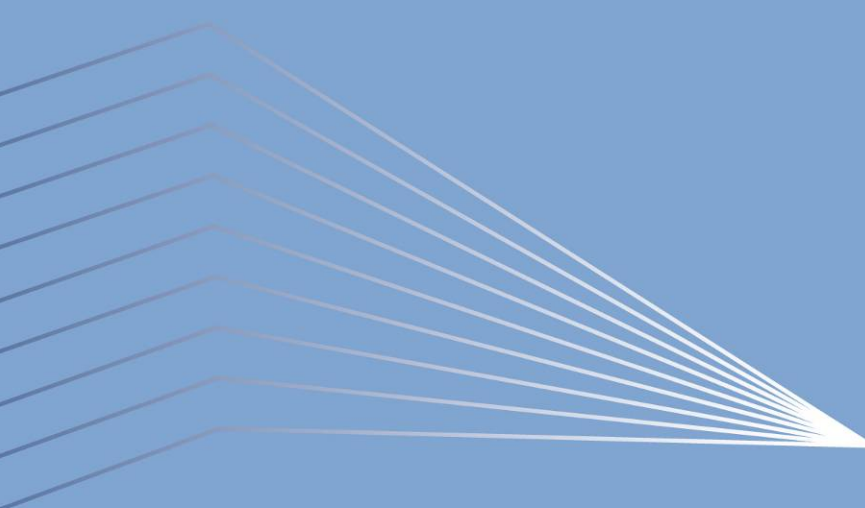


SHEARMAN & STERLING<sub>LLP</sub>



## FCPA Digest

Recent Trends and Patterns in the Enforcement of the  
Foreign Corrupt Practices Act

JANUARY 2011

SHEARMAN & STERLING<sup>LLP</sup>

# Recent Trends and Patterns in FCPA Enforcement

---

January 20, 2011

Philip Urofsky & Danforth Newcomb  
*Shearman & Sterling LLP*

Recent Trends and Patterns in FCPA Enforcement

---

**Table of Contents**

	<b>Page</b>
A Record Year .....	1
<i>Corporate Prosecutions</i> .....	1
<i>Individual Prosecutions</i> .....	3
Enforcement Strategies .....	4
<i>Jurisdiction</i> .....	5
<i>Foreign Companies</i> .....	5
<i>Monitors</i> .....	7
<i>Industry Sweeps</i> .....	8
<i>Inconsistent Theories of Parent Liability</i> .....	9
Statutory Interpretation .....	10
<i>Facilitation Payments</i> .....	10
<i>Instrumentalities</i> .....	11
<i>The Business Nexus</i> .....	13
Guidance on Compliance Programs.....	15
<i>Compliance Monitoring</i> .....	15
<i>Internal Controls</i> .....	16
<i>Compliance Responsibilities</i> .....	17
<i>Gifts and Entertainment</i> .....	18
International and U.S. Legislation and Regulations .....	18
<i>U.K. Bribery Act</i> .....	18
<i>U.S. Legislation and Regulations</i> .....	19

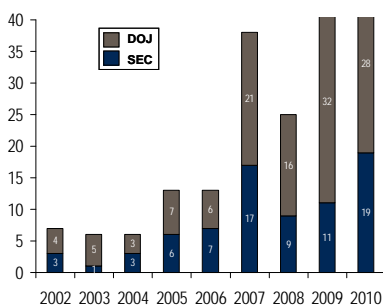
## Recent Trends and Patterns in FCPA Enforcement

After a relative lull in 2009 in large corporate enforcement actions, 2010 saw a resurgence in corporate cases against large corporations, with over \$1.7 billion in total penalties. Strangely, however, with very few exceptions, most of these cases have involved non-U.S. companies. Clearly, U.S. companies are not in the clear, but the DOJ's focus in the short-term seems to be very much on putting pressure on non-U.S. companies to comply with global anti-corruption agreements, particularly when those companies' home countries are less than aggressive in enforcing their own corruption laws. At the same time, as reflected in the charges against 22 members of the military and law enforcement industry (the "SHOT-show" cases), the TSKJ and *Panalpina* matters, the tobacco wholesalers matters, and the pharma initiative, the U.S. government clearly is pursuing high-profile enforcement actions hoping to encourage compliance in entire industry sectors.

The cases that were brought in 2010 provide valuable, albeit not uncontroversial, guidance from the authorities as to the scope and meaning of the statute. In particular, the *Panalpina* cases provided insight into which types of payments the government believed fell outside the facilitation exception. The *Alcatel-Lucent* matter offered guidance as to the meaning of the government "instrumentality." Finally, the *Technip* and *Snamprogetti* cases provided confirmation that the government will use "correspondent account" jurisdiction as well as conspiracy law to reach foreign companies engaged in corrupt conduct.

On the other side of the coin, some of the government's cases appear to blur the lines or muddy the waters when it comes to the limits of the statute. In several cases, such as *Pride International*, *Panalpina*, and *Royal Dutch Shell*, the theories used to hold parents accountable for the acts of subsidiaries and vice versa appear to be unclear. In others, such as *Pride International* and *Tidewater*, the connection of the alleged conduct to "obtaining or retaining business," a critical element of the statute was not pleaded or, worse, was pled in a way that suggests that virtually any bribe that improves a company's profitability is sufficient – a result that is not consistent with established precedent and the language of the statute.

Total SEC/DOJ Matters Initiated: 2002-2010



In the next year, we expect to see a number of trials of individuals as well as additional corporate matters. As always, these matters may well bring some clarity to some of these existing unsettled areas of the law.

### A Record Year

#### *Corporate Prosecutions*

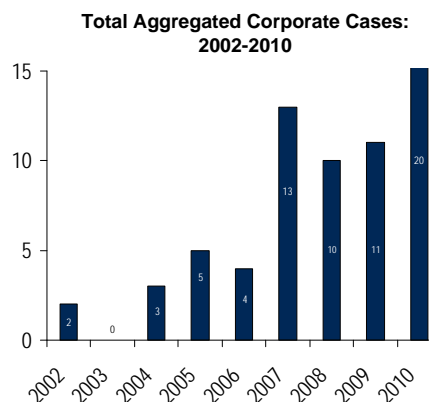
In terms of gross numbers, in 2010 the DOJ charged or otherwise alleged (*e.g.*, with deferred prosecutions)

## Recent Trends and Patterns in FCPA Enforcement

violations of the FCPA against 28 companies<sup>1</sup> and the SEC charged 19 companies.<sup>2</sup> Taken together, this amounts to 47 corporate prosecutions in 2010, approximately the same number as 2009.

As we noted in our last *Trends & Patterns*, however, statistics are malleable things. In many cases, the government charged several affiliated companies in a single action and in others both the DOJ and the SEC charged the same company. If we count such matters as single consolidated cases, then the total number of corporate cases for 2010 was 20, exceeding that of any previous year.

Total penalties imposed on corporations in 19 of these matters (*Lindsey Manufacturing* has not settled) amount to a record-setting \$1,782,720,952. In addition, *BAE* and *Innospec* agreed to pay approximately \$50,000,000 to the U.K. authorities to settle related U.K. enforcement actions.



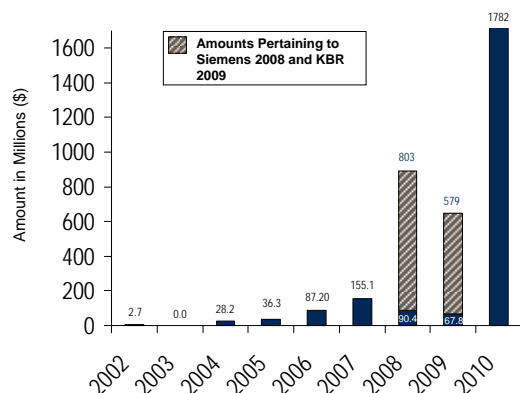
This is an impressive number and exceeds all previous years. These fines are not, however, evenly distributed. Fully two-thirds (\$1.1 billion) of this \$1.7 billion in fines derive from three matters – *Technip*, *Snamprogetti*, and *BAE*, cases in which the companies each paid over \$350 million in combined penalties. If *Daimler*, *Panalpina*, and *Alcatel* are included, in which each paid close to \$100 million, then these six cases account for 80% (\$1.36 billion) of the total penalties. It is also interesting, of course, to note that all six of these companies are non-U.S. corporations.

<sup>1</sup> This number excludes the criminal information filed against *Mercator*, which was part of a settlement of the *Giffen* case, originally filed in 2004.

<sup>2</sup> This number excludes the *GE* matter here, as it involved only Oil-for-Food kickbacks that were charged as FCPA books-and-records violation but not FCPA bribery. In several other cases (*Daimler*, *ABB*, and *Innospec*), the government charged both FCPA bribery and separate crimes related to the Oil-for-Food program.

## Recent Trends and Patterns in FCPA Enforcement

**Total Criminal and Civil Fines Imposed on Corporations:  
2002-2010**



What does this mean for the rest of the companies? For the remaining thirteen matters, the average penalty has been approximately \$20 million, with six of those matters resulting in fines under \$10 million. Admittedly, even that amount, particularly when added to the costs of investigation and, in some cases, the cost of a corporate monitor, is not inconsequential. It does, however, call into question some of the outlandish claims made on both sides of the aisle – that the consequences of a FCPA violation are in all cases severe and dissuasive or that the enforcement penalties

are out-of-control, extreme, and crippling.

Finally, we have often heard that an FCPA charge can be the death knell for a company but, apart from sole proprietorships, we have never seen a company put out of business as a result of a FCPA enforcement action. Until now, that is. In 2010, *NEXUS Technologies*, which had been indicted in 2007 for paying bribes to Vietnamese officials and was days away from trial – what would have been the first corporate FCPA trial since 1988 – entered a guilty plea in which it admitted that its business was permeated with corruption and, accordingly, agreed to cease operations in the U.S. and Vietnam. Given that its four most-senior executives all entered pleas at the same time, this conclusion was not surprising.

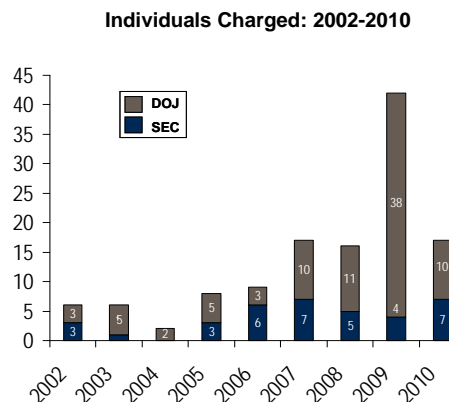
### *Individual Prosecutions*

2009 saw a sharp spike in the number of individuals charged, mostly from the 22 individuals charged in the SHOT cases and seven of the eight executives of *Control Components*. In 2010, both agencies continued to hold individuals accountable, charging sixteen individuals with FCPA offenses. Of these, the DOJ charged ten individuals, including four individuals associated with one company, *Lindsey Manufacturing*, as well as the cooperator in the SHOT case. The SEC, in turn, charged seven individuals, including four employees of *Alliance One* (one of whom was also charged in 2010 by the DOJ) and two individuals affiliated with *Innospec* (one of whom was previously charged by the DOJ). Of the individuals charged in 2010, one pleaded guilty while all of the individuals charged in the SEC cases settled.

The DOJ also began to clear its backlog of charged individuals from years past. Twelve individuals – ten of whom were charged in previous years – pleaded guilty in 2010. Further, although, in contrast to 2009, there were no trials in 2010 and there are still 40 individuals pending trial, several trials are scheduled to commence in the first six months of 2011.

## Recent Trends and Patterns in FCPA Enforcement

Thirteen individuals were sentenced in 2010, with wildly varying results. Two individuals in the *Nexus* case, both of whom cooperated with the government, received probation, while two others in the same matter received 9 and 16 months. At the other end of the spectrum, the court in the *Haiti Telecom* case imposed much more severe sentences, with two sentences of 48 and 57 months. By far the most severe sentence was that imposed on *Diaz* in the *PECC* case of 87 months and \$1.1M in fines.



There have also been some odd cases in which the courts resisted the severe sentences recommended by the government and either departed downward or used different Sentencing Guideline calculations to impose much shorter terms. For example, in the *Green* case, in which both husband and wife were convicted of paying significant bribes to a Thai official and of profiting handsomely from it, the government sought ten years, the Probation Office recommended a year and a day, and the court departed downward to six months incarceration and six months home confinement. Further, having already ordered the criminal forfeiture of most of the Greens' possessions – their home, car, company, and pension fund – the court permitted them to pay restitution of \$250,000 at a rate of \$50 per month. Not surprisingly, the government has filed an appeal. In *Giffen*, a case that encountered significant difficulties in pre-trial discovery, the government eventually agreed to a resolution that involved no jail time whatsoever.

Finally, it is of note that several, although not all, of the defendants who were sentenced last year were required to pay fines, with most ranging between \$25,000 and \$40,000. In one case, however, *Ousama Naaman*, who acted as *Innospec's* agent, was forced to pay an aggregate civil penalty of over \$1.3 million including a fine, disgorgement, and interest and is still awaiting sentencing in the criminal case.

### Enforcement Strategies

As in years past, the enforcement actions brought in 2010 provide insight, albeit sometimes clouded, into the DOJ's and the SEC's views of the scope and meaning of certain aspects of the statute, as well as their enforcement priorities and strategies. In doing so they are at times helpful and at other times opaque or, even worse, disturbing. As always, however, it is important to remember that although these agreements may have been hotly negotiated, in the end each of

## Recent Trends and Patterns in FCPA Enforcement

---

the companies and individuals settled. Thus, none of the government's interpretations, or its view of how the law applied to the facts, has been subjected to a searching judicial examination in the context of a contested adversary proceeding.

### *Jurisdiction*

In *Siemens* and *Halliburton/KBR*, we saw the first indication that the DOJ and the SEC intended to make good on previous claims that they possess territorial jurisdiction over foreign companies based on overseas financial transactions involving U.S. dollars – a theory premised on the fact that virtually all such transactions clear through correspondent banking accounts in the United States. In those cases, in which other clearly territorial acts such as meetings, payments, and transfers from U.S. bank accounts, were charged, the “correspondent bank account” jurisdiction was not critical to the case, but clearly provided an indication of the government's views. In our comments at the time, we speculated that these allegations were targeted at KBR's foreign joint venture partners, all of whom were identified as unindicted co-conspirators in the *KBR* case.

In 2010, we saw the other shoe drop in the *Technip* case. Although, as in the companion case against *Snamprogetti*, the DOJ charged a conspiracy between Technip, the other TSKJ partners, and the agents with overt acts in the U.S. (mostly communications with KBR), the substantive FCPA bribery counts in both the DOJ's and the SEC's pleadings alleged jurisdiction almost entirely based on U.S. dollar bank transfers from the Netherlands to Switzerland and Japan. How often the government will use this aggressive basis for jurisdiction and whether it would stand up if challenged in court remains to be seen. At this time, none of the cases currently pending for trial turn on this jurisdictional allegation.

### *Foreign Companies*

Of note, a significant majority of the corporations charged in 2010 are non-U.S. companies. Again, the numbers can be sliced and diced in different ways. For example, on an overall basis, 23 non-U.S. companies are named in various DOJ and SEC pleadings. Some of these, however, are foreign subsidiaries of U.S. parents and, one, although incorporated offshore, has its principal offices and operations in the U.S. Accordingly, as a practical matter, eleven of the twenty corporate matters brought in 2010 involved non-U.S. companies.<sup>3</sup>

---

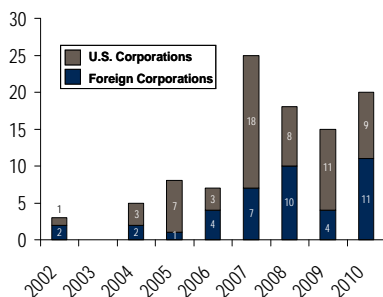
<sup>3</sup> Non-U.S. companies: *ABB*, *Alcatel-Lucent*, *BAE*, *Daimler*, *Innospec*, *Noble*, *Panalpina World Transport*, *Royal Dutch Shell*, *Snamprogetti/ENI*, *Technip*, and *Transocean*.

U.S. companies: *Alliance One*, *GlobalSantaFe*, *Lindsey Manufacturing*, *Natco*, *Pride International*, *RAE Systems*, *Tidewater*, *Universal*, and *Veraz*.

## Recent Trends and Patterns in FCPA Enforcement

Moreover, as noted, six of the corporate matters, all of which involved non-U.S. companies, accounted for over 80% of the fines imposed in 2010. Overall, the eleven non-U.S. companies were responsible for 94% of the penalties imposed on corporations in 2010.

Total Corporate Matters Initiated: 2002-2010



We have noted the trend of the U.S. prosecuting foreign corporations for several years. Last year clearly represented a high-water mark, but the underlying reasons remain the same. In the thirty-three years since the FCPA was enacted in 1977 and the twelve years since the OECD Anti-bribery Convention became effective in February 1998, there have been very few non-U.S. prosecutions for transnational bribery. Although a recent OECD report highlights uneven gains in this area, it is clear that the U.S. government intends to continue using

its expansive view of jurisdiction under the FCPA to spur foreign governments to be more proactive – or face the consequence of seeing their domestic corporations hauled into U.S. courts.

There are, however, some subsidiary trends that indicate some progress in the international arena. In a number of cases over the past several years, the DOJ has agreed to resolutions that explicitly contemplate both U.S. and foreign enforcement. *Siemens*, of course, is one of the prime examples of this trend, in which the investigation was initiated in Germany and the final resolution involved coordinated pleas and settlements in Germany and the United States. In 2010, both *BAE* and *Innospec* involved coordinated investigations and resolutions in the U.K., with responsibility and penalties being allocated between the two countries in fairly transparent ways.

Finally, although not reflected in any specific enforcement actions, we have seen in our own matters, and understand from our colleagues, that in some cases the U.S. enforcement agencies are not only coordinating enforcement actions with foreign enforcement agencies but are even willing to defer to the foreign agencies during the investigative phase, monitoring and observing but not necessarily taking a leading role. In the end, of course, the test will be whether they will defer to a foreign enforcement authority's conclusions, even if the foreign enforcement authority ultimately declines to bring an action. It remains to be seen whether the U.S. authorities will (or should) stretch for jurisdiction in such circumstances, provided the foreign enforcement authority's decision is based on a credible investigation and grounded in the facts and the law, as opposed to some commercial national interest. As a practical matter, however, the U.S.

## Recent Trends and Patterns in FCPA Enforcement

---

authorities, which have the benefit of plea bargaining and alternative resolutions such as deferred prosecutions, will likely undertake an independent review. Indeed, we understand that in some cases foreign enforcement authorities faced with legal impediments to corporate liability have actually referred matters involving their own corporations to the U.S. authorities.

### *Monitors*

From 2004 until recently, the U.S. enforcement agencies have almost routinely required companies to retain an independent monitor for a period of several years. These monitors have been charged with evaluating a company's compliance program and controls as designed and implemented in the field and filing periodic reports to the government. Although many companies have reported positive experiences with the monitors, concluding that they provided valuable insight and spurred the company toward making necessary improvements in its compliance program and controls, others have complained of the cost and intrusiveness.

As we have noted in previous *Trends & Patterns*, beginning in 2009 the government began to adopt a more nuanced approach, drawing distinctions, not always in a transparent way, between companies. In some cases, the government did not require a monitor at all; in others it imposed a "monitorship-lite" under which a company is permitted to appoint its existing compliance advisor and to essentially "self-monitor," albeit with certain reporting requirements.

In 2010, we continued to see this trend, although with some interesting twists. For example, in *BAE*, *Technip*, and *Alcatel*, the companies were required to retain full-fledged compliance monitors. In each case, the government recognized some of the sensitivities involved in imposing a U.S. monitor on a foreign company. Thus, in *Technip* and *Alcatel*, the company was permitted to retain a French monitor and, although this monitor was to submit reports to the U.S. authorities, the agreement specifically provided that reports of new unlawful conduct should be made in the first instance to the French authorities. For *BAE*, the government had to accommodate a different concern – that the company is an integral part of the U.K.'s security apparatus. Thus, the agreement provided that the monitor would be a U.K. citizen with appropriate clearances; this has, in practice, turned out to be a difficult proposition, and the DOJ apparently vetoed the first set of candidates as unqualified. In *Daimler*, on the other hand, the company was permitted to retain the compliance consultant it had retained after the investigation commenced to counsel it on remediation.

In the *Panalpina* cases, the government appears to have gone to the other extreme and not imposed any monitors on any of the companies involved. This is all the more surprising given that the pleadings against Panalpina itself depict a company that deliberately failed to implement anti-corruption controls – indeed the former Chairman resisted them and the Board followed his lead – and paid bribes across the world both on behalf of its customers and for its own benefit. It

## Recent Trends and Patterns in FCPA Enforcement

---

is possible, however, that the company's significant remediation, which included, among other things, completely closing down its Nigeria operations, may have been a significant factor. It is less obvious why the government also did not impose a monitor on *Snamprogetti*, even though it had required all of the other TSKJ partners prosecuted to date (*Halliburton*, *KBR*, and *Technip*) to retain monitors.

### *Industry Sweeps*

The *Panalpina* matters involve the first coordinated industry initiative in recent FCPA history, having begun much earlier than the SHOT investigation. It is possible that the DOJ or the SEC may expand the investigation to other international freight-forwarders, but the focus here appears to have been on the oil & gas industry, and particularly on oil field services companies. If the goal of the investigation was to influence the entire industry, it appears that the message was received by at least some companies even before the investigation concluded, as at least one of the defendants (*Noble*) commenced an internal investigation and made a voluntary disclosure concerning conduct involving a different freight forwarder after learning of the Panalpina investigation.

The government's decision to pursue Panalpina's customers – and other oil & gas companies – was opportunistic in that the government had leverage over Panalpina through the *Vetco Gray* matter and was able to use the evidence from that matter as a guide to what types of payments other companies may have been making. Similarly, in the tobacco wholesaler cases (*Universal* and *Alliance One*), the government was fortunate in detecting that one company was using the same agent and making the same payments as the other.

We are aware of at least three other industry sweeps – the SHOT cases, the medical device investigations, and the pharma initiative. In each case, the government has been able to use knowledge gained from one investigation to expand it to other companies. In the SHOT case, BAE, the new owner of Armor Holdings had disclosed conduct involving, among others, *Richard Bistrong*. The government was able to persuade Bistrong to cooperate, and he agreed to introduce government agents to colleagues and acquaintances in the law enforcement and military supply industry, leading eventually to the arrest of twenty-two individuals. In the medical device investigation, the government has keyed off an earlier successful investigation into domestic kickbacks by hip-replacement companies. Finally, in the pharma initiative, the government was able to use the knowledge from previous pharmaceutical cases (*Syncor*, *Diagnostic Products*, *Micrus*, etc.) and ongoing investigations to identify alleged industry practices and then confront certain companies.

The pattern is clear. With new resources – a larger corps of FCPA prosecutors and support from a dedicated squad of FBI agents – the DOJ is more and more often applying traditional

## Recent Trends and Patterns in FCPA Enforcement

---

prosecution strategies in the FCPA arena. Rather than relying on one case to have an impact on a particular industry or market sector, the government is clearly dedicated to using the lessons learned in each investigation to reach similarly situated companies and individuals. In doing so, it will use the evidence from one investigation to launch undercover operations, to issue subpoenas, or to “invite” companies to cooperate.

### *Inconsistent Theories of Parent Liability*

The charging decisions in the *Panalpina* cases reflect both an established practice and some inconsistencies in terms of the government’s approach to a parent corporation’s liability for the actions of its subsidiaries. In theory, a parent company, if it is an issuer in the United States, is strictly liable for a subsidiary’s inaccurate books and records and ineffective internal controls. The test is different, however, under the FCPA’s anti-bribery provisions: for a parent company to be liable under those provisions for the corrupt conduct of its subsidiary, the government must have evidence that the parent directed, controlled, or authorized the subsidiary’s corrupt conduct, *i.e.*, that the subsidiary acted as the parent’s agent.

Over the years, a pattern has emerged in which the DOJ will bring FCPA bribery charges against a subsidiary, while entering into a side letter or non-prosecution agreement with the parent. If the parent is an issuer, the SEC will often bring a parallel civil action against the parent alleging, at a minimum, books & records and internal controls violations. When properly applied, this practice allows the government to impose liability on the appropriate parties – the subsidiary for corrupt conduct, the parent for inadequate controls – and, through the DOJ side letter and the SEC consent decree, to ensure that the parent is placed under a clear and enforceable obligation to address compliance failures throughout its corporate structure.

As we have pointed out in the past, however, the government at times deviates from this relatively clear demarcation of liability and charges the parent company with liability under the anti-bribery provisions without pleading all of the necessary predicate facts, *i.e.*, some evidence that the subsidiary was acting *for* the parent – as an agent or otherwise under the parent’s direction, authorization, or control. An early example of this practice was the SEC’s actions against *United Industrial Corporation*. See Shearman & Sterling, *Internal Control Failures Lead to Parent Liability* (June 2, 2009). In 2010, the DOJ appeared to follow the practice in at least one case. Although the DOJ charged *Pride International* with, *inter alia*, a substantive FCPA bribery offense based on a bribery scheme, laid out in detail in the pleadings, involving the company’s French and Venezuelan subsidiaries, it did not allege the parent’s involvement in the scheme apart from a bare, and unsupported, allegation in the charging language that the subsidiaries paid the bribes “on behalf of Pride International.” Obviously, as a matter of legal practice, it is problematic to charge a company without alleging in sufficient detail how the company violated each element of the offense. More alarming, however, is the possibility that

## Recent Trends and Patterns in FCPA Enforcement

---

the government is adopting *sub rosa* a theory that the parent's failure to implement effective internal controls is tantamount to willful blindness under the anti-bribery provisions. If that is the theory, it requires much more explanation that the government has provided thus far.

In other cases, such as *Halliburton/KBR*, *Panalpina*, and *Royal Dutch Shell*, the SEC did exactly the opposite, charging the subsidiary with violating the anti-bribery provisions while acting as an agent of its parent but not charging the parent itself with anti-bribery violations. The purpose of classifying the subsidiary as an agent of the parent issuer is clear: the SEC's jurisdiction requires some link to an issuer. That, however, is hardly sufficient to justify pleading an agency relationship without setting out its factual predicate. In cases such as *Royal Dutch Shell*, the pleadings are completely devoid of any indication that the parent directed the subsidiary's actions or that, beyond the fact that the subsidiary's profitability benefited the parent, that the subsidiary was acting on behalf of the parent – an essential predicate for an agency relationship. It is not clear why the SEC felt the need to stretch for jurisdiction in these cases; it had clear books & records jurisdiction over the parent and thus the ability to impose significant penalties and supervision.

### Statutory Interpretation

#### *Facilitation Payments*

In a number of recent cases, the DOJ and the SEC have brought cases in which at least some of the alleged payments appear to be facilitation payments. For example, in the *Wabtec* matter, the DOJ separately described “Ordering Payments,” “Product Inspection Payments,” “Clerical Payments to Receive Delivery Receipts,” and “Central Board of Excise and Customs Payments,” some of which appear clearly to have been made to obtain new business while others appear to have been more in the nature of expediting payments that were booked improperly. However, as the matter was settled through a Non-Prosecution Agreement and there was no charging document, the DOJ did not explicitly specify which payments fell into which category.

The *Panalpina* cases would appear to have provided a perfect opportunity for the government to provide guidance on which payments, if booked properly, would fall within the facilitation payments exception. Unfortunately, it did not do so, even in cases such as *GlobalSantaFe* in which the SEC appeared to distinguish between bribes and “other suspicious payments” but then incorporated all of the pleadings into the anti-bribery count.

The DOJ and SEC pleadings in the *Panalpina* cases are thus important mostly for defining what is *not* a facilitation payment. The amount of these payments varied from significant to relatively paltry sums. What would appear to distinguish many of these payments from mere facilitation payments, however, was that they were intended to obtain more than “routine governmental action” and were not made under circumstances “where there is entitlement to the action in question.”

## Recent Trends and Patterns in FCPA Enforcement

---

For example, the DOJ and the SEC charged as bribes payments to customs officials to avoid taxes and penalties for violations of customs regulations or to “disregard certain regulatory requirements relating to the temporary importation” of vessels and equipment. Further, in certain of the matters, the agencies charged as bribes certain payments allegedly intended to “expedite[] the importation of goods and equipment,” payments that might have been considered facilitation payments had they not also enabled the companies “to avoid the normal customs clearance process and the payment of official duties and taxes.”

Other factors that may have distinguished these payments from facilitation payments were the scope and duration of the payments. Certainly in the case of Panalpina as well as certain of the other companies, these payments were routinely made over many years in many countries. Further, in some instances the equipment or goods being imported was deemed essential to the companies being able to win or continue to work on lucrative projects.

### *Instrumentalities*

Some commentators – and defendants – have sought to make an issue over whether the FCPA’s definition of “foreign official,” particularly as it relates to officers or employees of “instrumentalities” of foreign governments, is unfairly ambiguous. Following their lead, the defendants in two cases last year argued that the FCPA did not apply to employees of companies that were “merely owned or partially owned” or “controlled or partially controlled” by a foreign government. In the *Nexus* case, the court summarily denied the defendants’ motion to dismiss, without a written opinion, and the defendants subsequently pleaded guilty. In *U.S. v. Esquenazi, et al.*, the court similarly rejected the defense argument in a short opinion, finding that the government had “sufficiently alleged that [certain individuals] were foreign officials by alleging that these individuals were directors in the state-owned Haiti Teleco” and that Haiti Teleco’s status as an instrumentality was a matter of fact for trial. The court further found that the FCPA’s definition of foreign official as it applied to employees of instrumentalities was not unconstitutionally vague, finding that “persons of common intelligence would have fair notice of this statute’s prohibitions.”

In the *Haiti Telecom* case, the government stated that it intends to introduce at trial evidence that the company was, prior to being privatized *after* the bribes were allegedly paid, owned by the Haitian government and “held a state-granted monopoly over land line telephone service in Haiti.” Further, the Director General of the company was appointed by the Haitian government, as was its Board of Directors. Finally, Haiti’s Central Bank, which formally held 97% of the company’s shares, was required by law to use any profits for the benefit of the public treasury, and the company was thus viewed as an “important source of revenue and . . . foreign reserves” for the state.

## Recent Trends and Patterns in FCPA Enforcement

---

Towards the end of the year, the government provided significant guidance on its view of the meaning of “instrumentality” through its charges against *Alcatel-Lucent*. In *Alcatel*, the company admitted that its subsidiaries paid bribes to officials of several telecom companies in a number of countries, and the government carefully outlined in the pleadings the factors that made such companies instrumentalities. These included:

- Companies that acted “for the government”;
- Officers and Boards appointed by the government;
- Government officials sitting on supervisory boards;
- Oversight by government agencies;
- Profits paid to the government;
- Government mandate or charter;
- Government veto over major expenditures;
- Government involvement in important operational decisions; and
- Government status as a “special shareholder.”

Moreover, although many of these entities were wholly-owned by a foreign government, in one case – Telekom Malaysia Berhad – the Malaysian government held only a 43% share. Nevertheless, the government viewed the Malaysian government’s ability to control the company’s decisions and to appoint its officers as important factors in establishing its status as an instrumentality.

Similarly, in *Pride International*, the DOJ concluded that PDVSA, the Venezuelan oil company, was a government instrumentality. Although the company undoubtedly acted in the commercial arena, the government noted that “the Government of Venezuela established PDVSA . . . to manage and control the exploration, production, refinement, and transport of oil as well as the exploration of natural gas in Venezuela.

As a practical matter, despite the parade of potential horrors posited by some commentators, the government has long stated its view that the relevant factor in determining whether a company is an instrumentality is whether a foreign government exercises “effective control.” As a result, although a company cannot proceed blindly, it does require an unduly difficult amount of due diligence in most cases to determine the relationship between a government and a company, even if that relationship changes over time through, *e.g.*, some form of creeping privatization or nationalization. Further, as a compliance matter, it is not entirely clear how serious an issue this is: most companies prohibit bribery or kickbacks to either public or private counterparties. Where it appears to become most relevant is in the area of gifts and entertainment, where promotional activities that may be acceptable with a commercial customer would raise concerns with a government customer.

## Recent Trends and Patterns in FCPA Enforcement

---

### *The Business Nexus*

The *Panalpina* cases and certain allegations in other cases are likely to reopen the debate as to the meaning of the “obtain or retain business” element. This element is recognized as a critical factor in narrowing the scope of the FCPA. How much it does so, however, has long been a matter of debate. In its 2004 decision in *U.S. v. Kay*, the Fifth Circuit appeared to have ended the debate, holding that the FCPA was not limited to bribes to obtain business from a foreign government or even to bribes that led “directly to the award or renewal of contracts.” Analyzing the indictment in that case, the court held that “bribes paid to foreign officials in consideration for unlawful evasion of customs duties and sales taxes *could* fall within the purview of the FCPA’s proscription.” (emphasis in original). The court warned, however, that the scope of the statute was not limitless, stating, “We hasten to add, however, that this conduct does not automatically constitute a violation of the FCPA: It still must be shown that the bribery was intended to produce an effect – here, through tax savings – that would ‘assist in obtaining or retaining business.’”

Although some of the bribes in the *Panalpina* cases were made to obtain contracts and other specific business advantages, most of the payments were made to customs or tax officials to reduce duties and taxes, to expedite customs clearances, or to evade import regulations. In the latter cases, the government made very little effort to link such payments to obtaining or retaining business. For example, in *Pride International*, the DOJ alleged a number of what it termed “bribery schemes,” including payments to a Mexican Customs Official “to avoid taxes and penalties for alleged violations of Mexican customs regulations relating to a vessel leased by Pride International.” Similarly, in *GlobalSantaFe*, the SEC alleged that through a number of “suspicious payments” the company “avoided costs and gained revenue.” Without more explanation, such barebones allegations create the impression that the government equates gaining revenue or reducing costs generally with “obtaining or retaining business.” That, however, is the very opposite of the holding in *Kay*:

Although we recognize that lowering tax and customs payments presumptively increases a company's profit margin by reducing its cost of doing business, it does not follow, *ipso facto*, . . . that such a result satisfies the statutory business nexus element. Even a modest imagination can hypothesize myriad ways that an unwarranted reduction in duties and taxes . . . could *assist* in obtaining or retaining business. . . but that is not to say that such a diminution *always* assists in obtaining or retaining business. There are bound to be circumstances in which such a cost reduction does nothing other than increase the profitability of an already-profitable venture or ensure profitability of some start-up venture. Indeed, if the government is correct that anytime operating costs are reduced the beneficiary of such advantage is assisted in getting or keeping business, the

## Recent Trends and Patterns in FCPA Enforcement

---

FCPA's language that expresses the necessary element of assisting in obtaining or retaining business would be unnecessary, and thus surplusage - a conclusion that we are forbidden to reach.

Reading between the lines of the pleadings, we can, in many cases, construct some theory of how certain of the payments might have fallen within the *Kay* rule, *e.g.*, some payments appear to have allowed the importers to bring in equipment and rigs without which they could not perform new or existing contracts. It is even possible that, similar to the facts in *Kay*, the importers could not have competed for existing or new business had they paid the full duties or taxes or complied with other local requirements. The pleadings, however, for the most part only hint at such an underlying rationale, leaving us to wonder exactly what does the government think the business nexus means today?

If properly plead, the FCPA is not that complicated a statute to understand. Four types of payments to officials are explicitly permitted: facilitation payments, *bona fide* promotion payments, other “lawful” payments, and common law extortion payments. Most other payments are prohibited, provided they are “to assist in obtaining or retaining business.” This does, however, conceptually leave a gap: payments that neither fall within the explicitly permitted categories nor satisfy the business nexus. Under common law principles, “everything that is not prohibited is permitted (*nulum crimen sine lege*), and thus it would appear that there are some bribes, apart from facilitation payments, that simply fall outside the scope of the statute.

On one level, this issue may mean little for corporations seeking to comply with the law: a bribe is a bribe is a bribe. When criminal liability is at issue, however, it is important that the borders of the statute be carefully limned. Unfortunately, the government’s pleadings in the *Panalpina* cases do more to blur than clarify the limits of the law. For example, in some cases, the DOJ did not even plead the language of the FCPA but used instead that of the OECD Convention. For example, in *Pride International*, the conspiracy count alleged that the payments in question were “to make corrupt payments to a Mexico government official in order to obtain or retain business *and to obtain other favorable treatment.*” Similarly, in the *Noble* Non-Prosecution Agreement, the DOJ stated that the FCPA was intended to prohibit bribes “for the purpose of obtaining or retaining business *or securing any improper advantage.*” In each case, the italicized language is simply not a part of the statutory element.<sup>4</sup>

---

<sup>4</sup> We do not mean to pick on the DOJ in this respect, as certain of the SEC’s allegations similarly departed from the statute’s language. For example, in *Tidewater*, the SEC alleged that the company “knew, *or was reckless in not knowing*” that payments to an agent would be used to pay bribes. Congress, however, *rejected* a reckless standard when it amended the statute in 1988, instead defining the requisite knowledge with reference to common law principles of “willful blindness” and “conscious disregard.”

## Recent Trends and Patterns in FCPA Enforcement

---

The problems of this approach are clearest in analyzing the various charges involving payments to tax officials. When is a payment to reduce taxes a payment to assist in obtaining or retaining business? In *Tidewater*, the SEC and the DOJ alleged that Tidewater had paid, through an agent, Azeri tax officials to “resolve local Azeri tax audits in a Company subsidiary’s favor” and “to improperly secure favorable tax audits” resulting in a savings of \$820,000; in *Pride International*, the SEC alleged that Pride International had paid a tax consultant designed by a Kazakh tax official to obtain a reduction in taxes and penalties. Although the SEC did at least allege in its complaint against Tidewater that one of the tax audits related to payments of payroll taxes on an ongoing project, in neither case did the government explicitly allege what “business” was obtained or retained, leaving open the possibility that it deems the reduction in taxes itself to be the “business.” In contrast, in *Alliance One*, the DOJ explicitly tied bribes of tax inspectors who had “threatened to shut down” one of the company’s subsidiaries, stating that the purpose of the bribes was “to influence the acts and decisions of the Kyrgyz Tax Inspection Police *and to secure DIK’s continued ability to conduct its business* in Kyrgyzstan.” It is thus not clear whether the government views *all* payments to reduce taxes as being “to assist in obtaining or retaining business,” an interpretation contrary to *Kay*, or whether these particular reductions in taxes have some clear connection, not set out in the pleadings, to obtaining or retaining business under a more common understanding, *e.g.*, a contract, a project, or a sale.

### **Guidance on Compliance Programs**

#### *Compliance Monitoring*

Although the role of independent monitors has been the focus of much debate, there has been much less attention paid to self-monitoring. A company’s ability to demonstrate that it is capable of monitoring itself and has done so is a significant mitigating factor when dealing with the government. As far back as *Monsanto* in 2005, the DOJ included the concept of periodic reviews of the effectiveness of a compliance program as an essential element of the compliance program itself. Similarly, the U.S. Sentencing Guidelines were recently amended to include “monitoring and auditing to detect criminal conduct” and “evaluat[ing] periodically the effectiveness of the organization’s compliance and ethics program” as essential elements of an effective compliance program. Similarly, the OECD’s *Good Practice Guidance on Internal Controls, Ethics, and Compliance*, issued in February 2010, provided that a company should undertake “periodic reviews of the ethics and compliance programmes or measures, designed to evaluate and improve their effectiveness in preventing and detecting foreign bribery, taking into account relevant developments in the field, and evolving international and industry standards.” This concept of monitoring is reflected in the SEC’s complaint against *Alliance One*, in which it notes that “despite . . . extensive international operations” the company had “failed to establish a program to monitor compliance with the FCPA by its employees, agents, and subsidiaries.”

## Recent Trends and Patterns in FCPA Enforcement

---

### *Internal Controls*

The FCPA's internal controls provisions apply only to issuers, but there are obviously other statutes, both in the U.S. and elsewhere, that require accurate records, and even in cases against non-issuers, the enforcement agencies are clearly focused on the adequacy of internal compliance procedures.

What, then, constitutes sufficient internal controls? In the past year, the SEC and the DOJ have continued to provide some guidance, mostly in the form of negative examples, *i.e.*, what not to do. This trend continued in 2010, with the government in particular focusing on due diligence on third parties and the implementation of an effective compliance program.

The *Technip* matter, for example, offers two key pieces of guidance. First, joint venture partners are obligated to ensure that the joint venture has adequate anti-bribery controls. In this respect the SEC particularly noted that the Technip executives assigned to the joint venture were aware of the FCPA's prohibitions but had not implemented controls to ensure compliance with the Act. This critique is particularly interesting given that the FCPA requires non-majority participants in a company only to "proceed in good faith to use its influence, to the extent reasonable under the circumstances," to cause the company to implement adequate controls. In this case, where none of the four partners had majority control, the SEC appears to have held all responsible for the lack of controls.

Second, adequate controls include meaningful due diligence *and* ongoing supervision of agents. In the *Technip* matter, the SEC noted that although Technip required potential agents to complete a basic questionnaire, "[n]o additional due diligence was required, such as an interview of the agent, or a background check, or obtaining information beyond that provided by the answers to the questionnaire" and implicitly agreed with a senior executive of Technip, whom it cited, that Technip's due diligence procedures were "perfunctory" and "conducted so that Technip would have some documentation in its files of purported due diligence." The SEC made the same point in the *ABB* matter, noting that ABB had to approve its subsidiary's execution of certain lucrative contracts, yet it had "failed to conduct any due diligence on the use or payments to [the] agent and other companies" involved in obtaining those contracts. Similarly, in *BAE Systems*, the DOJ noted that the company "maintained inadequate information related to who its advisors were and what work the advisors were doing to advance the [company's] business interests." Further, BAE "did not take adequate steps to ensure that its marketing advisors' and agents' conduct complied with the standards of the FCPA" and "possessed no adequate evidence that its advisors performed legitimate activities to justify the receipt of substantial payments."

The *Snamprogetti* matter provides guidance on the responsibility of a parent for its subsidiary's controls. In this case, although there is a single allegation that ENI, Snamprogetti's indirect parent, approved Snamprogetti's entry into the TSKJ joint venture, there is no allegation that it

## Recent Trends and Patterns in FCPA Enforcement

---

participated in the joint venture itself or otherwise approved particular practices. Nevertheless, the SEC held ENI responsible for having “failed to ensure that Snamprogetti conducted due diligence on agents hired through joint venture in which Snamprogetti participated.”

At the bottom line, a company that seeks to demonstrate that it has adequate internal controls must demonstrate a sensitivity to risks and red flags and an ability to respond appropriately. For example, in *ABB*, the SEC recited a litany of failures to demonstrate that ABB had not devised and maintained effective controls: “the extent and duration of the illicit payments to foreign officials, the large number of ABB subsidiaries involved in these bribery and kickback schemes, ABB’s knowledge from the prior Commission action of illicit payments by other ABB subsidiaries, the improper recording of millions of dollars of illicit payments in ABB’s books and records, ABB’s failure to detect these irregularities, and ABB’s failure to conduct sufficient due diligence on local agents and others” Further, once problems are identified, a company must address it seriously. *Daimler*, for example, adopted an integrity code in 1999. According to the DOJ, however, it “subsequently failed to make sufficient efforts to enforce the code, train employees on compliance . . . , audit the use of [improper accounts], or otherwise attempt to ensure that the company was not continuing to make improper payments . . . .”

The risks of failing to implement and enforce a program were demonstrated in the *Alcatel* matter. On paper, *Alcatel* appeared to have had an adequate program for conducting due diligence on third parties and having that due diligence reviewed by a specially designated compliance employee. Nonetheless, the government’s pleadings outline numerous compliance failures indicating that the company failed to ensure that the program was effective as implemented. Indeed, the government viewed Alcatel’s failure to implement and to enforce its program as so serious that Alcatel became only the second company (after *Siemens*) to be charged with *criminal* violation of the FCPA’s internal controls provisions.

### *Compliance Responsibilities*

In December 2009, in *AGCO*, the SEC harshly criticized the company’s finance department for being “‘blind loaders’ who input information . . . without any adequate oversight role.” The government continued to expand on this theme in 2010. For example, in *ABB*, the SEC critiqued ABB’s controls, noting that “despite the amount and volume of the payments, and the fact that certain of the payments were made not to the companies submitting invoices but to the personal bank accounts of individuals, ABB failed to conduct any review of these payments.” Similarly, in *Universal Corporation*, the DOJ noted that the company’s finance personnel, both at the parent and subsidiary level, had approved commission payments to an agent “even though (a) some of the payments were described as ‘special expense’ payments; (b) there was no contractual basis for the payment of the additional commission amounts; (c) the payments were to an account unassociated with the Agent; (d) the instructions that were provided when wiring the money indicated that Universal should not identify the agent or that the amounts were for

## Recent Trends and Patterns in FCPA Enforcement

---

‘special expenses;’ and (e) the payments were above the standard five (5) percent commission typically paid by Universal Brazil to its agents.”

In *Daimler*, both the DOJ and the SEC expressed concern over structural issues that could limit the effectiveness of the finance department’s compliance function. The DOJ noted, for example, that the business unit financial controllers had only “dotted central reporting lines” but otherwise reported directly to the local sales organization. It further noted that the internal audit department was “understaffed and decentralized,” its personnel were “located . . . across the world,” and auditors reported to local management “who were focused on sales performance, were able to heavily influence the types of issues examined by internal audit employees, as well as the remedial steps, if any, recommended by them.” Similarly, the SEC noted that “accounting and legal personnel often reported to top sales management, rather than independent, centralized departments with compliance functions.”

Companies’ legal advisors have similarly come under criticism when they fail to embrace a compliance role. In *Universal Corporation*, the DOJ noted that a subsidiary’s financial records “were maintained with insufficient oversight or review by Universal’s legal, finance, or compliance departments.” Similarly, in *Daimler*, the SEC alleged that “the Company’s internal audit, legal, and finance and accounting departments, which should have provided checks on the activities of the sales force, instead played important roles in the subversion of internal controls and obfuscation of corporate records.”

### *Gifts and Entertainment*

Vast amounts of corporate resources are devoted to evaluating and monitoring gifts and entertainment of officials. Although, at some level, a rule of reasonableness ought to apply, the risks of crossing the line were evident in several of last year’s matters. For example, among the charges against *ABB* was that it had paid for a Mediterranean cruise vacation for Mexican officials and their wives. In *Alliance One*, the SEC charged that the company had provided “watches, cameras, laptop computers, and other gifts to Chinese and Thailand tobacco officials; dinner and sightseeing expenses during non-business related travel to Alaska, Los Angeles, and Las Vegas for Chinese and Thailand government delegations.” Similarly, the DOJ alleged that *BAE* had provided Saudi officials with travel and accommodations, security services, real estate, automobiles, and personal items.

## **International and U.S. Legislation and Regulations**

### *U.K. Bribery Act*

On the international front, the U.K.’s Bribery Act has garnered the most attention. After many years of false starts, the British Parliament finally enacted, in the waning days of the Labour government, a modern anti-bribery statute, with expansive jurisdiction and broad scope. Unlike

## Recent Trends and Patterns in FCPA Enforcement

---

the FCPA, the statute covers commercial bribery and does not have an exception for facilitation payments nor, for that matter, for *bona fide* promotional expenses.

Most of the attention has been on the U.K. Act unique offense, applicable only to companies and partnerships, of “failing to prevent bribery.” This provision has two aspects of interest. First, its extraterritorial reach is potentially quite broad, reaching companies and partnerships established outside the U.K. but which “carry on” a business (or part of a business) in the U.K. In theory, this could create liability for a foreign parent whose Chinese subsidiary pays a bribe in China merely because the parent also has a subsidiary in the U.K.

Second, the new offense contains a unique affirmative defense that will allow a company to avoid liability if it demonstrates that it had in place “adequate procedures” designed to prevent such bribery. What constitutes adequate procedures is still a matter of debate within the U.K., and, as a consequence, the U.K. government delayed the implementation of the Bribery Act to allow it to consult over the guidance it is required to give on such procedures. The guidance is currently available in draft only, and it is, at this point, fairly general and largely tracks the OECD *Good Practices* and the U.S. Sentencing Guidelines.

It is important to note, however, that this new offense is not the exclusive means of prosecuting corporations for corruption. The corporate offense is largely intended to fill the gap between the U.K. standard of corporate criminal liability, which typically requires the involvement of a managing director or board member, and less demanding standards, such as those in the U.S., that hold corporations strictly liable for the acts of their employees and agents. Thus, where the requisite standard is met, the U.K. authorities may still prosecute a corporation for other bribery offenses for which there is no similar affirmative defense.

### *U.S. Legislation and Regulations*

In the United States, there have been a number of discussions concerning the scope and effectiveness of the FCPA and various proposals to strengthen, weaken, or otherwise improve the statute. Late in the year, for the first time in years, a Congressional committee, the Senate Judiciary Subcommittee on Crime and Drugs, held a hearing examining FCPA enforcement. Comments from Senator Arlen Specter (D-PA) criticized DOJ enforcement for failing to result in prison sentences for business executives responsible for company violations; Sen. Amy Klobuchar (D-MN) called on the DOJ to offer more guidance to American businesses on complying with the FCPA. With this Congress reaching the end of its term, there will not be any new legislation in the near term.

In the regulatory arena, the SEC has issued draft regulations and requests for comment to implement the Dodd-Frank whistleblower provisions. These provisions provide a bounty and protection from retaliation for individuals who report wrongdoing by an issuer to the SEC that

## Recent Trends and Patterns in FCPA Enforcement

---

results in aggregate sanctions of over \$1,000,000. The draft regulations seek to walk the fine line of encouraging reporting while, at the time, supporting internal compliance mechanisms. Thus, for example, the SEC has proposed to give the whistleblower credit for reporting his concerns to an issuer's internal compliance function, thus allowing the issuer to conduct an internal investigation, evaluate its merit, and determine whether a voluntary disclosure is merited. The regulations also provide more details about which categories of persons – auditors, internal compliance personnel, culpable individuals – cannot qualify as whistleblowers and under what circumstances. Finally, the drafts provide more details about how the amount of the bounty will be determined and how it will be allocated when there is more than one qualified whistleblower.

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

For more information on the topics covered in this issue, please contact:

**Philip Urofsky**  
Washington, DC  
London  
+1.202.508.8060  
purofsky@shearman.com

**Danforth Newcomb**  
New York  
+1.212.848.4184  
dnewcomb@shearman.com

**Stephen Fishbein**  
New York  
+1.212.848.4424  
sfishbein@shearman.com

**Paula Howell Anderson**  
New York  
+1.212.848.7727  
panderson@shearman.com

**Patrick D. Robbins**  
San Francisco  
+1.415.616.1210  
probbins@shearman.com

**Richard Kelly**  
London  
+44.20.7655.5788  
richard.kelly@shearman.com

**Jo Rickard**  
London  
+44.20.7655.5781  
jrickard@shearman.com

**Richard Kreindler**  
Frankfurt  
+49.69.9711.1420  
rkreindler@shearman.com

**Markus S. Rieder**  
Munich  
+49.89.23888.2119  
markus.rieder@shearman.com

Jill Aberbach, Amanda Kosonen, and Ashley Walker, members of the FCPA team in Washington, DC and New York provided substantial assistance in preparing this memorandum.