Can I Save This Agent? Analyzing a Company's Liability for an Agent's Actions Under the Foreign Corrupt Practices Act

David Simon, Rohan Virginkar and Matthew White, Foley & Lardner LLP

I. Introduction

Imagine this scenario: Golf Course Inc. ("GCI"), a publicly-traded U.S.-based golf course design company, decides to expand into international markets. After evaluating various countries, it decides to design courses in a Middle Eastern country. Having no local contacts or experience with that country's property or zoning regulations, GCI hires a local agent to help facilitate its expansion and to assure compliance with local laws. After several successful endeavors, the company is impressed with the agent's work, never having encountered any roadblocks with zoning compliance, environmental regulations or otherwise. Several years into the business relationship, the agent mentions in passing that he had extensive "contacts" with local government officials noting that his cousin sat on the country's national assembly. After learning this information, GCI wonders whether these relationships had any effect on how easily it navigated through notoriously difficult local regulations. As a result, the company begins closely examining invoices from its agent, and notices several line items of substantial payments for "additional assessments" and "urgent processing." Without any independent knowledge of the country's law, GCI is unsure of the propriety of these payments. It is certain, however, that without this agent, GCI would be unable to continue its profitable business ventures in this Middle Eastern country.

Multinational companies, particularly companies operating in the developing world, frequently hire third-party agents or consultants to help them open new markets or to operate more efficiently and effectively. Outsourcing such activities is not without risk, as U.S. law can create liability for the company and its officers for the actions of third parties acting on its behalf. One area of particular risk involves potential liability under the United States' Foreign Corrupt Practices Act ("FCPA"). Under the scenario described above, GCI has reason to believe that the actions of its agent may have created FCPA liability for the company. Management is faced with critical and difficult questions, including whether the agent has caused the company to violate the law and whether GCI can continue its important relationship with the agent.

II. The FCPA's Prohibitions, Application to Agents, and Enforcement Environment

A. The FCPA Generally

The FCPA generally prohibits the payment of anything of value to foreign government officials in order to obtain or retain business, and requires certain companies to maintain books and records which accurately, and in reasonable detail, reflect the company's transactions.[1] As illustrated by the examples discussed below, U.S. corporations can be held liable for acts of foreign subsidiaries, as well as for the acts of third-party intermediaries retained by the parent corporation or its subsidiary. U.S. citizens or residents who were employed by or acting on behalf of foreign-incorporated subsidiaries can also be liable for FCPA violations.[2] Importantly, the FCPA reaches not only payments made directly by a covered person, but also *indirect* payments—those made "while knowing" that all or some of that payment will be given to a foreign government official.[3] Here, "willful blindness", is a proxy for actual knowledge on the part of the actor. Thus, a company can be held liable for the acts of its agents if the agent makes a prohibited payment and the company knew of those payments or was willfully blind to the prospect that the agent would engage in prohibited conduct on the company's behalf.

The key issue in determining whether a company was "willfully blind" is whether it was presented with "red flags" that should have given it reason to know its agent was violating or would violate the FCPA. In the scenario above, GCI was presented with several "red flags" in connection with its relationship with its Middle Eastern agent and now must decide what to do and whether the relationship with the agent can be salvaged.

B. Increased FCPA Enforcement

In recent years, the SEC and DOJ, who jointly enforce the FCPA, have dramatically increased law enforcement actions against both corporations and individuals suspected of violating the FCPA. In the first quarter of 2010, enforcement authorities brought or resolved charges against thirty-six companies and individuals. The amounts of fines and penalties in these actions has also greatly increased, as the record-setting $800 million Siemens AG settlement illustrates. Not only are corporations targeted, but the government increasingly has gone after individual officers, directors and other executives in connection with FCPA violations. For example, DOJ recently prosecuted several executives of Control Components, Inc. ("CCI"), two of whom already have pleaded guilty and agreed to prison sentences of five years.[4]

Between 2007 and 2010, authorities have brought nearly 100 enforcement actions involving the conduct of intermediaries. In the second largest enforcement matter to date, Halliburton and KBR were alleged to have paid more than $180 million dollars in "consulting fees" to two agents for use in bribing Nigerian officials.[5] The companies agreed to pay more than $579 million in criminal fines and disgorgement of profits.

III. Using Agents – Risks Under the FCPA

A. Common Examples of Liability Created by Agent Action

FCPA liability for agent actions frequently arises in two contexts. First, as with the hypothetical GCI, a company may employ an agent in good faith, yet still may face liability when the agent engages in bribery on the company's behalf. In an SEC action against Oil States International, the company's subsidiary hired an agent to assist it in complying with Venezuelan oil and gas laws and customs requirements. However, with approval of employees at the subsidiary, the agent bribed officials at the national oil company in order to ensure that the company's operations were not interrupted.[6]

The other common situation involves cases where an entity either knows of, or affirmatively aids, an agent whose sole purpose is to bribe foreign officials in order to obtain or retain business for the entity. In the *Siemens* prosecution, the company made over $1.4 billion of payments to foreign officials in various countries in order to secure lucrative contracts.[7] Money was paid by agents who were employed by the company solely for the purpose of engaging in bribery while attempting to shield the parent company from liability. This scenario often arises in countries with corrupt, autocratic regimes. For example, many companies doing business in Iraq with the Saddam Hussein regime during the United Nations' sanctions program now find themselves facing prosecution for FCPA violations. In these cases, companies paid kickbacks to Iraqi officials, often through agents who had been retained for the purpose of making and concealing these illegal payments, in order to circumvent the sanctions. In addition to corporations, several executives—and even one agent—involved in these schemes have been prosecuted.[8]

B. Willful Blindness and Red Flags

FCPA liability also may be incurred where there is a failure to make a reasonable inquiry about suspected wrongdoing. It is in this context that "red flags" raised by the actions of an agent become critical. Indeed, several FCPA enforcement actions have been based on conduct by third parties on behalf of a company, to which the company remained willfully blind.

The recent prosecution and conviction of handbag impresario Frederic Bourke illustrates the perils of willful blindness. Bourke was indicted and tried in connection with his investment of more than $8 million with Viktor Kozeny, charged with knowing Kozeny gave Azeri officials millions of dollars in cash, stock and other gifts to ensure that these officials would privatize the state oil company through a rigged auction that only members of Kozeny's investment consortium could win.[9] Although Kozeny actually paid the bribes, DOJ alleged that Bourke directed funds to Kozeny, and must have known about the bribes. At trial, the prosecutors offered evidence that Bourke "consciously avoided" learning about the bribes, namely by failing to inquire about them after being told about the payments by Kozeny's aides. The jury was instructed that they could convict if they found Bourke knew of, or took steps to avoid learning of, the payments. The jury found Bourke guilty of conspiring to pay bribes to government leaders in violation of the FCPA. [10]

C. FCPA Red Flags Involving Agents

"Red flags," when ignored, can later form the basis for a willful blindness theory of FCPA liability, and there are many examples of enforcement actions based on the existence of FCPA red flags coupled with a failure to take remedial action. These can often appear in the context of actions by agents retained to represent an entity.

i. Agent Relationships with Government Officials

The "red flag" in the GCI hypothetical above involves use of an agent who is either related to, or has a close relationship with, a government official. In the enforcement action involving Statoil ASA, a Norwegian oil and gas company, the company retained as a consultant the son of an Iranian politician influential in awarding oil and gas contracts, and agreed to pay more than $15 million in fees to the consultant, which resulted in it being awarded a lucrative oil and gas exploration contract.[11] Ultimately, the company paid a criminal fine of $10.5 million and disgorged $10.5 million in profits.[12]

Similarly, in an SEC action against Avery Dennison, the company was accused of hiring an ex-government official whose wife was still in a position of government influence.[13] Even though the company was able to discover and stop any illegal payments before they were made, this "red flag" found its way into a larger enforcement action involving the company, which eventually cost it more than $500,000 in penalties and disgorgement of profits.[14] Similarly, for Siemens, among the many allegations was that the company employed a former presidential advisor, the wife of a former president and a well-connected technical consultant.[15] Such close connections are not, in and of themselves, illegal. However, the companies discussed here had a duty to conduct further due diligence once they became aware of these risks but failed to do so.

ii. Improper or Unexplained Invoice Fees

Another common "red flag" involves invoice fees that are either clearly improper, or otherwise vague or unexplained, as with the hypothetical where GCI was invoiced for "additional assessments" and "urgent processing." In an action involving Helmerich & Payne, Inc., that company's customs brokers in Argentina and Venezuela paid nearly $185,000 in kickbacks to customs officials in order to clear their products through customs. Those bribes were vaguely described in the agent's invoices as "additional assessments," "extra costs," and "urgent processing".[16] Similarly, for AGCO Corporation—that company saw a sudden substantial increase of payments to agents in Iraq, but failed to question why the cost for providing the same historical services increased.[17] Predictably, the extra fees turned out to be kickbacks to Iraqi government officials, creating liability for the company once discovered. Failure to properly record agent and other fees can also lead to violations of the books and records provisions of the FCPA. In *Siemens*, the company transferred money to various intermediaries around the world, recording these transfers as "business consulting fees", when in reality the money was simply being funneled to foreign government officials.[18]

iii. Doing Business in "High Risk" Countries

Sometimes, the very country where a company is doing business can be a "red flag" necessitating inquiry and due diligence. In the case involving Tyco International Ltd., the SEC cited the historical reputation for official corruption and bribery present in South Korea and Brazil.[19] The SEC similarly noted in many of the "Oil for Food" complaints that the companies knew or should have known that kickbacks were a prerequisite for doing business with Iraq, yet companies nonetheless approved inflated contracts.[20] In the GCI hypothetical above, the nameless Middle Eastern country does not proclaim its "high risk," but it bears noting that of the Middle Eastern countries surveyed for Transparency International's Corruption Perceptions Index for 2009, only Qatar, UAE, Bahrain and Oman had a score in the top quartile of the 180 countries surveyed. This is a fact that any company should at least consider before engaging an agent.

iv. Failure to Conduct Adequate Due Diligence

Companies also face liability for failing to conduct adequate due diligence on third parties engaged on their behalf. Liability may be incurred where a company fails to conduct its due diligence in researching a potential agent before his or her hire, but also when that diligence does not continue during the agent's tenure.

In a case involving Baker Hughes, the company had an FCPA certification procedure in place for its agents, but was accused of failing to follow it by both failing to initially ensure that the agent complied with the company's FCPA policy, and by failing to investigate the agent's noncompliance. Similar situations were presented in the "Oil for Food" cases. For example, in *AGCO*, the company was cited for its contract with a Jordanian agent lacking FCPA language, as well as for the fact that the agent had not undergone any FCPA compliance training.[21]

Where a company has an agent certification process in place, an agent's refusal to sign a compliance agreement can also be a "red flag". However, mere certification of compliance alone is not enough to avoid FCPA liability. In the case involving Chevron Corp., the SEC accused the company of relying on an ineffective compliance certification process.[22]

D. Other Red Flags

In addition to those discussed above, various other "red flags" may present themselves in the third-party agent context, such as when an agent:

- places reliance on. or advertises his political or governmental contacts, as opposed to substantive expertise;
- is unwilling to agree to certify compliance with the FCPA or other laws and company policies, including subjecting subject its books and records to audit by the company;
- wants to use anonymous subcontractors or keep the engagement secret;
- wants payment through suspicious means, possibly to a foreign-located bank account or in a non-local currency;
- has a poor reputation, or there are rumors of prior improper payments, other unethical business practices, or has been investigated for, charged with, or convicted of corruption allegations; or,
- is listed in databases cataloging known corruption risks like the World Bank List of Debarred Firms or the Specially Designated Nationals list.

IV. Dealing with "Red Flags"

Responding to "red flags" can be difficult, as adverse action against the agent is often fraught with peril. The agent may be a valuable consultant and formal discipline could expose the company to legal liability or increase government scrutiny, even where there is ultimately no wrongdoing. Disciplining or terminating an agent may also trigger reporting obligations, because in any subsequent litigation or governmental investigation, the act may also be considered an admission. Ultimately, the decision of whether to terminate a third party consultant is difficult, and should be governed by the facts and circumstances of each particular case. A company should tailor its response to allegations of misconduct to the specific context and factors present in each situation, and should carefully consider whether the agent should be disciplined or terminated.

In evaluating its response, a company should keep several factors in mind. First, determine which "red flags" are present and, after vigilantly identifying potential suspicious circumstances, evaluate their seriousness. Certain "red flags," such as refusing to certify compliance with FCPA compliance policies, are so severe that they often require termination of the relationship. Others, such as relations to government officials, merely require additional investigation and evaluation. Also consider whether this is the first time the agent has come under scrutiny. If not, it may be advisable to conduct a more detailed review than would be called for by the allegations themselves. Finally, consider any countervailing factors which suggest a legitimate interpretation of the conduct. In the hypothetical involving the unexplained fees, it is possible they are legitimate expenditures. Additional inquiry into the nature of the conduct allows for better understanding of the conduct.

Any response should be proportionate to the seriousness of an offense, the extent to which the agent was put on notice that the conduct at issue was contrary to company policy, and the need to protect the company from liability. Sometimes, a company should suspend the relationship for some time, pending further investigation. Other times, it is appropriate to respond with additional training on internal compliance policies. Other remedial measures may include compliance or financial audits, compliance certifications from the agent and from end-users, and even additional due diligence investigations into the circumstances of a violation. Where there have been clear indications of violations of the law, it may be appropriate to terminate the agent. Given the implications of such an act, including on the ability to access information needed to conduct a thorough investigation of the alleged wrongdoing, the timing of termination should be considered.

How wrongdoing is dealt with is frequently a consideration by the government in evaluating whether to bring an enforcement action and potential penalties. For example, in *Oil States*, discussed above, the company's prompt investigation and remedial action, including termination of the agent and disciplining of several employees, was one reason the SEC decided to forego disgorgement and fines.[23]

In the GCI hypothetical above, there are several key issues the company must consider before determining whether it can "save" its agent.

1. First, GCI should evaluate the "red flags" present:
   - It should understand its agent's government relationships, including whether any of these could have an effect on GCI's business.
   - It should also understand specifically what the questionable payments were for. What exactly was the "urgent processing" fee, why did it cost $5,000, and was that amount reasonable and customary?
2. Next, GCI should investigate if other "red flags" are present by:
   - Reviewing the due diligence performed on the agent at the time of engagement and the agent's compliance history;
   - Interviewing the agent, and analyzing its conduct in light of the FCPA, local law and practice;
   - Interviewing any of its employees who interact with the agent to assess whether there is any conduct that could potentially create liability under the FCPA; and,
   - Reviewing payments to the agent, including an assessments and analysis of fees paid.
3. After investigating, GCI should evaluate whether the agent's conduct will subject it to FCPA liability.
   - If the thorough internal investigating finds a proper basis for the expenditures, no indication of improper payments to government officials and no other red flags, GCI should be able to continue its relationship with the agent.
4. Even if the agent can be "saved," GCI should nevertheless ensure its agent's ongoing FCPA compliance. This includes mandating FCPA compliance training and certification and periodic monitoring/auditing of the agent's compliance.
5. Finally, as described below, GCI should update its compliance program to ensure future compliance with the FCPA.

V. Importance of FCPA Compliance Programs

In the hypothetical, how could GCI have better insulated itself from potential FCPA liability? Preventing agents from engaging in improper activity cannot always be controlled. What can, however, is the effectiveness of FCPA compliance programs, which is a factor considered by enforcement authorities in assessing penalties for FCPA violations. An effective compliance program begins with a clearly articulated corporate policy prohibiting violations of the FCPA and other applicable anti-corruption laws. It also should reflect the promulgation of a compliance code, standards, and procedures designed to detect and deter violations of the FCPA and other anti-corruption laws, and should otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance.

In addition, effective compliance policies should require officer, director, employee and agent training and certification of FCPA compliance. There should also be at least one senior corporate officials within the organization with day-to-day responsibility for the implementation and oversight of FCPA policies, standards and procedures. The program should also include an effective system for reporting violations, policies that allow an effective response to possible violations, and appropriate disciplinary procedures.

In situations involving third-party consultants, corporate compliance programs should include additional provisions, including pre-retention due diligence, designed to: (1) weed out agents likely to make bribes or are otherwise unsuitable for the job contemplated; (2) document the basis for hiring decisions, and (3) in the event of a violation, establish that the company adequately vetted the agent to forestall any claims of willful blindness.

A company should also secure, in writing, the agent's pledge to abide by the company's FCPA compliance policies. It may also be advisable to require annual certifications of FCPA compliance from key agents, distributors, joint venture partners, and employees. A company's FCPA compliance policy should also allow for both post-retention oversight of third-parties and the maintenance of complete records and files relating to such due diligence and oversight. Contracts with agents should also include provisions that are reasonably calculated to prevent and detect FCPA violations. These provisions may, depending on the circumstances, include: (a) representations and undertakings relating to compliance with the FCPA; (b) the right to conduct audits of books and records; and (c) termination rights if there is any breach of any anticorruption law or a breach of representations and undertakings related to such matters, including the ability to disclaim and reverse any economic benefit that would otherwise be received based on the actions of the third-parties. Additionally, it may be advisable to consider contract clauses establishing an agent as an independent contractor and reserving the company's right to review the third-party's retaining of subcontractors. Finally, the program should call for regular compliance training, including the training of agents, distributors, consultants, and other representatives in order to assure FCPA compliance.

Ultimately, in the GCI hypothetical above, the determination of whether the company can "save" its agent will be resolved only after a thorough examination of the circumstances and a proper remedial plan has been tailored. However, the discussion here provides best practices with which the company can insulate itself against FCPA liability for the actions of its agent abroad.

The authors are attorneys in the White Collar Practice Group of Foley & Lardner LLP. They have conducted numerous FCPA internal investigations in Asia, Africa, the Middle East, South America and Europe and routinely advise corporations on matters involving FCPA compliance.

---

[1] In addition to the antibribery provisions, the FCPA also contains provisions imposing requirements with respect to record-keeping and accounting practices. These provisions apply to all issuers having securities that are registered with the SEC.

[2] 15 U.S.C. §§ 78dd-1(g) to -2(i). Even issuers who own only a minority share in a corporate entity can be held liable for an FCPA violation if they failed to use good faith to use their influence to cause that entity to maintain books, records and accounting controls pursuant to the standards set forth in the FCPA. 15 U.S.C. § 78m(b)(6).

[3] 15 U.S.C. §§ 78dd-1(a)(3), -2(a)(3), -3(a)(3). The definition of "knowing" under the statute is available at 15 U.S.C. §§ 78dd-1(f)(2), -2(h)(3), -3(f)(3). The standard is drawn from the Supreme Court's test for "willful blindness," which is satisfied if the defendant "is aware of a high probability of [a fact's] existence, unless he actually believes that it does not exist." *Leary v. United States*, 395 U.S. 6, 23 (1969), *cited in United States v. Reyes*, 302 F.3d 48, 54 (2nd Cir. 2002).

[4] Plea Agreement, *United States v. Covino*, No. 08-336 (C.D. Cal. 2008); Plea Agreement, *United States v. Morlok*, No. 09-00005 (C.D. Cal. 2009).

[5] *See* SEC Press Release No. 2009-23, SEC Charges KBR and Halliburton for FCPA Violations (Feb. 11, 2009).

[6] Cease-and-Desist Order, Exchange Act Release No. 53,732 at 4 (April 27, 2006), available at http://www.sec.gov/litigation/admin/2006/34-53732.pdf.

[7] *SEC v. Siemens Aktiengesellschaft*, No. 08-cv-02167 (D.D.C. 2008).

[8] *See* Complaint, *SEC v. Turner*, No. 10-cv-01309 (D.D.C. 2010).

[9] *See* DOJ Press Release No. 09-210, Connecticut Investor Found Guilty in Scheme to Bribe Government Officials in Azerbaijan (July 10, 2009), available at http://www.justice.gov/usao/nys/pressreleases/July09/bourkefrederickverdictpr.pdf.

[10] *See* DOJ Press Release No. 09-1217, Connecticut Investor Frederic Bourke Sentenced to Prison for Scheme to Bribe Government Officials in Azerbaijan (Nov. 11, 2009), available at http://www.justice.gov/opa/pr/2009/November/09-crm-1217.html.

[11] Complaint at 3-8, *United States v. Statoil, ASA.,* No. 06-cr-00960 (S.D.N.Y. 2006).

[12] *See* DOJ Press Release No. 06-700, U.S. Resolves Probe Against Oil Company that Bribed Iranian Official (Oct. 13, 2006), available at http://www.justice.gov/opa/pr/2006/October/06_crm_700.html.

[13] Complaint at 3-4, *SEC v. Avery Dennison Corp.,* No. 09-cv-05493 (C.D. Cal. 2009).

[14] *Id.* at 4.

[15] Complaint at 15, 20, 25, *SEC v. Siemens Aktiengesellschaft*, No. 08-cv-02167 (D.D.C. 2008).

[16] Cease-and-Desist Order, Exchange Act Release No. 60,400 at 4 (July 30, 2009).

[17] Complaint at 8, 11, *SEC v. AGCO Corp*., No. 09-cv-01865 (D.D.C. 2009).

[18] Complaint at 2, *SEC v. Siemens Aktiengesellschaft*, No.08-cv-02167 (D.D.C. 2008).

[19] Complaint at 18-19, *SEC v. Tyco International Ltd.,* No. 06-cv-02942 (S.D.N.Y. 2006).

[20] *See, e.g.,* Complaint at 8-9, *SEC v. AGCO Corp*., No. 09-cv-01865 (D.D.C. 2009).

[21] *Id.* at 11.

[22] Complaint at 9-10, *SEC v. Chevron Corp.*, No. 07-cv-10299 (S.D.N.Y. 2007).

[23] Cease-and-Desist Order, Exchange Act Release No. 53,732 at 5 (April 27, 2006).