

SO YOU WANT TO BUY A BUSINESS: THE ROLE OF THE FCPA IN INTERNATIONAL ACQUISITIONS

The recession has lessened and all that cash your Company has been hoarding for the rainy days of the Obama years is burning a hole in your CEO's pocket. He has his powder dry and is ready to make a big bang by going on a buying spree, targeting overseas entities, to beat the competition in coming out of your industry's downturn. The Legal Department is told to put together an acquisition squad and to be ready to go at a moment's notice. The job assigned to you is to make sure that your acquisition does not run afoul of the Foreign Corrupt Practices Act (FCPA) and to prepare a list of FCPA based due diligence that the Law Department should focus on to perform on the Target Company. What should be on your list? In the recent article, "*FCPA Due Diligence in Acquisitions*," Securities and Commodities Regulation, Vol. 43, No. 2, January 20, 2010, lawyers from Squire Sanders, thoroughly explored this topic, through a hypothetical case it was based upon a "real life scenario". Some of their suggestions included the following suggestions.

I. Who is the Owner of the Target Company?

An initial inquiry should be made into the ownership structure of the target company. If any portion of the entity is owned or held by a government or governmental entity then such an entity is covered under the FCPA as a "foreign governmental instrumentality". There are several factors to consider in making such a determination. Some of these factors include: percentage ownership of the target company; control exercised over the target company; and how are the employees of the target company described by their country's government.

II. Are Agents involved in the Transaction?

Many times a "consultant" will be used in facilitating the purchase of a target company in a country outside the United States. If there is a clear and articulated business case for the Agent to be involved in the transaction, there should be due diligence on the Agent. It should include some a review of the Agent's credentials, ownership structure and financial records going back 3 to 5 years. Lastly, it is also critical to know the reputation of the Agent in the country's business community. If the Agent passes all these reviews, you establish a business relationship with a strong written contract.

III. Does the Target Company want you to pay for Travel?

What if the Target Company desires your business to pay for a representative to come to the US to visit your facilities? Such a trip falls under the FCPA and its proscription of "offering or promising anything of value". However, if there are legitimate business expenses which can be paid by the US purchasing company under the FCPA. The key is to evaluate each travel and entertainment request. Generally, coach class travel and hotel expenses such as room charges, business center and telephone charges related to business

can be reimbursed. Personal room expenses such as minibar, Pay-for-Movies and spa fees at the hotel should not be reimbursed. Receipts should be provided for any charges and if possible, the third party service provider should be paid directly rather than reimbursement of the Target Company's representative. Entertainment and business dinners can be reimbursed if there is a legitimate business purpose but personal, including the family expenses of the Target Company's Representative, cannot be reimbursed under the FCPA. Lastly, do not give a "per-diem" in cash.

IV. Did the Target Company make any "Red Flag" Payments

In your company's financial due diligence of the Target Company, did any evidence of "Red Flag" payments turn up which warrant further investigation? If such "Red Flags" arise, the US purchasing company must not turn a blind eye. If there is reason to believe that payments of the Target Company may violation the FCPA, further investigation is mandated. The recent conviction of Frederick Bourke for engaging in "conscious indifference" in that he knew, *or should have known*, that bribery and corruption was involved in the proposed acquisition, demonstrates the power of the FCPA in the acquisition arena. Red Flag areas would include the discovery of payments for gifts, entertainment, use of agents, facilitation payments or other payments which could not be adequately accounted for are discovered.

V. Are the Books and Records Reasonable?

In addition to its anti-bribery provisions, the FCPA also requires that a company keep such books and records which reasonably reflect the transactions of the entity and that there are proper internal controls. A key in this area is if the Target Company has any payments which are labeled as "miscellaneous" or there are payments which cannot be reasonably described. Gifts, entertainment and business expenses need to be recorded and documented. Internal controls are required to show that the Target Company has its statements in accordance with some form of accepted accounting principles.

VI. What Happens Afterwards?

Your Company has completed all the above steps but your due diligence has turned up items which cannot be resolved before your Company's President wants to fire that dry powder. What can you do? In Opinion Procedure Release 08-02, the Department of Justice gave its opinion on the steps required by a US company contemplating a such a transaction. This opinion held that if Halliburton, in purchasing a Target Company, satisfactorily completed a rigorous, DOJ-mandated 180-day FCPA and anticorruption due diligence work plan after the closing, then the DOJ did not "presently intend" to take enforcement action against Halliburton for any disclosed unlawful pre-acquisition conduct by the Target Company within 180 days of the closing. Halliburton was not the successful bidder for the Target Company but the DOJ's flexibility and Halliburton's open dialogue with the DOJ indicates there will be increased involvement between companies and regulators during FCPA acquisition due diligence.

VII. The End

The potential liabilities for failing to engage in pre-acquisition FCPA due diligence can be severe. Just how severe can be demonstrated by the eLandia acquisition of Latin Node. The FCPA Blog reported that “eLandia also disclosed that its purchase price for Latin Node “was approximately \$20.6 million”. After the acquisition, eLandia discovered that Latin Node had engaged in bribery and corruption. eLandia investigated, albeit after the purchase, and self-reported the violations to the DOJ. eLandia was assessed a \$2 million fine, shut down Latin Node as an operating business and wrote off the entire purchase. For those of you keeping score at home, that is several years of pre-acquisition due diligence, plus legal fees for the FCPA investigation added to the fine, purchase price, business shut down and full financial write-off.

So what’s the moral of this story? You can keep your powder dry but you must engage in full FCPA due diligence in any overseas transaction before moving forward.

This publication contains general information only and is based on the experiences and research of the author. The author is not, by means of this publication, rendering business, legal advice, or other professional advice or services. This publication is not a substitute for such legal advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified legal advisor. The author, his affiliates, and related entities shall not be responsible for any loss sustained by any person or entity that relies on this publication.

© Thomas R. Fox, 2010