[t]he word 'corruptly' connotes an evil motive or purpose, an intent to wrongfully influence the recipient." S. Rep. No. 95-114, at 10 (1977). *See, e.g., United States v. Liebo,* 923 F.2d 1308 (8th Cir. 1991) (bribery of officials of the government of Niger in order to influence acts and decision of the Ministry of Defense). In the *Liebo* case, the district court stated, " 'an act is corruptly' done if done voluntarily and intentionally, and with a bad purpose of accomplishing either an unlawful end or result, or a lawful end or result by some unlawful method or means." The Eighth Circuit approved this formulation. *Id.* at 1312. Like *Liebo,* most enforcement actions brought under the statute have involved extreme cases of corrupt behavior.

Consider a U.S. company that has entered into a joint venture in the telecommunications industry. Its foreign partner is a local businessman who is influential in government circles because he is a close friend of the President, and he is also an official of the government's tourism board. Thus, because of his position on the tourism board, he is likely a "foreign official" under the FCPA, but any influence he might wield on behalf of the joint venture is not likely to derive from his official position. Indeed, his official position may be the result of his personal influence. If his participation in the transaction satisfies his obligations under local law with respect to, for example, conflicts of interest, is it nonetheless an FCPA violation if he uses his personal influence to secure a telecommunications license for the joint venture?

The FCPA's element on "influence" encompasses four payment situations:

(1) payments to influence any act or decision of a foreign official in his or her official capacity;
(2) payments to induce the official to do or omit to do any official act in violation of his or her lawful duty;
(3) payments to secure any improper advantage; or
(4) payments to induce the official to influence any act or decision of a foreign government or instrumentality.

15 U.S.C. §§ 78dd-1(a)(1), 78dd-2(a)(1), and 78dd-3 (a)(1)./80/

This series of payment situations that can lead to violations substantially muddies the waters for any transaction that involves the participation of a government official, such as in the hypothetical described above. The first two prongs of this element clearly require a linkage between the actions of the official and his or her official capacity or duty. The third and fourth prongs are not so clear. The text of the third and fourth prongs suggest that ***any*** attempt by an official to influence government decision making or "secure an improper advantage," even if it is outside his or her position's authority and not in violation of his or her lawful duties as a government official, may be problematic.

Notwithstanding the literal language of the fourth prong, most enforcement actions and several DOJ releases have suggested that a nexus between a foreign



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official's "official" duties and his or her business dealings is an important element of an FCPA violation. *See, e.g., SEC v. ABB Ltd.,* Civ. No.1:04CV1141 (RBW) (D.D.C.), Lit. Rel. No. 18775, July 6, 2004 (state oil company officers and employees paid in relation to oil services contracts); *SEC v. Schering-Plough,* Civ. No. 1:04CV00945 (PLF) (D.D.C.), Lit. Rel. No 18740, June 9, 2004 (donations to charity headed by director of health fund with approval authority over pharmaceutical purchases); *In the Matter of BJ Servs.,* SEC Accounting and Auditing Enforcement Rel. No. 1972 (Mar. 10, 2004) (customs official paid to prevent deportation of equipment and customs penalties); *United States v. Kay,* 359 F.3d 738 (5th Cir. 2004) (customs officials paid for reduction in customs duties); *In the Matter of Baker Hughes, Inc.,* SEC Accounting and Auditing Enforcement Rel. No. 1444 (Sept. 12, 2001) (tax officials for reduction of tax assessment); *United States v. Cantor,* Cr. 687 (S.D.N.Y. June 4, 2001) (bank administration official for award of contract to provide holograms for bank notes); *United States v. Rothrock,* Cr. No. 343 (W.D. Tex. June 13, 2001) (state company official in charge of approving procurement contract); *compare* FCPA Opinion Procedure Rel. 96-02 (Nov. 25, 1996) (in permitted transaction, state-owned enterprise that would serve as sales representative was not in a position to influence procurement decisions of potential future customers and was under regulatory control of different and separate ministry-level organization); FCPA Opinion Procedure Rel. 95-02 (Sept. 14, 1995) (in permitted transaction, some passive shareholders of joint venture were foreign government officials, but none was employed by government ministry responsible for awarding business to joint venture); FCPA Review Procedure Rel. 86-01 (July 18, 1986) (engagement of Members of Parliament in the United Kingdom and Malaysia in various capacities permitted due to absence of linkage between official duties and proposed business undertakings); FCPA Review Procedure Rel. 80-04 (Oct. 29, 1980) (director of state-owned company permitted to enter into an unrelated business relationship subject to disclosure and other conditions).

Some enforcement actions, however, imply that this nexus is not required. In the *Ashland Oil* case, for example, the SEC took action against a bribe to an unofficial adviser to use his personal influence with the Sultan of Oman. The desired business (an oil concession) had little to do with the official's formal responsibilities (he was a general economic adviser who was later posted to Oman's permanent U.N. mission). *See SEC v. Ashland Oil, Inc. and Orin E. Atkins* (Complaint for Permanent Injunction), 2 FCPA Rep. at 696.95, 696.97 (July 8, 1986). This was, however, a case of clear corruption.

The *Lockheed* prosecution also did not hinge on ties between official duties and the type of influence exerted. In that case, Lockheed took on Dr. Leila Takla as a local consultant to generate business in Egypt. During the contract, Dr. Takla was elected to the Egyptian parliament, rendering her a foreign official. Although any influence she possessed appeared to antedate her elevation to Parliament, rather than deriving from that position (Parliament in Egypt being essentially a figurehead authority), the DOJ indicted Lockheed for violations of the FCPA under what is now the fourth "influence" prong. *See United States v. Lockheed Corp.* (Criminal Information), 3 FCPA Rep. at 699.175 (Jan. 27, 1995) (Lockheed Information). Lockheed did not admit to liability on the FCPA count of the indictment, and ultimately pled guilty to one count of criminal conspiracy to violate the FCPA./81/ As a result, the aggressive theory of the prosecution in this case was not tested.

The third prong ("securing any improper influence"), inserted as a result of the 1998 amendments deemed necessary to implement the OECD Convention, does little to clarify the issue. The phrase's analog in the OECD Convention resides not in the *quid pro quo* element of the offense, but rather in the "obtaining or retaining business" element. OECD Convention, art. 1, ¶ 1. However, Congress inserted the language into the *quid pro quo* element due to concerns by U.S. enforcement officials that inserting it in the business element would unduly narrow the broad interpretation traditionally given to the latter element. Attempting to address this incongruity, the appeals court in *Kay and Murphy* stated that the statute "now prohibits payments to foreign officials not just to buy any act or decision, and not just to induce the doing or omitting of an official function ... but also ... to secure an 'improper advantage.' " *United States v. Kay,* 350 F.3d 738, 754 (5th Cir. 2004). While it mostly merely paraphrases the



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statute, this formulation by the court suggests that a nexus between official duties and any actions to secure the improper advantage is not required.

Thus, despite the clear weight of most FCPA enforcement actions, *Ashland* and *Lockheed,* as well as the potential reach of the "improper advantage" prong as discussed in *Kay,* suggest that the tourism official's exercise of influence in the above hypothetical is potentially problematic, despite the fact that it may have been exercised outside the scope of his official duties. In our view, the FCPA should not be read automatically to bar U.S. companies from having legitimate relationships in other countries with persons who may incidentally wear government hats and, as noted at the start of this section, the DOJ apparently agrees with this view. We would argue instead that a joint venture or other arrangement with a foreign government official may be viewed as "corrupt" only if there is some clear evidence of an intent to use that relationship (or its actual use) in a manner that would offend local law or create an "improper advantage" that violates generally accepted notions of fair play.

### C. Joint Ventures with a Foreign Government

The final paradigm transaction involves an investment in collaboration with the government of a foreign country or a foreign instrumentality. The FCPA does not forbid joint ventures with government entities. *See, e.g.,* FCPA Opinion Procedure Rel. 97-02 (Nov. 5, 1997) (payment of a donation directly to a government entity, and not to a foreign government official, does not implicate the FCPA); FCPA Opinion Procedure Rel. 96-02 (Nov. 25, 1996) (retention of state-owned enterprise as marketing representative); FCPA Opinion Procedure Rel. 92-01 (Feb. 1992) (venture between U.S. oil company and Pakistan's Ministry of Petroleum and Natural Resources). As discussed above, the Commentaries to the OECD Convention distinguish between governments and state-owned enterprises having "public functions" and "normal commercial" functions. Having the government as a partner, however, raises several FCPA issues.

#### 1. Local Laws Requiring Government Participation

In some countries, local law requires that the government or a government-owned enterprise must act as a partner in any joint venture. This is especially true in certain sectors, such as natural resources or defense services and equipment. A written legal requirement for such government participation would allow a U.S. partner to raise the "local law" affirmative defense against challenges to the arrangement as a whole. In FCPA Review Procedure Release 92-01, for example, Pakistani law required participation by the government petroleum ministry. The DOJ took no action against this arrangement, apparently in part due to that legal requirement. *See also* FCPA Review Procedure Rel. 88-01 (May 12, 1988) (participation by company intending to build factory in Mexico in Mexican government debt-equity swap program).

The local law defense may not insulate all aspects of the transaction, however. For example, foreign legal requirements governing payments to the government or state-owned enterprise may create FCPA risks. The DOJ, in FCPA Opinion Procedure Release 93-02 (May 11, 1993), approved a sales agreement between a U.S. company and a government-owned business. Local law gave the instrumentality exclusive rights to purchase and import defense equipment for the country's armed forces and required the military to deal only through the instrumentality. Further, to do business with the military, local law required that all foreign suppliers enter a written agreement agreeing to pay the government-owned business a percentage of the total contract price for the sale of defense equipment. The U.S. company refused to sign such an agreement and instead agreed to pay all commissions directly to the country's treasury or to allow the military to deduct that commission from the purchase price. The DOJ approved the transaction when it was clear that "the company will make no payments to the government-owned business or to any foreign officials."

Does Release 93-02 mean that profits from an investment venture must be paid directly into the foreign government's treasury? That interpretation seems extreme, but it, nevertheless, highlights the limitations of the defenses offered by general legal requirements requiring government participation. If, for example, the foreign joint venture partner asks that its profit share be transferred offshore, FCPA concerns should be triggered./82/



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### 2. Treatment of Government Personnel

Partnership with a government entity implicates all of the potential FCPA issues that arise from business relationships with foreign officials. For example, directors and managers of the joint venture are likely to be government officials. Their compensation is subject to FCPA compliance. *See* § IV.D.1.b. below and FCPA Opinion Procedure Rel. 93-01 (Apr. 20, 1993).

The formation and management of such joint ventures often requires the training of or travel by government personnel. "Necessary and reasonable expenses" for training that are related to the business venture or generally to the "efficient performance" of the officials' duties have been approved by the DOJ. *See* FCPA Review Procedure Rel. 92-01 (Feb. 1992).

The statute allows an affirmative defense if payments made to foreign officials are "reasonable and bona fide expenditure[s]" for travel and lodging directly related to promotion of services or the execution of a contract. 15 U.S.C. §§ 78dd-1(c)(2) and 78dd-2(c)(2). The DOJ has also sanctioned U.S. companies' paying reasonable expenses for promotional travel by foreign officials to the United States. *See* FCPA Review Procedure Rel. 83-02 (July 26, 1983) (promotional tour of U.S. facilities by general manger of foreign instrumentality and his wife during their previously scheduled vacation); FCPA Review Procedure Rel. 83-03 (July 26, 1983) (tour of site inspections and meetings by a Singapore official to help promote sales to a Singapore instrumentality); FCPA Review Procedure Rel. No. 193-15 [85-1] (July 16, 1985) (inspection trip by French government officials responsible for licensing proposed chemical plant of similar plant in United States to address environmental and management concerns).

## D. Other General FCPA Issues in Investment Transactions

Several other potential FCPA issues can arise in the investment context. These issues can arise in any of the three paradigmatic structures discussed in this part.

### 1. Valuation/Compensation Issues

One of the DOJ's published "red flags" under the FCPA is whether a foreign agent or partner is receiving "compensation that is excessive." In the investment context, "compensation" can relate both to payments to an investment partner related to the valuation of the venture itself, and to the compensation of directors or officers of a joint venture.

#### a. Consideration Paid to Foreign Partners

The first issue is what consideration is being given for the foreign partner's interest in the new venture. This consideration can be the total package of equity, fees for services, and other sources of revenue or in-kind benefit from the investment.

In the agency or trade context, one approach that is frequently used to establish that the proposed compensation of the foreign party is not excessive is for a company to produce benchmarks, or "comparables." These can be based on similar transactions of the company in-country, around the world under similar conditions, or by other companies. Even in the agency and trade context, where there may be industry norms, the gathering of "comparables" is not always an easy task. The less customized the product and the transaction, the more difficult it will be to generate persuasive comparables.

In the investment context, the need for comparables to demonstrate the reasonableness of the financial package offered to a foreign partner may also arise. But in investment transactions, which tend to be extensively negotiated and tailored to the circumstances of the parties, locating benchmarks on which to judge a transaction may be extremely difficult. And some potentially relevant commercial benchmarks (*e.g.*, investment banking fees) offer little comfort due to their size.

This difficulty may be a two-edged sword; if it is difficult for a company to establish reasonableness, it may also be difficult for the DOJ to establish unreasonableness except in very extreme situations. In the *Ashland Oil* case referred to earlier, Ashland purchased a chrome mine in Zimbabwe for approximately $25 million, when more objective asset assessments and contemporaneous transactions involving a portion of the assets showed the value to be far less. In that case, the government could argue that these data showed the investment essentially to be worthless. There was also credible evidence in that case that the investment was a *quid pro quo* for the seller's use of influence on



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Ashland's behalf in an unrelated transaction. *See SEC v. Ashland Oil, Inc. and Orin E. Atkins* (Complaint for Permanent Injunction), 2 FCPA Rep. 696.95, 696.97 (July 8, 1986).

Where there is an established business, with a history of earnings and profits that a U.S. company buys into through a merger and acquisition or other transaction, the task of testing reasonableness is easier. But in a "greenfield" equity investment, who is to say that the local investor's equity contribution should have been valued at only 10 percent instead of 30 percent? Who is to say that the in-kind contribution of a foreign partner should have been valued at a fraction of its stated value? Who is to say that a premium of 50 percent for the obtaining of a key concession or license is excessive? Obviously, certain kinds of interests — preferential returns not matched by contributions, carried interests, guarantees given to the foreign partner, incentive payments, and the like — raise questions on their face. But absent such unusual features, it is difficult to justify second-guessing the parties in a truly arm's-length negotiation, where there is no evidence of an improper *quid pro quo.* If the investor has contemporaneous credible evidence establishing the basis for the valuation on legitimate grounds, the government may have difficulty meeting its burden of proof (though such evidence may not deter an extensive investigation).

Another difficult issue that arises in the investment transaction is where a foreign partner pays full value for his or her interest, but the interest is in a business that is anticipated to be a highly lucrative one. In that situation, the simple selection of a person as one's investment partner may involve the conferring of a benefit that is disproportionate to the value that is paid at the outset. The disproportionality creates the risk that an FCPA violation might be alleged. This theory, sometimes referred to as the "golden goose" theory, has never been tested in any court decision or Review/Opinion Procedure Release.

Since the reasonableness of the return could not be proven in this situation, the best response to any argument that the giving of the "golden goose" constituted a violation may be a demonstration of the legitimate reasons for the selection of the local partner and the absence of any linkage to an official action, decision, influence, or advantage. If that local partner happens to wear an official hat in some capacity, even if unrelated to the business of the joint venture, the FCPA risk from a "golden goose" transaction is obviously greater, for the reasons discussed above in § IV.B.

The best one can say about valuation issues in the investment context is that FCPA concerns in this area, unlike other aspects of the statute, tend to work in the same direction as a U.S. investor's commercial concerns, rather than at cross-purposes. A U.S. investor interested in cutting the best deal is going to want to be certain that the in-kind contribution of its foreign partner is not overvalued, and that the foreign investor is not receiving an unjustified return from the venture. At the end of the day, any element of return that cannot be justified on objective facts, and could be characterized as compensation for the exercise of official influence, direct or indirect, will be as vulnerable in the investment context as in the trade context. As in the trade context, however, the analysis will be highly fact-specific.

**b. Director and Officer Compensation**

Where directors or corporate officers of the joint venture are foreign government officials, FCPA issues arise whether the foreign partner is a government-owned entity or not. In particular, payments to these individuals or the giving of other value (*e.g.,* stock options) as compensation for their positions require FCPA scrutiny.

One DOJ release illustrates these issues. In FCPA Opinion Procedure Release 93-01 (Apr. 20, 1993), a U.S. company entered a joint venture to supply management services to a business operated by a "quasi-commercial entity ... wholly owned and supervised by the government of a former Eastern bloc country." The board of directors of the joint venture included employees of the foreign instrumentality, who were to be paid directors' fees commensurate with their normal employment income from the foreign partner. Under the parties' agreement, the directors' fees would be paid in the first instance by the joint venture, but they would ultimately be completely reimbursed by the foreign partner either from the foreign partner's share of the venture's net profits or from other sources. The DOJ stated that it would not take enforcement action under these facts because of the reimbursement plan and an undertaking by the U.S. partner to educate the foreign directors



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regarding avoidance of possible FCPA violations, but it is noteworthy that the issue was considered sufficiently unclear by the parties to merit an Opinion Request.

A more recent release, FCPA Opinion Procedure Release 01-02 (July 18, 2001), involved a planned consortium that would bid on and engage in a prospective business relationship with the government of the foreign company's home country. The chairman and shareholder of the foreign company that was the prospective venture partner acted as an adviser to one of his country's senior government officials and was himself a senior public education official. Although a number of safeguards, including substantial recusal provisions, were cited as a basis for the DOJ's decision to take no action in this case, the issue of payment of director's fees or appropriate levels of shareholder compensation were not discussed in the release.

Despite the fact that the more recent release did not address the issue, Release 93-01 highlights just how far the FCPA, read aggressively, can intrude into the investment relationship. It also focuses on two issues. First, is the compensation for foreign directors or officers proportionate to their services rendered, and comparable to the going rate for such services as determined by appropriate benchmarks? If so, the FCPA risk should be reduced. Outsized compensation is a "red flag" for enforcement purposes. Second, how is the directors' compensation ultimately funded? An arrangement that prevents the U.S. partner from directly paying the foreign director/official also reduces liability. Characteristically, the release does not state whether only one of these would be sufficient to insulate the U.S. company.

**2. Social Benefits**

Foreign investors in certain types of projects (for example, natural resource concessions) have historically been asked by the host government to contribute to the development of local infrastructure near the project, such as roads, ports, schools, medical facilities, and worker housing. Requests for such social benefits are especially common for projects in remote areas.

Giving such social benefits or participating in government programs is not a per se FCPA violation. *See* FCPA Review Procedure Rel. 88-01 (May 12, 1988) (U.S. company participated in Mexican government's debt-equity swap program in connection with proposed construction of heater production plant); FCPA Opinion Procedure Rel. 95-01 (Jan. 11, 1995) (U.S. company donated $10 million to defray construction and equipment costs for new medical facility in region where the company's new production plant would be operated). The key issue is who is the beneficiary. If the additional investment requirement or donation goes to the general treasury or is otherwise paid directly to a government entity, the DOJ has stated that, absent other facts or circumstances that raise "red flags," the FCPA does not apply. *See* FCPA Opinion Procedure Rel. 97-02 (Nov. 5, 1997). If, on the other hand, the investor subcontracts the work to a company owned by a government official, or the beneficiaries of the infrastructure work are not the general public, there may be an FCPA issue.

More difficult issues are raised by host country requests that foreign investors establish scholarships or educational foundations for local children. One objective of such requests is often to benefit the children of foreign officials responsible for approving or overseeing the project. The first Review Release issued under the FCPA concluded that creating a scholarship fund for the children of a government official was not a per se violation. A U.S. company proposed a fund for the American education and support for the adopted children of an honorary official of the host country. The official's duties were ceremonial only and did not involve substantive decision making. The natural parents of the children, who were also government employees, also were not in a position to use influence. The U.S. company stated that it received no suggestion of preferential treatment by the government in return for the fund's establishment and did not expect business resulting from the fund. The DOJ stated that it would not take enforcement action. *See* FCPA Review Procedure Rel. 80-01 (Oct. 29, 1980).

As this release suggests, the FCPA risk may again turn on the identity of the beneficiaries. A scholarship for the children of government officials who made substantive decisions affecting the company's interests (as opposed to purely ceremonial officials) could be problematic./83/ If, on the other hand, the scholarship or foundation is



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based on neutral, merit-based requirements and is open to all applicants, there is less risk of exposure. Even an open-applicant scholarship or foundation may need to be carefully monitored, however, to ensure that it does not in fact accept only the children of government officials.

Giving the donation through a charitable organization, one option frequently considered by companies in this context, does not eliminate the risks. The donation through a charity may require due diligence on the part of the charity, and the development of suitable safeguards to ensure the funds are sued for the intended purpose.

**3. Lobbying and Influencing Legislation**

Foreign lobbying also raises potential FCPA issues. For example, if a joint venture or the U.S. partner in a prospective joint venture pays for the travel and entertainment of a foreign legislator in part to convince him or her to introduce legislation that would change the business regulatory environment to allow the joint venture to enter a new line of business, is there an FCPA violation? This question, in part, implicates the last element of an FCPA violation, sometimes called the "business purpose" test.

Under the statute, the ultimate objective of a corrupt payment must be to obtain, retain, or "direct business to any person." The focus of this element is on specific business benefits, not on nonbusiness interests. This element has been the subject of recent litigation in the *Kay* case. Reversing a district court decision that narrowed the applicability of this element to exclude payments for favorable tax or customs assessments, the court of appeals for the Fifth Circuit summarized the effect of the element: "Congress intended for the FCPA to apply broadly to payments intended to assist the payor, either directly or indirectly, in obtaining or retaining business." *United States v. Kay,* 350 F.3d 738, 755 (5th Cir. 2004).

There is an argument that an attempt to influence general legislation is thus too removed from the directly or indirectly obtaining of business to be covered by the FCPA. The oft-cited example is the *United Brands* case, which involved bribery to a Honduran minister to obtain a reduction in a general export tax that would benefit the U.S. company. *See* the Foreign Trade Practices Act of 1983: Hearing on H.R. 2157 Before the Subcomm. on Int'l Econ. Policy & Trade of the House Comm. on Foreign Affairs, July 12, 1983, at 284-85 (discussion of *United Brands* case as not violative of the FCPA)./84/

Congress focused on this ambiguity in its debate of the 1988 FCPA amendments. The final legislation specifically rejected a House proposal that would have prohibited payments to procure " 'legislative, judicial, regulatory or other action in seeking more favorable treatment by a foreign government.' " While the conference report stated that the FCPA prohibits corrupt payments for the "carrying out of existing business ... such as [for] ... obtaining more favorable tax treatment (the *United Brands* context)," it also makes clear the "retaining business" should not be construed so broadly as to prohibit companies from lobbying or other "normal representations to government officials." H.R. Conf. Rep. No. 100-576, at 918-19 (1988)./85/

Whether a payment is merely part of legitimate lobbying or is violative of the FCPA is ultimately a factual question. In the language of the *Kay* appeals court, the test is whether the bribery "was intended to produce an effect that would assist in obtaining or retaining business." *United States v. Kay,* 359 F.3d 738, 743 (5th Cir. 2004) (and that met the other elements of the offense)./86/ At least one case, the *BellSouth* matter, indicates the types of circumstances where enforcement officials may see the line as having been crossed and may, therefore, prosecute as FCPA violations payments for lobbying activities. *SEC v. BellSouth Corp.,* 1:02-CV-0113 (N.D. Ga. Jan. 15, 2002), Lit. Rel. No. 17310. In that case, the payments were made to an otherwise qualified consultant who was married to a legislator in charge of the committee with telecommunications oversight responsibility. The fact that her responsibilities included an effort to change foreign ownership restrictions of the telecommunications law was also highlighted by the government.

As even a partial reading of the above sections indicates, the FCPA raises especially difficult issues in the investment context due to the lack of official guidance, inherent valuation difficulties, and the myriad of roles that governments and foreign officials can play in different types of transactions. A company's best protection in the face of uncertainties arising both from U.S. law and the burgeoning international efforts is an



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effective risk avoidance and internal compliance program.

### V. Avoiding FCPA Violations in Investment Transactions

To minimize FCPA risks, there are two types of general safeguards a company investing abroad should build into its everyday business operations and its potential business relationships. The first is a company-wide internal compliance program to address the requirements of the FCPA and to educate corporate personnel. Such a compliance program should include the actions of the company's foreign affiliates if the company is an "issuer" and may be desirable even for a company that only meets the definition of a "domestic concern." The second type of safeguards is transaction-specific and focuses on effective due diligence. These measures are similar to what should be undertaken in a trade context, but often are more complex and more difficult in investment transactions, especially with regard to ongoing monitoring.

#### A. Compliance Programs

Although details will vary from company to company, the basic elements of an effective corporate compliance program have grown over the years./87/ A program that approximates "best practices" in the FCPA compliance area would include

- a statement of company policy to comply with the FCPA, along with other indicia showing a culture of compliance;
- articulation of compliance standards through accessible policies and procedures;
- procedures to ensure accurate books and records and sufficient internal controls;
- senior-level responsibility (at both director and management levels) for compliance;
- procedures to identify and exclude high risk individuals who could use discretionary authority to engage in improper conduct;
- procedures for the due diligence and vetting of third-party relationships;
- systems to ensure appropriate contract provisions and other safeguards are in place in all relationships with third parties;
- education and training measures for relevant company personnel and, as appropriate, for agents and other third parties;
- periodic review and updates of the program that account for changing risk conditions faced by the company, prior program effectiveness, and external metrics;
- provisions for whistleblowing, internal investigations, and sanctions for violations;
- disciplinary mechanisms for violators and personnel in major compliance roles who fail to detect violations; and
- where appropriate, provisions for applying the necessary management and financial control over the operations of foreign affiliates, whether wholly owned by the company or joint ventures with foreign partners.

These programs may address other payment issues as well, including foreign (host country) antibribery legislation, campaign contribution rules, tax provisions, foreign exchange controls, gifts, charitable contribution restrictions, and other payments issues governed by applicable U.S and foreign law.

The last of these elements (controls over foreign affiliates) may be the most difficult to set up; however, as shown by several cases (*IBM, Baker Hughes,* and *ABB*), foreign affiliates are an increasing source of potential liability to their issuer parent companies through the operation of the FCPA's accounting provisions. At minimum, close attention should be paid to ensuring the sufficiency of the company's "good faith" efforts to assure that the affiliates are following the FCPA internal control and accounting rules, as required by the Act for all "issuers." As noted above, it should also provide training and advice for foreign employees and venture partners to use in fulfilling any contractual obligations not to make corrupt payments.

#### B. Transaction-Specific Measures

When confronted with a specific transaction or opportunity, several transaction-related measures are prudent.

##### 1. Due Diligence

As discussed above, the initial "due diligence" regarding FCPA issues is extremely important in avoiding and making judgments about potential risks. When a company seeks to invest in a particular country, it should



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investigate, among other things, that country's reputation for bribery, the reputation and experience of the individuals with whom it is proposing to deal and any government positions or relationships they may hold, and the legal regime of the proposed host country. Due diligence can be time-consuming, since the relevant information is not always easy to obtain, but it should be a prerequisite to any deal. Due diligence should cover the following:

**a. The Proposed Partner or Acquiree**

Companies considering doing business abroad with a local business partner or consultant should perform adequate research into the reputation, background, ownership and management structure, and past performance of that person or entity. Sources such as the Commerce and State Departments, the local U.S. embassy, and local counsel, among others, can provide useful information on a proposed business partner. The increasing use of the FCPA accounting provisions as enforcement tools suggests that, at least in an acquisition or merger context, due diligence should include a review of financial statements to spot potential payments issues and to assess their compliance with relevant generally accepted accounting principles.

A well-documented due diligence effort, reasonable in scope, the results of which show a commercial basis for pursuing the investment relationship is also evidence that a company entered into such a relationship in good faith and without corrupt intent.

**b. Proposed Partner's Official Position**

The company should determine whether the proposed partner is, or is controlled by, a government official or a person who could be deemed a "foreign official" because he acts in an official capacity or is a member of royalty. If the partner is a government official, the company should educate itself about the duties and authority of that position within the context of the host country's government structure. If the partner is a company, the due diligence should attempt to pierce the corporate veil enough to determine the identity of the controlling interests.

**c. Reasonableness of Valuation/Compensation and "Comparables"**

The U.S. company should be confident that the consideration to be given to its business partner is in line with the "going rate" for the services to be rendered or the value to be added to the joint venture. In conjunction with its due diligence efforts it should, therefore, gather adequate information to support the reasonableness of any compensation or profit arrangement. Exorbitant fees and/or profit-sharing provisions that do not appear to be commensurate with the services to be rendered or the value of contributions given increase the possibility of raising DOJ suspicion of an FCPA violation.

The "going rate" may be determined by looking at payment practices or rates of return in the host country or for comparable investments elsewhere. As noted earlier, finding a benchmark for "comparables" can be difficult in new markets, in new or highly customized types of transactions, or where circumstances have materially changed.

**d. Country Conditions**

The U.S. investor should be familiar with the government structure of the host country. This includes knowledge of investment rules and restrictions and familiarity with the agencies or instrumentalities that might have jurisdiction over the transaction.

The company should also be aware of the host country's reputation for corruption, since a history of bribery can raise a red flag that may be a factor leading to imputed knowledge of corrupt activities.

**e. Local Laws**

An investor should also seek the advice of local counsel for guidance on issues that will affect its ability to go forward with the deal as proposed or conduct business in the country in question. If the business partner is a government official, for example, the U.S. company must determine whether local law allows the official to make outside investments, or requires recusal from certain official functions. Also, a foreign government may impose official requirements, such as local sourcing or hiring, on companies seeking to do business that could pose FCPA compliance problems for a U.S. company. Offset rules are also relevant.

Identifying and understanding the applicable law can often be difficult, and a formal opinion from local counsel on some of the issues may be required. Indeed,



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several review releases cite opinions on the legality of arrangements under local law as a favorable factor./88/ Because working through local law issues and acquiring such an opinion can take time, the U.S. investor should initiate its analysis of these issues at the beginning of its overall evaluation of the proposed transaction. Advance warning of possible local law obstacles can give the investor time to either resolve such problems without voiding the deal or terminate negotiations early if the problem is insurmountable.

Furthermore, as noted above, it is an affirmative defense under the FCPA that a U.S. party's actions were taken in accordance with the written laws of a foreign country. Although this is a defense, and may not, in the DOJ's view, be exculpatory, the risk calculus is likely to change materially if legality under local law can be established. Likewise, if the foreign country law compels the relationship — for example, by requiring a local agent or partner — that may be helpful./89/

#### f. Business Justification

A U.S. company should also be able to articulate the business justification for entering the joint venture or investment with the foreign partner. As discussed in § IV., a set of legitimate business reasons for dealing with a particular partner (*e.g.,* business expertise, potential for servicing the investment, or the like) is extremely useful for both screening the transaction internally and for preparing any defense to a possible future FCPA allegation. A business justification that is grounded primarily or solely on the foreign partner's influence may not be helpful.

### 2. Contractual Provisions

The U.S. company should carefully consider what measures need to be built into the contractual documentation to reduce the risk of FCPA violations. Boilerplate clauses binding the foreign partner to obeying applicable law or the FCPA are insufficient, since often these partners are not subject to FCPA jurisdiction. The contract should be viewed as an opportunity to educate the foreign partner and to build a structure that will minimize the risk to the U.S. company.

The appropriate contractual provisions will vary with each transaction. Set forth below are several areas that should be considered.

#### a. Representations and Warranties

In the terms of the contract, types of representations to consider requesting of the foreign partner may include

- — that no corrupt payments were made to "foreign officials" in connection with entering into or securing necessary approvals for the relationship;
- — the absence of government officials as owners or in other relevant positions in the company;
- — that its participation in the transaction is permitted by local law;
- — that no portion of the proceeds paid by the U.S. company into the venture will be used to fund payments in connection with securing government approvals, an improper advantage, or improper influence from or of a "foreign official"; and
- — that its books and records are accurate and complete.

#### b. Antibribery Covenants

Covenants that may be helpful from the foreign party include

- — advising the U.S. partner of any accession to an official position during the course of the relationship, including through a change of control; and
- — conducting future business in compliance with the FCPA or international anticorruption standard.

Rather than seeking a covenant to comply with the FCPA, to which foreign parties may not be fully subject and to which they may object, this covenant should spell out the substantive elements of an antibribery violation. A contract provision denying any authority to the foreign partner to take actions on the joint venture's or its own behalf that would create a risk of exposure for the U.S. partner under the FCPA may also be desirable.

#### c. Financial and Payment Terms

The financial terms must be scrutinized for any appearance of excessiveness of unusual windfalls. In some situations, the U.S. party may also want to document reasons for agreeing to particular compensation provisions. Consideration should be given to payment terms — such as restrictions on offshore payments — that may increase risk.

#### d. Accounting and Auditing

In some circumstances it may be appropriate to ask the



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foreign partner, if it is in a position of controlling the joint venture, to agree to maintain accurate and complete books and records for the joint venture. The U.S. partner may want to have the power to audit the joint venture's expenses and invoices with reasonable notice.

**e. Termination**

The U.S. partner may want to seek the right to terminate the relationship if any representations and warranties turn out to be materially untrue or if the foreign partner breaches any of its covenants, or if a change in position creates a material risk of liability (although this latter standard has been criticized by the DOJ in FCPA Opinion Procedure Release 01-01, May 24, 2001). Such a termination right requires consideration of buyout issues, which, particularly in the context of an operating project, can pose difficult valuation questions. As a lesser remedy, the investor may wish to reserve the right not to contribute capital to the venture if it has reasonable concerns that the contribution could be used to make a payment that could expose it to FCPA liability.

**f. Indemnification**

The U.S. partner may seek a right of indemnification for any damages caused by the foreign partner's breach or failure of warranty. While enforcement of this right may be problematic, it may, nevertheless, be useful as

- — a deterrent; and
- — evidence that all reasonable measures to prevent a violation were taken.

**g. Management Rights and Structure**

Finally, the U.S. investor may wish to ensure that the management structure of any joint venture or other entity it jointly controls with a foreign partner allows it to protect itself from possible actions by the venture that might expose the investor to possible FCPA liability. Appointment rights, a veto right on the budget of or payments made by the venture, and rights of audit are all potentially relevant. Managers for the U.S. investor should receive extra training to enable them to spot issues that may arise.

### C. Monitoring Performance

A U.S. company should constantly monitor the performance of an investment or joint venture to ensure that any future red flags are promptly addressed and that necessary remedial action is promptly taken. This may include the auditing of expenses and invoices, including review of any third-party payments, and the monitoring of any changes in official government position of the foreign business partner. As noted earlier, the ongoing operations of a joint venture in which a U.S. shareholder does not have operational control, or shares operational control with another party, raise particular monitoring challenges to avoid situations in which the U.S. shareholder could be argued to have authorized, approved, or have knowledge of, a particular action by another party.

## VI. Conclusions and Recommendations

Investment transactions raise a host of FCPA issues. Some are analogous to issues arising in the trade arena. Others are unique to the investment context. This chapter concludes with a set of guidelines to aid U.S. companies investing abroad in identifying potential FCPA problems.

Regulatory guidance on the FCPA, sparse to begin with, is even sparser for investment issues. Using the DOJ's "Red Flag" Guidelines as a starting point, we suggest that the following factors could serve as red flags in the investment context:

- — The country in which the investment will be made has a history of corruption.
- — Due diligence on the proposed foreign partner suggests possible ethical issues.
- — The proposed foreign partner is owned by a key government official or a close relative or business associate of such an official.
- — The U.S. company hears rumors that the foreign partner has a "silent partner" who is a high government official.
- — The joint venture partner's structure is non-transparent and/or relies on entities established in nontransparent havens associated with criminal activity.
- — The foreign partner cannot contribute anything to the joint venture except influence.



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— There is a significant mismatch between the foreign partner's economic interest in the venture and its contributions.

— The values ascribed to assets contributed by the foreign partner to the joint venture are excessive.

— The foreign partner insists on having sole control of any host country government approvals.

— The proposed relationship with the foreign partner is not in accordance with local laws or rules including, when government officials are involved in the commercial relationship, civil service rules, concerning outside interests.

— The foreign partner refuses to agree to reasonable financial and other controls in the joint venture.

While not all inclusive, identifying problems on this list is the first step a U.S. investor should take in determining whether the issues discussed in this chapter must be addressed in a particular transaction.

## ENDNOTES

/1/ 15 U.S.C. §§ 78dd-1(a), 78dd-2(a).

/2/ *Id.* § 78m.

/3/ I.R.C. § 162(c).

/4/ International Anti-Bribery and Fair Competition Act of 1998, Pub. L. No. 105-366, 112 Stat. 3302. See § II. below for a discussion of some of these changes.

/5/ *See, e.g.,* L.A. Low, "Consequences for FCPA Compliance: What Sarbanes-Oxley Has Wrought," *Corp. Compliance & Reg. Newsletter* (Sept. 2003).

/6/ Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745.

/7/ *See* "Sentencing Guidelines for United States Courts," 69 Fed. Reg. 28994 (May 19, 2004). On January 12, 2005, the Supreme Court determined that mandatory application of the Sentencing Guidelines was unconstitutional, though the Guidelines would remain as one of many potential advisory factors that judges could use in determining an actual sentence. *United States v. Booker,* Nos. 04-104 and 04-105 U.S. LEXIS 628 (U.S. Jan. 12, 2005). Even though the Guidelines are now considered advisory, it is likely that U.S. enforcement officials will continue to look to the Guidelines's standards for effective compliance programs in weighing decisions to prosecute in individual cases.

/8/ *SEC v. Montedison, S.p.A.,* 1:96CV02631 (RWR) (D.D.C.), Lit. Rel. No. 16948, Mar. 30, 2001; *SEC v. ABB Ltd.,* 1:04CV1141 (RBW) (D.D.C.), Lit. Rel. No. 18775, July 6, 2004.

/9/ Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, Dec. 17, 1997 <www.oecd.org/daf/nocorruption/0,2688,en_2649_34859_1_1_1_1_1,00.html>.

/10/ Inter-American Convention against Corruption, Mar. 29, 1996 </www.oas.org/juridico/english/ treaties/b-58.html>.

/11/ *See* European Union Convention on the Fight against Corruption Involving Officials of the European Communities or Officials of the Member States of the European Union, 1997 O.J. (C195) 1, 25.06.1997 (May 26, 1997).

/12/ "African Union Convention on Preventing and Combating Corruption," July 11, 2003 <www.africa- union.org/official_documents/treaties_%20conventions_%20protocols/ convention%20on%20combating%20corruption.pdf>

/13/ U.N. Convention against Corruption, Dec. 9, 2003, <www.unodc.org/pdf/crime/convention_corruption/signing/convention-e.pdf>

/14/ These include procurement rules for the World Bank and the Inter-American Development Bank, anti-corruption guidelines for companies doing business with the European Bank for Reconstruction and Development, and the actions of the European Union (EU) to develop protocols and a convention in this area. *See* World Bank, "Guidelines: Procurement under IBRD Loans and IDA Credits," ¶ 1.14 (May 2004), <siteresources.worldbank.org/Intprocurement/resources/procurement-May-2004.pdf>; Inter-American Development Bank, "Basic Procurement Policies and Procedures," ¶ 1.4, <www.iadb.org/ros/prm/english/docs/policies.pdf>; European Bank for Reconstruction and Development, "Guidelines for Sound Business Standards and Corporate Practices," Pub. No. 2829, 27/08/97 (Sept. 1997). *See also* Joint Statement of Multilateral Development Banks, "The Fight against Corruption," Dec. 9, 2004, <www.iadb.org/oii/joint_statement.cfm/english.htm>.

/15/ *See, e.g.,* "List of Debarred Firms: Fraud and Corruption," <web.worldbank.org/wbsite/external/projects/procurement/debarred.html>.

/16/ The relationship between these universes of subject persons is discussed in § II.A.2.

/17/ In 1988, Congress added a provision to the FCPA granting the DOJ civil injunctive and subpoena authority with respect to "domestic concerns." *See* Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, § 5003(c), 102 Stat. 1107, 1421 (1988).

/18/ Under this vicarious liability provision, the definition



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of "knowing" is broader than actual knowledge. A company is deemed to "know" that its agent will use money provided by the company to make an improper payment or offer if it is aware of, but consciously disregards, a "high probability" that such a payment or offer will be made. 15 U.S.C. §§ 78dd-1(f)(2)(B), 78dd-2(h)(3)(B), and 78dd-3(f)(3)(B). The purpose of this standard is to prevent companies from adopting a "head-in-the-sand" approach to the activities of their foreign agents and partners. *See* H.R. Conf. Rep. No. 100-576, at 920 (1988).

/19/ The more ministerial of these approvals may well fall under the exception for routine governmental action, discussed below in § II.A.3.; the discretionary decisions do not. The line between ministerial and discretionary is not always a clear one. We note that the scope of this element has been challenged recently in U.S. court. In the case of *United States v. Kay,* 200 F. Supp. 2d 681 (S.D. Tex. 2002), a federal district court held, as a matter of law, that bribes to customs officials in order to reduce import taxes did not meet the statute's definition of "obtaining or retaining business." On February 4, 2004, the U.S. Court of Appeals for the Fifth Circuit reversed that decision, holding that the district court erred in holding as a matter of law that such payments could never fall within the scope of the FCPA; rather, the inquiry is factual, examining whether "the bribery was intended to produce an effect — here, through tax savings — that would 'assist' in obtaining or retaining business." *United States v. Kay,* 359 F.3d 738, 756 (5th Cir. 2004). This decision is discussed below in § IV.B.3.

/20/ 15 U.S.C. §§ 78dd-1(g), 78dd-2(i).

/21/ "Residency" is not defined in statute; presumably, the test for jurisdiction would use the immigration standards for permanent residency. *See, e.g.,* 8 U.S.C. § 1101(a)(20).

/22/ There are some jurisdictional limits to the law's coverage. Any non-U.S. citizens subject to the FCPA's coverage would have to be subject to the personal jurisdiction of the United States before they could be prosecuted. Indeed, recently an FCPA conspiracy charge was dismissed against a Swiss attorney allegedly acting as an agent for a U.S. domestic concern based on the court's interpretation of the pre-1998 amendment FCPA, which excluded such agents from criminal penalties if they were not "otherwise subject to the jurisdiction of the United States." *United States v. Bodmer,* 342 F. Supp. 2d 176 (S.D.N.Y. 2004).

/23/ Again, any non-U.S. citizen would have to be subject to the personal jurisdiction of the United States.

/24/ For example, what if telephone service in Country X, a target for a U.S. company's investment, is not "routine" even though it would be in the United States? The cases and review releases do not answer this question, although it is possible that the DOJ might ultimately apply U.S. concepts of "routineness" in a particular situation.

/25/ The legislative history of this provision states that "the absence of written laws in a ... country would not by itself be sufficient to satisfy" the defense. H.R. Rep. No. 100-576, at 922 (1988).

/26/ Although enforcement officials have noted that such requirements may not fully insulate companies from issues; for example, a law might require participation by a local company, but may not call for one owned by a foreign official.

/27/ The DOJ has identified several factors as "red flags" that should warn U.S. companies of potential FCPA violations. The existence of one or more of these factors in a transaction could be considered sufficient to alert a U.S. company to the "high probability" of an improper payment or offer by a foreign agent:

— a history of corruption in the country in question;
— unusually high commissions or "unusual payment patterns or financial arrangements";
— the agent or venture partner is related to a government official or the agent's company is owned in part by a government official or his or her family, or has been recommended by an official;
— a refusal by the venture partner or representative to certify that they will not make payments or cause the principal to violate the FCPA;
— the agent or venture partner has an apparent lack of qualifications or resources to perform the work agreed upon; or
— there is a lack of transparency in accounting and expense records, or the agent or venture partner has requested that the company prepare false invoices or any other type of false documentation.

"Foreign Corrupt Practices Act: Antibribery Provisions," <www.usdoj.gov/criminal/fraud/fcpa/dojdocb.html> (Mar. 15, 2002).

/28/ *See SEC v. Ashland Oil, Inc. and Orin E. Atkins* (Complaint for Permanent Injunction), 2 FCPA Rep. 696.95, 696.97 (July 8, 1986); *United States v. Saybolt N.A. and Saybolt Inc,* Cr. No. 98CR10266WGY (D. Mass. Aug. 18, 1998).

/29/ *United States v. Halford,* 01 Cr. No. 221 (W.D. Mo. Aug. 2001); *United States v. Reitz,* 01 Cr. No. 222 (W.D. Mo. Aug. 2001); *United States v. Robert Richard King and Pablo Barquero Hernandez,* Cr. No. 01-190 (W.D. Mo. June 2001).

/30/ *See SEC v. Monsanto Co.,* Case No. 1:05CV00014 (D.D.C. Jan. 6, 2005), Lit. Rel. No. 19023 (2005); *SEC v. Triton Energy Corp., Philip Keever, and Richard McAdoo,* No. 97CV00401 (Complaint and Undertakings) (D.D.C. Feb. 27, 1997); *In the Matter of Baker*



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*Hughes, Inc.*, Exch. Act Rel. No. 34-44784 (2001); *United States v. Kay and Murphy*, 200 F. Supp. 2d 681 (S.D. Tex. 2002); *SEC v. Chiquita Brands Int'l, Inc.*, Civ. No. 1:01-02079 (D.D.C. Oct. 3, 2001); *SEC v. BellSouth Corp.*, Exch. Act Rel. No. 34-45279 (2002).

/31/ *SEC v. Triton Energy Corp., Philip Keever, and Richard McAdoo*, No. 97CV00401 (Complaint and Undertakings) (D.D.C. Feb. 27, 1997).

/32/ *In the Matter of International Bus. Machs.*, Exch. Act Rel. No. 34-43761 (2000).

/33/ Specifically, the count used a provision of the Money Laundering Control Act, 18 U.S.C. § 1956 (a)(2), which criminalizes the interstate or international transfer of funds or monetary instruments to promote a specified unlawful activity — in that case, the bribery of a foreign official. This provision was also used in the indictment of the U.S. citizen James Giffen in early 2003 for alleged bribes to officials of the government of Kazakhstan, *United States v. Giffen*, No. 1:03-cr-00404-WHP, 2004 U.S. Dist. LEXIS 24132 (S.D.N.Y. Dec. 2, 2004).

/34/ The United States opted out of the illicit enrichment provisions for constitutional reasons related to the presumption of guilt. *See* Resolution of Ratification of the Inter-American Convention against Corruption, ¶ (a)(4), *reprinted in* S. Exec. Rpt. 106-15, Report of the Committee on Foreign Relations, at 9 (2000).

/35/ For an overview of the Convention and a comparison to the FCPA, see Low, Atkinson & Bjorklund, "Comparison of the Inter-American Convention against Corruption and the U.S. Foreign Corrupt Practices Act," 38 *Va. J. Int'l L.* 243 (1998).

/36/ This mechanism was ratified by the OAS General Assembly in June 2001. The first country reviews began in February 2003. *See* <www.oas.org/jurisdico/spanish/corresp_mex.htm>.

/37/ *See* "OECD Convention: Ratification Status," <www.oecd.org/dataoecd/59/13/1898632.pdf> (Jan. 28, 2005).

/38/ Commentaries on the Convention on Combating Bribery of Officials International Business Transactions, Nov. 21, 1997, *reprinted in* 37 I.L.M. 1, 8 (1998) (hereinafter Commentaries).

/39/ For a detailed discussion of the OECD Convention and its effects, see Lucinda A. Low, "The New Global Legal Framework: The OECD, OAS, and Council of Europe Antibribery Conventions: New International Standards and National Anticorruption Laws: Challenges for Effective Implementation and Enforcement," Conference of the International Bar Association, International Chamber of Commerce, and Organization for Economic Cooperation and Development, "The Awakening Giant of Anticorruption Enforcement," Paris, France, Apr. 22-23, 2004.

/40/ However, the Convention's commentary suggests that conformity with local law would be considered a defense and that small "facilitating" payments are not prohibited, both of which are consistent with the FCPA. *See* Commentaries, ¶ 1(8).

/41/ OECD Convention, art. 3(1).

/42/ *Id.* art. 3(2).

/43/ *Id.* art. 3(3).

/44/ Commentaries, ¶ 21.

/45/ Commentaries, ¶ 24.

/46/ Criminal Law Convention on Corruption, Jan. 27, 1999, Council of Europe, European Treaties, ETS No. 173, <conventions.coe.int/treaty/EN/searchsig.asp/NT=174&CM=8&DF=> (hereinafter COE Criminal Convention). As of the end of 2004, thirty parties (though not the United States) had ratified this convention.

/47/ Civil Law Convention on Corruption, Nov. 11, 1999, Council of Europe, European Treaties, ETS No. 174, <conventions.coe.int/treaty/en/treaties/html/174.htm>. At the end of 2004, twenty-two parties had ratified or acceded to this convention.

/48/ *See* Council of Europe, "Final Communique of the 102d Session of the Committee of Ministers," May 4-5, 1998, <press.coe.int/cp/98/320a(98).htm> (announcing adoption of Resolution (98)7 creating the GRECO). GRECO was activated in the summer of 1999; at the end of 2004 it had thirty-eight members, plus observers from the EU and several international organizations. The United States joined GRECO in September 2000.

/49/ COE Criminal Convention, arts. 7, 8.

/50/ *Id.* arts. 5-6, 9-11.

/51/ *Id.* art. 14.

/52/ *Id.* art. 18(1).

/53/ *Id.* art. 18(2).

/54/ *Id.* art. 18(3).

/55/ *See* European Union Convention on the Fight against Corruption Involving Officials of the European Communities or Officials of the Member States of the European Union, 1997 O.J. (C195) 1, 25.06.1997 (May 26, 1997); "African Union Convention on Preventing and Combating Corruption," July 11, 2003, <www.africa-union.org/official_documents/treaties_%20conventions_%20protocols/convention%20on%20combating%20corruption.pdf>.

/56/ Instead, APEC has agreed on a series of measures to promote transparency and reduce corruption. *See* APEC Course of Action on Fighting Corruption and Ensuring Transparency (Sept. 2004) <www.apecsec.org.sg/apec/apec_groups/other_apec_groups/anti-corruption.html>.

/57/ U.N. Convention against Corruption, Dec. 9, 2003, <www.unodc.org/pdf/crime/convention_corruption/signing/convention-e.pdf>.

/58/ *See* "U.N. Asset Recovery Project in Nigeria," <www.unodc.org/unodc/en/corruption_projects_nigeria_project2.html>.



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/59/ This chapter does not speak to the issue of debarment or contracting ineligibility of the person found to have engaged in corrupt practices, but rather focuses on the property acquired through such practices. However, the Convention would not preclude debarments or declarations of ineligibility by national authorities.

/60/ The FCPA has been traditionally held not to confer such rights. *See Lamb v. Phillip Morris, Inc.*, 915 F.2d 1024 (6th Cir. 1990), *cert. denied,* 111 S. Ct. 961 (1991); *J.S. Serv. Ctr. v. GE Tech. Servs. Co.*, 937 F. Supp. 216 (S.D.N.Y. 1996).

/61/ *See* Report of the *Ad Hoc* Committee for the Negotiation of a Convention against Corruption on the work of its first to seventh sessions, Addendum, Interpretative notes for the official records (*travaux préparatoires*) of the negotiation of the U.N. Convention against Corruption, A/58/422/Add.1, note 38, Oct. 7, 2003, <www.unodc.org/unodc/en/corruption/session_7/422f.pdf>.

/62/ 28 U.S.C. § 1350. The Alien Tort Claims Act, or, as some prefer to call it, Alien Tort Statute (ATS), is a 1789 statute which gives to aliens a right of action for a tort only in violation of the law of nations or a treaty of the United States. Most of the cases to date have involved alleged torture, genocide, and other acts alleged to violate the law of nations (customary international law) rather than a treaty. The U.S. Supreme Court recently held, in *Sosa v. Alvarez-Machain,* 542 U.S. ___, 124 S. Ct. 1627, L. Ed. 2d 263 (2004), that the ATS, although jurisdictional, permits actions based on a limited set of claims of international law violations.

/63/ For a more detailed analysis of this issue, see Lucinda A. Low, "Towards Universal Anticorruption Standards: The United Nations Convention against Corruption and Other International Anticorruption Treaties: Too Much of a Good Thing?" Conference of the International Bar Association, International Chamber of Commerce, and Organization for Economic Cooperation and Development, "The Awakening Giant of Anticorruption Enforcement," Paris, France, Apr. 22-23, 2004.

/64/ "Combating Multilateral Development Bank Corruption: Hearing before the Senate Committee on Foreign Relations," 108th Cong., 2d Sess. (2004) (statement of Guido Penzhorn, SC, Advocate and Senior Counsel, Durban Bar).

/65/ The company might be able to bring certain payments under the exception for "routine governmental action," but if the official decision is a discretionary one, the exception is not available.

/66/ Even an asset sale has not always shielded acquirors from potential liability in the international regulatory arena. In the *Sigma Aldrich* case, an administrative law judge at the Department of Commerce held that successor companies can be held liable for the preacquisition export control violations of companies they acquire, even in circumstances where an acquisition is structured as solely the purchase of assets or partnership interests. *In the Matter of Sigma Aldrich,* Case Nos. 01-BXA-06, 07, 11, Aug. 29, 2002, <www.bxa.doc.gov/enforcement/casesummaries/ sigma_aldrich_alj_decision_02.pdf>. After this ruling, the company agreed to a settlement that included a $1.76 million fine. BIS Press Release, "Sigma-Aldrich Pays $1.76 Million Penalty to Settle Charges of Illegal Exports of Biological Toxins," <www.bxa.doc.gov/news/2002/sigmaaldrichpays4acquisition.htm>. Thus, while Commerce Department officials trumpeted the expansive reading given to potential successor liability, the case went untested by the federal courts. While DOJ officials have cited this case in presentations on due diligence, in our view it does not represent settled law on the question of successor liability in asset sales in the FCPA context.

/67/ We do not mean to imply that the presence of an official interest is automatically a violation. Although such interests raise significant issues, enforcement officials have recognized that not all transactions with foreign officials will be violations of the law.

/68/ While beyond the scope of this chapter, we note that under current DOJ guidelines, this cooperation likely included a waiver of the attorney-client privilege with regard to the subject of the investigation.

/69/ *See* ABB Press Release, "ABB Concludes Compliance Review of Upstream Oil, Gas and Petrochemicals Business," July 7, 2004 (discussing due diligence aspects).

/70/ Several recent enforcement actions have required companies to retain independent third-party FCPA experts to perform periodic audits of the program's operation for a term of years, reporting any gaps or issues directly to U.S. enforcement officials. While periodic assessments and testing of compliance programs are recommended standard procedures, the requirements established in this releases are remedial, designed to correct programs found to be inadequate.

/71/ Of these factors, (1) and (2) appear to be critical ones from a statutory standpoint. The importance of (3) is not obvious, as the control issue implicated by the ownership share cuts both ways under an FCPA analysis. Factors (4) and (5) presage the more developed safeguards in Opinion Release 01-01, highlighting the DOJ's emphasis on transparency to the U.S. government and the ability to withdraw from any "tainted" relationship.

/72/ *Monsanto* also involved alleged payments by a U.S. employee of the parent company. *SEC v. Monsanto*



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*Co.,* SEC Lit. Rel. No. 19023 (Complaint) (Jan. 6, 2005).

/73/ In the *IBM* case, while lack of action related to active management likely saved the parent from a criminal antibribery violation, the parent still incurred a $300,000 fine for accounting violations due to its consolidation of the Argentine affiliate's financial results. *In the Matter of International Bus. Machs.,* Exch. Act Rel. No. 34-43761 (2000).

/74/ Again in the *Triton Energy* case, a parent/subsidiary situation, the SEC complaint against the parent company alleged violation of both the antibribery and the accounting provisions. The complaint noted, however, that the U.S. parent did not know of or authorize the payments. This may explain why the settlement plea was only as to the books and records provisions. *SEC v. Triton Energy Corp., Philip Keever and Richard McAdoo,* No. 97CV00401 (Complaint and Undertakings) (D.D.C. Feb. 27, 1997).

/75/ Several countries that represent the highest priorities for U.S. investments abroad are also considered by business groups to be some of the most corrupt. Transparency International has ranked international business perceptions of corruption in various countries for several years with their Corruptions Perception Index (CPI). The CPI ranks countries relatively *vis-à-vis* other countries (1 being the least corrupt) and on a scale designed to show level of corruption on an absolute basis (10 being least corrupt). In the 2004 edition of the CPI, several investment targets were ranked as substantially corrupt using both methods, including Mexico (64 out of 145; 3.6 out of 10), the People's Republic of China (71 out of 145; 3.4 out of 10), India (90 out of 145; 2.8 out of 10), and Russia (also 90 out of 145; 2.8 out of 10). *See* "Corruption Perceptions Index 2004," <www.transparency.org/pressreleases_archive/2004/2004.10.20.cpi.en.html>. Thus, some of the most difficult FCPA challenges will likely occur in the countries that are likely high priorities for U.S. companies' investments abroad.

/76/ Whether a person is a "foreign official" for FCPA purposes is likely not the only relevant legal issue, however. Not only may domestic official bribery statutes be relevant, but commercial bribery statutes as well. Many countries, in recent years, have enacted laws criminalizing private commercial bribery on the same footing as official bribery. Several of the international conventions mentioned earlier encourage this step. Although the United States has no federal commercial bribery legislation, at least two-thirds of U.S. states have such legislation.

/77/ Officials of the U.S. DOJ have, on various occasions, unofficially expressed the view that "instrumentality" status can arise even when the government does not have majority ownership or affirmative control. In public discussions, they have variously asserted that even a small level of equity ownership, or control devices such as "golden" shares, may provide the factual basis for finding that the entity is an instrumentality. Although a number of litigated cases and some published summaries of opinions rendered under the Opinion Procedure involve state-owned enterprises, in none of them has the status of the entity involved as an instrumentality been litigated or even discussed. In its first (Phase I) report to the OECD on implementation of the OECD Convention, the United States stated: "[t]he Department of Justice ... has not adopted a bright-line test for determining which [state] enterprises are instrumentalities. Among the factors that it considers are the foreign state's own characterization of the enterprise and its employees, *i.e.,* whether it prohibits and prosecutes bribery of the enterprise's employer as public corruption, the purpose of the enterprise, and the degree of control exercised over the enterprise by the foreign government." Response of the United States to OECD Phase I Questionnaire ¶ 1.1, DAFFE/IME/BR(98)8/ADD1/FINAL (Oct. 30, 1998) <www.usdoj.gov/criminal/ fraud/fcpa/firstqu.htm>.

/78/ The DOJ has also confirmed that payments made directly to government entities, and not to foreign government officials, do not implicate the FCPA. *See* FCPA Opinion Procedure Rel. 97-02 (Nov. 5, 1997).

/79/ The DOJ employed similar tactics once before when it tried, unsuccessfully, to use a conspiracy theory to prosecute foreign officials who accepted bribes but who were not subject to the FCPA. *See United States v. Donald Castle and Darrell W.T. Lowry,* 2 FCPA Rep. 698.6906 (5th Cir. 1991).

/80/ The *Kay* court of appeals, noted that this "*quid pro quo*" element is at the "core of criminality" for any FCPA offense. *United States v. Kay,* 350 F.3d at 743.

/81/ *See United States v. Lockheed Corp.* (Plea Agreement), 3 FCPA Rep. 699.185 (Jan. 27, 1995). This case contained several facts that were unhelpful to Lockheed. For example, when Dr. Takla joined Parliament in 1987, she sent correspondence to Lockheed stating that her husband, the president of "Dr. Leila I. Takla, Inc." would from that time handle Lockheed's matters. Thus, she acknowledged the possible FCPA issue, but established a system by which her retainers would still be paid to her family. *See* Lockheed Information at 699.177-78.

/82/ In the *Giffen* case, Kazakh government orders required that bidding oil companies pay signing bonuses into designated accounts. All the accounts were represented to be official, legitimate accounts of the government, and based on public reports some evidence was obtained to confirm this. Many of the allegations against



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Mr. Giffen contend note that he (an agent of the government of Kazakhstan) improperly diverted portions of these payments to offshore accounts held by Kazakh government officials. As the case is ongoing, it is unclear what liability, if any, might attach to the payors.

/83/ Such scholarship programs have been investigated by Congress in its recent review of Riggs Bank's relationship with the President of Equatorial Guinea. See Minority Staff of Permanent Subcomm. on Investigations, S. Comm. on Governmental Affairs, 108th Cong. 2d Sess., "Money Laundering and Foreign Corruption: Enforcement and Effectiveness of the Patriot Act," July 15, 2004.

/84/ There are also issues raised by the First Amendment interest in petitioning a government for redress. This interest has been recognized in the U.S. antitrust laws as applying to efforts to petition a foreign government.

/85/ These "normal representations" apparently do not extend to paying government officials to facilitate payment of a preexisting government contract. In *United States v. Vitusa Corp.* (Plea Agreement), 3 FCPA Rep. 699.158 (Apr. 13, 1994), Vitusa, a U.S. company, pled guilty to an FCPA violation that involved making a payment to a foreign official in the government of the Dominican Republic in order to secure the Dominican government's final payment of an outstanding balance owed to Vitusa under a government contract for milk powder. The attempt to secure payment was interpreted as a attempt to "obtain and retain business" with the Dominican government, not as a lobbying effort. Nor do they encompass payments to government officials to secure favorable audit determinations or tax results, as occurred in the *Baker Hughes* and *Triton Energy* cases discussed earlier.

/86/ As noted above, even if FCPA concerns can be addressed, lobbying can raise issues in countries which have adopted "trading in influence" laws to implement provisions of the Council of Europe's Criminal Law Convention against Corruption. Similar provisions are contemplated by the U.N. Convention, though it is not yet in effect. Thus, in a world of increasing international standards, multinational investors must comply with multiple, and sometimes inconsistent, requirements.

/87/ In November 2004, the U.S. Sentencing Commission amended the U.S. Sentencing Guidelines for the sentencing of organizations to include most of the elements described below as part of the elements that comprise an "effective compliance program" in order to receive credit in the sentencing calculation process. *See* 69 Fed. Reg. 28994 (May 19, 2004). While the recent Supreme Court decision in *United States v. Booker,* Nos. 04-104 and 04-105 U.S. LEXIS 628 (U.S. Jan. 12, 2005), makes the Guidelines no longer mandatory, U.S. enforcement officials will likely consider the amended requirements on compliance programs to represent the minimum standard of compliance.

/88/ However, even a local opinion may not be sufficient in face of a contrary FCPA interpretation. *See* FCPA Opinion Procedure Rel. 94-01 (May 13, 1994) (disregarding opinion of local counsel that the general director of a state-owned enterprise is not considered an "official" in host country).

/89/ This fact is probably not dispositive, however, since the law is in most cases unlikely to mandate the choice of a particular company or individual.



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