

Morgan Lewis

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Federal Securities

Developments in SEC Enforcement:
The Foreign Corrupt Practices Act

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Christian R. Bartholomew
Morgan, Lewis & Bockius LLP

200 S. Biscayne Boulevard
Miami, Florida 33131-2339
305.415.3400

1111 Pennsylvania Avenue, NW
Washington, D.C. 20004
202.739.6400

cbartholomew@morganlewis.com

Topics of Discussion

- Overview of the FCPA
- SEC Enforcement Trends
- 2009 Predictions
- Selected Recent Cases

Overview of the FCPA

FCPA's Two Prongs

ANTI-BRIBERY PROVISIONS:

Prohibits bribery of foreign government or political officials for the purpose of obtaining or retaining business or securing any improper business advantage

ACCOUNTING PROVISIONS:

Requires SEC-registered or reporting issuers to make and maintain accurate books and records and to implement adequate internal accounting controls

Books and Records

SEC registrant or issuer must “make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer”

- Materiality and scienter not required
- “In reasonable detail” substitutes for materiality to prevent using off-the-books slush funds and the like
 - *Reasonableness standard does not require exactitude; it contemplates a prudent man standard*

Internal Controls

SEC registrant or issuer must “devise and maintain a system of internal accounting controls sufficient to provide reasonable assurance that:

1. Transactions are executed in accordance with management’s authorization,
2. To maintain accountability of assets,
3. Access to assets is permitted only in accordance with management authorization, and
4. Recorded accountability for assets is compared with existing assets at reasonable intervals and appropriate action is taken with respect to variances.

Reach of the Accounting Provisions

- All issuers and reporting companies (*narrower* than anti-bribery provisions)
- All payments and transactions, not just bribes or corrupt payments (*broader* than anti-bribery provisions)
- Subsidiaries: 50% or less voting power requires that parent “proceed in good faith to use its influence, to the extent reasonable” to cause the subsidiary to maintain adequate controls

Potential Penalties for Books & Records Violations

Corporation:

- \$500,000 civil penalty or gross gain to the company
- Disgorgement

Individual:

- \$100,000 civil penalty or gross gain
- Fines shall not be paid, directly or indirectly, by the company

Other Risks

Criminal Prosecution

Disgorgement of Profits

Debarment

Independent Monitor

Civil Litigation

Multiple Investigation
Costs

Back Taxes

Interest

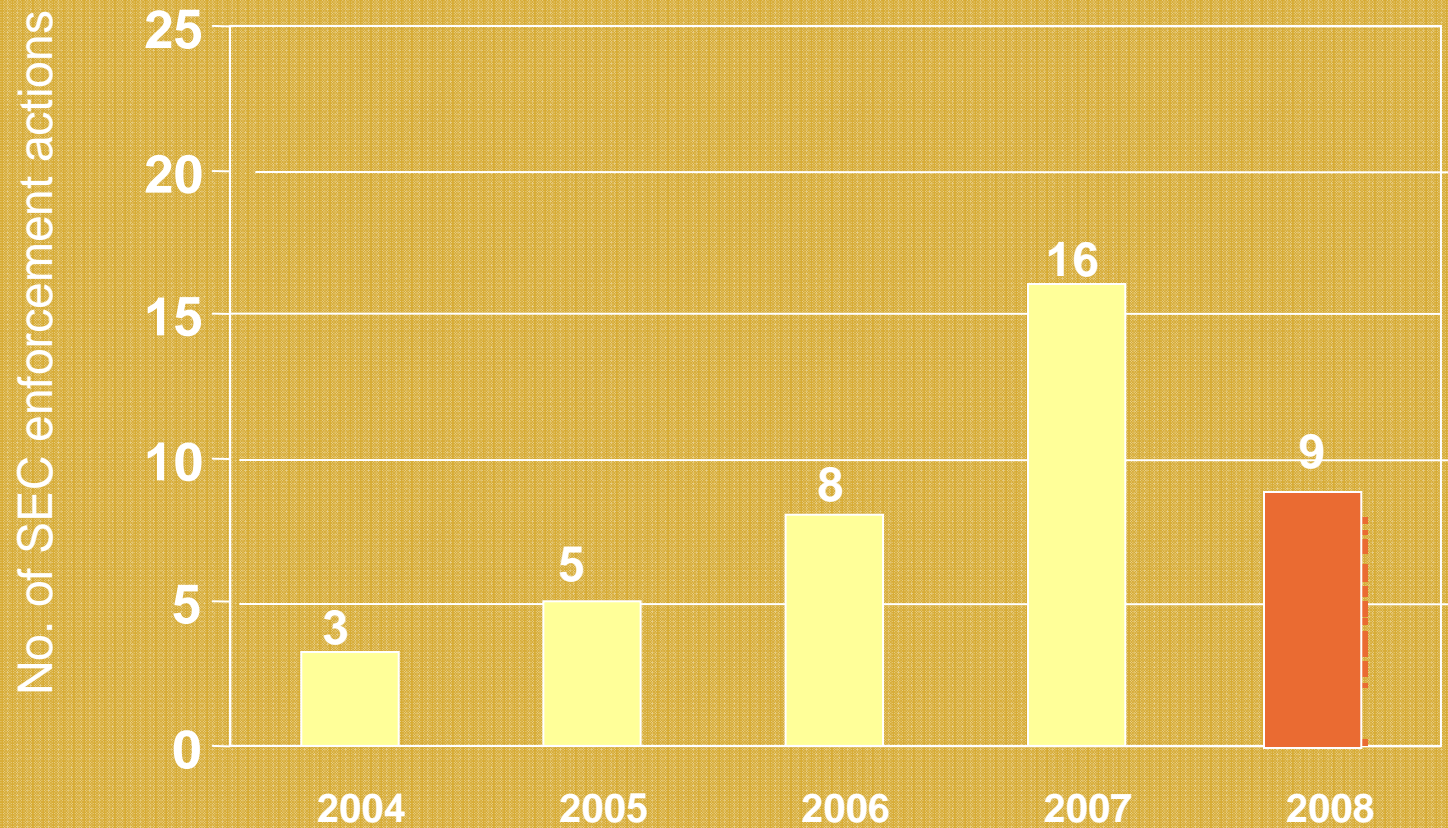
Diversion of Management

Share Price

Rescission of contracts,
permits

SEC Enforcement Trends

Continued Robust Enforcement



Just the tip of the iceberg!

More to Come...

75-100 companies
have disclosed in
SEC filings that they
are under investigation
for FCPA violations



Casting a Wide Net

Deterrence achieved through broad enforcement:

- Widespread Frauds – *Siemens*
- Discrete Misconduct – *Charles Martin (Monsanto)*
- Small Payments – *Con-Way*
- Individuals – *Jack Stanley (Halliburton)*

“SEC will seek fines if DOJ cannot prove bribery”

~~ Cheryl Scarboro (Assoc. Director, Div. of Enforcement)

- Robert Philip (*Schnitzer*)
 - CEO of Schnitzer allegedly approved bribes and failed to implement controls or maintain proper books and records
 - Disgorged \$170k in salary and bonuses
 - Paid \$75k civil penalty
- Monty Fu (*Syncor*)
 - Chairman of Syncor failed to implement controls
 - Reckless in not knowing payments made and falsely recorded in books and records
 - Paid \$75k civil penalty

Large Penalties are the Norm

- **Halliburton:** prospective settlement: \$382 million fine and \$177 million disgorgement
- **Siemens:** \$450 million fine and \$350 million disgorgement
- **Fiat:** \$17.8 million in fines, penalties, disgorgement
- **Willbros:** \$32 million in fines, penalties, disgorgement
- **AB Volvo:** \$19.6 million in fines, penalties, disgorgement

2009 Predictions

1

The New Administration: A New Sheriff in Town?

- Expect same or greater level of enforcement activity
- Pressure to self report and have robust programs given how much press there has been (especially Siemens)
- Prosecution of both *big* (Siemens) and *small* (Nexus) companies and payments will continue

2

Industries to Watch: Sovereign Wealth Funds and Financial Institutions

The recent boom of sovereign wealth funds is an area at the top of DOJ's hit list.

~Steve Tyrrell, Chief of the Fraud Section, DOJ Criminal Division

- Money is a scarce resource
 - SWFs are source of capital in tight credit markets
 - Nationalized banks and State-owned entities (Iceland, UK)
- Factors
 - Passive investors without control rights?
 - Special access or quid pro quo?
 - Regulation vs. control

3

Coordinated Enforcement

- Agency Coordination will continue to rise
 - **Antitrust**
 - *Bridgestone* = first ever joint FCPA/antitrust prosecution
 - ABB Ltd. and Halliburton also under investigation
 - **Export Control**
 - *Nexus* (Dep't of Commerce, Office of Export Enforcement)
 - *Shu Quan-Sheng* (Arms Export Control Act)
 - **IRS**
 - *Willbros*
 - *PCI/Martin Self*

4

Private Litigation

- Shareholder lawsuits
- RICO, Fraud
- Breach of Fiduciary Duty
- Unfair Competition

Selected Recent SEC Enforcement Cases

SEC v. Siemens Aktiengesellschaft

(December 15, 2008)

- Siemens, which trades ADRs on the NYSE, and its global subsidiaries paid more than \$1.3 billion in bribes to foreign officials worldwide over the past decade
- Following a German investigation, Siemens disclosed potential problems to U.S. authorities
 - In largest FCPA settlement in history, Siemens paid a \$450 million criminal fine and \$350 million in disgorgement
 - Siemens pleaded guilty only to a criminal violation of the books and records provisions in light of its extensive and unprecedented remedial action and cooperation; it otherwise faced debarment in government contracting for a bribery conviction
 - Siemens has spent nearly \$2 billion in investigative costs and worldwide penalties to date

SEC v. Con-Way, Inc.

(August 27, 2008)

- Emery Transnational (acquired by Con-way) allegedly made “hundreds of small payments” to Philippines customs officials for favorable treatment. Emery reported only net profits to Con-Way, and Con-Way did not require additional financial details.
 - Con-way consented to C&D and paid a \$300,00 penalty
 - Con-Way self disclosed to the SEC and implemented new reporting and compliance requirements on Emery and provided additional FCPA training

SEC v. AB Volvo

(March 20, 2008)

- AB Volvo settled charges that two of its subsidiaries conspired to commit wire fraud and to violate the FCPA's books and records provisions by paying illicit kickbacks for contracts under the U.N. Oil-for-Food Program
- To conceal the kickbacks, the subsidiaries inflated prices by 10% and mischaracterized the payments as "after-sales service fees"
 - The company settled with the SEC, agreeing to pay a \$4 million civil penalty and approximately \$8.6 million in disgorgement of profits in connection with kickbacks its subsidiaries paid to the Iraqi government in violation of the books and records and internal controls provisions of the FCPA.
 - AB Volvo also agreed to pay a \$7 million criminal penalty to the Department of Justice pursuant to a deferred prosecution agreement.
 - In assessing penalties, both the DOJ and the SEC recognized AB Volvo's thorough review of the improper payments and their implementation of enhanced compliance policies.

SEC v. Lucent Technologies, Inc.

(December 21, 2007)

- SEC charged Lucent spent more than \$10 million on leisure travel and entertainment for Chinese officials
- SEC alleged improper recording in books and records, lack of internal controls to detect and prevent improper payments, and failure to train employees to understand the FCPA's application to their business
 - Lucent agreed to a permanent injunction against future violations of the Securities Exchange Act of 1934 and agreed to pay a \$1.5 million civil penalty
 - Lucent entered a nonprosecution agreement with the DOJ and agreed to pay an additional \$1 million fine

SEC v. Robert W. Philip

(December 13, 2007)

- SEC charged former chairman and CEO of Schnitzer Steel Industries, Inc. with violating antibribery, recordkeeping, and internal control provisions of the FCPA by approving more than \$200,000 in cash bribes and other gifts at Chinese government-owned steel mills
 - Philip agreed to pay more than \$250,000 to settle the charges
 - SEC also alleged Philip authorized \$1.7 million in bribes to steel mills in China and South Korea which generated \$500 million in additional revenue
 - In October 2006, Schnitzer Steel paid \$7.7 million in disgorgement to settle with the SEC and \$7.5 million in penalties to settle related criminal charges with the DOJ

SEC v. Monty Fu

(September 28, 2007)

- Syncor International's former subsidiary, Syncor Taiwan, made illegal payments to doctors in public and private hospitals
- Monty Fu (former Syncor chairman) settled charges of violating and aiding and abetting Syncor's violation of the books and records and internal accounting controls provisions of the FCPA
 - Payments listed as "Advertising and Promotions" totaled approximately \$30,000/year from 1989-1993 and \$170,000/year from 1997-2002
 - Fu must pay \$75,000 civil penalty to SEC

SEC v. Baker Hughes

(April 26, 2007)

- Baker Hughes paid \$5.2 million to agents knowing that it was intended to bribe government officials in Kazakhstan and was awarded a significant contract that generated \$219.9 million in gross revenues
- Also made other questionable payments in Angola, Nigeria, Indonesia, Russia, and Uzbekistan
 - Baker Hughes violated earlier cease and desist order for payments made in Indonesia, Brazil, and India
 - Company entered SEC settlement and DOJ deferred prosecution agreement
 - To SEC, \$23 million in disgorgement and prejudgement interest; \$10 million more for violating cease and desist order
 - To DOJ, \$11 million criminal fine

Recent Cases

- **Enforcement actions**

<http://morganlewis.com/documents/fcpa/FCPAEnforcementActions.pdf>

- **DOJ Opinion Releases:**

<http://morganlewis.com/documents/fcpa/FCPAOpinionProcedureReleases.pdf>

Christian R. Bartholomew

Mr. Bartholomew is a partner in the Litigation Practice Group at Morgan Lewis; he maintains offices in Washington, D.C., where he is the leader of the Litigation group, and Miami. Prior to joining Morgan Lewis, he spent five years as Senior Trial Counsel of the Southeast Regional Office of the SEC, where he specialized in accounting and financial disclosure cases and litigated the seminal W.R. Grace “earnings management” case. Mr. Bartholomew now represents public companies and financial institutions and their senior officers and directors in connection with SEC enforcement matters and securities class actions.

He can be reached at **305.415.3400**, **202.739.6400** or **cbartholomew@morganlewis.com**.



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