The U.S. Government Expects You to Be "Your Brother's Keeper" - And If You Fail, It Can Fine You and Send You to Jail for *Something Someone Else Did!*

Part 2 in a Series

John W. Brooks
Senior International Counsel
619.699.2410
jwbrooks@luce.com
www.luce.com/johnwbrooks

More Information.

For more information about the FCPA and how to create an effective FCPA Compliance Program for your company, please phone your principal Luce Forward lawyer or contact the author of this article at jwbrooks@luce.com. Last month's article on FCPA basics, follows this e-Update.

SUMMARY

As reported in Part 1 of this series last month, the Securities and Exchange Commission (SEC) and the Department of Justice (DoJ) are stepping up government enforcement of the law known as the "Foreign Corrupt Practices Act." One of the government's most fertile fields for finding FCPA violations is in the far away overseas parts of your business - and it involves what your partners, agents and consultants are doing in those places. You may be tempted to respond "I can't control their every action." And that may be true. But your government says it doesn't care, and you may still be in trouble.

Strict or Vicarious? What's the Difference?

If one of your **company's employees** commits an FCPA violation, your company is strictly liable - that means it has no defenses - under an ancient legal theory called *respondeat superior*. But if one of your company's **business partners, agents, or consultants** steps over the FCPA line (intentionally or unintentionally), a different theory of liability comes into play called ***vicarious liability***, but the result can be the same. Why? Because it's the government's position that your responsibilities extend beyond your own company and its employees to include the conduct of certain third parties, such as your joint venture partners, sales agents, subcontractors, distributors - and that often ambiguous and hard to classify figure, the **overseas consultant**. The government says you can't ignore signs these ***"business partners"*** of yours may be violating the FCPA, because, it argues, you're the one that put them in a position that was conducive to FCPA violations in the first place.

A Longish - But Perhaps Useful - Example to Illustrate a Basic Point

Let's say you're a C-Level officer of a large U.S. medical products company, and you're in ***acquisition mode***. Your acquisition target is a UK medical devices company ("StentsRUs") with a hot new model that would fit perfectly into your product line. Some time ago Stents had hired an Indian consultant named Gupta who advised contracting with a well-known Indian distribution company ("HinduMed") to handle Stent's sales in the Indian market. HinduMed's management was Western-trained (mostly 'MIT PhDs') and very entrepreneurial. Stents has a business plan for India that gives first year discounts to HinduMed in order to stimulate first year purchases. One might think, "Basic Marketing 101," right?

But what you don't know is that HinduMed had conceived a plan to convert this ***manufacturer's discount*** program into an ***agent's commission*** program for local public and private hospital managers, offering to pay those managers the discount money as a commission for recommending the purchase of Stent's hot new product. The commission program - no surprise - is a roaring success, and HinduMed's sales were going through the roof when one of its employees, mad about something, tips the payments to the British Serious Fraud Office (a UK analog to the US DoJ). While the SFO investigation is going on, an Indian Customs Officer requests a small payment from consultant Gupta to speed up the clearance of Stents' medical devices through Indian Customs. Gupta makes the payment, but is annoyed and emails Stents' VP Sales requesting reimbursement. The VP Sales at that very moment happens to be having dinner in Shanghai with a PRC government hospital administrator when he receives the email on his Blackberry. VP Sales reads the Blackberry message while continuing with dinner and ordering two more glasses of Louis Treize cognac for his Chinese guest.

Those are the **background** facts. Fast forward **to the present**. Your company starts its *pre-acquisition due diligence* and, in the process, your staff discovers HinduMed's clever program to "convert a manufacturer's discount into an agent's commission." You - and your C-level acquisition counterpart from Stents - meet to discuss "this Indian mess" and to ponder: ***Whose problem is it?*** At the risk of telling you more than you really want to know, it's **everyone's** problem *if the acquisition goes through* - **except** perhaps the disgruntled employee who may in fact end up with a "whistleblower's reward." What you *care about most*, I'll bet, is whether **your company** is in trouble, and - come to mention it - whether **you're in trouble yourself**. And the answer is, if the acquisition goes through, **"Yes."**

Why Am I (and My Company, Of Course) in Trouble?

It's a "sins of the father" sort of thing. **Your company would be in trouble** because Stents, your acquisition target, would also be in trouble under *other laws* - the OECD Convention for Combating Bribery, for instance and the upcoming (next April) UK Bribery Act - and if your Company acquires Stents, *Stents'* troubles will become your troubles, because in most situations liabilities of the target **pass involuntarily** to the acquiror at closing.

As for yourself, **you'd be in trouble** because you knew (or during the course of the due diligence **would have had reason to know**) that violations of the FCPA by someone else you didn't even know had taken place thousands of miles away from your home office in the US. Whew! That's a pretty long story to illustrate ***vicarious liability***. But if you're really interested, you can click on the button just below to find seven recent real-life FCPA enforcement actions penalizing companies - and their executives - for acts done by or through agents and others. You will also see that the penalties are staggering and occasionally involve jail terms.

Fines and Jail Terms

Royal Dutch Shell (November 2010).

One of its subsidiaries hired a **customs broker** to make payments to Nigerian customs officials to obtain preferential treatment. Shell and the subsidiary have agreed to pay about $18 million in profits disgorgement and prejudgment interest to settle SEC charges.

Transocean, Inc. (November 2010).

Transocean made payments to an international **freight forwarder** and a **door-to-door courier service** to expedite the import of goods and equipment into Nigeria. Transocean has agreed to pay penalties of over $7 million to settle SEC charges. In related criminal proceedings, Transocean and an affiliate agreed to pay $13.4 million to settle DoJ charges.

Pride International, Inc. (November 2010).

Overseas subsidiaries of Pride made payments in multiple countries for illicit purposes, which payments (believe it or not) were not correctly recorded in the subsidiaries books and records, and consequently were incorrectly recorded on the books and records of the corporate parent. Pride has agreed to pay over $23 million in profits disgorgement and pre-judgment interest to settle SEC charges, together with related criminal penalties of over $32 million to settle DoJ charges.

Noble Corporation (November 2010).

Noble, headquartered in Switzerland but with an office in the U.S., authorized payments by its Nigerian subsidiary to the **subsidiary's customs agent** for forwarding to the Nigerian government in exchange for import permits. Noble has agreed to pay about $5.5 million in profits disgorgement and prejudgment interest, the amount of the penalties being reduced as a result of Noble's "self-reporting" and cooperation during the investigation. (More on the **pros and cons** of "self-reporting" next month.)

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Richard Bistrong (September 2010).

Bistrong, a former VP International Sales of Armor Holdings, a military equipment manufacturer, pleaded guilty to making $4.4 million in illicit payments to foreign government customers through **overseas agents** and **other intermediaries** and faces **five years** in prison and a $250,000 fine.

Juan Diaz (July 2010).

Diaz, a Florida business man, pleaded guilty to making about $1 million in bribes to Telecommunications D'Haiti, a government-owned telecoms company, on behalf of three U.S.-based telecoms companies. Diaz reportedly laundered the money **through another company**. He now faces **57 months in prison**, the forfeiture of over $1 million, restitution payments of $73,000 and **three years of supervised release after prison**.

John Warwick (June 2010).

Warwick, the President of Overman Assosciates, a U.S. engineering firm, as well as the former President of its **Panamanian affiliate** Ports Engineering Consultants Corporation (PECC), pleaded guilty to making about $200 million in illicit payments to former Panamanian government officials to secure no bid business concessions for PECC. Warwick now faces **37 months in prison**, the forfeiture of $331,000 and **two years of supervised release after prison**.

What Could I Have Done to Stay Out of Trouble?

Preventive measures, of course, are *fact-specific* and *"one size does **not** fit all,"* but here are some **due diligence** ideas you should consider instead of blindly exposing yourself and your company to vicarious liability for the actions of someone else.

- Inform yourself about your prospective business partner, sales agent, distributor, or consultant. Find out who its officers, directors and shareholders are and determine whether any of them (or their family members) are foreign government (or under the upcoming UK Bribery Act, foreign public) officials. Obtain and review its financial statements.
- Assess your prospective partner's credentials; determine whether it has and strictly enforces anti-corruption ethics and compliance policies.
- Conduct background checks through public or proprietary sources.
- Contact the U.S. Embassy or Consular Office in the countries or territories where your business partner will be representing you for "on the ground" information about its anti-corruption reputation.
- Interview your proposed business partner and ask about corruption issues in the countries or territories in which it will be representing you, how it has dealt with those issues in the past, and how it will deal with them as your business partner.
- Enter into a Foreign Business Partner Agreement detailing not only your prospective partner's ethical duties but also its compliance reporting obligations to you.

Coming Next.

Part 3 of this Series (next month) will focus what to do if you discover someone in your company may have committed an FCPA violation, whether that discovery is made by **your own people**, the U.S. or a **foreign government**, or a **whistleblower**.

The U.S. Government Wants to Put You in Jail for Breaking This Law . . . and Your Chances of Going Are Increasing!

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SUMMARY

The Securities and Exchange Commission (SEC) and the Department of Justice (DoJ) are stepping up enforcement of the law known as the "Foreign Corrupt Practices Act." This comes in the face of continuing complaints by U.S. business leaders that the FCPA unfairly ties the hands of U.S. companies and their overseas affiliates by denying them the ability to compete on a level playing field with their direct competitors in other countries. But neither the SEC nor the DoJ is losing any sleep over these complaints. In fact, they're getting tougher.

Put 'Em in the Slammer. Less than a year ago the Attorney General in charge of FCPA enforcement at the DoJ said in a major policy speech that ***"Put simply, the prospect of significant prison sentences for individuals should make clear to every corporate executive, every board member, and every sales agent that we will seek to hold you personally accountable for FCPA violations."*** If his intention was to catch the attention of the U.S. business community, he clearly succeeded. Since then, the internet has buzzed with advice on what U.S. business leaders should do - not only how to comply with the law, but how to react if and when they're caught not complying with it.

Who's at Risk?

The FCPA covers ***all*** U.S. companies (big or little, public or private), together with all their employees and agents, all their overseas affiliates and partners, and ***all*** U.S. individuals wherever located.

What's the Law?

The FCPA prohibits bribery of foreign officials. There are ***five*** elements to an FCPA Violation: **1)** a payment or promise of ***anything of value***; **2)** to a foreign official, political party official, candidate for office or official of public international organization (Foreign Official); **3)** by you or your company, or its employees/agents in the U.S., or its employee/agents ***outside*** the U.S., or by a foreign person ***inside*** the U.S. assisting in the payment or promise; **4)** for the corrupt purpose of influencing an official act or decision of the Foreign Official; **5)** to assist you or your company ***obtain or retain business***, to ***direct business*** to any person, or to secure ***an improper advantage***.

Is That All?

No. You can be liable for a ***promise of payment***, even if payment is never made. ***Foreign officials*** include almost everybody even remotely connected to government, including officials of public international organizations, political parties and candidates for foreign political office - and perhaps even to their family members. ***Anything of value*** includes not only cash, but information, testimony of a witness, loans, promises of future employment, scholarships, sports equipment, trips, and the like. ***Corrupt intent*** means intending to induce the recipient to misuse his position or to influence someone else to do so. The business to be obtained/retained does not have to be with the foreign government, so long as the payment/promise is for the purpose of securing ***an improper advantage*** in obtaining/retaining any business with anybody. And finally, you don't have to know a payment by an overseas employee/agent will be passed on to a foreign official so long as you're aware there's a ***substantial possibility it might be***.

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Who Enforces This Law?

The SEC enforces FCPA bribery and FCPA accounting violations by public companies, and the DoJ has exclusive jurisdiction over criminal violations. The SEC and DoJ share jurisdiction over civil violations.

What Are the Penalties?

The FCPA imposes both ***civil and criminal penalties***. Civil penalties for anti-bribery violations include fines up to $10,000 for companies or individuals ***per violation***. Civil penalties for accounting violations range up to $500,000 for companies and $100,000 for individuals ***per violation***.

Criminal penalties for anti-bribery violations include fines of up to $2 million for companies and $250,000 for individuals, again ***per violation***, and jail terms for individuals of up to five years. Criminal penalties for accounting violations range up to $25 million for companies and $5 million for individuals.

Note that these penalties are ***per violation***, and the FCPA cases brought by the government typically include ***multiple counts*** of alleged violations. In 2009, the average FCPA violation fine was $7 million and the highest was $579 million. Twenty individuals were indicted, and, as you might have guessed by now, an individual's fines are ***not indemnifiable*** by his or her employer or principal.

Recent Penalties Assessed

Just six years ago (2004), the DoJ brought only ***three*** FCPA criminal cases. In 2009, this number had climbed to **34**. This year the DoJ has over **120** open FCPA investigations. So far in 2010, the SEC and DoJ have announced civil and criminal fines against nine companies and 31 employees and agents amounting to **over $1.1 billion**, and the DoJ has obtained jail terms amounting to a **collective 16 years** for these employees and agents as guests in our federal prison system. Additionally, in the single largest FCPA prosecution ever against individuals, there are proceedings in progress involving over 20 company employees and agents with possible criminal fines in excess of $5 million and a collective 110 years in jail terms for the individuals involved.

A Glimmer of Leniency From the DoJ?

Effective just yesterday (November 1), the Sentencing Guidelines of the DoJ were amended to give compliance credit (lowering the penalty level) to companies like yours if 1) you have an ethics and compliance program (Program) in place with the persons responsible for the operation of the Program reporting directly to your Board or one of its committees, 2) your Program manages to detect an FCPA violation before it's discovered (or reasonably could have been discovered) by persons "outside" your company, 3) you promptly report the violation to the appropriate governmental authorities, and 4) no one responsible for the Program either participated in the reported violation, condoned it, or willfully ignored it.

Given the draconian consequences (only some of which are described above) of getting caught violating the FCPA, setting up a Program would seem to be a "no brainer."

Coming Next.

Part 2 of this Series (next month) will focus on the **types of FCPA risks** facing **you** and **your company** as a result of actions of **your overseas partners, agents and consultants** that you may know little or nothing about until you hear from your government - which, believe it or not - may want to put **you** in jail for **someone else's** actions.