

# Foreign Corrupt Practice Act

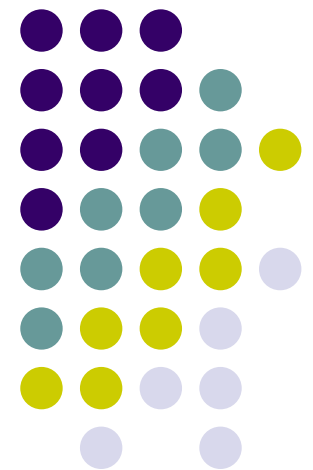
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## Presenters:

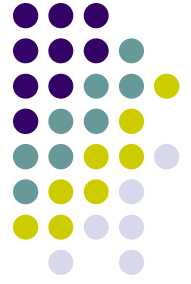
Nina Gross – Deloitte Financial Advisory Services

Jim Lord – Assistant United States Attorney,  
Seattle, Washington

Sheryl Vacca, Moderator – Deloitte & Touche



# Introductions



## Nina Gross

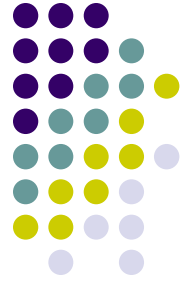
- is the SE leader of the Deloitte FAS Foreign Corrupt Practices Act Forensic & Dispute Services practice. Her experience includes numerous corporate internal and external fraud investigations across a range of industries, including, energy, mining, technology, healthcare, manufacturing, consumer products, and publishing. Ms. Gross has investigated violations of the FCPA, financial statement fraud, and kickback schemes. She has advised Audit Committees, senior corporate officials, investors and international donor development banks regarding corruption prevention and detection, investigative strategies and loss recovery efforts. Ms. Gross served under US Securities & Exchange Commission Chairmen David Ruder and Richard Breeden, as the Director of the Office of Legislative Affairs, from 1987 through 1990



# Introductions

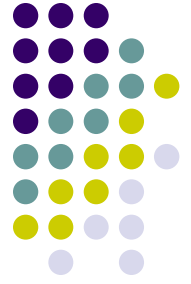
## Jim Lord

- has served as an Assistant United States Attorney (AUSA) since 1988 both in Miami and Seattle. During his tenure as an AUSA, Mr. Lord initially specialized in Organized Crime prosecutions involving La Cosa Nostra and Asian and Russian Organized Crime groups, and has served as the coordinator of the Organized Crime Strike Force in Seattle. He now is the coordinator of the Corporate Fraud Task Force for the Western District of Washington, a Cybercrimes and Computer Hacking (CHIP) attorney, and a member of the Procurement Fraud Task Force. His present area of expertise involves the prosecution of white collar criminal cases, including securities fraud, cybercrimes, intellectual property, and health care fraud cases. Mr. Lord's cases have involved extensive coordination with foreign law enforcement and governmental officials in numerous countries, including Bulgaria, Cambodia, China, Hong Kong, Greece, Malaysia, Russia, and Vietnam.



# Today's Agenda

1. Risks of International Business
2. Introduction to the Foreign Corrupt Practices Act
3. Anti-Bribery Provisions of the FCPA
4. Accounting/Books and Records Provisions
5. Other Legislation
6. DOJ Opinion
7. Enforcement Actions
8. FCPA "Red Flags"
9. Cooperation Considerations
10. McNulty Memorandum
11. Questions



# Risks of International Business

## Risks Associated with International Business

- Financial Loss
- Potential Impact to Merger and Acquisition transactions
- Potential Impact to Shareholder Value
- Potential Impact to Brand Image
- Potential Negative Publicity
- Potential Loss of Key Relationships
- Violation of Local Country Laws, FCPA Act and Sarbanes-Oxley Act
- Civil and Potentially Criminal Prosecution



# Risks of International Business (cont.)

## Reasons Fraud/Bribes Occur in Less Developed Countries

- Countries vulnerable to corruption (Transparency International Index)
- Some countries more tolerant of their companies engaging in corruption
- Possibility of more “willing participants” – bribes often supplement wages
- Economic pressure
- Greater distance from corporate headquarters
- Possibility of weaker/poorer internal controls
- Less understanding of US laws or norms
- Possibility of inadequate monitoring
- Corporate oversight
- Internal Audit



# Risks of International Business (cont.)

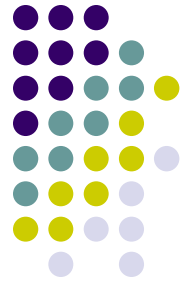
## Fraud in Developing Countries

### Transparency International 2005 Corruption Perceptions Index

Top 10 (Indices $\geq$ 8.7)	Bottom 10 (Indices $\leq$ 2)	Select Countries (7 < Indices < 2)
Iceland (9.7)	Angola	Japan
New Zealand (9.6)	Georgia	Portugal (6.5)
Finland (9.6)	Indonesia	Cyprus (5.7)
Denmark (9.5)	Azerbaijan	Italy (5)
Singapore (9.4)	Paraguay	South Africa (4.5)
Sweden (9.2)	Chad	Greece (4.3)
Switzerland (9.1)	Myanmar	Brazil (3.7)
Norway (8.9)	Nigeria	Mexico (3.5)
Australia (8.8)	Bangladesh	Iran (2.9)
Austria (8.7)	Haiti	India (2.9)

Source: Global Corruption Report 2005. Transparency International ([www.transparency.org](http://www.transparency.org))

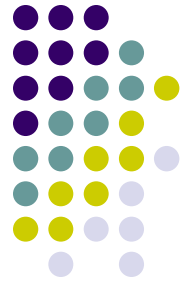
# FCPA – History and Background



## Origins of Foreign Corrupt Practices Act

- US statute enacted in 1977 after Watergate and foreign bribery “slush funds” involving U.S. companies. Substantially amended in 1988 and 1998 (to expand law and bring FCPA into conformity with OECD Convention).
- The FCPA makes it illegal for a U.S. person (or non-U.S. person while in the U.S.) to corruptly offer or give money or anything of value, directly or indirectly through agents or intermediaries, to foreign officials or political parties or candidates to obtain or retain business.
- The FCPA requires U.S. companies to establish accounting and recordkeeping controls that will prevent the use of “slush” funds” and “off-the-books” accounts – used by some companies in the past to facilitate and conceal questionable payments.
- Penalties include fines up to \$2,000,000 per violation for companies and \$100,000 and/or up to 5 years imprisonment for individuals.
- Individuals are subject to criminal liability under the FCPA, regardless of whether the company is found guilty or even prosecuted.

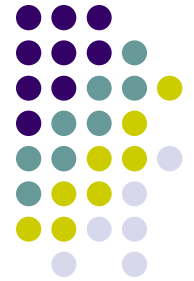




## FCPA – History and Background (cont.)

### Impact of Sarbanes-Oxley Act of 2002:

- Requires Certifications of Executives on Statements (Section 301)
- Internal Controls (Section 404)
- Disclosure of financial fraud
- Requires Reporting Up
- The establishment and maintenance of internal control over financial reporting has been required of public companies since the enactment of the FCPA in 1977
- The Sarbanes-Oxley Act has brought new focus to internal controls and also encouraged companies to devote adequate resources and attention to the maintenance of those controls.

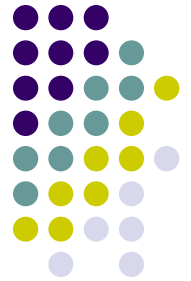


## FCPA – History and Background (cont.)

### Why does there appear to be a new focus on the FCPA?

- Voluntary disclosures in post Enron environment.
- New/additional sources of allegations.
- World governmental attitudes – OECD Anti-Bribery Convention and national legislation.
- Anti-terrorism financing scrutiny – cross border governmental cooperation.
- Sarbanes-Oxley – certification and internal controls
- Board of Directors/Audit Committee expectations
- Increase in M&A (Mergers & Acquisitions) FCPA due diligence.
- The Statute – though the Courts have expanded
- Pervasiveness of corruption in certain markets – Bribe Payer's Index
- Difficulty of detection
- Challenges for compliance as Multi-National Corporations expand into new markets
- Decentralized operations in developing countries
- New/unknown business partners/ventures

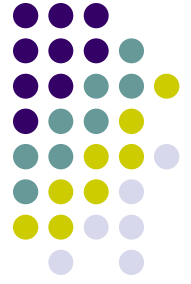
# FCPA – History and Background (cont.)



## Enforcement Trends

- Compliance Standards Rising
- Certain industries and countries are under scrutiny
- Prosecution of individual corporate officials as well as corporate entities
- Source of allegations
- Whistleblower protections
- Source of the alleged bribe does not have to be in the U.S.
- The actions of an agent, consultant, representative and “business partners” acting “on behalf” of the company generally attributed to the company .
- The government has established a nexus by virtue of a single e-mail between the U.S. and the foreign subsidiary.
- Actions of the foreign subsidiary can be attributed to the U.S. parent even if sub goes to great lengths to disguise illegal payments
- Successor Liability
- Foreign “issuers” subject to FCPA

# Anti-Bribery Provisions

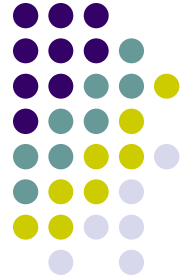


## Overview of Provisions

A company cannot corruptly make an offer, promise, or payment of "anything of value" to a "foreign government official" or politician for (1) "the purpose of influencing his or her official actions," (2) "inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official; or (3) "securing any improper advantage."

*15 U.S.C § 78dd-1 et seq.*

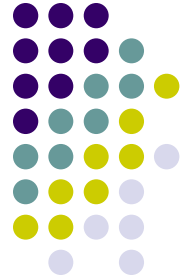
# Anti-Bribery Provisions (cont.)



## Covered Items/Persons

- What Constitutes a Bribe?
- Anything of Value
  - Certainly Cash Payments
  - Excessive Commissions (above ordinary)
  - Expensive Gifts: Jewelry, Travel, etc.
  - Employment of an unqualified relative
  - College scholarship for a child
- Personal Favors
- Payments through intermediaries where the benefit inures to a foreign official

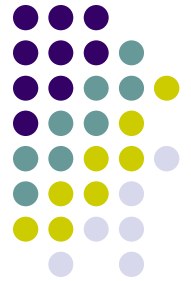
# Anti-Bribery Provisions (cont.)



## Who is a Government Official?

- Nearly anyone in Government
- Ministers, Officials, etc.
- Any Employee of any Government Agency
- Doctor or nurse at state owned hospital
- Politicians or Political Parties or International Organizations (Int'l Olympic Committee)
- Private persons who have a responsibility similar to those of government employees

# Anti-Bribery Provisions (cont.)



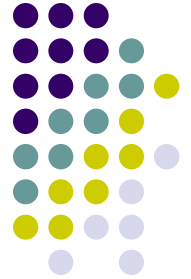
## Exceptions to the Anti-bribery Provisions

### Facilitating Payments or “Grease Payments”:

- Facilitating payments - “payments to expedite or secure the performance of a routine governmental action by a foreign official, political party, or party official.” Facilitating payments are given to secure or accelerate performance of a nondiscretionary act that an official is already obliged to perform.

\*\*Note that this exception does not permit payments made for the purpose of obtaining a particular substantive decision from a governmental agency.

# Anti-Bribery Provisions (cont.)



## Exceptions to the Anti-bribery Provisions (cont.)

### Affirmative Defenses:

- Payments (bribes) that are legal in the foreign official's country (rarely applicable)
- Payments of expenses incurred by foreign officials (travel, lodging) in connection with the promotion, demonstration, or explanation of products or services, or the performance of a contract
- Policy regarding these types of payments should be clearly articulated and followed.

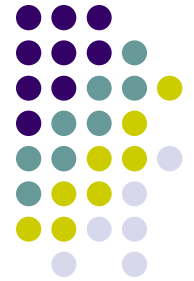


# Accounting/Books and Records Provisions



## Requirements:

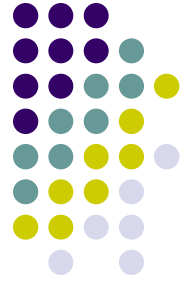
- All publicly held companies must keep records that clearly indicate how their assets are used.
- Companies must devise and maintain an adequate system of internal controls. The internal controls must be sufficient to provide reasonable assurances that:
  - Transactions are executed in accordance with management's general or specific authorization.
  - Transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP and to maintain accountability of assets.
  - Access to assets is permitted only in accordance with management's general or specific authorization.
  - The recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.



# Accounting/Books and Records Provisions

## Accounting Provisions and Foreign Officials

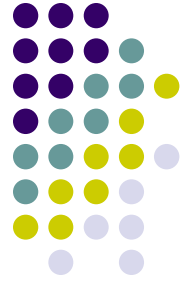
- As with the Anti-Bribery provisions, the FCPA accounting provisions do not apply directly to a U.S. company's foreign affiliates. Nevertheless:
  - **May be deemed to be the “agents” of the U.S. parent**
  - **May have U.S. citizen employees who are subject to the FCPA**
- SEC holds U.S. issuers accountable for inadequate internal controls or books and records when subsidiaries disguise bribes or even if U.S. issuer does not know or have reason to know that the books and records of the subsidiary are inaccurate
- Company will be required to assure compliance by affiliates it controls
  - **With affiliates in which its voting power is 50% or less, a U.S. company must make a “good faith effort” to cause compliance**



## Other Anti-Bribery Legislation

### **The Anti-Corruption movement has spread abroad**

- Ten years ago, the FCPA was the only legislation of its kind
- Now 36 countries have similar laws thanks to an anti-bribery convention adopted by the Organization for Economic Cooperation and Development in 1997
- There are also regional anti-corruption treaties in Latin America, Europe and Africa



## Other Anti-Bribery Legislation (cont.)

### **The Anti-Corruption movement has spread abroad (cont.)**

- One country with no such legislation is China
- Outreach effort underway by the OECD to China
- For now, China remains a looming problem with many potential pitfalls
- It doesn't matter that passing through payments in China is the way of doing business there
- It will not help to claim that you thought you were paying a kickback to a private individual
- Some companies have gone so far as to treat all third parties in China as government entities, since Chinese regulators are involved in any business enterprise



# The DOJ Opinion Process

DOJ has established an opinion process by which any U.S. company or national may request a formal opinion from DOJ concerning enforcement intentions under the FCPA regarding any proposed business conduct

- DOJ encourages the use of the opinion process
- The AG will issue an opinion within 30 days of receiving all information it requires to issue the opinion
- If the AG approves the proposed business conduct, a presumption will arise in any subsequent enforcement action that the conduct was lawful
- DOJ will not provide opinions based on hypothetical facts



## The DOJ Opinion Process (cont.)

### When should you consider seeking a formal opinion?

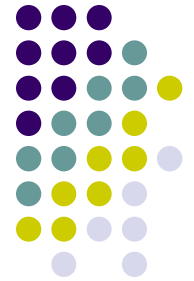
- When you are operating in a grey area and there is no clear answer
  - Can be particularly useful in determining:
    - Who is a foreign official.
    - Whether a payment is a routine facilitating payment.
    - Whether a payment is lawful under foreign law.



# Enforcement Actions

## **ABB Ltd/Vetco Gray**

- Violations discovered during merger due diligence
- ABB's U.S. and foreign subsidiaries made over \$1.1 million in payments to government officials in Nigeria, Angola and Kazakhstan in order to obtain and retain business
- First suit brought by the SEC under the FCPA against a foreign issuer for bribes made by a subsidiary
- ABB agreed to pay a \$10.5 million penalty
  - plus \$5.9 million in disgorged profits (now standard)
- Sale of ABBs subs were delayed many months until settlement of the allegations
- Acquirers of subs had to agree to very stringent compliance program
- ABB DOJ Opinion Release sets a new standard for "robust" FCPA compliance
- Unprecedented sanction in a case involving voluntary disclosure of misconduct to the SEC and DOJ, particularly as ABB and its subsidiaries were acknowledged to have fully cooperated in the investigation



## Enforcement Actions (cont.)

### Schering - Plough

- Polish subsidiary made “donation” of \$75,000 to a “bona fide” charity headed by an official of a State Owned hospital
- SEC determined payment was made to “induce” and “influence” purchase of Schering-Plough pharmaceuticals by the state owned hospital and was improperly classified as a donation
- Case sends clear message that Officials at State-Owned Enterprise (SOE) are considered Government Officials
- Schering Plough cited for weak internal controls and required to hire and pay an independent “compliance monitor”
- Schering-Plough also agreed to pay \$500,000 civil fine
- Message – weak internal controls even in a remote foreign subsidiary is a violation of the FCPA

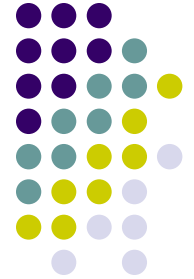




# Enforcement Actions (cont.)

## Monsanto

- Monsanto made over \$700,000 in illicit payments to at least 140 Indonesian government officials (SEC claims that records were made that were intended to conceal the source and true nature of the payments), including a \$50,000 payment, in 2002, to an Indonesian official to alter an environmental impact statement
- The \$50,000 payment was recorded in the company's books and records as a "consulting fee"
- SEC and DOJ finding of anti-bribery and books & records violations
  - Payment to influence an EIS is considered an "unfair advantage"
  - Improper disclosure of payment is violation of FCPA accounting provision
- Company voluntarily disclosed findings of internal investigation to DOJ and SEC
- DOJ agreed to defer prosecution for three years based on Monsanto's agreement to cooperate and existing compliance program
- Monsanto paid \$1 million in criminal penalty to the DOJ and a \$500,000 civil penalty to settle unrelated Indonesian bribery allegations brought by the SEC



## Enforcement Actions (cont.)

### Triton

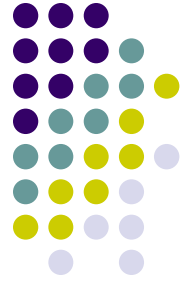
- Triton made payments of almost \$450,000 over a two-year period to Indonesian government auditors and other officials to obtain lower tax assessments on Triton's oil and gas operations
- Payments were recorded as ordinary business expenses
- CEO ordered destruction of all copies of an internal audit memo raising questions about corrupt activities
- Triton agreed to pay a penalty of \$300,000. Furthermore, one of Triton's officials agreed to pay a penalty of \$50,000



# Enforcement Actions (cont.)

## Lockheed/Titan

- In connection with post M&A due diligence, Titan and Lockheed Martin initiated an internal investigation upon discovering bribery in African subsidiary (Benin)
- Titan paid \$3.5 million in “fees” to its Benin agent which was passed on to the re-election campaign of the President of Benin. Payments were made to obtain an increased management fee for its telecommunications project in Benin
- Titan officer directed the payments be falsely invoiced as services by the agent
- Lockheed/Titan voluntarily disclosed findings of joint investigation to the DOJ and SEC and cooperated with the investigation
- Substantial cost/implications of Lockheed’s Successor liability
- Lengthy SEC delay approving merger ultimately led to Lockheed dropping offer
- DOJ and SEC found that Titan violated the anti-bribery, books and records, and internal controls provisions of the FCPA
- No FCPA compliance program, limited due diligence and systemic breakdown of internal controls
- FCPA penalty - \$28.5 million



# FCPA “Red Flags”

## “Red Flags” – indicators of possible FCPA violations

The Justice Department and the SEC have identified FCPA red flag scenarios which serve as a guide for companies engaged in international business with foreign agents, partners and joint ventures

- Off-the-book accounts whereby, for example, payment is made to an individual who then diverts part of the proceeds to a separate account for unexplainable reasons.
- Vendors who make unusual requests, such as back date or alter invoices, or ask for payments by unusual means.
- Vendors requests over-invoicing or checks to be make out to “bearer” or “cash”.
- The payment or transaction is made in a country with a widespread history of corruption



# FCPA “Red Flags” (cont.)

## Additional “Red Flags”

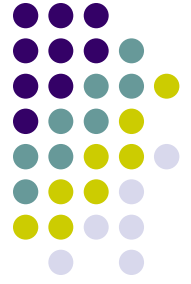
- An employee wants to work with a third party that either refuses to confirm that they will abide by the provisions of the FCPA or disclose their identity.
- Advertising representative asks for commissions that are substantially higher than the “going rate” in that country among comparable service providers.
- An unusually large credit line for a new customer, unusually large bonus or similar payment, or substantial and unorthodox upfront payment is requested.
- A vendor has family or business ties with local government officials; or has a bad reputation in the business community.
- A potential government customer or authorizing agency recommends a vendor.
- Information is kept to a small number of officers within the corporation or shell companies are created to receive revenues or facilitate transactions.



# FCPA “Red Flags” (cont.)

## Additional “Red Flags” (cont.)

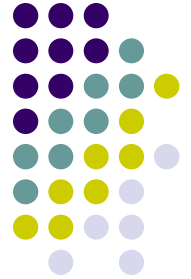
- False accounting entries.
- Payments for schooling or for scholarships for the children of foreign officials.
- Purchasing or renting properties from foreign officials or their relatives.
- Hiring companies or individuals closely associated with foreign officials or their relatives.
- Payments to charitable organizations headed by foreign government officials.
- Gifts, hospitality and entertainment of foreign government officials or relatives.
- Past press reports of payoffs and bribes.
- Acquisitions in high corrupt countries in vulnerable industries.
- Inadequate documentation.



# FCPA “Red Flags” (cont.)

## The Importance of FCPA Due Diligence

- The resounding caveat of the FCPA is to know with whom you are dealing throughout the venture
- Companies must gather a clear understanding of all foreign partners, agents, consultants and marketing representatives
- This understanding should include an assessment of the reputation of the representatives as well as any relationships between the representatives and government officials
- Understand the corruption risks of the country in which you are doing business



# Cooperation Considerations

- A corporation should strongly consider reporting an FCPA violation to the DOJ and/or the SEC
  - DOJ needs to know what the company is doing in connection with its internal investigation so it can provide input
  - DOJ will look unfavorably on a company that comes in at the end of a year-long process with a final report that has been fully wrapped up
  - In much better position if reported promptly rather than at the conclusion of an internal investigation





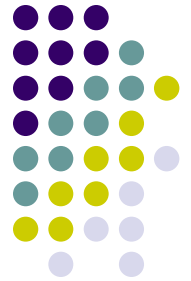
## Cooperation Considerations (cont.)

- A corporation should cooperate fully with the Government.
- make witnesses available
- provide documents
- turn over interview and witness statements
- strongly consider disclosing the results and conclusions of the internal investigation
- strongly consider waiving the attorney-client privilege, particularly where advice of counsel is a potential defense.



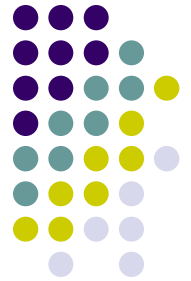
# McNulty Memorandum

- The “McNulty Memorandum” was issued by Deputy Attorney General Paul McNulty on December 12, 2006
- It revised DOJ’s principles of federal prosecution of business organizations
- Prior to the “McNulty Memorandum,” prosecutors operated under the “Thompson Memorandum” and the “McCallum Memorandum”
  - Prosecutors could request corporations to waive the attorney/client privilege and work product doctrine
  - Prosecutors could consider a corporation’s refusal to waive as a factor in evaluating the corporation’s cooperation
  - Prosecutors could consider a corporation’s advancement of attorney’s fees as a factor in evaluating the corporation’s cooperation
  - No prior approval was required from DOJ before insisting on waiver or considering these factors
  - Each USAO simply was required to have a formal written policy setting forth the internal procedures required for obtaining authorization to seek a waiver of the attorney/client privilege or work product doctrine



## McNulty Memorandum (cont.)

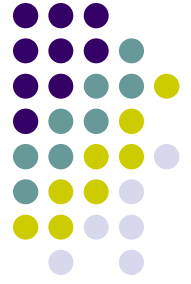
- Under the McNulty Memorandum, DOJ consultation and/or approval is required before seeking a waiver
- Pure factual information is treated differently from nonfactual privileged material or work-product
- To seek a waiver of purely factual information requires approval of the USA after *consultation* with the Assistant Attorney General for the Criminal Division
- However, once requested, a corporation's refusal to waive can be considered by the prosecutor in determining whether the corporation has cooperated in the Government's investigation
- To seek a waiver of nonfactual privileged communications or work product requires the *approval* of the USA and the Deputy Attorney General
- A prosecutor cannot consider a corporation's refusal to waive this type of information in determining whether a corporation has cooperated



## McNulty Memorandum (cont.)

- However, where the nonfactual information sought constitutes contemporaneous legal advice and an “advice of counsel” defense is asserted, or the crime/fraud exception to the attorney/client privilege applies, the same authorization process applies as for requesting a waiver of purely factual information
- Regardless of the type of information involved, voluntary waiver by a corporation can always be considered by the prosecutor as a positive factor when evaluating a corporation’s cooperation
- Prior to considering advancement of attorney’s fees as a factor, a prosecutor must demonstrate that in view of the totality of the evidence, the advancement of fees is indicative of an intent to impede the government’s investigation, and obtain approval from the USA and the Deputy Attorney General

# Questions?



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