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The Foreign Corrupt Practices Act: Risk-Management and Compliance Strategies For High-Tech Companies

Gregory Husisian
Foley & Lardner LLP
3000 K Street, NW, Suite 600
Washington, DC 20037-5143
202.945.6149
ghusisian@foley.com

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GREGORY HUSISIAN
FOLEY & LARDNER LLP

INTRODUCTION[1]

Just past its 30th birthday, the Foreign Corrupt Practices Act of 1977[2] (the FCPA or the Act) today poses the greatest liability risks ever for U.S. firms and other covered entities pursuing business opportunities abroad. Chiefly, this risk arises due to the increased risk of prosecution by the U.S. government, the government's increased appetite for large fines, and an increased risk of multiple prosecutions due to other countries having adopted FCPA-equivalent laws.[3]

These changes are ones of emphasis and enforcement rather than a wholesale change in how the FCPA operates. The Act has changed little in its basic parameters over the years. Congress unanimously passed the statute in 1977 following an SEC report disclosing that more than 400 U.S. companies, including 117 of the *Fortune* 500 companies, made "questionable payments" to foreign officials.[4] The FCPA, as enacted, criminalized the making of "corrupt" payments to foreign government and political officials and adopted rigorous recordkeeping requirements for public companies and their overseas subsidiaries.

Recent events have sharply increased the risks posed by the Act. One of the key changes is the newfound affection for the Act by the SEC. For the first 25 years of the Act, the SEC focused on accounting systems and controls and issued largely

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[1] Portions of this article are drawn from material contained in *The Foreign Corrupt Practices Act: Coping with Corruption in Transitional Countries*, an FCPA textbook published by Oceana Publications in 1997 and co-authored by the author of this article with Jeffrey Bialos. All material has been updated to reflect the 1998 amendments to the law and recent trends in enforcement of the FCPA.

[2] Pub. L. No. 95-213, 91 Stat. 1494 (codified at 15 U.S.C. §§ 78dd-1 and 78dd-2, as amended). The Act has been amended twice, once as part of an omnibus trade bill passed in 1988, *see* Omnibus Trade and Competitiveness Act of 1988, Foreign Corrupt Practices Act Amendments, Pub. L. No. 100-418, tit. V, subtit. A, pt. 1, §§ 5001-5003, 102 Stat. 1107 *et seq.* (1988 amendments), and once to implement the changes required when the United States implemented the Organization of Economic Development's anti-corruption initiative. *See* International Anti-Bribery and Fair Competition Act of 1998, Pub. L. No. 105-366.

[3] Notably, Article 9 of the OECD Anti-Bribery Convention requires that signatories provide "prompt and effective legal assistance" to each other in both criminal and civil proceedings. A list of the major countries that have adopted FCPA-equivalent legislation is provided at www.oecd.org.

[4] Securities and Exchange Comm'n, Report on Questionable and Illegal Corporate payments and Practices, 94th Cong., 2d Sess. (Comm. Print 1976) (SEC Report). The SEC confirmed over $300 million in known payments.

routine decisions (with a few notable exceptions). Although the SEC frequently used the FCPA provisions as a means of generally ensuring accurate recordkeeping by covered companies, and occasionally used it as a means of going after companies that had hidden suspect payments on their books, the heavy lifting of enforcing the anti-bribery provisions of the FCPA was largely left to the U.S. Department of Justice (DOJ). No more. With the SEC generally taking the issue of corporate governance very seriously in the post-Enron, Sarbanes-Oxley world, the SEC has found the FCPA's bookkeeping provisions to be an extremely useful tool. Frequent SEC cooperation with the DOJ enhances the SEC's ability to use the FCPA as a broad-based corporate-governance club.

Two other developments also cannot be overlooked: the increased willingness of the U.S. government to extract large, multi-million dollar fines or settlements, and the increasing internationalization of anti-bribery efforts. While large fines were once the rarity reserved for the most egregious cases, such as the $24.8 million settlement in the 1994 Lockheed case,[5] outsized fines are no longer a rarity. In fact, 2007 marked the first of three consecutive years in which total FCPA fines and settlements passed the $100 million mark, including the payment of the (then) largest criminal fine ever, $11 million by Baker Hughes.[6] Further, with other countries both enacting their own anti-corruption laws and showing similar willingness to assess large fines on companies like Siemens, the risk of multiple investigations into suspected payments is more than theoretical. Even when this does not occur, frequent exchanges of information between governments increases the risk of governmental investigation.

Just as the FCPA's prohibitions cut with more force in certain countries where corruption is more common, so, too, does the impact of the Act vary depending upon the industry at issue. Although there are no provisions in the FCPA requiring special enforcement vigor for certain industries, the reality is that some industries, by their very nature, are natural enforcement targets due to the high degree of government involvement in the industry, the large amount of money at stake, or the political nature of the industry.

Many high-tech industries—especially companies in the life sciences/biotech industries—have characteristics that put them in this category. Although these industries historically have not been blessed with the same degree of enforcement activity as some perennial recidivists, such as defense and energy, these industries

[5] *See United States v. Lockheed Corp.*, 94 CR 226 (N.D. Ga. June 22, 1994). Lockheed pled guilty to a single count of conspiracy to violate the FCPA and paid a $21.8 million fine and a $53 million civil settlement. *Id.* at 7.

[6] *See* Thomson West, Foreign Corrupt Practices Report (July 2007) at 1, *reprinted in* The FCPA Reporter, July 2007 Supplement. In addition to the criminal fine, Baker Hughes also agreed to pay $23 million in disgorgement and prejudgment interest and to pay a civil penalty of $10 million more for violating a 2001 cease-and-desist order prohibiting violations of the books and records provisions of the FCPA. *See id.*; *SEC v. Baker Hughes, Inc.*, Accounting and Auditing Enforcement Rel. No. 2602 (Apr. 26, 2007); *United States v. Baker Hughes Servs. Int'l, Inc.*, No. H-07-129 (D.C. Tex. Apr. 11, 2007) (plea agreement).

are likely to be a source of increased future enforcement activity. The attributes that put them in the cross hairs include:

- a high degree of regulation, leading to frequent interaction with government officials;
- frequent and often large transactions, making government approvals and purchases extremely valuable;
- frequent interactions with state-owned entities, thereby inserting FCPA prohibitions into essentially commercial transactions;
- the worldwide scope of the industry, leading to growth opportunities in numerous economies rated high for their generally lax ethical standards; and
- the frequent use of distributors and agents—two areas where FCPA violations are particularly likely, due to the decreased control of the hiring firm over third parties.

The recent enforcement activity against Siemens illustrates the risks of the FCPA for high-tech companies. Siemens, accused of paying $1.9 billion in bribes to land contracts around the globe, paid a fine equivalent to $290 million to European authorities. This fine, however, was eclipsed when the U.S. government, after conducting its own investigation of Siemens, imposed a criminal fine of $450 million and total fines exceeding $800 million. The total corruption-related fines and disgorgement of profits paid by Siemens exceeded *$1.6 billion*, making previous record holders, such as Lockheed, Baker Hughes, and Vetco seem like recipients of mild slaps on the wrist.

Further upping the ante is that the DOJ and the SEC now expect more than one-size-fits-all compliance programs. Just telling employees that bribes will not be tolerated, and putting in place plain-vanilla policies and reporting hotlines, is no longer enough. Today, the U.S. government expects a company to have a policy that is tailored to its industry in general, as well as the particular business environments faced by the company specifically. It expects that training will not be cursory, given out to new hires and then forgotten. Accounting controls are not just to be maintained; they must be regularly tested as well. Moreover, the government expects that companies will follow up with ongoing training effective enough to ingrain the anti-corruption message within the corporate culture.

Implementation is key. But effective compliance presupposes a working knowledge of the law, which is why this article provides a general overview of the FCPA, with a focus on areas of special concern to high-tech companies. The article then highlights ways in which companies can address these risks, including through the establishment of a compliance program tailored to the needs of high-tech companies. It covers not only the basics of setting up a compliance program, but also ways in which companies should administer the program to avoid the all-too-common problem of improper implementation of a well-meaning, but ultimately ineffective, program. A comprehensive list of common "red flags" follows in the Appendix.

The Basic Antibribery Prohibitions, Exceptions, and Penalties

The FCPA both prohibits certain corrupt payments to foreign government and political officials and requires that all third-party payments and other transactions be accurately reported on the books and records of public companies. Although the two provisions are administered by two different agencies (the DOJ and the SEC, respectively), the high degree of cooperation between the agencies can make such distinctions academic. The broad ability of each agency to pursue suspect payments and to negotiate far-reaching settlement agreements covering a wide range of transgressions allows each agency, at least in the case of issuers, to roam far and wide.

The FCPA Antibribery Prohibition: Who, What, to Whom, Why, How, and by What Means[7]

The FCPA antibribery provisions, which are broad in scope, prohibit:

- certain issuers of U.S. securities, domestic concerns, their officers, directors, employees, and agents thereof, stockholders acting on behalf of such firms, and U.S. individuals;
- from using the mails or any means of interstate commerce (except in the case of U.S. persons, where no such connection is needed);
- corruptly;
- in furtherance of an offer, payment, promise to give, or an authorization of an offer, payment, or gift, or anything of value;
- to any foreign official, foreign political party, or candidate for political office, or member of a public international organization,[8] or to any other person while knowing that the payment would be passed on to a government official;
- for the purpose of: (i) influencing any act or decision of that foreign official; (ii) inducing that official to use influence to affect or influence any act of a foreign government or its instrumentality, in order to assist such issuer or domestic concern in directing business to any person or in

[7] The topics covered in this section are presented in more detail in Jeffrey P. Bialos and Gregory Husisian, The Foreign Corrupt Practices Act: Coping with Corruption in Transitional Economies (1997) at 29-56.

[8] "Public International Organization" is designated pursuant to an Executive Order and includes approximately 70 organizations.

obtaining or retaining business with any person; or (iii) "securing any improper advantage"[9]

Each of these elements must be satisfied before an FCPA violation can occur:

Who. The list of parties subject to the FCPA is long and not always clearly defined.

- ***Issuers.*** Coverage extends to any corporation that has a class of securities registered, or that is required to file reports, under the Securities and Exchange Act of 1934 (the 1934 Act) (hereinafter, issuers).[10] This includes foreign companies that issue securities in the United States and, therefore, are required to file reports under the 1934 Act.
- ***Domestic Concerns.*** This includes: (1) any individual who is a citizen, national, or resident of the United States; or (2) any corporation, partnership, association, joint-stock company, business trust, unincorporated organization, or sole proprietorship that has its principal place of business in the United States, or which is organized under the laws of a state of the United States or a territory, possession, or commonwealth thereof, and officers, directors, employees, and agents of these entities, regardless of their nationality.[11]
- ***Foreigners Acting on U.S. Soil.*** The FCPA was amended in 1998 to implement the Organisation for Economic Cooperation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.[12] The 1998 amendments to the FCPA extended coverage to any person who takes an act in furtherance of an FCPA violation while on U.S. soil, even if the person would otherwise not be covered by the FCPA.[13] According to the amended FCPA, any person who takes even a single act in furtherance of an FCPA violation while in the United States is subject to the law's strictures.[14] In these situations, there is no need to satisfy any of the constitutional requirements for minimum contacts since the very presence of the

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[9] 15 U.S.C. §§ 78dd-1 (issuers), 78dd-2 (domestic concerns).

[10] 15 U.S.C. §§ 78dd-1(a), 78dd-2.

[11] *Id.* § 78dd-2(h).

[12] The OECD is one of a number of conventions designed to combat bribery, including the Inter-American Convention Against Corruption (1996), the European Union Convention on the Fight Against Corruption Involving Officials of the European Communities or Officials of the Member States of the European Union (1997), the African Union Convention on Preventing and Combating Corruption (2003), and the U.N. Convention Against Corruption (2003).

[13] *See* International Anti-Bribery and Fair Competition Act of 1998, Pub. L. No. 105-366.

[14] *See* 15 U.S.C. § 78dd-2.

person in the United States is considered per se proof that the standards have been met.

- ***Company Officials.*** Officers, directors, employees, or agents of issuers or domestic concerns, or any stockholder thereof acting on behalf of such issuers or domestic concerns, are directly covered by the Act.[15]

In some circumstances, the statute can be applied to foreign individuals who are directors, employees, or agents of domestic concerns at issuers and "over whom jurisdiction otherwise exists,"[16] even if they have not performed an act in furtherance of an FCPA violation on U.S. soil. If a foreign person has "purposefully established minimum contacts" in the United States,[17] such that the defendant "should reasonably anticipate being haled into court" within the United States,[18] then U.S. courts have jurisdiction and the FCPA can be applied.[19] For example, a Russian citizen serving as an agent or employee of a U.S. company potentially can be held liable for a proscribed payment provided that he or she is subject to U.S. jurisdiction and has acted on behalf of the U.S. company.

What. The FCPA broadly defines the proscribed bribery to include acts in furtherance of any offer, payment, promise to pay, or authorization of the payment of any money, or offer, gift, promise to give, or authorization, of anything of value.[20] "Anything of value" is defined very broadly. For example, in the June 2004 FCPA enforcement action against Schering-Plough Corporation, a pharmaceutical company, the SEC alleged that a donation to a charity—which provided no tangible monetary benefit to the foreign official—was sufficient to confer something of "value" on the official, apparently on the theory that the foreign official welcomed the donation and hence "valued" it.[21]

It is significant that the statute applies to any conduct "in furtherance" of proscribed payments and not just the payment itself, since this means that any subject person who participates in a plan to authorize a covered payment can potentially be held

[15] *Id.* §§ 78dd-1(a) (issuers), 78dd-2(a) (domestic concerns).

[16] *Dooley v. United Tech. Corp.*, 803 F. Supp. 428, 440 (D.D.C. 1992); *accord Fragumar Corp., N.V. v. Dunlap*, 925 F.2d 836 (5th Cir. 1991).

[17] *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 474 (1985).

[18] *World-wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 297 (1980).

[19] *See, e.g.*, *Dooley*, 803 F. Supp. at 440 (finding jurisdiction based upon the defendants conducting business meetings in, sending faxes to, and calling people in, the District of Columbia).

[20] *See* 15 U.S.C. §§ 78dd-1(a) (issuers), 78dd-2(a) (domestic concerns).

[21] *See In re* Schering-Plough Corp., Exchange Act Release No. 49,838 (June 9, 2004), 2004 SEC LEXIS 1185; SEC v. Schering-Plough Corp., Litigation Release No. 18,740 (June 9, 2004), 2004 SEC LEXIS 1183.

liable. The FCPA also "does not require that the [proscribed payment] be fully consummated or succeed in producing the desired outcome."[22] A U.S. firm that formulates a corrupt plan and takes some concrete action to further the scheme probably has taken sufficient actions to violate the FCPA.[23] Finally, covered persons who conspire to violate the FCPA,[24] or who aid, counsel, or cause someone else to violate the FCPA, violate U.S. law.[25]

To Whom. The statute does not cover proscribed payments to private foreign persons but does outlaw payments made to foreign officials, foreign political parties, party officials, or candidates for political office.[26] The term "foreign official" is, in turn, broadly defined to include an officer or employee of a foreign government or any agency, department, or instrumentality thereof, or any person acting in an official capacity for or on behalf of such government, department, agency, or instrumentality thereof.[27] The definition is very broad and covers everyone who works for a foreign government, including low-level officials, part-time workers, and even people with honorary titles.[28] The Act also was amended in 1988 to cover officials of public international organizations, such as the United Nations or the World Bank.[29] As discussed below, the blurred distinctions between public and private sectors in countries where privatization is ongoing makes for many difficult decisions as to whether a payment is covered by the FCPA.

Why. The FCPA reaches only conduct in furtherance of proscribed payments made to assist the firm in obtaining, retaining, or directing business to any person. In 1988, Congress clarified that these provisions also cover payments that are

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[22] S. Rep. No. 114, 95th Cong., 1st Sess. 10 (1977) (Senate Report), *reprinted in* 1977 U.S.C.C.A.N. 4108; *accord* H.R. Rep. No. 640, 95th Cong., 1st Sess. (1977) at 7-8 (House Report).

[23] A difficult issue, not directly addressed by the Act or its legislative history, is whether a very preliminary act, such as depositing money into a bank to use as a payment, constitutes an act "in furtherance" of a prescribed payment. The status of such preparatory acts likely would be adjudicated on a case-by-case basis, and depends upon all the facts and circumstances and whether the FCPA's scienter requirements have been met. *See generally* Senate Report, *supra* note 22, at 3-4.

[24] 18 U.S.C. § 371.

[25] *Id.* § 2.

[26] 15 U.S.C. §§ 78dd-2(2)(A)(i) (issuers), 78dd-2(3)(A)(i) (domestic concerns).

[27] 15 U.S.C. §§ 78dd-1(f)(1) (issuers), 78dd-2(h)(2) (domestic concerns).

[28] For example, in *United States v. Young & Rubicam*, 3 FCPA Rep. 698.38 (D. Conn. 1989), one of the "public officials" involved was a Jamaican citizen who was not even a full-time government employee.

[29] A "public international organization" is defined as an organization that is designated by Executive Order pursuant to section 1 of the International Organizations Immunities Act, 22 U.S.C. § 288, or an international organization designated by the President.

intended to create a better business environment for the bribing corporation.[30] In effect, then, this requirement potentially can be met if the proscribed payment is given "for business purposes."[31] Further, the case of *United States v. Kay*, in which the Fifth Circuit allowed the U.S. government to proceed against payments in return for low import taxes, emphasizes that "obtaining or retaining business" can be defined basically as any activity that saves or makes money.[32] The business to be gained does not have to be with the foreign government; the key is that the recipient of the payment must be an official of the government, a political party, or a candidate for office.

How. The FCPA states that only proscribed payments made with "corrupt" intent are culpable under the Act. This scienter requirement is a key issue in determining FCPA liability. While the statute itself does not define the term "corrupt," the legislative history states that "corruptly" means a purpose to "induce the recipient to misuse his official position in order to wrongfully direct business to the payer or his client, or to obtain preferential legislation or a favorable regulation" and "connotes an evil motive or purpose, an intent to wrongfully influence the recipient."[33] "Corrupt intent" does not mean that the scheme must have originated with the person making the payment; rather, the antibribery provision "cover[s] payments and gifts intended to influence the recipient, regardless of who first suggested the payment or gift."[34]

By What Means. Finally, because the FCPA is a federal statute, the government also must show some connection between the violation and interstate commerce.[35] The practical effect of this requirement, however, is slight. Any connection with interstate commerce—a single telephone call, e-mail, or physical letter sent in furtherance of a conspiracy—is sufficient to satisfy this requirement.[36]

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[30] This requirement was added to avoid situations in which a U.S. corporation might bribe a foreign official to get better treatment for its business that did not involve a specific transaction.

[31] 15 U.S.C. §§ 78dd-1(a) (issuers), 78dd-2(a) (domestic concerns).

[32] *See United States v. Kay*, 359 F.3d 738 (5th Cir. 2004).

[33] Senate Report, *supra* note 22, at 3-4; *see also United States v. Liebo*, 923 F.2d 1308, 1312 (8th Cir. 1991) (approving jury instructions that stated that "the term 'corrupt' meant that 'the offer, promise to pay, payment, or authorization of payment must be intended to induce the recipient to misuse his official position or to influence someone else to do so,' and that 'an act is "corruptly" done if done voluntarily [a]nd intentionally, and with a bad purpose of accomplishing either an unlawful end or result, or a lawful end or result by some unlawful method or means'").

[34] Senate Report, *supra* note 22, at 11.

[35] "The term 'interstate commerce' means trade, commerce transportation, or communication among the several States, or between any State and any place or ship outside thereof." House Report, *supra* note 22, at 13.

[36] This includes even an "intrastate use of a telephone or other interstate means of communication and the interstate use of any other interstate instrumentality." *Id.*

Further, this requirement of some interstate involvement was altogether eliminated for any U.S. person. As noted above, since the 1988 amendments, for U.S. persons, the FCPA applies "irrespective" of any showing of the involvement of interstate commerce.[37] This amendment means that the FCPA in effect permanently adheres to any U.S. persons, regardless of where they are located, and that any actions taken abroad, even if they do not involve the use of the mails or other domestic commercial instruments, are covered by the Act.

Payments Through Intermediaries

The FCPA also prohibits payments made through intermediaries, such as sales agents, distributors, consultants, and contractors. It is unlawful for an issuer, domestic concern, or other covered person to make a payment to any person while "knowing" that all "or a portion of the payment will be offered, given, or promised, directly or indirectly, to any foreign official, foreign political party, or official thereof."[38]

Although in theory the use of intermediaries provides some FCPA protections because it has to be shown that a payment was made to the third party with the "knowledge" that some of it would be passed on to a government official, in reality the additional protection offers little advantage. Once a payment has occurred, even benign transfers of funds can look suspicious, and it is difficult to establish that sufficient due diligence was performed or that adequate monitoring of the relationship occurred. Only in the case of formal joint ventures, if there is minority ownership, is it generally possible to provide concrete proof to indicate a true lack of knowledge (i.e., through evidence showing a lack of control). So the reality is, in most circumstances, the use of intermediaries often increases the risk of an FCPA violation (due to the lessened degree of control over the intermediary's actions) while offering little concrete advantages in terms of staving off FCPA liability (using arguments of no knowledge).

The key issue with respect to payments to intermediaries is whether the requisite "knowledge" that the money was intended for a corrupt purpose can be shown; this must be proven in addition to the requirements noted above. To be prosecuted under the FCPA for third-party payments, a person must "know" that all or a portion of the money given to a third party will be used for a proscribed purpose. A person is deemed to have knowledge if he:

- "is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur"; or

[37] *See* 15 U.S.C. § 78dd-1.

[38] 15 U.S.C. §§ 78dd-1(a)(3) (issuers), 78dd-2(a)(2) (domestic concerns).

- "has a firm belief that such circumstance exists or that such result is substantially certain to occur."[39]

On balance, the 1988 amendments (which were supposed to clarify this requirement) do not appear to have significantly limited liability for prescribed payments to intermediaries. On the one hand, the legislative history states that "simple negligence" or "mere foolishness" is not sufficient for liability.[40] On the other hand, the FCPA's new formulation goes beyond "actual" knowledge and remains broad and somewhat uncertain in its coverage. Although the legislative history states that "knowledge" is not equivalent to "recklessness,"[41] the statute retains liability where it can be established that "a person is aware of the high probability of the existence of such circumstance" but does not have actual knowledge.[42] Moreover, Congress also made it clear that the law still applies to "conscious disregard," "willful blindness," or "deliberate ignorance" of known circumstances that should reasonably alert one to the "high probability" of violations of the Act.[43]

The difficulty is ascertaining the dividing line between "recklessness," which Congress says is not covered by the statute, and "conscious disregard," which is. Recklessness apparently is excluded because of the requirement that a party must be aware of "a high probability" of the existence of a fact. In criminal law, recklessness generally exists when a person is "aware that his conduct might cause the result, though it is not substantially certain to happen."[44] In contrast, the legislative history embodies the congressional intent to cover "conscious disregard" in situations where the defendant has consciously chosen not to ask about what he had "reason to believe" he would discover.[45]

Further complicating the calculus is that the DOJ and the SEC have been very aggressive in their interpretation of what constitutes "willful blindness." Even though the statute and legislative history state that the actor must have failed to inquire because he wished to avoid knowledge *that a corrupt payment would be* made, the

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[39] 15 U.S.C. §§ 78dd-1(f)(2) (issuers), 78dd-2(h)(3) (domestic concerns).

[40] H.R. Conf. Rep. No. 576, 100th Cong., 2d Sess. H2115 (1988) (Conference Report).

[41] *Id.*

[42] 15 U.S.C. §§ 78dd-1(f)(2) (issuers), 78dd-2(2) (domestic concerns).

[43] Conference Report, *supra* note 40, at 919-21. The legislative history notes the intent of the Congress was to adopt the same standard of "willful blindness" found in other areas of U.S. law. *See id.* (citing various cases).

[44] Walter R. LaFave and Austin W. Scott, Jr., *Criminal Law* 239 (1986).

[45] Conference Report, *supra* note 40, at 921.

view of the agencies seems to be that failure to inquire for any reason is sufficient.[46] The bottom line is that the difference between "conscious disregard" and "recklessness" is not always apparent; some courts have even equated the two terms. Hence, what facts will allow a court to infer culpability under the FCPA likely will vary from case to case.

Management officials cannot "take refuge from the Act's prohibitions by their unwarranted obliviousness to any action (or inaction), language, or other signaling device that should reasonably alert them of the high probability of an FCPA violation."[47] If a corrupt payment is found to have been made, the DOJ could infer knowledge, after the fact, where the company was aware of very suspicious circumstances and yet failed to inquire further.[48] Thus, where suspicious circumstances exist, the failure to inquire still could result in potential liability under the FCPA when combined with an "act in furtherance" of a corrupt payment.

Antibribery Exceptions and Affirmative Defenses

In an effort to remove uncertainty over the status of certain payments considered innocuous, the FCPA's 1988 amendments created three relatively limited exceptions from liability (which are set forth in the Act as either "exceptions" or "affirmative defenses").

Reliance on these exceptions is inherently tricky. As affirmative defenses, the burden of invoking them is on the party seeking their protection. In each case, an acknowledged payment is to be made to a foreign official, meaning that there are inherent gray areas. In effect, the covered entity is forced to argue that it has engaged in a "legal" payment/bribe.

All this is of special importance to one particular type of high-tech company: those operating in the life sciences and pharmaceutical industries. In these industries, it is common and accepted for certain kinds of payments to occur, including the provision of free medical samples to doctors (who may be employed by a state-owned hospital) and sponsorship of medical seminars (which may be attended by, or feature speakers from, a foreign government). It is important to remember that

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[46] A very important element of the standard that is often ignored is that the person has to have ignored inquiring into suspicious facts *for the purpose of avoiding knowledge of a corrupt payment. See, e.g.*, Conference Report, *supra* note 40, *citing United States v. Jacobs*, 475 F.2d 270 (2d Cir. 1973) ("If you find that a defendant acted with reckless disregard of whether the bills were stolen and with a conscious purpose to avoid learning the truth, the requirement of knowledge would be satisfied"). Neither the DOJ nor the SEC, however, appear to give much credence to this requirement, so it appears to be of limited utility in determining how to proceed.

[47] Conference Report, *supra* note 40, at 919.

[48] In the context of other statutes, the failure to investigate suspicious activity has been ruled to have satisfied a "knowing" standard. For example, in *United States v. Kaplan*, 832 F.2d 676 (1st Cir. 1987), an attorney had received past complaints that the bills he was submitting to insurance companies were too high. Because the attorney had made no effort to investigate, he was imputed with knowledge of the fraud.

where a state-owned entity or instrumentality is involved, every single employee, from top to bottom, is considered to be a government "official." For this reason, it is especially important for compliance programs in these industries to include very specific procedures for dealing with the application of the appropriate exception.[49]

Facilitating Payments. It is common in emerging markets and other countries for minor government officials to supplement their pay by extracting extra payments for performing functions they are supposed to perform anyway (moving merchandise through customs, and so forth). To alleviate uncertainty that small payments for nondiscretionary acts would be covered by the Act, the original FCPA created an exception for payments made to lower-level officials "whose duties (were) essentially ministerial or clerical."[50] The distinction between lower- and higher-level officials with discretionary functions proved clearer in theory than in practice, however, and created more rather than less uncertainty. The FCPA's original language raised questions such as whether a small expediting payment to an official charged with granting a license would be exempt, even though the official had some discretionary functions. To avoid such dilemmas, the 1988 amendments changed the focus from the official receiving the money to the nature of the action requested.

Specifically, the amended FCPA now exempts "any facilitating or expediting payment" to any foreign official, "the purpose of which is to expedite or to secure the performance of a routine governmental action" by the official.[51] Congress carefully defined the term "routine governmental action" to cover actions ordinarily and commonly performed by a foreign official in:

- obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;
- processing government papers, such as visas and work orders;
- providing police protection, mail pickup and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country;

[49] A 2004 DOJ Release covered this topic. As summarized therein, the request was concerning a comparative law seminar to be put on by a U.S. firm, where the requestor would pay for conference rooms, interpreter services, receptions and meals, transportation costs, hotel accommodations, and translation and printing of seminar materials for Chinese government officials. The requestor stated that it had no business before the entities that might send officials, was allowing the foreign ministries to select who would attend, would pay all costs directly to providers, would not advance funds or pay reimbursements in cash, and would not provide any free gifts to attendees, among other representations. The DOJ indicated it would take no enforcement action. *See* DOJ Release No. 2004-01 (Jan. 6, 2004). The DOJ reached a similar result, based on similar representations, with regard to trips to the United States by foreign officials. *See* DOJ Release No. 2004-03 (June 13, 2004), DOJ Release No. 2004-04 (Sept. 3, 2004), and DOJ Release No. 2007-01 (Jul. 24, 2007).

[50] Pub. L. No. 95-213, 91 Stat. 1494, § 104(d)(2); *see also* Adam Fremantle and Sherman Katz, "The Foreign Corrupt Practices Act Amendments of 1988," 23 *Int'l Law*. 755, 762 (Fall 1989).

[51] 15 U.S.C. §§ 78dd-1(b) (issuers), 78dd-2(b) (domestic concerns.).

- providing phone service, power and water supply, loading and unloading cargo, or protecting perishable products or commodities from deterioration; and
- actions of a "similar" nature.[52]

In other words, if the official has a clear obligation to perform a responsibility, with no real discretion in its performance, then he theoretically can be offered a payment to do his job without violating the FCPA. And yet, even in this situation, extreme care must be taken because of the inherent ambiguities in the application of this exception. DOJ officials, for example, have publicly stated that even a payment for a purely ministerial act, such as giving clearance for a ship to leave port or a plane to land or leave, could be subject to special scrutiny if the payment involved is high. There is not a lot of case law defining what "routine governmental action" means, so extreme care must be taken when applying this exception.

A cautionary tale is provided by *United States v. Vitusa Corp.* In that case, an American company was owed money by the foreign government, which the foreign government refused to refund even though there was no question as to either liability or the amount to be refunded. A senior government official indicated that the money would not be refunded unless he received a payment. Even though the actions of the official were in many ways ministerial—to expedite the payment of a refund that undoubtedly was owed—Vitusa ended up pleading guilty to violating the anti-bribery provisions because it made a payment to secure its refund.[53] Thus, even if a payment is made to an official with discretionary authority to "expedite" a decision he is obligated to make, the application of the exemption can be difficult because, after the fact, it may be difficult to prove that the payment was made purely to facilitate a timely decision rather than to influence the substantive decision itself.

The exception for routine governmental actions does not go far beyond the list provided above. The revised FCPA itself states that the exception for "routine governmental actions" does not apply to "any decision by a foreign official whether, or on what terms, to award new business to or to continue business with a particular party, or any action taken by a foreign official involved in the decision-making process to encourage a decision to award new business to or continue business with a particular party."[54] Such payments are not lawful if made to an official in order to

[52] *Id.* §§ 78dd-1(f)(3)(A) (issuers), 78dd-2(h)(4)(A) (domestic concerns).

[53] *See* Lillian V. Blageff, Guide to the Foreign Corrupt Practices Act at 1-10, *reprinted in* Thomson West, The FCPA Reporter.

[54] *Id.* §§ 78dd-f(3)(B), (issuers), 78dd-2(h)(4)(B) (domestic concerns); *see also* Conference Report, *supra* note 40, at 921 (noting that the Act does not apply to actions with respect to governmental approvals, including permits and licenses, which involve an "exercise of discretion by a government official where the actions are the functional equivalent of obtaining or retaining business for or with, or directing business to, any person").

seek discretionary actions (e.g., licenses or permits) directed at obtaining or retaining business. This limitation to the exception creates some uncertainty to its application and limits its usefulness.

It is fairly common for U.S. companies to note the exception and to provide dispensation in their compliance policies for facilitating payments. Although this practice complies with the FCPA, it ignores a very important point: facilitating payments are nearly always against the law of the country where they are given. Since local law also governs the transaction, a single-minded focus on the existence of the U.S.-based FCPA affirmative defense is myopic. Even if it is legal under U.S. law, it usually will not be in the foreign country.

For this reason, the trend in compliance programs is to prohibit even the payment of facilitating payments that would otherwise be allowed under the FCPA. The advantages of this approach are multiple—in addition to complying with the requirements of foreign law, companies have discovered that allowing facilitating payments often contributes to a culture of corruption and gives a sense that the company is willing to skirt the outer limits of what is allowed. In addition, employees in the field who are not well versed in the nuances of the FCPA often have a difficult time discerning the line between facilitating and impermissible payments. The payment of facilitating payments also raises issues regarding the proper recording of expenses, since companies often are reluctant to describe them accurately in their books and records.

As a compromise, some companies take the middle ground of allowing facilitating payments, but only after their approval by a compliance officer or the general counsel's office. Doing so provides a good way to centralize decision-making and to ensure that foresight goes into determining whether a payment truly is a facilitating payment and not an FCPA-illegal payment. Other companies are even stricter, and flat out prohibit facilitating payments except in cases involving the physical safety of their employees.

Actions Legal Under Foreign Law. Congress also has created an affirmative defense for payments found to be lawful under the written laws and regulations of the foreign official's country.[55] This defense removes conflicts between the FCPA and foreign law.

In practice, this seemingly broad defense is of little use in avoiding liability. Because it is an affirmative defense, the burden is on the party asserting it to prove its applicability. The dangers of doing so are underscored by a DOJ Opinion Release where the DOJ states that it considered a director of a state-owned enterprise to be a "foreign official" despite an opinion from a foreign attorney that the director would

[55] 15 U.S.C. §§ 78-dd-1(b) (issuers), 78dd-7(b) (domestic concerns).

not be considered an official under local law.[56] Further, in developing countries, relying on uncertain local laws that are constantly in flux is inherently dangerous.[57]

One common situation where payments tend to be authorized is for gifts. Congress rejected an amendment that would have provided for an affirmative defense for any "nominal" payment, gift, offer, or promise of anything of value to a foreign official that constituted a "courtesy, a token of regard or esteem or in return for hospitality" if it is of "reasonable value in the context of the type of transaction involved, local custom, and local business practices."[58] Nonetheless, if the foreign government allows for such payments, they would be allowed under this provision.

To rely on the defense, at a minimum, a U.S. firm would want to obtain an opinion from qualified foreign counsel that foreign laws authorize the payment in question. Even if it can do so, great care should be used when relying on this defense, since an error in judging whether a payment is authorized means that, by definition, an FCPA violation potentially has occurred.

Reasonable and Bona Fide Expenditure. Congress also created an affirmative defense to FCPA antibribery liability for payments that are "reasonable and bona fide expenditure[s] such as travel and lodging expenses, incurred by or on behalf of a foreign official" that are "directly related" to:

- "the promotion, demonstration, or explanation of products or services"; or
- "the execution or performance of a contract with a foreign government or agency thereof."[59]

This defense means that bona fide expenses associated with promotional activities are lawful. Expenses such as minor gifts given so that lawmakers can evaluate a product, or paid trips to a local factory to educate them on its operation, have been found permissible by the DOJ in multiple opinion releases.

This is a very valuable exception for the life sciences and pharmaceutical industries in particular. In these industries, there is frequent need for government tours of factories to establish that proper industry standards for the preparation of medications and use of equipment are being followed. Further, this exception is

[56] *See* DOJ Release 94-1 (May 13, 1994).

[57] Even if the gift is legal under foreign law, the FCPA's recordkeeping requirements, discussed below, still require that it be properly disclosed in the payer company's financial records.

[58] Conference Report, *supra* note 40, at 922. The provision was passed by the Senate, but was rejected in Conference. *Id.* A gift that is a product sample, however, or another small gratuity, may, in some circumstances, be permissible as a bona fide promotional expense or as a payment that is legal under foreign law.

[59] 15 U.S.C. §§ 78dd-1(c)(2) (issuers), 78dd-2(c)(2) (domestic concerns).

routinely relied upon as a means of justifying the payment of expenses for government officials who need to attend educational conferences, which often are sponsored or put on by private companies.

Despite the inclusion of the exception, Congress stated that if a payment or gift is "corruptly made, in order to obtain an official act or omission," then "it cannot be a bona fide, good-faith payment, and this defense would not be available."[60] This exception is in a certain sense not a true affirmative defense because it does not apply where the basic elements of the antibribery prohibition have been met; it only means that bona fide promotional payments are lawful where no corrupt purpose is present. Thus, the key is distinguishing truly corrupt payments provided to obtain or retain business from legitimate promotional expenses. As a practical matter, this suggests the need for significant caution in paying the promotional expenses of any foreign officials with discretion to make business decisions affecting the U.S. concern.

In contrast to the foreign law affirmative defense, this defense is frequently useful. The DOJ has opined on such expenses on numerous occasions, and often stated that it would not take enforcement action against the payment, generally because it was agreed that the payment would be disclosed to the foreign government concerned and that the payments would be accurately documented and subject to audit.[61]

Antibribery Penalties

The FCPA, as amended, establishes stiff penalties for violations of the antibribery provisions:

- criminal penalties of not more than $2,000,000 for corporations (double the fine allowed in the original Act) and $100,000 for individuals (10 times the original fine),[62] and prison sentences of not more than 5 years, or both;

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[60] Conference Report, *supra* note 40, at 922.

[61] *See, e.g.,* DOJ Release No. 81-02 (Dec. 11, 1981) (corporation proposed sending samples of beef, its primary product, to prospective purchasers of that beef in the Soviet Union; the DOJ declined to take enforcement action against the plan because the packages of beef, individually worth about $250, were being sent to foreign government officials for inspection, testing, and sampling, and to make the representatives aware of the quality of the beef, and because the beef was provided to the people in their capacity as representatives of the government agency); DOJ Release No. 83-03 (July 26, 1983) (declining to take enforcement action where the Department of Agriculture for Missouri, and a private company, were planning to pay the travel expenses of one official of the government of Singapore, where the trip was intended to demonstrate to the official the facilities available in Missouri); DOJ Release No. 83-02 (July 26, 1983) (company proposed paying expenses of a general manager of a foreign government entity so that the official could see the new facilities of the U.S. country; the DOJ declined to take enforcement action where the expenses related to extending a stay already planned, and miscellaneous expenses would be paid directly to the service providers, and not to the official); DOJ Release No. 85-01 (July 16, 1985) (the DOJ declined to take enforcement action when a U.S. corporation proposed to pay expenses of French officials to tour the U.S. plant that was similar to the design of the plant to be build in France and to show them the features and environmental controls contained in the plant).

[62] 15 U.S.C. §§ 78dd-2(g), 78dd-2(g)(2)(A), 78dd-2(g)(2)(B) (domestic concerns), 78ff(c)(1)(A), 78ff(c)(2)(A), 78ff(c)(2)(B) (issuers).

- fines of up to $100,000 or imprisonment for up to 5 years for any director, officer, stockholder, employee, or agent who willfully violates the FCPA; and
- civil penalties of not more than $10,000 for issuers or domestic concerns, or for officers, directors, employees, agents, or stockholders of domestic concerns or issuers acting on behalf of such issuers or domestic concerns.[63]

The Act has other strong enforcement mechanisms. Any antibribery fines levied on individuals may not be paid by the firm,[64] and directors and officers can be prosecuted even if the company is not.[65] The 1988 amendments also authorize the attorney general to bring suit to enjoin any act or practice of a domestic concern if it appears that someone connected with that concern is about to violate the FCPA.[66] The SEC also has the general authority, pursuant to the 1934 Act, to do the same.[67] Liability for a violation may persist for years; although the applicable statute of limitations is 5 years,[68] there is some authority that the government has the discretion to extend this time period.[69]

In certain circumstances, the same fact pattern that gives rise to an FCPA violation also could lead to a violation of other federal antifraud provisions, which Congress intended would concurrently apply in these circumstances.[70] Certain federal agencies will debar or suspend parties found to have violated the FCPA from participating in any procurement activity,[71] and a company found to violate the FCPA may have difficulty obtaining export licenses.[72] If the bribe results in the

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[63] 15 U.S.C. §§ 78dd-2(g) (B), 2(g)(2)(C), (domestic concerns), 78ff(c)(1)(B), (c)(2)(C) (issuers).

[64] *Id.* § 78dd(2)(g).

[65] *See* 1988 Trade Act, Pub. L. No. 100-418, § 5003(b), 102 Stat. 419, 15 U.S.C. § 78ff(c)(2)(B) (deleting the "Eckhardt Amendment," which formerly prohibited prosecution in these circumstances). Some courts had found that, under the 1977 law, an employee could not be held liable for a bribe if the company had only been found guilty of a conspiracy to violate the FCPA. *See*, *e.g., United States v. McLean*, 738 F.2d 655 (5th Cir 1984), *cert. denied*, 470 U.S. 1050 (1985).

[66] 15 U.S.C. § 78dd-2(d)(1).

[67] *Id.* § 78u(d)(1).

[68] This is truth both for criminal violations of the FCPA, *see* 18 U.S.C. § 3282, and civil violations. *See* 28 U.S.C. § 2462.

[69] *See SEC v. Rind*, 991 F.2d 1486, 1491 (9th Cir. 1993) (stating that limitation periods "do not bind the United States when it sues to vindicate a public right or interest, absent a clear showing of Congressional intent to the contrary").

[70] Conference Report, *supra* note 40, at 1951.

[71] *See* 48 C.F.R. § 9.406-2.

[72] *See* 22 C.F.R. § 120.1(b). This happened with regard to a Lockheed, when the State Department barred the issuance of export licenses because of the indictment of a Lockheed subsidiary on FCPA charges.

award of a contract at the expense of a U.S. competitor, this could, in theory, give rise to treble-damage antitrust actions. Further, if an FCPA violation results in a significant charge to earnings, shareholders might file lawsuits under various securities laws. In addition, although there is no private cause of action for a violation of the FCPA's accounting or antibribery provisions, an FCPA violation can be a predicate act under the Racketeer Influenced and Corrupt Organizations Act (RICO)[73] or the federal money laundering law.

FCPA RECORDKEEPING REQUIREMENTS

The FCPA's Basic Requirements

In its 1976 Report, the SEC stated that "[the] most devastating disclosure that we have uncovered in our recent experience with illegal or questionable payments has been the fact that, and the extent to which, some companies have falsified entries in their own books and records."[74] The specific instances the SEC highlighted were:

- ***Unrecorded Transactions:*** Many companies kept off-the-books slush funds that made tracking bribery difficult.
- ***Falsified Records:*** Some companies were making bribes but recording them as a different payment (e.g., a payment was made to a government official, but booked as occurring to a third party).
- ***Misrepresentations:*** Some companies were correctly entering their transactions but incorrectly labeling than (e.g., the firm paid $100,000 to a sales agent, when the firm knew he was going to pass on half of it to a government official).

The FCPA addressed these problem areas by establishing explicit recordkeeping requirements and accounting controls for publicly traded companies. The FCPA requires all issuers to "make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer."[75] In essence, this means that: (1) companies must follow generally accepted accounting principles (GAAP); and (2) be able to determine, with reasonable precision, that their actual disbursements are in accordance with the books and records. The issuer accordingly must "devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances" of four things:

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[73] *See*, *e.g.*, *Environmental Tectonics v. W.S. Kirkpatrick & Co.*, 847 F.2d 1052 (3d Cir. 1988) (allowing FCPA violations to establish private rights of action under RICO), *aff'd* 493 U.S. 400 (1990).

[74] SEC Report, *supra* note 4, at 29.

[75] 15 U.S.C. § 78m(b)(2)(A).

- that "transactions are executed in accordance with management's general or specific authorization";[76]
- that transactions are recorded in such a way as to allow preparation of a report that is in conformity with generally accepted accounting principles;[77]
- that "access to assets is permitted only in accordance with management's general or specific authorization";[78] and
- that "the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences"[79]

A longstanding issue is the level of exactitude to which a company's records and controls must conform—that is, is the standard absolute, is there a de minimis exception or, like other aspects of U.S. securities law, is there a materiality standard? In resolving this issue in the 1988 amendments, Congress adopted the middle-ground standard of "reasonable assurances" and "reasonable detail."

On the one hand, the "prudent" man standard is designed to clarify that the records and control requirements do not "connote an unrealistic degree of exactitude or precision."[80] On the other hand, this standard is higher than the materiality standard that generally applies in accounting. The net result is that the records must be sufficient to "satisfy prudent officials [as in] the conduct of their own affairs."[81]

An additional issue is how to deal with small amounts that otherwise would not be captured by the normal details of accounting. Here, the answer is clear: even small amounts that would not be considered "material" in an accounting sense are supposed to be tracked. Thus, small payments to foreign officials and disbursements from petty cash for gifts or entertainment for foreign officials, which probably need not be entered on a company's posted financial results for

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[76] *Id.* § 78m(b)(2)(B)(i).

[77] *Id.* § 78m(b)(2)(B)(ii).

[78] *Id.* § 78m(b)(2)(B)(iii).

[79] *Id.* § 78m(b)(2)(B)(iv).

[80] *Id*. In further recognition that the FCPA should not impose unnecessary and costly burdens on issuers, Congress in 1988 also codified the SEC enforcement policy that penalties not be imposed for insignificant or technical infractions or inadvertent conduct with respect to a company's record controls. 15 U.S.C. § 78m(b)(6); *see id*. § 78m(b)(4) (criminal penalties shall not be imposed for failing to comply with the FCPA's books and records unless a person knowingly circumvents a system of internal controls or knowingly falsifies books, records, or accounts kept pursuant to the FCPA).

[81] 15 U.S.C. § 78m(b)(7); Conference Report, *supra* note 40, at 917.

accounting reasons, nonetheless must still be recorded to satisfy the FCPA's accounting requirements.

Accounting Penalties

An issuer or other subject person who violates the FCPA's recordkeeping provisions also faces significant criminal and civil penalties.

The 1988 amendments codify the long-standing SEC enforcement policy that "penalties not be imposed for technical infractions."[82] The law accomplishes this by providing that "criminal penalties shall not be imposed for failing to comply with the FCPA's books and records or accounting control provisions."[83] The law thus reserves criminal liability for situations in which an issuer or other subject person "knowingly circumvents" or "knowingly falsi[fies]" documents or a system of internal accounting controls.

The Sarbanes-Oxley act increased the maximum penalty for violations for both criminal and civil acts. The books and record provisions offer the harshest penalties, which far exceed the penalties that can be imposed for actual bribes. Penalties may include:

- imprisonment of up to 20 years[84];
- individual fines of up to $5 million[85]; and
- corporate fines of up to $25 million for "willful" violations.[86]

The Act also prohibits anyone from furnishing false, misleading, or incomplete information to an accountant who is in charge of auditing the books, including internal accountants.[87] Civil penalties are available under the 1934 Act, including the possibility of the SEC bringing civil or injunctive actions to remedy any accounting errors.[88] In addition, if the statement results in a false or misleading

[82] *Id.* at 916.

[83] *Id.*

[84] 15 U.S.C. § 78m(b)(4).

[85] 15 U.S.C. § 78ff(a).

[86] *Id.*

[87] *Id.* § 78dd-2; *see* 17 C.F.R. § 240.13b2-2.

[88] *See, e.g.*, *In the Matter of Playboy Enterprises, Inc.*, Exchange Act Release No. 17,059 (Aug. 13, 1980).

accounting statement, then the speaker opens himself up to private lawsuits by anyone who trades a security based upon the misrepresentation.[89]

One thing to keep in mind with regard to both civil and criminal penalties is the wide discretion that the U.S. government enjoys in terms of how many violations of the law have occurred. The liability provisions of the statute are very wide open regarding what considers a single act in furtherance of an FCPA violation, and the government often parses acts so that what appears to be a single bribery scheme is stretched into multiple violations (i.e., if the parties have agreed to a $100,000 bribe, payable in four payments, the government could consider each payment to be an FCPA violation, as well as each time the payment was not recorded, and so forth). Further, in settlement negotiations, whatever requirement there is that the fine be tied to specific instances of improper conduct disappears. Thus, the U.S. government has the ability to seek a wide range of penalties, with little oversight.

ESTABLISHING AND IMPLEMENTING AN EFFECTIVE COMPLIANCE PROGRAM

Most corporations are now on round two or even three of their compliance efforts. Spurred by increasingly common headlines about FCPA investigations and record fines, as well as a general increase in fealty to corporate conduct responsibilities in the wake of the Sarbanes-Oxley Act, which requires issuers to establish and maintain adequate internal controls for financial reporting and senior managers to state their confidence in the effectiveness of the controls, many corporations have been taking a fresh look at their corporate compliance programs. The Sarbanes-Oxley requirement that companies annually assess their internal controls structures and procedures also has increased attention to anything related to tracking funds, including FCPA controls. Benchmarking against industry norms is increasingly common, as is scrutiny of governmental criticisms of the codes of violators as new investigations are announced or indictments launched.

As a result, the bar has been raised. One of the chief benefits of a compliance program is to demonstrate, after a violation has occurred, that rigorous procedures were in place to prevent just such an occurrence. A good compliance program helps make the case for the government to lower the potential level of punishment, a result that only occurs when a compliance code is both rigorously prepared and faithfully implemented. Compliance programs that would have seemed models 5 or 10 years ago today appear pro forma against this heightened bar.

Many companies only grudgingly implement compliance programs, viewing them as an impediment to conducting business. This mindset fundamentally misconstrues not only the purpose of a compliance program, but also what it means to manage a

[89] 15 U.S.C. § 78r.

multinational corporation properly. The essence of management is that the company knows that management dictates are regularly executed and that its corporate policies and goals are being properly served. The corporation cannot operate properly unless it has a firm grip on how its funds are being disbursed and has assurances that its corporate interests—including its interest in avoiding crimes that can result in adverse publicity and huge fines—are being implemented, even by employees or intermediaries operating far from corporate headquarters.

A good compliance program is not a stand-alone entity; it is an integral part of the corporation's overall internal controls. Many of the goals of an FCPA compliance policy—accurate recordkeeping, proper controls over disbursements, avoidance of illegal activity—are goals of the overall corporation. Internal controls, although costly to impose, allow greater precision in how the business of the firm is managed. Properly functioning internal controls are designed to ensure the proper management of the firm's many assets—its funds, its reputation, and its business opportunities. Viewed from this perspective, a compliance program is only an extension of the kind of risk and asset management that any corporation should want to impose of its own volition.

The old mind set was to view a compliance as a cost and business burden. This mindset led to more frequent violations, as employees who viewed compliance as a technical barrier against getting business were always looking for ways to skirt what seemed to be unnecessarily naive restrictions that did not take into account the rough-and-tumble business world found in some countries. But in today's business environment, where the U.S. government expects companies to have a culture of compliance, the better mindset is to view compliance as a means of ensuring the proper discharge of basic corporate responsibilities by moderating and controlling risk scenarios. A good compliance program not only is useful to deter violations of the FCPA; it also helps to detect the violation once it has occurred, to prevent the violation from growing into a pattern, and to allow the company conduct an internal review to put in place appropriate remedial measures based upon full knowledge of the facts. By serving all these functions, a compliance program is a key investment in risk mitigation, thereby helping the firm carry out its corporate objectives in a prudent and managed fashion.

Establishing a Program: General Principles

A good compliance program serves four complementary purposes: (1) educating employees about anti-bribery and recordkeeping requirements; (2) effectively communicating that the company is serious about its anti-bribery initiatives, and that they are not just window dressing to be discarded when they get in the way of an important sale; (3) providing a means by which employees can easily distinguish between clear-cut areas where few FCPA concerns are present and those where involvement of experts is necessary; and (4) providing a means of monitoring adherence to policies and encouraging the early reporting of problems so that the company can take ameliorative action.

Many companies approach adherence to the FCPA anti-bribery requirements as a front-line issue separate from the accounting requirements. This is a mistake. There is a natural interaction between anti-bribery policies and internal accounting controls, which provide a necessary check on, and means of discovering, the illicit payments forbidden by the anti-bribery policies. An effective system of accounting controls deters illegal payments at the same time that it ensures accurate recordkeeping. Treating the two areas as a holistic whole in the planning, implementation, and monitoring stages leads to a more effective program.

Certain principles should be respected in the formation of compliance programs. A company should:

- Apply a uniform standard across the company for all divisions and countries of operation. While it can be tempting to relax standards when operating in a country that is more freewheeling, doing so communicates a message that anti-bribery requirements are a hurdle to be skirted as closely as possible. Additional problems arise when employees move from one country or division to another and unnecessarily confront differing standards.
- Promulgate a clear policy that takes away decision-making in “gray areas” from employees who are not experts in the FCPA to people, either at corporate headquarters or in the general counsel’s office, who are well versed in the law.
- Provide comprehensive training, which companies should give to all new hires and regularly supplement, at least for key employees who have frequent government contact. These people include those in sales and marketing, key management, employees who operate abroad, and finance employees.
- Prepare a written compliance policy that includes both a recitation of the law and real-world examples that are relevant to the industry and business.
- Prepare procedures in advance for dealing with foreign agents, distributors, and joint venture partners, including model FCPA provisions and procedures for performing due diligence that can be tailored to meet individual situations as they arise.
- Establish procedures to ensure tight control over the distribution and tracking of expenditures.
- Develop procedures to ensure the retention of all due diligence and FCPA compliance actions.
- Set up a structure for deciding whether a potential FCPA violation exists by people who are independent of the transaction and who have no pressure to approve suspect transactions.
- Establish procedures for the confidential reporting of suspected problems.

- Establish procedures to evaluate potential FCPA violations and to investigate them.

The same consistent support of the anti-bribery requirements should be mirrored on the accounting side. There not only need to be strong and consistently followed procedures for the accounting of payments, but also senior-level responsibility for the maintenance of controls designed to give the corporation strong assurances of how its money is being spent.

The basic elements companies should include in a compliance program are well summarized by the FCPA case of *United States v. Metcalf & Eddy*. In that case, the company entered into a consent decree with the U.S. government in which the company agreed to a wide range of compliance obligations, including adherence to the books and records portions of the FCPA (even though the company was not an issuer). The elements that Metcalf & Eddy agreed to included:

- a “clearly articulated” corporate policy;
- assignment of responsibility for compliance to one or more senior company officers;
- establishment of an independent committee to review contracts retaining agents and consultants;
- due diligence procedures for potential agents, consultants, distributors, and other business partners;
- procedures designed to inhibit discretion of corporate authority to persons at risk of making payments;
- regular training, including training of agents, distributors, consultants, and other representatives;
- an effective reporting system for company employees to report possible violations;
- appropriate disciplinary mechanisms for employees violating policies;
- antibribery clauses in all contracts with consultants or business partners, including periodic certifications, prior approval of any subcontractors, and termination clauses for violations;
- books and records and internal accounting requirements identical to requirements imposed on issuers under the Act;
- periodic certifications on FCPA compliance to USAID and other U.S. government entities based on independent outside audits; and

- periodic reviews of the compliance program by outside law firms or auditors.[90]

In putting these requirements into practice, a company will need to tailor the program to its industry and needs. The program should contain elements to show that the company is establishing a culture of compliance. The compliance standards should be accessible and written in plain English. The program should allocate senior-level responsibility at both the management and director levels. The program should have procedures both governing the training and monitoring of employees and to ensure that third parties are subjected to adequate due diligence. Responsible officials must have both the authority and the responsibility to implement the program and to use company resources to monitor, audit, and test the compliance procedures to ensure that they are faithfully implemented. The program should contain provisions to allow the reporting of problems, such as for anonymous whistle blowing, and also to follow up in a meaningful way on valid concerns. The program should state that the company will severely discipline violators of the policy. Finally, the company should regularly update the policy to incorporate new lessons as the company encounters problems and new legal developments as the interpretation of the law becomes more concrete through the announcement of enforcement actions.

The involvement of senior management does not end once the program is rolled out. The goal is to foster a corporate culture where compliance is viewed as part of the corporate mission rather than a barrier to completing transactions. Employee performance reviews should place some weight on an employee's adherence to compliance standards. The company should have procedures for employees to report compliance concerns that are independent of normal business channels, so the employee knows he can share concerns without fear of retribution. Companies should establish procedures for the vetting of third-party relationships, including through the performance of systematic due diligence that is reviewed by people who are not directly associated with the completion of the transaction.

A question that sometimes arises is how a company should coordinate an FCPA compliance program with a firm's overall compliance program, which often covers such U.S. laws as sanctions, anti-boycott, money laundering, and import/export. Some companies separate out FCPA training as a means of emphasizing it. But the best way for the company to proceed is to integrate the program to the fullest extent into a global program that covers all compliance issues. Many of the elements of these compliance programs, such as reporting hotlines and training, can be approached as an integrated whole. Setting up a single line of communications for

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[90] *United States v. Metcalf & Eddy*, Civ. No. 1:00cv 12,566 (D. Mass. Dec. 14, 1999), *summarized in* Homer E. Moyer, Jr., James G. Tillen, and J. Matteson Ellis, "The U.S. FCPA in 2006: Increased Enforcement, Alternative Dispositions, Compliance Monitors, and Other Developments," *reprinted in* The FCPA Reporter at 11-31.

employees who have questions regarding compliance programs is advantageous, since it requires that they learn only one method of consultation.

Implementing a Program

Even the best program, if not properly implemented, will be ineffective. Worse yet, failure to meet the standards of an established program, in and of itself, can be taken as proof that the company did not exercise reasonable care in carrying out its FCPA obligations. It accordingly is necessary to establish procedures designed both to monitor and to ensure compliance dictates are carried out. Doing so may require periodic auditing designed to probe both the adequacy of financial controls and the fealty of key employees and outside partners to the FCPA's requirements. Many firms believe that it is a best practice to require annual certifications of FCPA compliance from key agents, distributors, joint venture partners, and employees. Changes in corporate organization, such as the acquisition of a controlling stake in what formerly was a minority owned subsidiary, also can change the required level of accounting controls and increase the risk of culpable anti-bribery violations.

Proper implementation of a program depends on establishing from the outset that the firm has a culture of compliance and that short-term profit gains at the expense of an increased risk of an FCPA violation will not be tolerated. Communication of this message is best served by including business people within the presentation of the FCPA policy. Too often firms turn over implementation of the FCPA policy to the lawyers, which makes it seem like there is a tension between the compliance program and the firm's business objectives. Further, the company should not implement the program purely as a top-down initiative. The company should involve appropriate division people and presentations of the program should, where possible, involve local business people who are aware of the situation on the ground and can offer practical advice on how to implement the program.

Typical Steps in Designing a Program. A proper program cannot be designed in a vacuum. It should be put in place only after careful consideration of the company's business, its operating environment, and its culture. The basic steps companies should follow are to: (1) identify the risks based upon where the company does business and the specific industry in which it operates; (2) determine what controls are needed in light of the identified risks; (3) assess what resources are available to administer a compliance program; (4) determine how the program will be implemented; (5) determine what controls will be needed to ensure adequate tracking and following of expenses; (6) determine how implementation will be monitored; (7) identify steps needed to allow the confidential reporting of problems; and (8) identify steps to ensure that the program is regularly updated.

The precise compliance program should reflect the individual company's requirements, including its own procedures for tracking payments, its specific corporate organization, and its business interests. But the following general considerations for each of these steps form the core of the design of the program:

- ***Risk Identification.*** The first step is to consider the risks posed by the company's business activities. This includes an evaluation of where the company does business, its particular product line, and the company's history of compliance issues. Companies should consider not just the company's FCPA risk profile, but also of whether it has run into trouble in other areas, including for export control or import violations, which could indicate a careless corporate culture toward compliance issues. The degree of interaction with foreign government officials also should be carefully considered.
- ***Control Identification.*** The next steps is to determine what controls have already been established, and their adequacy and defects, as compared to what controls should be in place in an ideal world. Auditor letters, such as SAS 30 warnings from accountants, should be considered, but a more far-reaching inquiry than is required by accounting-driven evaluations should take place.
- ***Resource Identification.*** The controls for the company to implement must be commensurate with the resources available. A company should not, for example, put in place a program that demands substantial due diligence of every foreign agent hired if it has not made the decision to fund such activities. Otherwise, it risks setting itself up to look like it has failed to meet its own compliance standards. Once the risk and necessary controls have been identified, a realistic sense of the cost of a program, and the resources needed to run it, must be developed.
- ***Scope and Objectives Identification.*** The next step is to evaluate the scope and objective of the program: who needs to be covered; what level of education is required; what monitoring needs to occur, and so forth The level of training and oversight should vary depending upon the person at issue and his responsibilities. The level of oversight, and appropriate liaisons at the director and management level, should be considered as well.
- ***Compliance Procedures.*** Companies should implement proper controls on a company-wide basis. Companies should create models for typical situations, including hiring agents, setting up joint ventures, hiring distributors, and conducting due diligence. Companies also should consider how payments and disbursements are to be controlled. They should put in place procedures for dealing with red flags as they arise and to ensure that potential violations that are unearthed are investigated in a meaningful fashion.
- ***Accounting Procedures.*** In evaluating compliance procedures, companies should give simultaneous both to compliance procedures and to internal accounting controls. The two naturally work together, with the accounting controls being a useful tool to ferret out substantive violations of the FCPA. An effective set of accounting controls is the final step in ensuring that illegal payments are not made and incorporates

review and approval guidelines designed to detect and deter questionable payments.

- ***Testing Procedures.*** It is impossible to have a strong compliance program unless it is regularly tested, probed, and analyzed. It is not enough just to create a good compliance program and then to let it run unattended. Instead, companies should monitor all procedures, including by ensuring that all contracts for distribution agreements, joint ventures, and consultants have included FCPA clauses, regular annual certifications are gotten from key employees and third parties, and that controls designed to monitor disbursements are regularly followed. Due diligence procedures need to be monitored to ensure that they are regularly being followed.
- ***Reporting Procedures.*** A key element is reporting procedures. Companies should have clear procedures in place from the start regarding when the compliance officer will take care of things, when the general counsel's office gets involved, and when senior management and directors will be informed. The Sarbanes-Oxley financial control reporting requirements also indirectly come into play when companies are deciding how involved senior management should be and when apparent FCPA failures draw into play suspicions that a company's internal controls are not adequate to meet required corporate standards.
- ***Updating Procedures.*** Finally, the days of putting a compliance program in place and then leaving it unattended are long gone. With the increasing number of SEC and DOJ investigations, state of the art is a constantly moving target. The best practice is that the general counsel's office, or other responsible person, regularly monitor developments in the field and regularly incorporate them into an updated program that will reflect the latest thinking on FCPA enforcement and compliance.

Companies should monitor compliance by direct observation, by supervising the program, and by testing the controls. One increasingly common way of ensuring the last element is to conduct FCPA audits. Modeled somewhat loosely after export control and import audits, which have long been a fixture for many exporters, these are intended to stress-test FCPA procedures by picking high-risk transactions at random to see how the compliance program was implemented. A well-designed FCPA audit will look at the range of potential issues, including due diligence, third party hiring and monitoring, reporting of issues, and monitoring the flow of money. Companies should take all of this into account at the outset and design procedures dealing with these potential problems into the basic setup of the program.

Typical Elements of a Compliance Program. As noted above, the patience of the DOJ and the SEC with one-size-fits-all FCPA compliance programs is long gone. Since most companies have moved beyond these cookie-cutter programs to more sophisticated programs that are tailored to the business environment of the particular company, the DOJ and SEC are unlikely to view generic programs as state of the art should a problem arise. Still, all successful programs share certain elements, which typically include:

- ***A Written Policy Statement.*** A policy statement is just what it sounds like. It is a statement from the head of the company that succinctly sets out the company's commitment to comply with the law in all of its business activities, including with regard to the payment of bribes. The company should write the policy statement in straightforward, plain English and should state that it is the responsibility of each employee to abide by the company's anti-bribery policies. It also should stress the importance of timely and accurate accounting for all payments, regardless of purpose.
- ***A Manual of Business Ethics and Procedures.*** A business manual should include not only a complete copy of the company's policies, but also real-world examples of some of the tricky areas that can arise, such as payments for travel and lodging, dealing with foreign officials, company policy on facilitating payments, and so forth. The manual should present detailed information about reporting, company procedures for approving payments, standards for entertainment of government officials, and sample forms for proper accounting for expenditures. The manual should contain any relevant local laws governing payments.
- ***Education and Training Programs.*** A good education and training program has both a written and a presentation component. The program should use real-world examples, such as case studies drawn from actual problems confronted by the company in the past. Training should occur for both new employees and annually for long-time employees. The company should maintain an attendance log. Each employee should sign an acknowledgment form showing that he has reviewed the compliance materials and understands his responsibilities to comply with the company's program.
- ***A Methodology for Tracking Payments Accurately.*** A system for employees to turn in all receipts, and to keep track of all disbursements and the nature of the transaction, is part of any compliance program. The goal is to allow the timely and accurate recording of all disbursements. Although the FCPA only imposes this requirement for issuers, all companies operating internationally should have a similar system in place, since it is impossible to track payments without proper tracking of disbursements.
- ***A System of Reporting Suspected Violations.*** Most companies either set up a compliance committee or have a senior individual who is responsible for coordinating all anti-bribery initiatives. The person or committee should be someone who is not involved in business-generating activities, whose judgment might be colored by business issues. If the compliance officer is not the general counsel, the company should establish procedures for regular coordination with the company's

legal department. Although the precise elements of the reporting system will vary depending upon how the company and the program are structured, common elements are reporting hotlines and procedures for the anonymous reporting in writing of suspected violations. The compliance officer should be a direct report of the president or CEO of the company.

A compliance program should have a mechanism for the periodic check of compliance; otherwise, standards tend to slip and there is no mechanism to revisit problems that were not initially noticed. An internal audit and compliance review should evaluate company and employee compliance and identify procedures that the company needs to modify or strengthen.

The precise way in which these basic elements are implemented will vary, depending upon the size of the company, its business, its corporate structure, and so forth, but some combination of these elements is needed to ensure a satisfactory program.

After a program is implemented, internal actors and outsiders should audit it to test both the accounting and anti-bribery programs to make certain that they are being consistently implemented. A recent trend is for companies to benchmark their FCPA policies against other companies in their industries to ensure that they are keeping up with evolving compliance standards and best practices in the industry. A proper review, however, will go beyond ensuring that the terms of the compliance program are state of the art. Companies also need to check the implementation of the program by making certain that people are aware of policies and that the requirements of the policy are being followed. Special emphasis, too, needs to be put on any changes in the organization that have occurred since implementation of the policy, including modifications to relevant local laws or changes in the company (establishment of new subsidiaries or hiring of new agents, distributors, and so forth).

Many companies will undertake top-to-bottom reviews of their policies every three to five years, by either an independent legal or auditing firm. Testing of FCPA controls differs from testing of other compliance areas, in that it involves careful risk assessment as a means of focusing inquiry. While it is not possible to test every transaction in evaluating the rigor of the program, companies can focus on areas of highest risk and working backwards. Auditors will focus on areas where the most money is generated or where corruption risk is highest (based upon business or country-of-operation factors) as areas of special interest. Auditors also should focus on areas of the most common violations, including expense reports, overpayments to vendors, credit invoices, payments to distributors, travel expenses and reimbursements, and any direct payments to government officials, however classified. Focus on these areas can make testing a viable option that can be repeated on a regular basis.

Anticipating Problems: Setting the Stage for Internal Investigations

An additional issue that needs to be anticipated in any compliance program is the establishment of an internal investigation structure. No matter how strong a firm's compliance program, at some point there will need to be some kind of internal investigation. Thus, even if they do not form a part of the compliance materials that are handed out to employees, a proper compliance program will have established procedures in place for deciding when and how the company will conduct an internal investigation.

There are no one-size-fits-all investigation parameters. Trying to anticipate every twist and turn of how investigations will proceed is foolish and unnecessary. Rather, what is needed is a basic blueprint that the company can modify as the investigation unfolds, including basic requirements for when an investigation should begin, when it should be expanded, when management should be informed, when the company should consider bringing in outside help to run the investigation, and other basic guideposts.

The company should have a set of procedures that allow for a graduated response, adaptable to new facts as they are revealed, and that will quickly and thoroughly develop the relevant facts. Not every fact pattern will require the same level of commitment to an investigation, so the initial goal is to delve down and determine how much resources the company should put into the investigation.

One issue that trips up many internal investigations is that they are inherently fraught with conflicts of interest. The key conflicts include the internal (the fact that the company needs to balance the need to uncover genuine problems against the costs and undoubted distractions of conducting an investigation) and the personal (the fact that employees may have different interests, such as privacy, than the company). A well thought out compliance program will anticipate these conflicts of interest and minimize their intrusion into the conduct of internal investigations.

In deciding how to set up an internal-investigation procedure, the six key questions that need to be addressed are: (1) when is there enough information to set a formal investigation into motion (i.e., who determines, what standard will be used, and so forth); (2) how much resources should be put into an investigation; (3) who should be involved; (4) when should senior management be consulted/involved; (5) when should outside counsel/investigators be brought in; and (6) what steps should be taken in case disclosure needs to take place (preservation of the steps of the investigation, protection of privilege, and so forth). More specifically:

Most companies use a tiered-investigation strategy. The typical progression is based upon the level of alarm raised by the facts. Usually companies start with local investigation, often directed by someone who is designated as an investigator at the regional or headquarters level, with the basic goal of determining whether there is a real issue. If facts appear to warrant further inquiry, generally the general counsel's office will become more involved to ensure proper protection of evidence and involvement of people who can appreciate the subtleties of evidentiary and FCPA points. The general counsel also can determine whether facts appear serious enough to report to senior management. Generally, the next step—and it is a quantum leap in terms of intensity—is to consider the hiring of outsiders to conduct a full-blown investigation. Outside counsel and forensic experts can delve into records and conduct a total investigation. The final and most dreaded step is to consider reporting to the DOJ and the SEC.

A good progression will take into account the need for the interplay of headquarters and local actors. It is important to establish from the outset how this progression will play out so that the chain of responsibility is clear. When an investigation is occurring, it is common to find that red flags were long present but that nobody took responsibility for delving into them. Establishing a clear progression that places responsibilities not only on the general counsel's office but also on pre-determined local people helps ensure that this does not happen.

A question that always arises is, what scenarios should a company investigate, and which should it ignore? The easy advice is: investigate everything. But as desirable as this would be from a pure FCPA perspective, it ignores the fact that companies can receive an incredible amount of tips and innuendo that in the end turn out to be meaningless noise. Companies need to assess credibility at the outset to determine which tips merit serious follow up and commitment of a substantial amount of resources, and which receive lower priority.

That does not mean that the decision as to whether to investigate should prejudge things. It is impossible in many cases to separate out the vague tips that turn out to be rumor from the serious ones that merit close scrutiny without some kind of coordinated response from headquarters and local company officials. Anything that looks at all credible should be examined on some level, since failure to do so is exactly the kind of behavior that can lead DOJ or SEC investigators to conclude that the company was "sticking its head in the sand" and trying to avoid gaining knowledge of a violation.

Most companies that operate in multiple jurisdictions have a pretty good idea of which business units are most likely to be flashpoints. Some companies that operate worldwide have set up matrices to help inform the decision as to whether they should investigate. This can be important, since it helps focus the company from the beginning in its thoughts about which areas of the company are most likely to lead to FCPA problems. This thinking can then carry over to the decision as to whether an investigation should be ramped up. Events or tips that might seem innocuous in certain areas of the world can appear much more ominous when a business unit that has frequent government contact, or that operates in a country that ranks high on rankings of corruption, is at issue.

Compliance in Multiple Jurisdictions

Companies also should harmonize compliance programs to avoid problems incurred by companies that balkanized their compliance systems. The thought was that compliance programs should be tailored to the countries or regions where the companies operate to reflect more closely the standards of the different countries. This was an especially common approach in companies that were built by merger or that relied heavily on joint ventures when operating abroad, which often left a patchwork of compliance programs.

The problem with this approach is that it results in differing standards for different regions. Often, the regions where FCPA issues are the most difficult and most likely to arise are the ones where local control over internal investigations is most problematic. Involving people who are most sensitive to the nuances of the FCPA is essential, and these people often are not local.

To avoid this problem, most companies try to ensure that procedures are in place to centralize the reporting of problems. Companies should have one standard applied when deciding whether investigation should occur. While a lot of the investigative heavy lifting can be done locally, and probably should be because those are the people who are closest to the situation, the involvement of the general counsel's office, or some other centralized ethics authority, is essential. Companies should set up procedures from the start to designate both local and centralized responsibility for internal investigations so that companies can tap these pre-planned resources if it appears that there is a problem.

Anticipating Serious Investigations

Companies should give thought at the outset regarding when to involve senior management. Of all the topics to be covered, this one is the hardest to provide parameters for ahead of time. Obviously, senior management should be told when there are glimmers that the problem is serious and widespread, and should not (or should be told only in summary form as part of periodic reports) when there are not. Most problems fall in between, making it difficult to tell what to do.

Centralization of reporting helps take care of this problem. The general counsel or the chief ethics officer should make the call, not local employees. This ensures that someone with a feel for the sensibilities of U.S. law is consistently making the judgment call.

Companies also should give thought regarding when to involve outsiders. Companies differ greatly on this issue. Some companies take the view that compliance is an internal matter, best explored and monitored by the company itself. For these companies, bringing in forensic experts and intrusive outside lawyers is a true last resort. Other companies take the opposite view and seek analysis of myriad issues, papering their files with opinions of outside counsel on their FCPA issues, thereby creating a paper trail of concern should the government come knocking with questions.

Most companies, of course, are in the middle, choosing to balance the costs and intrusiveness of outside investigation against the benefits. The benefits are, of course, considerable: protecting documents with attorney-client privilege, increased ability to get to the truth, bringing to bear expert analysis gained from prior investigations, and establishment of a strategy from the start if a case needs to be set up for eventual presentation to the DOJ or the SEC.

No real guidelines can be set up in advance for when outside counsel should be brought in. This really is a you-know-it-when-you-see-it area. For most companies, the trigger point is when it appears that an FCPA issue is part of a larger pattern. If it appears that there is a systemic problem, and that the potential FCPA issues permeate a certain division or region, or even the company itself, then most companies will opt to bring in outsiders to ferret out the problems. At that point, the intrusiveness and cost are outweighed by the need to get the universe of problems out into the open.

An internal investigation necessarily covers a lot of ground. A host of issues need to be considered, including: how to determine if allegations of potential violations are credible; what steps need to be taken to preserve documents (both physical and electronic); how to evaluate the risks of potential third-party disclosure; how to get to and interview relevant witnesses; how to determine if there are any disclosure obligations; and other issues relating to the how and what of an investigation. These procedures should be considered at the outset so that they do not have to be made up on the fly.

It also should not be forgotten that both the DOJ and the SEC have huge discretion in how they deal with FCPA issues. Their options range from imposing criminal and civil fines and profit disgorgement down to nominal fines or even not prosecuting. There is little check on their actions, making it paramount that companies show that they have made every attempt to take the FCPA seriously in the event that they are investigated.

This mindset needs to permeate an internal investigation. The main goal of any investigation certainly is finding out what happened, but the potential effect on the prosecutorial decisions of the DOJ and the SEC cannot be discounted either. The agencies will be evaluating the thoroughness of any investigation in determining how they proceed.

In light of this reality, any investigation that has gone beyond the preliminary stages should take into account the potential impact of the case on the agencies. Companies should document every step of the investigation, with an eye towards showing the completeness of the investigation and that no evidence has been destroyed. In the event that the company decides not to follow up on any allegations of wrongdoing, the company should thoroughly document what factors informed its decision so that it can demonstrate that it acted on the basis of a proper analysis, even if it turns out that its decision later was proven to be wrong. Any disciplinary actions taken should be documented, including the reasons why that punishment was chosen, particularly if the person at issue continues to be employed by the company.

Companies should take particular care in conducting the investigation so as to keep in mind the differing interests of employees and the company. The company's response to an infraction may turn out to be shifting blame to the employee. It is essential in any interview or fact-finding that the company clearly warns employees that they are being investigated regarding a potential violation of U.S. law and that they have the right to counsel. Companies should document any employee waiver of this right to avoid later disputes.

Finally, on top of all the problems an internal investigation entails, companies also should consider the complications of dealing with foreign law. Every foreign country outlaws bribery, after all, and they by no means consider the FCPA to be the chief concern of companies operating within their borders. This means that the way an investigation is conducted has to take into account the requirements of both local and U.S. law. The fact that most foreign jurisdictions will cooperate with the U.S. government and share prosecutorial information only underscores the need for considering the impact of multiple jurisdictions having an interest in how the matter is handled.

A key issue is respecting the intersection of U.S. and foreign laws. Many foreign employees may be unclear regarding how and why U.S. law applies to them. A clear explanation of this topic is essential, in the event the conduct of the investigation becomes a targeted issue. Translation issues also can be problematic, and need to be taken into account. Further, many foreign countries, especially in Europe, have stringent employee-privacy laws. These laws can sharply restrict the scope of an investigation, and their violation can subject a company to substantial penalties. For this reason, the involvement of local counsel is often considered to be important when conducting a far-reaching FCPA investigation that touches on foreign countries.

The Perennial Problem of Agents and Distributors

Although the discussion of the "knowledge" requirement above lays out the basis of third-party liability, the perennial problems posed by agents and distributors merit special discussion in the compliance context. Because agents and distributors are used so often by many companies, no compliance program can function in these industries unless it successfully deals with intermediaries.

The DOJ and the SEC look askance at attempts to place agents outside the confines of a company's FCPA compliance responsibilities. For example, in *In the Matter of Oil States Int'l, Inc.*,[91] a key point in the SEC charge was that the subsidiary of an issuer hired a consultant without providing any formal training or education to the consultant. Even more ominously, in its 2007 complaint charging Baker Hughes Inc. with violations of Section 30(A), the SEC relied on a theory that the "knowledge" requirement was satisfied where the "company failed to adequately assure itself that such payments were not being passed on" to a foreign official.[92] This standard of failure to inquire, while at odds with the amendment of the knowledge standard in 1988 to eliminate liability where there was only a "reason to know" of a corrupt payment, nonetheless raises the stakes whenever an intermediary is employed.

Hiring a local sales or hiring a distributor or agent presents special problems in complying with the FCPA. The chief asset of many agents or distributors is their connection to the government or state-owned enterprises—a relationship that may or may not be disclosed to foreign parties. Even if disclosed, the relationship is both the primary allure to the arrangement and its greatest potential risk.

Due Diligence. A threshold question is whether to conduct a due diligence prior to the retention of an intermediary. The degree of due diligence companies should perform depends on a lot of factors, including the dollar value of the arrangement, the expected contact with government officials, and the country at issue. One common approach is to consider whether the transaction raises "red flags" like those listed in the Appendix to this article.

Due diligence is not a complete defense in the event that a corrupt payment is nevertheless made. While amending the FCPA in 1988, Congress expressly rejected a proposal that the conduct of a due diligence review would constitute an affirmative defense where the concern had procedures in place for detecting violations and had used due diligence to prevent the violation.[93] Nevertheless, the fact that such a reasonable inquiry was undertaken would, in all likelihood, mitigate the risk that the DOJ or the SEC would prosecute a U.S. firm for a corrupt payment by an agent or

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[91] 5 FCPA Rep. 699.9504 (2006).

[92] *See* SEC v. Baker Hughes Inc. and Roy Fearnley, Complaint H-07-1408 (Apr. 26, 2007) at ¶ 7. This formulation was repeated numerous times. *See*, *e.g.*, *id.* ¶ 6 (alleging a section 30(A) violation for an Angolan official where the company "failed to make an adequate inquiry"); *id.* (same for Nigeria, where "the company failed to adequately assure itself that such payments were not being passed on, in part, to Nigerian Customs officials); *id.* (same for officials in agent who worked in Kazakhstan, Russia, and Uzbekistan "under circumstances in which the company failed to determine whether such payments were, in part, to be funneled to government officials in violation of the FCPA").

[93] An early version of the 1988 bill in the House stated that "a firm could not be held vicariously liable for [anti-bribery] violates [of employees or agents] if it had established procedures 'reasonabl[y] expected to prevent and detect ' any such violation[s], and the officer and employee with supervisory responsibility for the offending employee's or agent's conduct used 'due diligence' to prevent the violation." House Report, *supra* note 22, at H2117. The House language was deleted during the Conference markup. Conference Report, *supra* note 40, at 922-923.

distributor, while the absence of due diligence would be considered a strong aggravating factor that would multiply the penalty imposed.[94]

Whether or not due diligence is required by the FCPA, it surely is prudent to conduct some inquiry before hiring an agent or entering into business with a distributor, given the frequency with which issues arise with intermediaries. As the DOJ and the Department of Commerce noted in a 2002 joint release, "[t]o avoid being held liable for corrupt third-party payments, U.S. companies are encouraged to exercise due diligence and to take all necessary precautions to ensure that they have formed a business relationship with reputable and qualified partners and representatives."[95]

Part of due diligence is to ensure that the agent or distributor being hired is up to the task. This does not just serve a business purpose. An intermediary that seems to be running a real business is less likely to be a front that only can operate due to illegitimate contacts within the foreign government. Any agent or distributor hired should demonstrate that it has a good understanding of local business practices, has adequate capital and resources necessary to finish the job contemplated, has adequate facilities for operation, and has the financial resources commensurate with the responsibility being trusted to it.

There are three basic goals for any due diligence inquiry: (1) to weed out, to the extent possible, people or firms who are likely to make bribes (or to be otherwise unsuitable for the job contemplated); (2) to document how hiring decisions were made, and why; and (3) to establish that, in the event a violation later occurs, there was no way that the hiring firm could have "known" about it because the agent or distributor was carefully vetted.

While the nature of the review may vary, depending on the identity of the intermediary, the nature of the circumstances, and other facts and circumstances, the following are a number of steps to consider:

- Contact the country desk at the State Department, the commercial attaché at the U.S. embassy in the foreign country, and that country's business desk at the Department of Commerce, and ask whether they have any records of improper conduct by the agent or distributor.
- Conduct a basic background check using Dunn & Bradstreet or consult the U.S. Department of Commerce Commercial Service.
- Contact any references provided to make sure that they actually exist and are willing to vouch for the character of your agent or distributor.

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[94] For example, the lack of any due diligence was cited as an aggravating factor in *United States v. Titan Corporation*, 5 FCPA Rep. 699.9287 (S.D. Cal. 2005).

[95] U.S. Dep't of Just and U.S. Dep't of Commerce, "Foreign Corrupt Practices Act: Antibribery Provisions" (Mar. 15, 2002).

- In some of the larger cities, where information is available, check local databases and/or police records to help determine if the person has a history of being involved in illegal or improper activities.
- If such resources are not available, local investigatory agencies may serve the same function.
- Establish written procedures governing how to hire sales agents or distributors. The goal of such procedures is to take all reasonable steps to ensure that agents do not appear likely to violate the FCPA and to isolate the actions of a "rogue" agent or distributor if it turns out that it is engaged in FCPA-illegal activity.

The level of inquiry required before hiring a sales agent or distributor will, of course, vary depending upon the facts, the presence of any red flags, and the degree of authority to be granted to the agent or distributor. Lower-level agents are of less concern to the home office; they can be hired and managed by local officials, subject to defined procedures written by the home office. But if the agent will be a key player, or have anticipated government contact, then the U.S. firm should consider exercising greater control.

In deciding which entities to subject to due diligence, companies should keep in mind recent enforcement activity of the U.S. government. Actions of both freight forwarders and Customs brokers have resulted in FCPA enforcement activity, and the U.S. government is likely to scrutinize arrangements that covered persons make with these companies. So, too, are foreign lobbyists a potential FCPA risk, given their frequent contact with foreign legislators. Companies should subject all of these entities, as well as traditional agents, to due diligence and treated as a potential FCPA risk.

One key due diligence goal is to establish that the agent is being properly compensated given the level of responsibility and work required. Doing so serves more than just the business purpose of not overpaying for services rendered, for a payment that is far in excess of what should be required suggests the possibility that the agent is dividing up the proceeds from the arrangement with a government official. A common way to evaluate the reasonableness of compensation is to construct a set of benchmarks within the country at issue, or in countries that are otherwise comparable, for similar work. Of course, this approach works better where the agent is performing relatively simple, often-hired tasks. Nonetheless, the approach does provide some guidance for complicated transactions even if the company cannot determine the level of "comparable" work.

Given the importance of due diligence, it is surprising how often firms are haphazard with the results of their due diligence. Companies should not just gather due diligence; they should analyze and summarize it. An adequate summary would note both the positive and negative information gathered and state with particularity how each negative element was dealt with. Companies should keep all information gathered for at least five years after the relationship with the agent or distributor at issue has been terminated.

Written FCPA Procedures. Once a potential agent or distributor has been identified, it should provide a signed, written questionnaire providing basic information, including: (1) the nature of the agent's or distributor's organization, when and where it was incorporated or registered to do business, and the names of all principals in the organization; (2) a statement that there are no government officials who own or are paid by the intermediary or, if there are, a full disclosure of their names and positions; (3) a copy of the agent's or distributor's most recent fiscal report; (4) a statement regarding whether any of the principals or employees are seeking political office; and (5) a statement regarding prior government positions held by the agent or distributor, or employees of same.

An additional topic, often overlooked, is how far to go in seeking control over subcontractors. The general approach of most companies is to leave the hiring of subcontractors to their agents or joint venture partners. While this can be an attractive proposition from a management standpoint—part of the reason an agent or a joint venture exists, after all, is to introduce this kind of decision-making authority by a knowledgeable local actor into the business relationship—it also is a risky approach from an FCPA standpoint. The U.S. government is likely to look at such arrangements, if they have resulted in an illegal payment, with a skewed eye, and to attribute the sins of the subcontractor back to the original hiring entity if there is any evidence of knowledge at all. Therefore, the better approach is to weigh all the factors that raise potential red flags and to set up vetting procedures, especially in countries or industries where problems are likely, and to get involved in the decision to hire subcontractors.

An additional key step is to use tightly worded contractual provisions to provide additional guards against FCPA violations. No agent or distributor should be paid until there is a written agreement in place that includes appropriate FCPA provisions. You want the agent or distributor to acknowledge the requirements of the FCPA, to agree to be bound by them, and to agree to punishment if a violation is suspected. The following are types of provisions for the U.S. firm to consider in intermediary contracts:

- The intermediary is an independent contractor with no authority to commit violations of the FCPA.
- The intermediary is aware of the requirements of the FCPA and agrees not to commit any action that would cause your firm to violate the FCPA. The clause should explicitly state that the intermediary agrees not to pass on any bribes to foreign officials and not just reference the Act.
- The intermediary is not an employer, officer, or representative of the foreign government, nor a candidate for office. The intermediary should also warrant that it will not run for office without first notifying the U.S.

firm and allowing it to take appropriate steps in light of this change in status.

- The intermediary will not assign its rights or duties under the agreement without prior written consent of the U.S. corporation.
- The intermediary agrees to allow the issuer's accounting firm to review the intermediary's books.
- The intermediary will conduct all purchases pursuant to an itemized list of expenses and in writing. All reimbursements will occur pursuant to check or wire transfer, never in cash.
- The intermediary agrees that certain expenses, including gifts to any government official exceeding $100, or expenses over a certain amount, shall be paid by the intermediary only after it gets approval from the U.S. corporation.
- The intermediary will keep accurate books that show the expenses, the person to whom any payment was made, and a detailed and accurate description of the services, with the company having the right to audit the intermediary's books to satisfy itself that no payment has occurred.
- The U.S. company will be excused from performance or payment if it has any reason to believe that there is any violation of either the U.S. or the foreign company's antibribery laws, with the agreement becoming void ab initio.[96]
- The intermediary will notify the U.S. firm if there are any relevant changes in facts, such as a member of the firm becoming a government official.

In addition, the best procedure is for agents and distributors to provide annual certifications that they are aware of the requirements of the FCPA, have not made any improper payments, and promise that they will not do so. Annual certifications have the advantage of providing a regular mechanism to capture new hires and also provide ongoing protections should the agent go off the rails and make a payment in violation of the FCPA.

CONCLUSION

Although there is only one FCPA, there is no one correct approach for creating and implementing an FCPA compliance program. The DOJ and the SEC expect that companies will give a great deal of thought to the best way to implement the FCPA's

[96] It has become very common for third-party agreements to contain these kinds of void ab initio clauses, or to contain requirements that all funds ever paid under the agreement will be returned if an FCPA violation is uncovered. The DOJ has cited this as a favorable factor in Releases. *See*, *e.g.*, DOJ Releases 94-1 (May 13, 1994) and 08-01 (Jan. 15, 2008).

requirements in light of the particular circumstances and industry involved. The use of a systematic, long-term compliance program that is faithfully executed will help ensure that violations remain the subject of newspaper headlines belonging to other companies, even for companies that regularly are required to operate in environments where requests for bribes are common.

Author

Gregory Husisian
Of Counsel
Foley & Lardner LLP
202.945.6149
ghusisian@foley.com

APPENDIX: FCPA "RED FLAGS"

General Red Flags

The following are general "environmental" red flags that do not, in and of themselves, indicate specific liability risks with respect to a particular transaction but nonetheless indicate the need for heightened vigilance in general.

Flag 1: Your company has received an "improper payment" audit in the past five years.

Flag 2: Payment in a country with widespread corruption and/or history of FCPA violations occurring in that country. Countries that are considered to fit this category include some Middle Eastern and Asian countries, and much of the former Soviet Union and Africa.

Flag 3: Widespread news accounts of payoffs, bribes, or kickbacks.

Flag 4: The industry involved has a history of FCPA violations. These industries include defense, aircraft, energy, and construction services.

Transaction-Specific Red Flags for Intermediaries

Flag 5: An agent, distributor, or joint venture partner refuses to provide confirmation of willingness to abide by the FCPA.

Flag 6: Family or business ties of an intermediary with a government official.

Flag 7: Bad reputation of the agent or rumors of prior improper payments or other unethical business practices by the intermediary. This is a key flag, and parties should document the good reputation and experience of the intermediaries they hire.

Flag 8: Listing of agent on databases listing known corruption risks like the World Bank List of Debarred Firms.

Flag 9: The intermediary requires that its identity not be disclosed.

Flag 10: The potential foreign government customer recommends the intermediary. This could suggest a coordinated scheme to divide a payoff.

Flag 11: The intermediary lacks the facilities and staff to perform the required services. This could suggest that the intermediary may be performing its job through corrupt payments rather than hard work.

Flag 12: The intermediary is new to the business.

Flag 13: The intermediary does not have much experience in the particular industry at issue.

Flag 14: The intermediary has violated local law, even if the violation is not related to bribery.

Flag 15: The intermediary wishes to use anonymous subcontractors.

Flag 16: Unusually large or frequent political contributions to a person or political party by the intermediary, which could suggest an arrangement for the direction of business to the intermediary.

Flag 17: Insistence on the involvement of third parties who appear to be unnecessary for the work required.

Flag 18: A proposed foreign partner is owned by a key government official or a close relative.

Flag 19: Rumors of a silent partner in a joint venture partner, distributor, or agent that is not disclosed by the intermediary.

Flag 20: An intermediary insists on having sole control over meetings with or approvals by a foreign government or government official.

Flag 21: The intermediary has an opaque structure or refuses to reveal the structure.

Flag 22: The intermediary reportedly is associated with criminals or criminal activity.

Flag 23: The proposed relationship is not in accordance with local laws or regulations, including rules dictating when a government official can be involved in a business relationship.

Flag 24: The intermediary attempts to assign its rights or obligations to another party.

Flag 25: The intermediary has an unexplained breakup with another company, which could suggest the discovery of illegal conduct in that relationship.

Flag 26: The intermediary has been investigated for, charged with, or convicted of corruption allegations.

Control-Based Red Flags for Intermediaries

Flag 27: A joint venture partner refuses to agree to reasonable financial controls.

Flag 28: A joint venture partner values assets contributed to the joint venture at an improper value.

Flag 29: A joint venture partner insists on maintaining two sets of books for tax or other purposes.

Flag 30: An intermediary refuses to allow auditing of its books.

Flag 31: An intermediary requests payment of inadequately documented or entirely undocumented expenses.

Flag 32: Any other odd request by an intermediary that reasonably arouses suspicion. For example, if an agent asks that certain invoices he backdated or altered, further inquiry is warranted.

Payment Requests by Intermediaries

Flag 33: Payment of a commission that is at a level substantially above the going rate for agency work in a particular country. An excessive commission might suggest that a portion of the funds is going to a foreign official. Then again, your agent might just be greedy.

Flag 34: Requests to work on contingency or bonus basis. Although such arrangements can be perfectly legitimate, they often are associated with suspicious activity.

Flag 35: Payment through convoluted means. If your agent asks for payment to a numbered account in the Bahamas, the DOJ or SEC could consider this failure to investigate culpable conduct under the FCPA.

Flag 36: Over-invoicing (i.e., the intermediary asks you to cut a check for more than the actual amount of expenses).

Flag 37: Requests that checks be made out to “cash” or “bearer,” that payments be made in cash, or that bills be paid in some other anonymous form.

Flag 38: Requests that payments be made to a third party.

Flag 39: Payment in a third country, which suggests a plan to divide the commission in the third country away from government scrutiny.

Flag 40: Agent or distributor requests for an unusually large credit line for a customer can be suspicious, especially if the customer is new.

Flag 41: Requests for unusual bonuses, one-time success fees, or extraordinary payments.

Flag 42: Requests for an unorthodox or substantial up front payment.

Flag 43: Requests for an increased level of compensation to the intermediary, without a commensurate increase in the amount of work to be performed.

Flag 44: Unexpected requests for reimbursement of entertainment expenses relating to foreign officials.

Flag 45: Any unusual payment requests, such as asking that invoices be backdated or altered.