The FOREIGN

Mitigating Bribery &

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"We are on the cusp of a new era where the rising pressures on bribe takers and bribe payers will become increasingly evident to growing numbers of people across the world. This will provide vital encouragement to support civil society action, law enforcement, and positive political change."

Frank Vogl, Transparency International in "Waging War on Corruption"

CORRUPTION IS EXPENSIVE, both financially and politically. It throttles development and stifles the economy by diverting public resources to private interests. It undermines the rule of law and enables corrupt leaders to entrench themselves in office—sometimes for decades. Corruption also creates an unfair marketplace by driving up prices and granting business advantages to dishonest politicians and businesses.

As the world reacts more and more forcefully to corruption blight, the price for those directly or indirectly involved in corruption-related investigations can be high—costing millions if not billions of dollars, in legal, financial and reputational costs.

Fighting corruption globally is a U.S. enforcement priority. The Foreign Corrupt Practices Act (FCPA) was enacted in 1977 (codified at 15 U.S.C. §§ 78dd-1, et seq.), but the last 9 years have witnessed an explosion in FCPA enforcement actions, with 325 prosecutions from 2005 through June 2014, compared with prosecutions in the single digits in prior years (Gibson Dunn, 2014 Mid-Year FCPA Update (July 7, 2014)). Law enforcement is also increasingly focused on holding individuals accountable for FCPA violations. As out-going Attorney General Eric Holder noted, the focus on individuals is important to fighting corruption because "corporate misconduct must necessarily be committed by flesh-and-blood human beings." (Hale, Christopher, *JDSupra Business Advisor*, "Recent Remarks by Officials Reinforce DOJ's Focus on Criminal Fraud Investigations and Prosecutions of Culpable Individuals").

CORRUPT PRACTICES ACT

Corruptions Risk in Financial Institutions

The significance of FCPA enforcement actions is not just in their numbers, but also in their incredible scope. The FCPA's jurisdictional scope extends to activity occurring outside the U.S. by non-U.S. persons. It also has resulted in actions targeting a range of industries from banking and nonbanking financial services, agriculture and entertainment, technology, health care, and consumer goods. As of September 2014, approximately 104 different companies disclosed on-going DOJ and SEC investigations targeting corruption activity in at least fifty different countries, led by China, Brazil, Russia, and India. (The FCPA Blog, "The Corporate Investigations List" and "Country Count for the Corporate Investigations List", October 2014.)

This article provides an overview of the FCPA's main provisions and broad jurisdictional reach; discusses the activities it prohibits; explains how U.S. financial institutions and their employees, globally, are exposed to FCPA risk; and explains how financial institutions can mitigate their legal, financial, and reputational bribery and corruption risk.

While a financial institution may not be able to control every action of their employees and third parties, it can educate its employees and third parties that bribery is prohibited, and they can create controls making it difficult to engage in bribery.

The Scope of the FCPA

The Foreign Corrupt Practices Act was enacted in response to public corruption concerns in the U.S. (e.g. the Watergate scandal) and overseas. By enacting the FCPA, the U.S. sought to preserve its credibility in the marketplace and promote ethical business practices with its economic and political allies, especially those in developing countries.

The FCPA has two main sections: the anti-bribery provisions and the accounting provisions.

Anti-Bribery Provisions

The FCPA makes it illegal to offer, pay, promise, authorize, solicit, or receive the payment of money or anything of value to or from officials of foreign governments with the intent to secure an improper advantage or obtain or retain business (15 U.S.C. §78dd-1; Resource Guide at 10). Even if the bribe is not made, or the recipient refuses the bribe, the FCPA can be violated.

U.S. Financial Institutions' Exposure to FCPA Risk

The anti-bribery provisions have broad jurisdictional reach, and apply to issuers, domestic concerns, and individuals and entities transacting within U.S. territorial jurisdiction. "Issuers" are U.S. or foreign companies with securities listed on a U.S. stock exchange or that are otherwise subject to SEC registration and filing requirements (15 U.S.C. § 78dd-1). Thus, foreign institutions with securities publicly traded in the United States fall under the FCPA's purview. "Domestic concerns" include U.S. citizens, nationals or residents, or corporate entities organized under U.S. laws or located in the United States (15 U.S.C. § 78dd-2). Officers, employees, agents, or stockholders of issuers, and domestic concerns, even where not physically present in the U.S., fall under the FCPA's jurisdiction. For example, a non-U.S. citizen working for a U.S. financial institution and living outside the U.S. is subject to the FCPA.

The FCPA also extends to persons and entities that engage, directly or indirectly, in any act in furtherance of a bribe within the U.S. or U.S. territories (15 U.S.C. § 78dd-2). An act in furtherance of a bribe can include the following:

- Telephone calls;
- Emails;
- Text messages;
- United States Postal Service mail;
- Wire transfers to or through a U.S. bank account (e.g. SWIFT transfers); and
- Travel across U.S. borders.

For example, in 2013 German company Bilfinger SE paid $32 million to resolve charges that it violated the FCPA, where its U.S. nexus stemmed from 1) a flight by a Bilfinger employee from Houston to Boston to discuss bribe payments and 2) a wire transfer from Houston to Bilfinger in Germany relating to the bribery. (Deferred Prosecution Agreement, *U.S. v. Bilfinger*, (S.D. Tex. Dec. 9, 2013)).

The FCPA's expansive jurisdictional reach to foreign companies and individuals—even those with minimal U.S. contacts—presents direct corruption risk to U.S. financial institutions serving foreign customers that maintain foreign offices. U.S. financial institutions can be exposed to corruption risk if they facilitate, aide, or abet foreign customers engaged in corruption through, for example, bank loans, project finance or joint venture projects. U.S. financial institutions can also be exposed to FCPA risk through the acts of their employees, globally, who may engage in bribery either as a bribe giver or a bribe recipient.

What is a Bribe?

Under the FCPA, a bribe is a payment of money or anything of value offered or provided with the intent to improperly influence a foreign official to obtain or retain business. A bribe can encompass literally *any* thing the recipient finds valuable, including money, gifts, travel accommodations, discounts, offers of employment or internships, tickets to sporting events, entertainment, side-trips on a business trip, charitable contributions, invitations to conferences/seminars, free use of property or goods, discounts and perks, and access and influence.

Whether a "thing of value" is provided with the intent to improperly influence a foreign official, depends on the facts and circumstances. The size and frequency with which a "thing of value" is given, along with cultural context, are important factors in determining whether a "thing of value" is a bribe.

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Gifts, Travel, and Entertainment

While companies often pay legitimate business expenses for clients related to gifts, travel, and entertainment, a number of FCPA prosecutions have involved companies that provided inappropriate gifts, travel, and entertainment to foreign officials to further business relationships. Recent enforcement actions included bribe payments in the form of sports cars, fur coats, country club membership fees, and all-expense paid holiday trips for officials and their wives.[1] Indeed, a string of FCPA prosecutions related to gifts, travel, and entertainment have severely crimped the willingness of a number of large financial institutions to provide these kinds of business expenses, including box seats at important sporting events (e.g. the World Cup) or conferences at lavish resorts.

"Foreign Official"

The FCPA prohibits bribes made to "foreign officials," a term broadly defined to include government employees at all levels (e.g. customs officials, finance ministers, heads of state); employees of public international organizations (e.g. the World Bank, International Monetary Fund, or the United Nations); representatives of political parties and candidates for office; and employees of entities that are wholly or partially state-owned, such as public utility companies, sovereign wealth funds, public oil and transportation companies, pension funds and hospitals (15 U.S.C. § 78dd-1(f)(1)(A)).

While bribes made to individuals that are not "foreign officials" do not violate the FCPA, U.S. financial institutions nevertheless face corruption risk and liability through prosecution of other laws including the Travel Act (18 U.S.C. §1952), state corruption laws, and foreign anti-bribery laws.

Obtaining or Retaining Business

The FCPA applies to corrupt payments intended to achieve a business purpose. Thus bribes violate the FCPA when they are made to gain an improper business advantage, such as favorable tax treatment, reducing or eliminating customs duties, receiving discounts on government contracts, circumventing licensing or permit requirements, preventing competitors from entering the market, or preferred market status.[2]

Facilitation Payments

Congress created a narrow exception in the FCPA for payments made for the purpose of expediting or securing "the performance of routine governmental action" (5 U.S.C. § 78dd-1(b)). "Routine governmental action" refers to non-discretionary acts ordinarily and commonly performed by a government official and involve services like processing visas and passports; obtaining permits, licenses or other official documents required to conduct business; scheduling inspections associated with contract performance or transit of goods; and providing phone service, power and water supply (U.S.C. § 78dd-1(f)(3)(b)).

However, a payment made to encourage an official to misuse his position or office (e.g., ignore a company's failure to secure proper permits or licenses) is not a facilitation payment. Similarly, payments made to reduce or eliminate customs fees, a non-routine governmental action, are bribes though a payment to expedite processing through customs, and may be considered a facilitation payment. Facilitation payments, though, should be made with caution as the vast majority of other countries' anti-bribery laws, such as the U.K. Bribery Act, do not permit facilitation payments.

Third-Party Bribe Payments and Agency Liability

Under the legal theory of agency, U.S. financial institutions can be liable under the FCPA for bribe payments made, directly or indirectly, by third-party agents (e.g. finders, consultants, business partners, or joint venture partners) acting on the bank's behalf (15 U.S.C. § 78dd-1(a)(3)).

If a financial institution knows, has reason to know, or fails to conduct sufficient due diligence that would have revealed the third-party agent is likely to engage in bribery on the bank's behalf, the bank may have FCPA criminal liability. Thus, where third-parties pay bribes when they are hired to seek out business opportunities or facilitate transactions with foreign officials on the bank's behalf, liability for those bribes can be imputed to the bank.

Similarly, U.S. financial institutions can be held liable for the acts of their employees under the same agency theory. This is the case even where the company did not have actual knowledge of the employee's corrupt activity. As discussed further below, companies may be able to protect against liability from their employees' corrupt activity if they implement effective internal compliance controls.

Accounting Provisions

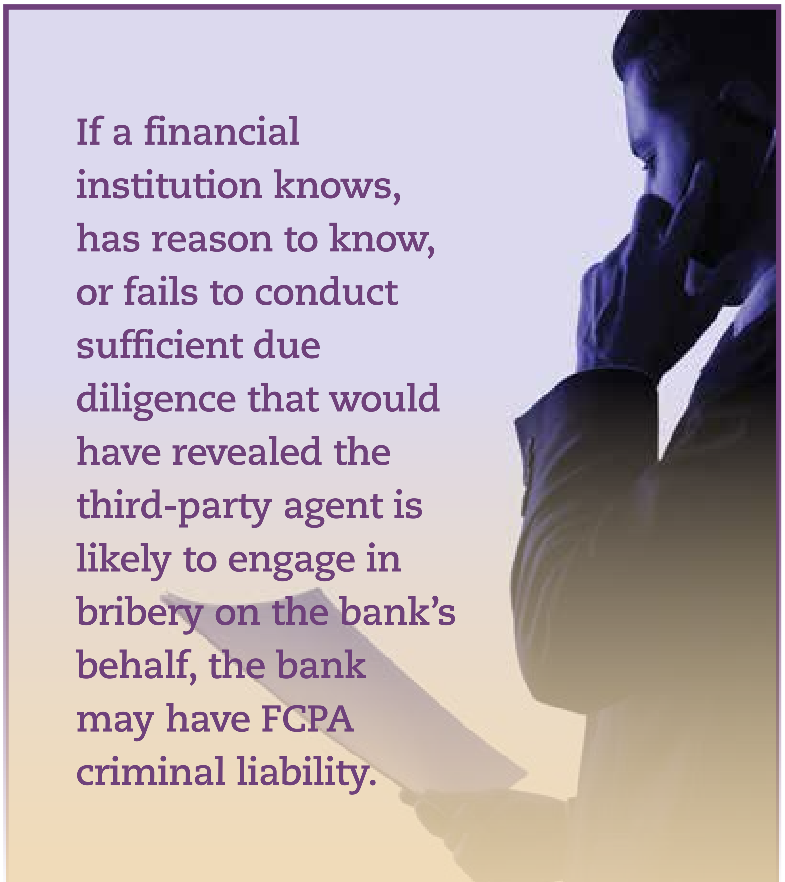
The anti-bribery provisions of the FCPA are supplemented by accounting and internal controls requirements for issuers. These are referred to as the "accounting provisions," and divided into the "books and records" provision and the "internal controls" provision.

Violations of the accounting provisions are generally easier to prove than violations of the anti-bribery provisions because there is no requirement that a false record or deficient control be linked directly to an improper payment. Rather, a company can be prosecuted for a payment under the accounting provisions if it is inaccurately recorded or attributable to a deficiency in internal controls.

Under the books and records provisions, companies may be liable for bribery activity—even where an anti-bribery violation cannot be proven—if a company does not identify a bribe payment as a "bribe" in its books and records (Resource Guide at 39).

Terms that may be used to mischaracterize bribes in books and records include:

- Commissions;
- Consulting Fees;
- Sales and marketing expenses;
- Miscellaneous expenses;
- Write-offs;
- Rebates/discounts; and
- Travel or entertainment expenses."



The internal controls provision requires companies to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that financial reporting and financial statements are reliable (15 U.S.C. § 78m(b)(2)(B)). The statute does not indicate the types of controls that should be implemented; rather, U.S. financial institutions should develop and maintain risk-based controls, including a compliance program to mitigate bribery risk. The failure to implement an adequate and effective anti-bribery compliance program can underpin an internal controls prosecution even where no actual bribery is alleged.

The internal controls provision is a powerful enforcement tool. A violation of this provision is a strict liability offense; the government does not need to prove that anyone at the company knew of the controls deficiency, only that there was a deficiency. For these reasons, the risk of a charge based on the internal controls provision alone should compel financial institutions to proactively police themselves against bribery activity.

Civil and Criminal Penalties

The FCPA is civilly and criminally enforced by the U.S. Securities and Exchange Commission (SEC) and the Department of Justice (DOJ). The DOJ may bring both criminal and civil charges against individuals and entities for FCPA violations. For each anti-bribery provision violation, corporations are subject to a $2 million fine, and individuals are subject up to $100,000 and 5 years in prison. For each violation of the accounting provisions, the DOJ may request a fine up to $25 million for corporations and up to $5 million for individuals and 20 years imprisonment.

For accounting provision violations, the government may assess a penalty that does not exceed the amount of the pecuniary gain to the defendant, or another amount based on the egregiousness of the underlying conduct. Penalties range from $7500 to $150,000 for an individual and up to $750,000 per violation for a company.

For any FCPA violation, individuals and companies may be barred from doing future business with the federal government, as well as other public organizations such as the World Bank.

Financial and Reputational Risk

In addition to the legal liability U.S. financial institutions face with FCPA violations, banks also face financial and reputational risk resulting from even just an allegation of bribery. Financial and reputational risk fall-out from bribery allegations may take the form of legal fees from external counsel hired to investigate the allegations, compliance costs to remediate internal control failures, plummeting stock prices, and the loss of future contracts and business opportunities. The financial and reputational impact of bribery allegations is well-illustrated by the FCPA investigation into Walmart. Even though no formal charges have been brought (and may never be brought), Walmart has reported spending over $400 million just investigating allegations of bribery in foreign jurisdictions and building out its anti-bribery compliance program to meet regulatory expectations.[3] In addition, the mere allegations of corrupt activity can trigger shareholder suits accusing company officers and directors of breaching their fiduciary duty by failing to identify and respond to bribery red flags. Such suits stemming from FCPA investigations were recently filed against Walmart and Hewlett Packard.[4]

Mitigating Bribery Risk

Given the potential detrimental consequences of bribery allegations—let alone actual litigation and settlements costs—anti-bribery compliance makes good financial sense. For U.S. financial institutions, implementing an anti-bribery compliance program is vital. When determining whether to prosecute a company, and the appropriate fine to be levied against it, law enforcement considers whether the company had an effective compliance program in place at the time the violation occurred.

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At a minimum, an effective anti-bribery compliance program must:

- Demonstrate commitment from senior management and institute a clearly articulated policy against bribery and corruption;
- Incorporate written procedures and internal controls that are reasonably designed to assure compliance with the FCPA, which may include due diligence, risk assessments, and incentives and disciplinary measures for policy violations;
- Provide appropriate training and education to personnel; and
- Provide for independent reviews or audits of the program.

Developing and implementing an anti-bribery specific compliance program significantly reduces a financial institution's FCPA risk by:

- Proactively preventing and detecting bribery;
- Protecting against a potential internal controls violation; and
- Potentially shielding the financial institution from FCPA liability, stemming from rogue employees who engage in bribery.

The prosecution of a former Morgan Stanley managing director illustrates the importance and effectiveness of implementing an anti-bribery compliance program, as protection against liability. In 2012, for the first time in an FCPA-related case, the DOJ declined to prosecute Morgan Stanley even though a managing director in its China offices engaged in an on-going and systematic bribery scheme with a Chinese official. Although Morgan Stanley could have been held liable for the managing director's acts under an agency theory, the DOJ found that Morgan Stanley had implemented an adequate and effective anti-bribery compliance program at the time the bribery occurred. The DOJ also found that the employee purposefully and intentionally violated the company's anti-bribery policies and procedures, and that Morgan Stanley frequently trained its employees, including the manager director, on its internal anti-bribery policies and procedures, as well as the FCPA and other anti-bribery laws. Morgan Stanley trained various groups of Asia-based personnel on anti-bribery policies 54 times; and Morgan Stanley trained the managing director on the FCPA seven times and reminded him to comply with the FCPA at least 35 times. In addition, Morgan Stanley fully cooperated with the investigation and did not have a history of engaging in such activity.[5] The managing director, on the other hand, was criminally charged with FCPA violations. He pled guilty and was sentenced to nine months in prison.

Conclusion

While FCPA prosecutions are costly from a legal, financial, and reputational perspective, proper anti-bribery compliance controls can significantly reduce these risks. Given the broad reach of the FCPA, U.S. financial institutions are exposed to great bribery risk through the acts of their employees and others engaging in business on their behalf. While a financial institution may not be able to control every action of their employees and third parties, it can educate its employees and third parties that bribery is prohibited, and they can create controls making it difficult to engage in bribery. Thus, having a robust compliance program to prevent and detect corruption and bribery is your best defense against legal, reputational, and even financial risk.

Former U.S. Deputy Attorney General Paul McNulty put it best when he said, "If you think compliance is expensive, try noncompliance." ■

For U.S. financial institutions, implementing an anti-bribery compliance program is vital.

Endnotes

[1] *See e.g.*, Complaint, *SEC v. RAE Sys. Inc.*, No. 10-cv-2093 (D.D.C. Dec. 10. 2010) (fur coat); *Daimler, supra* n. 16 (€300,000 armored Mercedes Benz vehicle).

[2] *See Kay,* 359 F.3d; Complaint, SEC v. Panalpina, Inc., No. 10-cv-4334 (S.D. Tex. Nov. 4 2010); Criminal Information, *U.S. v. Panalpina, Inc.*, No. 10-cr-765 (S.D. Tex. Nov. 4, 2010), *available at* http://www.justice.gov/criminal/fraud/fcpa/cases/panalpina-inc/11-04-10panalpina-info.pdf (last visited Aug. 4, 2014).

[3] Voreasco, David and Dudley, Renee, "Walmart Says Bribe Probe Cost $439 Million in Two Years," Mar. 26, 2014 *at* http://www.bloomberg.com/news/2014-03-26/wal-mart-says-bribery-probe-cost-439-million-in-past-two-years.html (last visited Oct. 28, 2014).

[4] Rubenfeld, Samuel, WSJ Blogs Corruption Currents, "Walmart Discloses Shareholder Lawsuits Detail," June 4, 2012, *at* http://blogs.wsj.com/corruption-currents/2012/06/04/wal-mart-discloses-shareholder-lawsuits-detail/ (last visited Oct. 28, 2014).

[5] DOJ, Press Release, Former Morgan Stanley Managing Director Pleads Guilty for Role in Evading Internal Controls Required by FCPA (Apr. 25, 2012), *available at* http://www.justice.gov/opa/pr/2012/April/12-crm-534.html (last visited Aug. 4, 2014).

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