Client Alert.

June 28, 2011

Deferred Prosecution Agreements Truly a "Game Changer" at the SEC for FCPA Violations?

By Paul T. Friedman and Crystal S. McKellar

The SEC's message is consistent and clear: companies that self-report Foreign Corrupt Practices Act ("FCPA") violations will have better outcomes than companies that do not voluntarily come forward. Critics counter by questioning the benefits of voluntary disclosure, pointing to SEC settlements in which companies that self-reported faced similar (or arguably worse) outcomes as companies that did not.[1] And self-reporting does not appear to protect companies from paying hefty monetary fines. After Rockwell Automation, Inc. recently self-reported FCPA violations at a Chinese subsidiary, the SEC nonetheless penalized the company with civil fines, disgorgement, and interest.[2]

Answering its critics, the SEC announced on May 17, 2011 that it had entered into its first-ever deferred prosecution agreement ("DPA") with Tenaris S.A. ("Tenaris"). The SEC was first authorized to use DPAs in early 2010 as part of a new SEC cooperation initiative that seeks to encourage self-reporting by companies through the lure of "cooperation tools." The cooperation tools include DPAs, non-prosecution agreements, and cooperation agreements. SEC Enforcement Director Robert Khuzami called the initiative a "potential game-changer."[3]

Tenaris was identified as a DPA candidate after it self-reported FCPA violations by employees in Kazakhstan and Azerbaijan. The SEC characterized the DPA as a "reward" for the company's voluntary self-reporting and cooperation.[4] But how much of a reward was it?

TENARIS DETECTS VIOLATIONS AND SELF-REPORTS

Tenaris is a global manufacturer of steel pipe products used in the oil and gas industries. According to the DPA, Tenaris employees bribed officials at a state-owned oil and gas company in Uzbekistan in order to gain access to its competitors' bid information during a competitive bidding process. As a result of the bribes, Tenaris won pipeline contracts worth approximately $4.8 million.[5] The bribery allegedly occurred in 2006 and 2007, and was not detected by Tenaris' internal anti-bribery controls.[6]

---

[1] *See, e.g.*, Bruce Hinchey, *Punishing the Penitent: Disproportionate Fines in Recent FCPA Enforcements and Suggested Improvements*, August 2010, http://works.bepress.com/bruce_hinchey/1.

[2] Order Instituting Cease and Desist Proceedings, *In the Matter of Rockwell Automation, Inc.*, (May 3, 2011), http://www.sec.gov/litigation/admin/2011/34-64380.pdf; *see* Brian Zabcik, *Reasonable Minds Can Disagree: SEC, Justice Part Ways on Rockwell Payments*, May 5, 2011, http://www.law.com/jsp/cc/PubArticleCC.jsp?id=1202493043778.

[3] SEC Release No. 2010-6 (Jan. 13, 2010), http://www.sec.gov/news/press/2010/2010-6.htm.

[4] SEC Release No. 2011-112 (May 17, 2011), http://www.sec.gov/news/press/2011/2011-112.htm.

[5] Tenaris Deferred Prosecution Agreement at ¶ 6(v).

[6] *Id.* at ¶6(f)-(y).

Tenaris first learned of possible wrongdoing at the company in early 2009. The company promptly retained an outside law firm to conduct a "world-wide investigation of its business operations and controls," reported the allegations of wrongdoing to the SEC and Department of Justice ("DOJ") at the outset of its investigation, and provided "extensive, thorough real-time cooperation" to the government.[7] According to the SEC, it was Tenaris' "immediate self-reporting" and "exemplary commitment to compliance, cooperation, and remediation" that made Tenaris a DPA candidate.[8]

DPA BENEFITS ILLUSORY?

But what benefits does the DPA truly provide? It brings no apparent financial advantage. Tenaris was required to pay full disgorgement plus pre-judgment interest, a total of $5.4 million, and also agreed not to seek reimbursement of taxes it had *already* paid on the disgorged amounts.[9] Though the SEC did not assess a civil fine on top of these amounts, this is not unusual. The SEC often forgoes civil fines in FCPA settlements, and those it does assess are often minimal.[10] For example, the SEC demanded disgorgement and interest only in the resolution of its 2010 FCPA enforcement action against RAE Systems, Inc.[11] The SEC settled its FCPA charges against Alcatel-Lucent—a company whose cooperation DOJ deemed to have been "limited and inadequate"—with a disgorgement-only fine.[12]

Most of the remaining provisions—enhanced compliance and reporting measures, an agreement to cooperate with the ongoing investigation, and a provision permitting the company not to admit or deny the relevant facts—are typical in traditional SEC enforcement resolutions. Tenaris' agreement to toll the statute of limitations, prolonging its exposure to civil enforcement, is not.

CONCLUSION

DPAs have been used with great success by DOJ. In such cases, the advantages are clear: the avoidance of criminal convictions, imprisonment for individuals, and potentially devastating collateral consequences for companies. Based upon Tenaris' example, it is less clear how companies will benefit from entering into DPAs with the SEC, much less that DPAs will be the "game changer" promised by the SEC last year.

---

[7] *Id.* at ¶ 6(aa)-(bb).

[8] SEC Release No. 2011-112 (May 17, 2011), http://www.sec.gov/news/press/2011/2011-112.htm.

[9] These financial penalties are in addition to a $3.5 million criminal penalty Tenaris paid the DOJ.

[10] Civil penalties made up just 4% of payments made to the SEC in connection with FCPA enforcement actions in 2010; remaining 96% consisted of disgorgement and interest payments. *See SEC Enforcement of the FCPA—2010 Year in Review*, FCPA Professor; available at http://fcpaprofessor.blogspot.com/2011/01/sec-enforcement-of-fcpa-2010-year-in.html.

[11] SEC Litigation Release No. 21770 (Dec. 10, 2010), http://www.sec.gov/litigation/litreleases/2010/lr21770.htm.

[12] SEC Litigation Release No. 21795 (Dec. 27, 2010), http://www.sec.gov/litigation/litreleases/2010/lr21795.htm. For a more detailed description of Alcatel-Lucent's FCPA settlement with the SEC and DOJ, please see our Client Alert from January 3, 2011, available at http://www.mofo.com/files/Uploads/Images/110103-Alcatel-Lucent-Settles-FCPA.pdf.

Contact

Morrison & Foerster's FCPA and Anti-Corruption Task Force:

Paul T. Friedman
San Francisco
(415) 268-7444
pfriedman@mofo.com

Carl H. Loewenson, Jr.
New York
(212) 468-8128
cloewenson@mofo.com

Randall J. Fons
Denver
(303) 592-2257
rfons@mofo.com

Robert A. Salerno
Washington, D.C.
(202) 887-6930
rsalerno@mofo.com

Daniel P. Levison
Tokyo
+ 81 3 3214 6717
dlevison@mofo.com

Sherry Yin
Beijing
+ 86 10 5909 3566
syin@mofo.com

Kevin Roberts
London
+ 020 7920 4160
kroberts@mofo.com

Ruti Smithline
New York
(212) 336-4086
rsmithline@mofo.com

About Morrison & Foerster:

We are Morrison & Foerster—a global firm of exceptional credentials in many areas. Our clients include some of the largest financial institutions, investment banks, Fortune 100, technology and life science companies. We've been included on *The American Lawyer*'s A-List for seven straight years, and *Fortune* named us one of the "100 Best Companies to Work For." Our lawyers are committed to achieving innovative and business-minded results for our clients, while preserving the differences that make us stronger. This is MoFo. Visit us at www.mofo.com.

Because of the generality of this update, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations.