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Foreign Officials

A Hot Bench Hears Oral Arguments in Historic Challenge to the Definition of "Foreign Official"

By Rebecca Hughes Parker

The Miami courtroom was packed for the recent oral arguments in *U.S. v Rodriguez and U.S. v. Esquenazi* – the first cases that have brought the question "Who is a foreign official?" squarely in front of a circuit court.

The Eleventh Circuit panel gave the case an hour of its time, instead of the usual thirty minutes. David Simon, a partner at Foley & Lardner LLP representing defendant Carlos Rodriguez, told The FCPA Report that the court entertained a lively discussion of the various tests used to determine what an instrumentality of the government is under the FCPA. "The court was engaged," he said. T. Markus Funk, partner at Perkins Coie LLP and lead attorney representing (with Perkins senior associate Mike Sink) defendant Joel Esquenazi, told The FCPA Report that the "court's active and insightful questioning shows that they haven't made up their mind. The critical 'enforcement' ball is still well in play."

The FCPA defines "foreign official" as "any officer or employee of a foreign government or any department, agency or instrumentality thereof," but many have clamored for more clarity on what an instrumentality of government is. See "Defendants in Haiti Teleco Case Urge the Eleventh Circuit to Limit 'Instrumentalities' to Entities that Perform Government Functions," The FCPA Report, Vol. 1, No. 1 (Jun. 6, 2012). There were other issues raised in the appeal as well, but white collar experts agree that the novel question with the potential to make the biggest impact involves the definition of instrumentality.

By some estimates, two-thirds of recent government FCPA enforcement actions have relied on the idea that an employee of a state-owned entity (SOE) is a foreign official (including employees of state-owned hospitals, for example). Thus, a change in that definition at the circuit level could have far-reaching implications for FCPA enforcement. See, e.g., "Pharma Giant Eli Lilly Agrees to $29.4 Million Consent Judgment to Settle SEC Charges of FCPA Violations Arising Out of Its Operations in Russia, China, Brazil and Poland," The FCPA Report, Vol. 2, No. 1 (Jan. 9, 2013).

It is possible that, if there is a change in the judicial interpretation of "instrumentality," and especially if challenges follow in other jurisdictions, the government may have to do a more rigorous examination of what a foreign entity actually does before it can decide if the suspected conduct falls under the FCPA. The Guidance published by the government as well as the government's charging approach may have to change. See "DOJ and SEC Officials Provide Candid Insight into the Recently Issued FCPA Guidance," The FCPA Report, Vol. 1, No. 13 (Nov. 28, 2012).

The Government and Lower Courts' Views of Instrumentality

Lower Courts

Two previous cases, both in the Central District of California, shed light on the determination of instrumentality. In *U.S. v. Carson*, four former employees

of Control Components, Inc. argued that for-profit businesses could never be instrumentalities of the state, and their employees were not foreign officials. The *Carson* defendants argued that the recipients of the defendants' bribes – including employees of China National Offshore Oil Company, Dongfang Electric Corporation and Petrochina – worked for commercial enterprises and therefore were not foreign officials. The court disagreed and ruled that such a determination is a question of fact to be decided by a jury. Among the factors to be considered, according to the court:

- How the foreign state views the entity and its employees;
- The level of control the foreign state has over the entity;
- The purpose of the entity's activities;
- What obligations and privileges the entity has and enjoys under the foreign state's law, and whether the state exercises controlling power to administer the entity's functions;
- The circumstances surrounding the entity's creation; and
- The level of state ownership in the entity, including the level of financial support, including subsidies, special tax treatment and loans.

In *U.S. v. Aguilar*, at issue were defendants' payments to senior officers of Mexico's federal electric utility company. As Ronald E. Wood and Jennifer L. Roche, attorneys at Proskauer Rose LLP, explained in The FCPA Report in May, the Aguilar court first rejected a blanket ban on all SOEs as instrumentalities – at least some SOEs, the court said, are formed and funded by the government. See "The Expanding Definition of 'Foreign Official' and its FCPA Implications," The FCPA Report, Vol. 2, No. 11 (May 29, 2013).

That court also weighed in on the legislative history, deeming it inconclusive, but noting the OECD's definition of foreign official. Wood and Roche pointed out that "the Convention's definition of foreign public official included 'any person exercising a public function for a foreign country, including a public agency or public enterprise' . . . '*regardless of [the enterprise's] legal form*, over which a government, . . . may directly or indirectly, exercise a dominant influence.' Given the Convention's similarity to the FCPA in construction and objective, and the 'regardless of legal form' language, the [*Aguilar*] court determined that the term 'instrumentality' as used in the FCPA is sufficiently consistent with what Congress intended in signing onto the Convention, to give it a similar meaning in the *Aguilar* case, and denied defendants' motion."

The *Aguilar* court listed a few additional factors to consider when evaluating whether the entity is an instrumentality of the government:

- The entity provides a service to the citizens;
- Key officers and directors are, or are appointed by, government officials;
- The entity receives substantial or exclusive governmental funding;
- The entity has power to administer its designated functions; and
- It is widely perceived and understood to be performing a governmental function.

The Resource Guide and the Royal Opinion Release

The Resource Guide discussed the instrumentality issue, calling it a question of fact. The government listed the factors in *Aguilar* and *Carson*, explained that they were demonstrative of what the government may consider when determining whether an entity is an instrumentality, but characterized them as non-exhaustive. James Tillen, Member of Miller & Chevalier Chartered, recently summarized those factors as

focusing on "ownership, government control, the status of the entity under local law and the function of the entity." See "Who Is a Foreign Official?," The FCPA Report, Vol. 2, No. 18 (Sep. 11, 2013).

A September 2012 DOJ Opinion Procedure Release echoed that sentiment. In that release, the DOJ opined that a member of a royal family who had no governmental authority and did no work for the government was not a foreign official. See "DOJ Issues Opinion Release Containing Guidelines on Whether a Royal Is a 'Foreign Official' Under the FCPA," The FCPA Report, Vol. 1, No. 10 (Oct. 17, 2012).

The DOJ laid out a multi-factor inquiry, not unlike the Guidance, *Carson* and *Aguilar*:

- the structure and distribution of power within a country's government;
- the royal family's current and historical legal status and powers;
- the individual's position within the royal family;
- the individual's past and present positions within government;
- the means by which an individual could come to hold a government position (e.g., royal succession);
- the likelihood that the individual would eventually hold a government position; and
- the individual's ability, directly and indirectly, to affect government decision-making.

The Three Arguments in the Esquenazi Case

Joel Esquenazi and Carlos Rodriguez were convicted for bribing employees of Haiti Teleco, a state-owned firm that provides telephone service to Haiti, to retain business for their Florida-based telecommunications company, Terra Communications. Esquenazi received a record-breaking FCPA sentence – 15 years in prison – and Rodriguez was sentenced to seven years. See "Seven Key Trends That Are Changing the FCPA Enforcement and Compliance Landscape," The FCPA Report, Vol. 2, No. 14 (Jul. 10. 2013) (chart of individual FCPA sentences).

On appeal, among other things, the defendants have challenged what they characterize as the improperly broad scope of the term "foreign official" in the jury instructions. The District Court instructed the jury as follows:

> An "instrumentality" of a foreign government is a means or agency through which a function of the foreign government is accomplished. State-owned or state-controlled companies that provide services to the public may meet this definition. To decide whether [Haiti Telecom] is an instrumentality of the government of Haiti, you may consider factors including but not limited to: (1) whether it provides services to the citizens and inhabitants of Haiti; (2) whether its key officers and directors are government officials or are appointed by government officials; (3) the extent of Haiti's ownership of Teleco, including whether the Haitian government owns a majority of Teleco's shares or provides financial support such as subsidies, special tax treatment, loans or revenue from government-mandated fees; (4) Teleco's obligations and privileges under Haitian law, including whether Teleco exercises exclusive or controlling power to administer its designated functions; and (5) whether Teleco is widely perceived and understood to be performing official or government functions. These factors are not exclusive, and no single factor will

> determine whether [Teleco] is an instrumentality of a foreign government. In addition, you do not need to find that all the factors listed above weigh in favor of Teleco being an instrumentality in order to find that Teleco is an instrumentality.

The panel that heard the oral arguments on October 11, 2013 consisted of Judge Adalberto Jordan, Judge Beverly Martin and Sixth Circuit Senior Judge Richard Suhrheinrich.

The Government's View: State-Owned Entity

The government has characterized Teleco as a company owned and controlled by the government, which held a state-granted monopoly over landline phone service. It pointed out that both the company's board of directors and its general director were appointed by executive order of the Haitian President, which order was signed by the Haitian Prime Minister and other ministers. The government argued that if Haiti Telecom were profitable, the profits would accrue to the Haitian government and the national bank, and that Teleco enjoyed benefits that other governmental entities do, such as tax relief.

The government also argued the statute was not vague, and the defendants were on notice that they were breaking a federal law when they bribed Robert Antoine, the Director of International Relations of Teleco, and Antoine's successor, Jean Rene Duperval, to obtain reductions on Teleco's invoices to Terra and the rates Terra paid to Teleco. The government has also argued that Teleco's status as a government instrumentality is reflected in Haitian law, which would subject Teleco officials to its prohibitions against official corruption. See "U.S. Government Counters Foreign Official Challenge in the Eleventh Circuit" The FCPA Report, Vol. 1, No. 7 (Sep. 5, 2012).

According to one lawyer at the hearing, who wrote about what he observed on the FCPA Professor's blog, the government attorney, Kirby Heller, told an inquiring judge that an instrumentality is "an entity through which government exercises its function, and has dominion and control." She was also reportedly asked how much ownership was needed to make the entity an SOE, and she said any amount – 10%, 15% – would suffice. Heller declined to discuss the hearing with The FCPA Report.

Rodriguez: Governmental Unit Test

Both Rodriguez and Esquenazi contend that "the government's test is wrong," Simon told The FCPA Report, and both contend that some government ownership is not enough to make an entity an instrumentality of the government. Both Simon and Funk cited the dangers of a vague statute carrying with it such harsh repercussions. "This goes back to some fundamental principles of criminal law," Simon said. "If a standard is this hard to figure out, you shouldn't put people in jail for violating it."

There are, however, some differences between the tests the two defendants advocate. Simon, on behalf of Rodriguez, argued in court that "an instrumentality means a unit of government," he said. This test, he said, is focused on the status of the entity as a part of the government, such as an agency or department. The questions to ask about an entity include: "Is this created by statute? Is it the sort of thing the foreign government has identified as something that it is going to do as part of being the government?"

Simon added, "When you get someone's business card, and they work for the government, it is pretty clear where they

work. There is a seal on the card, or some indicia that it is the government." He said there is "a clarity that we think our test promotes that is appropriate for criminal law and consistent with what Congress intended." Another example he said he gave to the court was the government shutdown – if you are furloughed, it is a pretty good indicator that you work for the government.

He said a holistic reading of the legislative history supports the governmental unit test: "Reading the legislative history as a whole, we come away with the conclusion that Congress did not intend for all commercial SOEs to be covered by this law. I think that is the fairest reading of the legislative history. The legislators were concerned about public corruption; this is a public corruption statute."

The statutory language also supports the governmental unit test, he said. "The way the statute describes it – agencies, departments and instrumentalities – we think that shows an intent to encompass units of governments."

The Haitian government could have made Haiti Teleco a governmental unit, he explained, if it had established it as an agency under a prime minister, for example. "The Haitian government could have created a Minister of Telecommunications to run the telephone system in the country and that telecommunications ministry would have been part of the government. If you worked for that ministry, you would be working for the government." Instead, Teleco was started as a private company and the government later stepped in as a creditor. "We know it is owned by the government, but that is not part of the government," he said.

In his brief, Rodriguez cites Eleventh Circuit precedent on the definition of instrumentality, stating that when the court addressed whether a private company that operated a Florida prison was an instrumentality of the state, it held that the term "instrumentality of a state" referred to "governmental units or units created by them."

Esquenazi: Core Function Test

During oral argument, Funk, on behalf of Esquenazi, urged the appellate court to lend the term "instrumentality" concrete meaning in accord with common cannons of statutory construction by requiring that the services performed by an instrumentality bear a direct relationship to "core government functions" – "[By adopting this statutorily-supported definition,] companies will no longer be dealing with what they see as an ever-moving enforcement target. The focus must be on the actual functions the business performs, not on its mere status as 'government owned' or 'government controlled,'" he told The FCPA Report.

"Setting aside, for now, that the ambiguity inherent in the 'government owned or controlled' language – the definition of which drew its own set of questions from the court – we argued that elemental principles of statutory construction require the entity at issue to perform a service that is akin to a core governmental function," Funk said.

"In this sense, our position represents what can be characterized as the middle ground between Mr. Rodriguez's principled 'the owned or controlled business must be a formal part of the government' definition of 'instrumentality,' and the jury instruction's largely untethered 'the business must perform somefunction' definition," he said.

Funk added that, "as we pointed out to the court, after all, the kind of business that does not perform 'some function' will not be in business very long." According to Funk, "to say, as

the jury instructions unmistakably did, that the 'government owned or controlled' business must perform 'some function' transforms the term 'function' from pivot to carousel. What is more, we also don't know what 'government control' means, nor does the statute define what it means for a government to 'own' a company. Justice Stewart's famous 'I know it when I see it' approach, in short, is not helpful when seeking to define the central terms of a criminal statute that mandates strict compliance from businesses around the globe," said Funk.

Funk also pointed out that in the September 2012 DOJ Opinion Procedure Release, discussed above, the government itself cites to *U.S. v. Carson*, and then goes to great lengths to examine what the actual core governmental functions of the entity were – namely, the foreign state's control over the entity, the purpose of entity's activities, the foreign state's characterization of the entity, the purpose of the entity's activities, the entity's obligations and privileges, and the circumstances surrounding the entity's creation. This "function, not status" approach is more in line with the test Esquenazi proposes, Funk noted, but is at odds with the instructions provided to the Esquenazi jury. "The jury instructions could not be more clear on this point: [An instrumentality is] 'a means or agency through which *a function* of the foreign government is accomplished. State-owned or state-controlled companies that *provide [any] services* to the public may meet this definition.'" (Emphasis supplied.)

Victim of a Shakedown?

Funk also told The FCPA Report that, aside from the instrumentality test, the difference between how the government presented his client Esquenazi in this case and in the case against Duperval is, as a matter of simple equities, telling. In its rebuttal (available here), the government explicitly presented Esquenazi as a victim of Duperval's extortion.

According to the transcript, the government attorney in the Duperval case told the jury that Duperval engaged in "shakedown" when taking the bribes from Esquenazi: "That's what a shakedown can be. 'I know you're entitled to seven cents, but what can I get to make it happen?' 'I'll give you $10,000 a month.' 'Sold.' That is the violation here. But I submit to you we've shown you that, that he got paid, and he agreed to do things only after he got paid."

Funk commented that "it is difficult to square the argument that Duperval held hostage legitimate debts Haiti Teleco owed Esquenazi and Rodriguez and used his [Duperval's] 'mastery of the art of the shakedown' to extort a ransom" with the government's theory, presented a mere seven months earlier in this case, that Esquenazi and Rodriguez were nothing more than "greedy businessmen" who attempted to "bribe their way out of their legitimate debts." Funk continued, "Far from a mere academic point, the difference between these two conceptions of the purported crime at hand is significant – 15 years' worth of significant."

It is not clear when the Eleventh Circuit panel will issue its decision, but Simon said, "It was clear the court was engaged with the issue, recognized the importance of this issue and were taking it seriously. That is all you can hope as party to a case like this. I felt pretty good that they are working hard to get this right and that is a good thing."