

Morgan Lewis

Overview of Recently Issued FCPA Guidance by DOJ and the SEC

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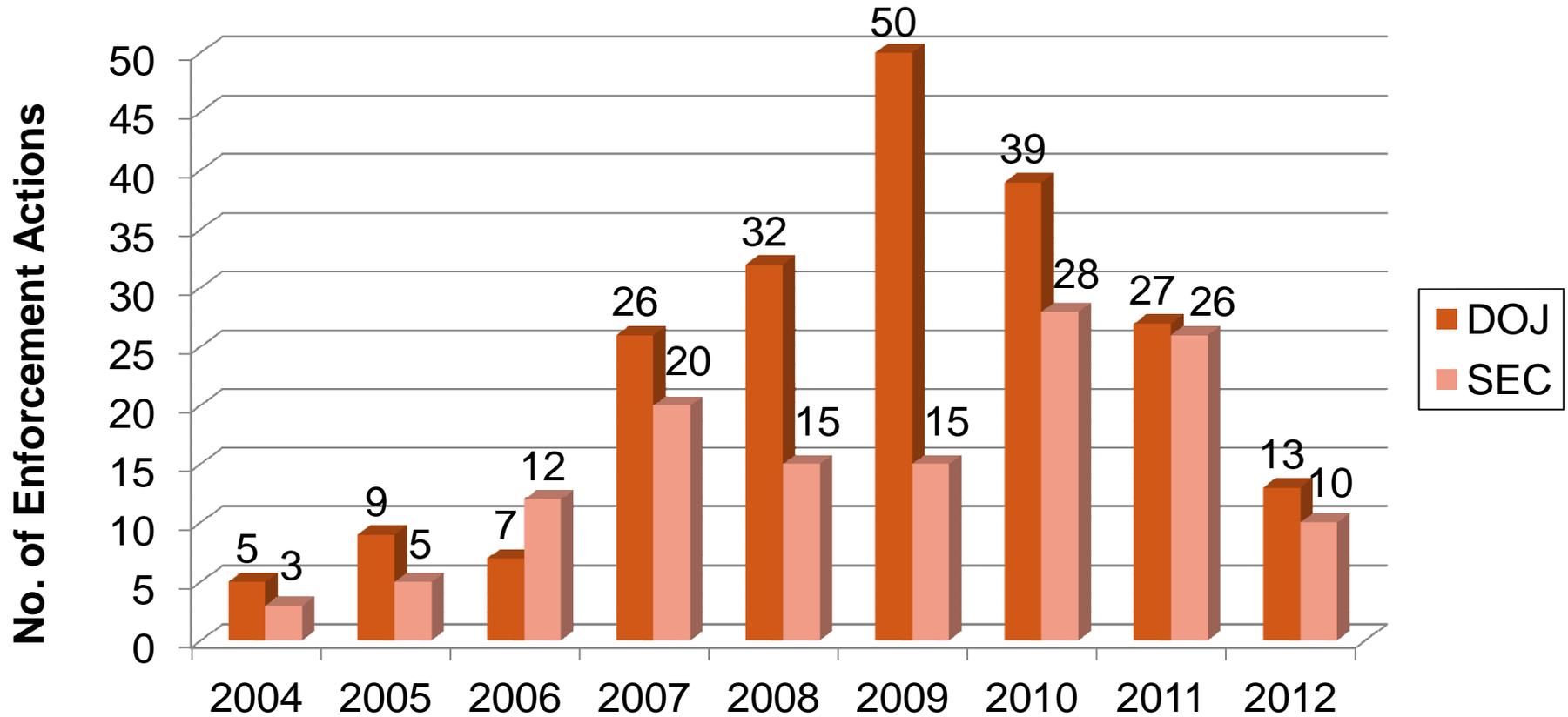
Philadelphia

Topics for Discussion

- Uncertainties in an Aggressive Enforcement Environment – Calls for Guidance
- Utilizing the Guidance
 - Understanding Corporate Liability
 - Resolving Enforcement Actions to Minimize Legal Exposure
 - Maximizing Compliance to Prevent Misconduct

Uncertainties in an Aggressive Enforcement Environment: Call for Guidance

Upward Enforcement Trend



Aggressive Enforcement Environment

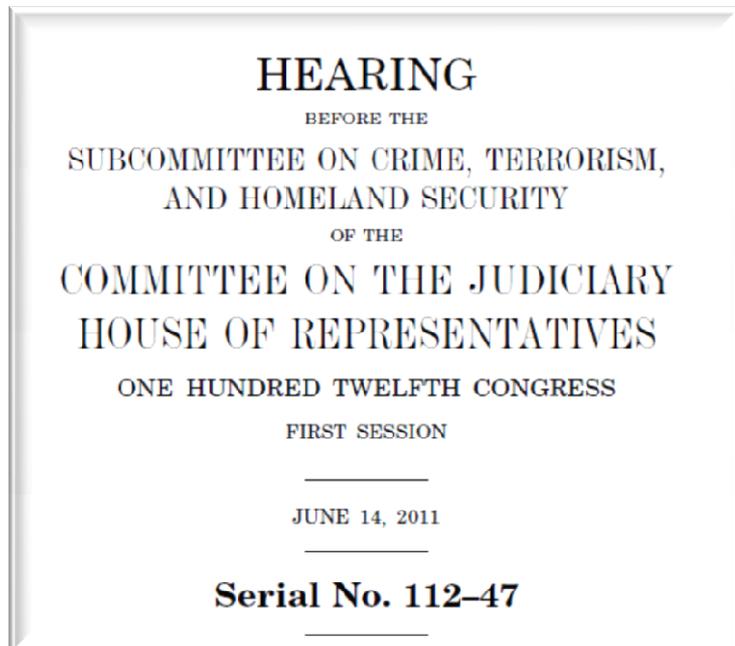
- Multi-million dollar fines and penalties
- Focus on individual prosecutions
- Use of traditional law enforcement techniques
- Specialized FCPA units
- New cooperation tools

Criticisms of FCPA

- Critics of the FCPA note ambiguity in statute's terms and enforcement
 - Broad definition of “foreign official”
 - Facilitation payments exception is not enforced in practice
 - Allows for expansive successor liability
 - Unclear intent requirement for corporate defendants
 - Lack of affirmative defenses
 - *Adequate compliance program*
 - *Safe harbor for post-acquisition due diligence*

Criticisms of FCPA: Ambiguity Chills Commerce

**Testimony of
George J. Terwilliger III, Esq.**



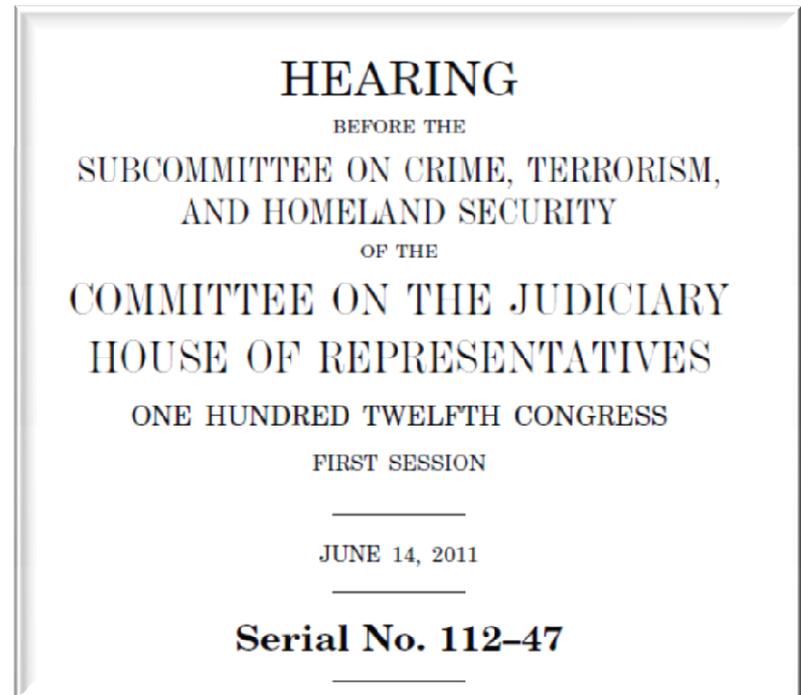
“In calculating the risk arising from FCPA compliance obligations against the benefits of a given business venture, uncertainties exist as to the requirements of the FCPA and its interpretation and application by enforcement authorities. When faced with that uncertainty, companies sometime forgo deals they could otherwise do”

Calls for Guidance

“The overwhelming majority of businesses operating in the U.S. . . . seek in good faith to ensure that they do not violate the requirements of the FCPA, and therefore would find meaningful advisory opinions and guidelines from both the DOJ and the SEC to be tremendously useful in reviewing and monitoring their conduct and practices, improving their internal controls and enhancing their compliance programs.”

Written Testimony

The Honorable Michael B. Mukasey



Calls for Guidance

- U.S. Chamber of Commerce's Institute for Legal Reform, among others, have called for additional guidelines on specific issues
 - Annually published guidance on sanitized declination decisions
 - Would provide clarity on specific factors leading to decision to decline enforcement action
 - *Proposed by Morgan Lewis attorneys George Terwilliger and Matt Miner*

Calls for Guidance

- Mounting pressure on DOJ and SEC to demonstrate actual benefits of self-reporting and cooperation as articulated in U.S. Attorney's Manual and *Seaboard Report*
 - Draft study by NYU Law Professors found no evidence that voluntary disclosure of wrongdoing led to lesser penalties
 - *Samuel Rubenfeld*, Study Says Voluntary Disclosure Doesn't Change FCPA Penalties, *WALL ST. J. CORRUPTION CURRENTS BLOG*, Sept. 6, 2012, <http://blogs.wsj.com/corruption-currents/2012/09/06/studysays-voluntary-disclosure-doesnt-change-fcpa-penalties/>

Response from Government

- Letter from Ronald Weich, Assistant Attorney General, to Rep. Sandy Adams (Aug. 3, 2011)
 - After FCPA Hearing, DOJ advised Congress of eight types of circumstances that have been present in matters that had been declined over previous two years
- Assistant Attorney General Lanny A. Breuer announces issuance of a guide in 2012 at 26th National Conference on the FCPA (Nov. 8, 2011)

FCPA: A Resource Guide to the U.S. Foreign Corrupt Practices Act

Overview

- **Purpose:** To provide information to businesses on views of DOJ and SEC regarding interpretation of statute and enforcement priorities
- **Input and insight concerning**
 - Overview of Anti-Bribery & Accounting Provisions
 - Principles of Federal Enforcement
 - Hallmarks of Effective Compliance Programs
- **Disclaimers:** Nonbinding and informal

Overview of the Anti-Bribery & Accounting Provisions:
Understanding Corporate Liability

Business Purpose

- FCPA liability is generally limited to the offering or giving anything of value to a foreign official to assist in “obtaining or retaining” or directing business to an individual
- May include:
 - Winning a contract
 - Influencing the government procurement process
 - Circumventing the rules for importation of goods
 - Obtaining exceptions to regulations

Few Revelations

- Legal interpretations consistent with past policy and practice of DOJ and SEC
- Blends statutory interpretation, case analysis, and best practices recommendations
- Presents government position on a few critical areas in easy-to-use package
 1. Definition of “Foreign Official”
 2. Definition of “Anything of Value”
 - *Gifts*
 - *Travel and Entertainment*
 - *Charitable Contributions*
 3. Available Defenses
 - *Bona Fide Expenditures*
 - *Facilitation Payments*
 4. Alternative Theories of Corporate Liability

“Foreign Official”

- “Instrumentality” of a foreign government may include state-owned enterprises or other entities controlled by the state
- Whether a particular foreign entity constitutes an “instrumentality” under the FCPA requires a fact-specific analysis of the entity’s
 - Ownership
 - Control
 - Status
 - Function

“Foreign Official”

- Factors to be considered in determining whether a foreign entity is an “instrumentality” include:
 - The foreign state’s extent of ownership;
 - The foreign state’s degree of control;
 - The foreign state’s characterization of the entity and its employees;
 - Purpose of the entity’s activities;
 - Exclusive or controlling power vested in the entity to administer its designated functions; and
 - Level of financial control of the foreign state.

“Foreign Official”

- Practical Guidance:
 - Entities are unlikely to qualify as an “instrumentality” *if government ownership is < 50%*
 - Past enforcement actions demonstrate that with sufficient control, entity may be an “instrumentality” absent 50% ownership by foreign government

“Anything of Value”

- No minimum value threshold
- Critical issue is corrupt intent
 - Given or promised with intent to improperly influence a government official
- “It is difficult to envision any scenario in which the provision of cups of coffee, taxi fare, or company promotional items of nominal value would ever evidence corrupt intent.”

“Anything of Value”

- Permitted Gifts
 - Small gifts and tokens of esteem or gratitude are appropriate
 - Hallmarks of appropriate gift giving
 - *Gift is given openly and transparently*
 - *Gift is properly recorded in books and records*
 - *Gift is provided only to reflect esteem or gratitude*
 - *Gift is permitted under local law*
 - The greater dollar value or extravagance, the more likely to demonstrate corrupt intent

“Anything of Value”

- Travel and entertainment expenses may be given or offered with corrupt intent

Examples of Improper Travel and Entertainment

- a \$12,000 birthday trip for a government decision-maker from Mexico that included visits to wineries and dinners
 - \$10,000 spent on dinners, drinks, and entertainment for a government official
 - a trip to Italy for eight Iraqi government officials that consisted primarily of sightseeing and included \$1,000 in “pocket money” for each official
 - a trip to Paris for a government official and his wife that consisted primarily of touring activities via a chauffeur-driven vehicle
-

“Anything of Value”

Five Questions to Consider When Making Charitable Payments in a Foreign Country:

1. What is the purpose of the payment?
 2. Is the payment consistent with the company's internal guidelines on charitable giving?
 3. Is the payment at the request of a foreign official?
 4. Is a foreign official associated with the charity and, if so, can the foreign official make decisions regarding your business in that country?
 5. Is the payment conditioned upon receiving business or other benefits?
-

- Charitable contributions are legitimate corporate outreach
- But may be used as a pretense for bribes or as a vehicle to conceal corrupt payments
- Proper due diligence and controls for charitable giving critical

Bona Fide Expenditures

- Under the FCPA, the following types of expenditures do not warrant enforcement action:
 - Travel and expense to visit company facilities or operations;
 - Travel and expenses for training; and
 - Product demonstration or promotional activities, including travel and expenses for meetings.

Bona Fide Expenditures

- Applicability of defense is a fact-specific inquiry
- Safeguards articulated in the Guidance
 - Do not select officials participating in a proposed trip, or select them based on predetermined, merit-based criteria
 - Pay all costs directly to travel vendors and/or reimburse costs only upon presentation of a receipt
 - Do not advance funds or pay for reimbursements in cash
 - Ensure that stipends are reasonable approximations of costs likely to be incurred
 - Do not condition payment of expenses on any action by the foreign official

Facilitating Payments

- Exception for facilitating payments construed as “narrow”
- Limited to payments made to further
 - Routine governmental action
 - Involving nondiscretionary acts

Examples of “Routine Governmental Action”

An action which is ordinarily and commonly performed by a foreign official in—

- obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;
 - processing governmental papers, such as visas and work orders;
 - providing police protection, mail pickup and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;
 - providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; or
 - actions of a similar nature.
-

Alternative Theories of Corporate Liability

- General principles of corporate criminal and civil liability apply
 - Successor liability
 - Agency liability under respondeat superior
- Proof of “willfulness” is not required to establish *corporate* liability
- Proof of corrupt intent is required
- Regulators focus enforcement actions where successors directly participate in violations or failed to stop them from occurring
 - Due diligence important for assessing scope of liability

Principles of Federal Enforcement:

Resolving Potential Enforcement Actions

Factors Considered in Deciding Whether to Open an Investigation or Bring Charges

- Existing Guidance
 - U.S. Attorneys' Manual *Principles of Federal Prosecution of Business Organizations*
 - SEC Enforcement Manual
 - SEC *Seaboard Report*
 - U.S. Sentencing Guidelines Chapter 8 (sentencing organizations)

Factors Considered in Deciding Whether to Open an Investigation or Bring Charges

- Nature and seriousness of the offense
- Risk of harm to the public
- Pervasiveness of the wrongdoing
- Whether the conduct is ongoing
- Corporation's history of similar misconduct

Types of Resolutions

DOJ

- Criminal complaints, informations, indictments
- Plea agreements
- Deferred prosecution agreements
- Non-prosecution agreements
- Declinations

SEC

- Civil injunctive actions & remedies
- Administrative actions & remedies
- Deferred prosecution agreements
- Non-prosecution agreements
- Termination letters & declinations

Self-Reporting, Cooperation, and Remediation – Impact on Resolutions

- Guidance offers distinctive new feature
 - Six “anonymized” historical examples in which regulators declined prosecution
 - Includes factors leading to declination decisions

Common Factors Contributing to Declination

1. Voluntary disclosure or self-reporting to enforcement agencies
2. Thorough internal investigation
3. Revised or strengthened existing compliance programs
4. Proactively remediated violations by terminating employees, severing third-party relationships, and/or withdrawing bid proposals
5. Existence of strong compliance program detected improper conduct

Common Factors Contributing to Declination: A Small Observation

- “The total amount of the bribes was small”
- “Total amount of the improper payments was relatively small”
- “Profits potentially obtained from the improper payments were very small”
- “Detected a potential bribe before a payment was made”

An Effective Compliance Program:
**Maximizing Compliance To
Prevent Misconduct**

Overview of Compliance Guidance

- SEC/DOJ Guidance is very helpful on compliance issues but could do more to account for realities of international business operations
- Three observations concerning the Guide's points on compliance:
 1. Compliance for compliance's sake is a waste of money:
 - *Compliance is a business risk management tool*
 - *Best judged on its effectiveness for mitigating risk*
 2. Pre-acquisition due diligence has significant limitations as risk-management tool
 3. Post-acquisition due diligence is far more effective and therefore more valuable and important
- Understanding that the FCPA's purpose to promote a level playing field, if U.S. companies and foreign competitors are not held to same standard, field is not level

Compliance Guidance

- Guide to Minimize Risk of Improper Conduct
 1. Acquisition-Related Guidance
 - *Pre-Acquisition Due Diligence*
 - *Post-Acquisition Review and Integration*
 2. Guidance Related to Ongoing Operations
 - *Hallmarks of Effective Compliance Program*
 - *Special Case: Vetting and Monitoring Third-Party Agents*

Pre-Acquisition Due Diligence

- The Guidance places significant emphasis on due diligence to reduce risk of incurring successor liability of acquired companies
 - Due diligence helps acquiring companies accurately value targets by identifying unenforceable contracts procured through bribery
 - Due diligence reduces risk that bribes and other improper payments will be continued following acquisition
 - Consequences of potential violations uncovered through due diligence can be handled efficiently
 - Comprehensive diligence demonstrates commitment to uncovering and preventing FCPA violations

Pre-Acquisition Due Diligence

Practical Tips to Reduce FCPA Risk in Mergers and Acquisitions

Companies pursuing mergers or acquisitions can take certain steps to identify and potentially reduce FCPA risks:

- **M&A Opinion Procedure Release Requests**: One option is to seek an opinion from DOJ in anticipation of a potential acquisition, such as occurred with Opinion Release 08-02. That case involved special circumstances, namely, severely limited pre-acquisition due diligence available to the potential acquiring company, and, because it was an opinion release (i.e., providing certain assurances by DOJ concerning prospective conduct), it necessarily imposed demanding standards and prescriptive timeframes in return for specific assurances from DOJ, which SEC, as a matter of discretion, also honors. Thus, obtaining an opinion from DOJ can be a good way to address specific due diligence challenges, but, because of the nature of such an opinion, it will likely contain more stringent requirements than may be necessary in all circumstances.
- **M&A Risk-Based FCPA Due Diligence and Disclosure**: As a practical matter, most acquisitions will typically not require the type of prospective assurances contained in an opinion from DOJ. DOJ and SEC encourage companies engaging in mergers and acquisitions to: (1) conduct thorough risk-based FCPA and anti-corruption due diligence on potential new business acquisitions; (2) ensure that the acquiring company's code of conduct and compliance policies and procedures regarding the FCPA and other anti-corruption laws apply as quickly as is practicable to newly acquired businesses or merged entities; (3) train the directors, officers, and employees of newly acquired businesses or merged entities, and when appropriate, train agents and business partners, on the FCPA and other relevant anti-corruption laws and the company's code of conduct and compliance policies and procedures; (4) conduct an FCPA-specific audit of all newly acquired or merged businesses as quickly as practicable; and (5) disclose any corrupt payments discovered as part of its due diligence of newly acquired entities or merged entities. DOJ and SEC will give meaningful credit to companies who undertake these actions, and, in appropriate circumstances, DOJ and SEC may consequently decline to bring enforcement actions.

Post-Acquisition Due Diligence

No.: 08-02

Date: June 13, 2008

Foreign Corrupt Practices Act Review

Opinion Procedure Release

The Department has reviewed the Foreign Corrupt Practices Act ("FCPA") Opinion Procedure request of Halliburton Company and its controlled subsidiaries ("Halliburton"), a U.S. issuer, which is currently considering making an additional bid to acquire the entire share capital of a company based in the United Kingdom ("Target"). Target is traded on the London Stock Exchange, has approximately 4,000 employees, and operates in over fifty countries, including throughout Africa, the Middle East, Asia, the former Soviet Union, South America, Europe, and North America. Target is involved in well flow management and provides specialized products and services in the upstream oil and gas industry. Target has a number of national oil companies as customers. A company formed by a consortium of primarily foreign investors ("Competitor") is also bidding to acquire Target. Competitor submitted the first, and more recently the highest, bid, which is unconditional.

- The Guidance also credits adequate post-acquisition due diligence where pre-acquisition diligence is not possible
 - Cites Opinion Procedure Release 08-02

Vetting Third-Party Vendors

- The Guidance recognizes significant risks posed by third-party vendors
- Common red flags associated with third parties
 - Excessive commissions
 - Unreasonably large discounts to distributors
 - Vague “consulting agreements”
 - Close familial, personal, or professional affiliations with foreign government officials
- Emphasizes need for appropriate vetting programs before engaging third parties

Vetting Third-Party Vendors

- Guiding principles for such a program include:
 1. Companies should understand the qualifications of their third-party business partners, including their reputations and relationships with government officials
 2. Companies should understand the business rationale for including a third party
 - *What is its role?*
 - *What services are to be performed?*
 - *Ensure that payment terms are comparable to typical industry/country standards*
 3. Companies should regularly monitor third-party relationships
 - *Exercise audit rights*
 - *Request annual compliance certificates*

Hallmarks of an Effective Compliance Program

- No “one-size-fits-all” approach
- Ten aspects of effective compliance programs
- Should be tailored to business’s specific risks, but provide hallmarks that could help companies prevent, detect, and remediate problems that occur
- Will also be considered by government agencies in assessing whether, and in what form, enforcement action should be brought
 - Case study example cites recent enforcement declination where robust controls were circumvented by rogue employee

Hallmarks of an Effective Compliance Program

1. Commitment from Headquarters-Level and Local Senior Management and a Clearly Articulated Policy Against Corruption
 - “Tone from the top”
 - Specific Considerations
 - *Clearly articulated standard*
 - *Communicated by senior management unambiguously*
 - *Adhered to scrupulously*
 - *Disseminated throughout the organization*

Hallmarks of an Effective Compliance Program

2. Updated Code of Conduct and Compliance Policies and Procedures
 - The most effective programs are clear, concise, and accessible to all employees
 - Policies should outline internal controls requirements, auditing practices, and disciplinary procedures for violations
3. Oversight, Autonomy, and Resources
 - Responsibility for and implementation of the program should be vested with specific senior-level executives
 - These individuals should have authority, autonomy, and resources to ensure the program is implemented effectively

Hallmarks of an Effective Compliance Program

4. Risk Assessment

- Programs tailored to the relative risk of a given transaction can save expenditure of resources on low-risk ventures

5. Training and Continuing Advice

- Steps should be taken to ensure that relevant policies and procedures are effectively communicated
- Should include periodic training and certification of directors, officers, employees, agents, and business partners

Hallmarks of an Effective Compliance Program

6. Incentives and Disciplinary Measures

- An effective program includes disciplinary procedures for violations; and
- Incentives for ethical conduct, such as making compliance a performance metric for management

7. Third-Party Due Diligence

- In addition to effective vetting programs, companies should also communicate their commitments to ethical and lawful conduct and seek assurances of the same

8. Confidential Reporting and Internal Investigation

- Effective program should include a means for internal reporting of misconduct
- Should also include an effective and well-funded procedure for investigating tips

Hallmarks of an Effective Compliance Program

9. Continuous Improvement

- Effective programs should evolve and be updated based on the company's business model, operating environment, and industry

10. Pre-Acquisition Due Diligence and Post-Acquisition Integration

- In addition to appropriate due diligence, effective programs should also have a means for promptly incorporating acquired companies into its internal controls program

Q & A



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