Avoiding FCPA Pitfalls in Emerging Mining Hotspots

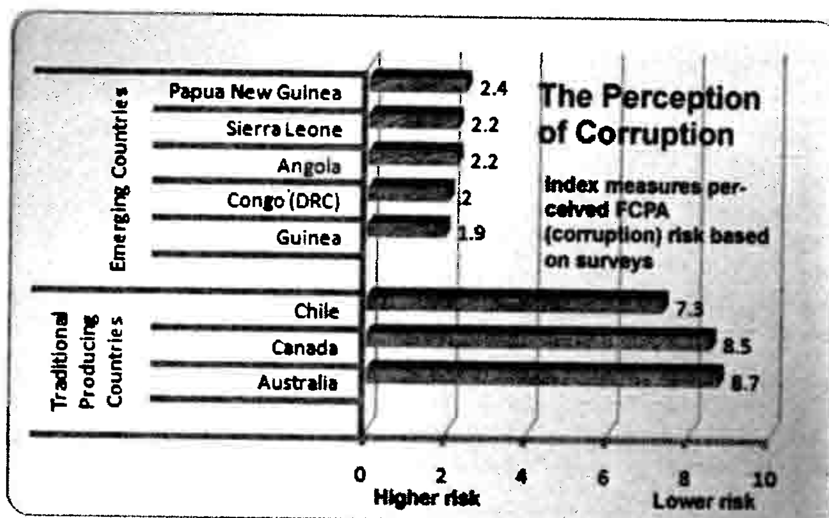
By Mike Koehler

A worldwide commodity boom, driven in large part by China's continued demand for raw materials, coupled with declining production opportunities in developed countries has created a "perfect storm" for Foreign Corrupt Practices Act (FCPA) non-compliance in the mining industry.

The FCPA was enacted in 1977 in response to widespread post-Watergate concerns that U.S. companies were securing foreign government contracts by making improper payments to foreign government officials. The statute contains two provisions, the anti-bribery provisions and the books and records and internal control provisions, and this article deals exclusively with the anti-bribery provisions which generally prohibit "Covered Persons" (defined below) from paying or offering: (i) "anything of value," (ii) to a "foreign official," (iii) in order to "obtain or retain business."[1] Each of these broad elements is discussed in more detail below.

As an initial matter, the FCPA's anti-bribery provisions apply equally to "Issuers" (any company with a class of securities registered with the Securities and Exchange Commission [SEC] or required to file reports with the SEC) and "Domestic Concerns" (any company with a principle place of business in the U.S. or organized under U.S. law).[2] Thus, all U.S. mining companies, whether publicly traded or privately held, are subject to the FCPA's anti-bribery provisions. Mining executives should know that the FCPA's anti-bribery provisions also apply to company employees, both U.S. citizens and forgeign citizens who act while in the U.S. in furtherance of an improper payment.[3]

The FCPA's anti-bribery provisions also apply to non-U.S. mining companies, such as BHP Billiton and Rio Tinto among others, whose securities (often in the form of American Depository Receipts) trade on U.S. exchanges and who similarly must file reports with the SEC. Such non-U.S. mining companies will be deemed an "Issuer" under the anti-bribery provisions and much recent FCPA enforcement activity has targeted the foreign business activity of non-U.S. "Issuers."[4] In announcing FCPA charges against a non-U.S. "Issuer," the U.S. Assistant Attorney General had these words of caution for foreign executives, "...the [FCPA] applies to foreign and domestic public companies alike, where the company's stock trades on American exchanges ... [t]his prosecution demonstrates the Justice Department's commitment to vigorously enforce the FCPA against all international businesses whose conduct falls within its scope."[5]



The Corruption Perception Index rates countries on FCPA risk, based on various surveys. As shown here, perceived risk is much higher for emerging-market countries than for traditional producing countries.

> Mining executives should have a firm grasp of the U.S. Foreign Corrupt Practices Act before pursuing business opportunities in emerging production hotspots.

Thus, "Covered Persons" under the FCPA's anti-bribery provisions include: (i) public and private U.S. mining companies; (ii) non-U.S. mining companies whose securities are traded on U.S. exchanges and who are required to file reports with the SEC; and (iii) mining company employees who are U.S. citizens or foreign citizens who act while in the U.S.

There is no U.S. territorial nexus required for the FCPA's anti-bribery provisions to be implicated and violations can be, and often are, premised on activity that takes place thousands of miles away from corporate headquarters.[6] Indeed, most of the recent FCPA enforcement actions concern business activity by U.S. companies that occur in foreign countries without the knowledge or involvement of any U.S. based employee.[7] For this reason, mining executives must be knowledgeable about the full spectrum of the company's business operations—not only those close to home, but also, and more importantly for FCPA compliance reasons, those operations far from corporate headquarters in emerging production hotspots.

To capitalize on higher commodity prices, mining companies are increasingly exploring production opportunities

in countries where corruption and bribery are endemic.[8] While these production opportunities may prove immensely profitable, with reward comes risks, and the lure of profits in emerging production hotspots can bring mining companies dangerously close to running afoul of the FCPA unless mining executives fully understand and appreciate the many nuances of the broad-reaching FCPA.

FCPA compliance should not be a new concept for the mining industry as companies have long operated in foreign countries. However, the FCPA compliance risks of doing business in emerging markets are much greater compared to the risks in traditional production countries.

The increased FCPA risk in emerging markets is supported by Transparency International's Corruption Perception Index (CPI), a composite index of corruption-related data from various expert and business surveys conducted worldwide. The lower the CPI rating (on a scale of 0-10) the more corrupt a country and its foreign officials are perceived to be.[9]

As the accompanying chart demonstrates, production opportunities are shifting from more developed, stable and less corrupt countries such as Australia, Canada and Chile to less developed, unstable and more corrupt countries such as Guinea, Democratic Republic of Congo, Angola, Sierra Leone and Papua New Guinea.

Mining executives should be mindful of the FCPA compliance risks associated with this production shift and this article is intended to give business leaders the necessary knowledge and tools to avoid FCPA pitfalls in emerging production hotspots.

Elements of an FCPA Anti-Bribery Violation

Three broad elements of an FCPA anti-bribery violation are discussed below: "anything of value," "foreign official," and "obtain or retain business." Every mining executive should have a firm grasp of these broad FCPA elements before pursing or expanding business opportunities in emerging production hotspots.

Anything of Value — It is presumed that all mining executives are well aware that delivering a suitcase full of cash to a foreign official in order to obtain or retain business is a violation of the FCPA's anti-bribery provisions. However, the notion that improper payment arrangements include only such cloak-and-dagger scenarios is misguided because the FCPA applies to a host of other less culpable, but potentially limitless, improper payment arrangements that mining executives should be able to recognize.

The term "anything of value" is not defined in the FCPA, yet it has been broadly construed to include not only cash or a cash equivalent, but also, among other things, discounts; gifts; use of materials, facilities, or equipment; entertainment; meals and drinks; transportation; lodging; insurance benefits; and promises of future employment. There is no minimum dollar amount associated with the "anything of value" element.

Moreover, the perception of the recipient and the subjective valuation of the item conveyed is often a key factor in determining whether "anything of value" has been given to a foreign official. For example, a June 2004 FCPA enforcement action represents perhaps the broadest interpretation of the "anything of value" element of an FCPA anti-bribery violation.[10] In this matter, the improper payments consisted of company donations to a bona fide Polish charitable organization, but they were nonetheless found improper because the founder and president of the organization was also the director of a government health fund that provided money for the purchase of the company's products throughout the country.[11] It was found that the donations constituted a thing of value to the official because they were subjectively valued by the official and provided him an intangible benefit of enhanced prestige.

Foreign Official — Resource extraction industries are perhaps more vulnerable to FCPA non-compliance than other industries because of the high level of interaction with host governments and/or state-owned or state-controlled enterprises (SOEs) in the production country. Mining companies are often party to a contract of work or production-sharing agreement with the host government or are a party to a joint-venture agreement with an SOE, either of which will govern the mining company's production and exploration activities and its rights and obligations relating to, among other things, taxes, exchange controls, royalties and repatriation. It may surprise mining executives to learn that individuals that they and other company employees interact with on a frequent basis are deemed "foreign officials" under the FCPA's anti-bribery provisions even though the individuals are not considered foreign officials under local law and likely do not even view themselves as foreign officials.[12]

The FCPA defines "foreign official" to include "any officer or employee of a foreign government or any department, agency, or instrumentality thereof...or any person acting in an official capacity for or on behalf of such government or department, agency or instrumentality."[13] It is clear that U.S. government enforcement agencies consider SOEs to be an "instrumentality" of a foreign government and that once the SOE is deemed an "instrumentality" of a foreign government every employee of the SOE—from the lowest to the highest ranking employee—will be considered a "foreign official" for purposes of the FCPA.[14]

Given the expansive scope of the "foreign official" element and the broad interpretation of that element by U.S. enforcement agencies, it is imperative that mining executives understand precisely who they are dealing with in emerging production hotspots.

Obtain or Retain Business — The "obtain or retain business" element of an FCPA anti-bribery violation is obviously met if a Covered Person gives a thing of value to a foreign official who then directly awards the company a government contract or other government business. However, the element can also satisfied by a host of situations other than obtaining or retaining government contracts or government business. In *United States v. Kay*, 359 F.3d 738 (5th Cir. 2004), the court held that making improper payments to foreign officials to lower corporate taxes and custom duties could satisfy the "obtain or retain business" element of an FCPA anti-bribery violating by providing an unfair advantage to the payor over competitors.

Since the *Kay* decision, there have been several FCPA enforcement actions where the improper payment to a foreign

official was not alleged to have influenced any government contract or business, but rather to have provided the company a general improper advantage compared with competitors doing business in the foreign country.

Thus, mining executives should also be aware of the FCPA risks associated with routine business activities such as importing heavy machinery to a production country and seeking various licenses and permits before production can occur. For instance, in February 2007, a company settled an FCPA enforcement action where improper payments were made to various Indian officials with discretionary authority over whether the company's product would receive various government registrations required before the company could sell its product in country.[15] Also in February 2007, a company and its foreign affiliates settled an FCPA enforcement action where improper payments were made to Nigerian customs officials to induce the officials to provide preferential treatment to the company's products in the customs process.[16] Foreign production opportunities are often subject to various environmental impact studies conducted by the host government. For this reason, mining executives should also be aware of a January 2005 FCPA enforcement action against a company for making improper payments to a foreign environmental official in an effort to repeal certain environmental regulations.[17]

In sum, mining executives need to be aware that a wide range of business activity can implicate the FCPA's anti-bribery provisions—not just securing government contracts or business.

Third Party Payment Provisions

Mining companies are not insulated from the FCPA risks of doing business in emerging production hotspots simply by doing business through third parties such as agents or representatives. Rather, mining companies are responsible under the FCPA for ensuring that improper payments are not made indirectly through others because FCPA anti-bribery violations can be based on the wrongful acts of third parties under the FCPA's third party payment provisions which prohibit improper payments made to any person while knowing that all or a portion of the payment will be offered or given to a foreign official.[18] The knowledge requirement is broad and can be satisfied by "willful blindness" even if a mining company does not have actual knowledge that a third party has made or intends to make an improper payment to a foreign official.[19]

An April 2007 FCPA enforcement action best highlights the FCPA compliance risks of using foreign agents or sales representatives.[20] In this matter, the improper payments principally focused on two sets of payments to agents to assist the company in obtaining SOE business in Kazakhstan. In the first, an agent approached the company several months *after* it submitted a bid on the SOE project and told the company it could "kiss goodbye the project and future projects" unless it paid the agent a commission.[21] Even though the agent performed no identifiable work in the connection with the project, the company paid the requested commission.[22] The company also paid an agent to assist in securing additional SOE business even though the company was aware that the agent's representative was a high ranking official with the same SOE the company was seeking to obtain business.[23]

While the facts of this recent FCPA enforcement action are rather egregious, it nevertheless reinforces the need for every mining company seeking business in emerging production hotspots to subject all third parties to effective FCPA due diligence. The scope of effective FCPA third party due diligence is beyond the scope of this article; however, mining executives, at a minimum, should be able to answer the following questions as to each business partner in an emerging production hotspot: what is the ownership structure of the third party, including all owners, partners and directors; and is the third party providing similar services to similar companies or otherwise qualified and competent to provide the anticipated services.

Ensuring FCPA Compliance

FCPA compliance challenges for mining companies in emerging production hotspots are numerous. However, the good news is that FCPA compliance is manageable. While the elements of a complete and effective FCPA compliance program are beyond the scope of this article, mining executives should think about the following issues when doing business or seeking business in emerging production hotspots.

Business Partners — Is the business partner, whether through contract or a joint venture, an SOE? If so, all employees of the SOE are deemed "foreign officials" under the FCPA's anti-bribery provisions and interaction with the foreign officials is subject to the FCPA.

Securing Business — Does the company engage an in-country agent or representative to assist in securing business? If so, what does the company know about the third party? Has due diligence been done?

Interaction with Foreign Officials — How are individuals within each business unit interacting with foreign officials (keeping in mind the broad definition of that term)? Are things of value being given to foreign officials such as gifts and/or extravagant entertainment? Are the individuals interacting with foreign officials properly trained on the FCPA?

Regulatory requirements — Is the company importing product into the country or does it need licenses or permits to conduct business in the country? If so, how is the company accomplishing these tasks and who is interacting with the relevant government agencies? If a third party agent or consultant is used in connection with any of these tasks what does the company know about the third party?

Personnel — Is there any ethical concern of any kind (whether or not related to interaction with foreign officials) with company employees operating in the region? Do any of the employees have a reputation for "cutting corners" in terms of other business practices or in following company policies and procedures? Often times, FCPA problems can be avoided because "bad apples" are violating other company policies and procedures before they violate the company's FCPA policies and procedures.

Competitors — Who are the competitors in the country? Is there any suspicion, no matter how strong or weak, that competitors are making improper payments to foreign officials in the country?

If so, the foreign official may be accustomed to such payments and may expect similar treatment from another company.

Any mining company that falls under FCPA jurisdiction and does business or seeks business in a developing nation must first understand and appreciate the significant FCPA risks. Failure to understand these risks can expose mining companies, executives and personnel to significant criminal and civil liability under U.S. law, harsh collateral sanctions, and cause damage to reputations. This article, while not providing an in-depth analysis of any one FCPA issue or compliance initiative, is intended to give mining business leaders the necessary knowledge and tools to legally, effectively and efficiently do business in emerging production hotspots.

References

1 15 U.S.C. § 78dd-1 et seq.
2 15 U.S.C. § 78dd-1, 78dd-2.
3 *See* 15 U.S.C. § 78dd-2, 78dd-3.
4 *See e.g.*, U.S. v. Vetco Gray UK Limited (S.D. Tex. 2007), U.S. v. Vetco Gray Controls, Inc. (same), SEC Litigation Release No. 18775 (July 6, 2004); U.S. v. Statoil, ASA (S.D.N.Y. 2006), SEC Release No. 54599 (Oct. 13, 2006); Siemens Form 6-K (April 26, 2007).
5 Assistant Attorney General Alice Fisher, DOJ News Release, "U.S. Resolves Probe Against Oil Company That Bribed Iranian Official" (Oct. 13, 2006).
6 *See* 15 U.S.C. § 78dd-1(g), 78dd2(i)
7 *See e.g.,* SEC Release No. 55281 (Feb. 13, 2007) (Dow Chemical Co.); SEC Release No. 49838 (June 9, 2004) (Schering-Plough Corp.).
8 *See, e.g.*, Patrick Barta "Tough Extraction – Miners' Daunting Task: Digging in Risky Zones," Wall Street Journal (May 31, 2007).
9 *See* www.transparency.org
10 *See* SEC Release No. 49838 (June 9, 2004) (Schering-Plough Corp.).
11 *See id.*
12 *See* DOJ Opinion Procedure Release No. 94-01 (May 13, 1994).
13 15 U.S.C. § 78dd-1(f)(1).
14 *See e.g.*, SEC Release No. 51724 (May 20, 2005).
15 *See e.g.*, SEC Release No. 55281 (Feb. 13, 2007) (Dow Chemical Co.).
16 U.S. v. Vetco Gray UK Limited (S.D. Tex. 2007), U.S. v. Vetco Gray Controls, Inc. (same), SEC Litigation Release No. 18775 (July 6, 2004)
17 *See* SEC Release No. 50978 (Jan. 6, 2005) (Monsanto Co.).
18 *See e.g.*, 15 U.S.C. § 78dd-1(a)(3).
19 *See e.g.*, 15 U.S.C. § 78dd-1(f)(2); *SEC v. GE InVision, Inc.* (N.D.Cal. 2005).
20 *See U.S. v. Baker Hughes Services Int'l, Inc.* (S.D.Tex. 2007).
21 *See id.*
22 *See id.*
23 *See id.*

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