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U.S. Foreign Corrupt Practices Act

An Open Forum with

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Introduction

The Foreign Corrupt Practices Act (FCPA) is not a new law, yet more and more companies are running afoul of the law. Enacted in 1977, the FCPA requires all companies under United States jurisdiction to provide accounting transparency and imposes sanctions on liable companies and individuals who engage in corrupt practices overseas.

In recent years the Unites States government has dramatically increased its efforts to enforce the law, which is jointly administered by the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC). According to a year-end-review released by Gibson, Dunn & Crutcher earlier this year, enforcement actions reached the second-highest level in the 34-year history of the FCPA, with a total of 48 cases.

To shed a light on how this crucial act really works, on September 17, 2012, USINDO hosted an Open Forum with Mr. Danforth Newcomb, a renowned and experienced expert on the enforcement of the FCPA. Amidst the solid attendance of many American and Indonesian companies, Mr. Newcomb presented his insights on the origin, significance, and provisions of the FCPA, as well as the effective compliance program that all companies can implement to avoid the unnecessary risk of prosecution.

This brief is USINDO's summary of his talk.

The Early Debate and Further Development of the FCPA

The precursor for the introduction of the Foreign Corrupt Practices Act (FCPA) first emerged in the form of public outcry as a response to the Watergate Scandal in 1970s, where American companies used their money to pay bribes to foreign governments and officials. To prevent further bribery of foreign officials and restore public confidence in the integrity of the American business system, President Jimmy Carter signed the FCPA into law on December 1977.

This initiative was later followed globally by the adoption of similar acts in many countries and regions in the world. The early adoption of the FCPA, however, clearly implies that the United States has the most extensive experience in combating the corporate bribery of foreign officials. It is therefore important to learn what those extensive experiences mean in terms of its level playing field and the development of this corporate anti-bribery initiative into a globally acknowledged necessity.

In the wake of its introduction, there were loud oppositions towards the legalization of the FCPA in the United States. Those objections were essentially understandable considering that the United States was the first and only country at that time that proclaimed 'Don't pay a bribe over there!' while other countries had not thought about the notion. The passage of the FCPA led many American companies to assert that the FCPA caused them to operate at a huge disadvantage compared to foreign companies who routinely paid bribes. In some countries, foreign companies were even permitted to deduct the cost of such bribes as business expenses on their taxes. The American companies were legitimately concerned that they could not compete at an equal level with other companies, given the limitation from the FCPA.

Those oppositions, however, could not put an end to the adoption of the FCPA – which only further highlights the significance and moral weights carried by this Act. The information surrounding the Watergate Scandal was heavily perceived by the Congress as a national embarrassment. In that context, the Congress believed that corporate bribery had a foreign policy implication, in the sense that it lent credence to the suspicion sown by foreign opponents of the United States that American enterprises exert a corrupting influence on the political process of their nations. The payment of bribes to influence the acts or decisions of foreign officials is unethical. It is counter to the moral expectations and values of the American public. In addition to this moralistic view, the adoption of the FCPA is also significant because the exposure of such activity could also have negative consequences for

the company involved. It could damage the image of a company, lead to costly lawsuits, and cause the cancellation of business contracts overseas.

In 1988, resistance toward the FCPA continued as the administration of President Ronald Reagan tried to repeal the Act. The opposing effort once again failed. But as a response to those lingering concerns, the United States began negotiations with the Organization for Economic Co-operation and Development (OECD) to obtain agreement of the United States major trading partners to enact laws similar to the FCPA. It marked the initial effort by the United States to encourage global adoption of the Act.

The efforts finally saw their first major development in 1997 when 33 member countries of the OECD agreed to sign the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, also known as the OECD Treaty. One year later, countries in Europe also followed the trend by adopting the European Treaty in 1998. In 2003, the latest wave prevailed with the legalization of the United Nations Treaty and African Treaty, indicating the expansive adoption of a corporate anti-bribery act in the true sense of global involvement.

The Provisions and Technicalities of the FCPA

As amended in 1998, the FCPA prohibits companies from making an offer or promise to pay money or anything of value to foreign officials for the purpose of obtaining or retaining business. Anything of value may be interpreted broadly to include travel, gratuities, physical gifts, and even charitable contributions, with no minimum amount of the payment. “Foreign official” is then defined as any officer or employee of a foreign government or any department, agency, and instrumentality, or any person acting in an official capacity for or on behalf of any such government or department, agency, and instrumentality. By this definition, scope of government officials thus varies by each country. As an example, doctors in China are locally considered as government officials.

Furthermore, the jurisdiction of FCPA applies broadly to American companies and individuals, companies that have issued securities registered in the United States, employees and agents or intermediaries of American companies, as well as foreign nationals and businesses that cause prohibited acts in the United States. Companies whose securities are listed in the United States are required to meet the accounting provisions of the Act. Those provisions require all companies under the jurisdictions of this Act to keep books and records that accurately and fairly reflect all business transactions, and to devise and maintain an adequate system of internal accounting controls.

The penalty for companies that violate the FCPA may vary in each case and mostly depend of the amount and scale of bribery involved. But generally in most cases, the penalty for companies and individuals that violate the Act is described in the table below.

FCPA Penalties		
	Corporations	**Individuals**
Criminal (prosecuted by DOJ)	Fines - $2 mil./ Twice Gain, No Gov. Contacts, Monitor	Prison, Fines - $2 mil, Probation
Civil (prosecuted by SEC)	Fines $25 mil, Disgorgement, Injunctions, Monitor	Fines $5 mil, Injunctions, Employment Bar

The table below further shows a comprehensive statistic of the most renowned FCPA cases that involve big-scale companies with a significant amount of penalty.

Top Criminal and Civil Penalties		
Matter	**Description**	**Fine and Civil Penalties**
Siemens (2008)	Payments through business consultant, payment intermediary, and other third parties	$800 million (+ € 596 in Germany)
Halliburton/ KBR (2009)	Payments through business consultant	$579 million
Magyar Telekom (2011)	Payment through business consultants and intermediaries	$95.8 million
Baker Hughes (2007)	Payments through business consultant	$44 million
Willbros (2008)	Payments through business consultant	$32 million
Chevron (2007)	Payments through sales intermediary	$30 million
Titan (2005)	Payments through business consultant	$28 million
Vetco Grey II (2007)	Payments through customs broker	$26 million
Biomet, Inc. (2012)	Payments through distributor	$22.9 million

Lockheed II (1994)	Payment to official's spouse	$22 million
Volvo (2008)	Payments through distributor	$19 million
CCI (2010)	Travel and entertainment and education expenses paid directly to government officials, other direct payments	$18.2 million
Lucent (2010)	Travel and entertainment expenses paid directly to government officials	$2.5 million

The above table shows that most of the top FCPA penalties involve intermediaries such as consultants and agents, which clearly suggest the need to carefully check and monitor the third party. It also factually indicates that SEC and DOJ have taken serious efforts and measures to uphold the FCPA, and boldly proceeded with the prosecution of companies that violate its provisions.

There are, however, two circumstances of affirmative defenses in which acts otherwise prohibited by the FCPA will not constitute a punishable violation. These affirmative defenses will shield the payer if the otherwise illegal payment was 1) lawful under the written laws and regulations of the recipient's country or 2) a reasonable and bona fide expenditure, such as travel and lodging expenses incurred by or on behalf of the recipient and directly related to product promotion, demonstration or explanation, or the execution or performance of a contract with a foreign government.

In other words, there must be a valid business reason for the payment other than to influence the recipient in favoring or awarding business to the payer. The burden of proof for the affirmative defenses is with the person or entity that has been charged with a violation of the FCPA, i.e. that the payment met the requirements of the affirmative defenses. A single violation of the anti-bribery provisions of the FCPA may place more than one person/entity in criminal and civil jeopardy. The business entity, as well as its officers, directors, employees, agents, or shareholders acting on behalf of the entity, may be penalized for a violation of the FCPA.

Avoiding the Risk: Internal Control by Implementing Effective Compliance Program

Realizing the severe consequences of violating the provisions of the FCPA, it is thus essential to carefully plan a proper precautionary measure in the form of effective compliance program. In developing an effective compliance program, management needs to design processes, tests, and systems that provide ongoing knowledge that the organization's anti-bribery efforts are operating as expected. Designing a system of controls that should work, but aren't operating effectively, is no defense in this case.

In every company, an effective compliance program should be implemented to ensure that information relating to critical areas of the organization's activities can be relied on. It must be applied to every key business function a company conducts: financial, regulatory, and operational. Under the FCPA requirements, the program needs to address all these aspects as they relate to anti-bribery and anti-corruption practices. Management needs to know that the company is in compliance with the FCPA requirements, that its employees are behaving appropriately and that the financial books and records properly and accurately record the company's transactions. Hiring experts to help design and implement well thought out internal control environments is often the surest means of obtaining quick and effective results.

In determining how to design internal controls to address the provisions of the FCPA, management should consistently keep these seven elements in mind:

1) Establish compliance and ethics *standards and procedures* to be followed by employees and other agents.
2) Board of directors must exercise reasonable oversight and *assignment of* overall *responsibility*.
3) Due diligence in *delegation* of substantial authority.
4) Implement *training* programs and *information* dissemination.
5) Implement *monitoring and auditing* systems, including use of a reporting system.
6) Implement and consistently enforce appropriate *disciplinary mechanisms.*
7) Respond appropriately to misconduct and take all reasonable steps to *prevent similar offenses.*

There are two advantages that a company can obtain if they implement an effective compliance program. First, the company can foresee and minimize the possible risk of being prosecuted since they will be more aware of the FCPA provisions and in control of all their internal activities, employees, and all third parties that represent them. It mandates that the management knows what is going on in the company. Transactions must be approved by a responsible authority. Assets can only be accessed with authorization. If proper controls are implemented, illegal payments become more difficult.

Another advantage is that, there will be significant incentives for companies that fully cooperate in complying with the provisions of the FCPA. Although there are no precise measures of the incentives, an effective compliance program will result in early detection and prevention of violation, as well as significant reduction of the consequences.

In the prosecution of a renowned violation by Siemens in 2008, for example, once they encountered the problem, they immediately changed their whole business approach and cooperated with the FCPA. As the SEC learned about this, Siemens was then given penalty mitigation where they could save billions of dollars' worth of fines. Another significant example is the recent decision earlier in September of this year by the DOJ not to prosecute Morgan Stanley as a company, but only the individuals responsible for the violation because of their goodwill of voluntary disclosure and the company's pre-existing compliance program.

In the end, it is necessary to acknowledge that the FCPA is here to stay and that its enforcement levels will likely increase in frequency. Determining where the risks reside and designing a program that detects and prevents those risks are both the challenge and necessity for the company if they want to achieve compliance under the FCPA. Doing the right thing is the best way to comply.

Questions and Answers

Q: In each case when companies are penalized with the imposition of a certain amount of fines, where does the money eventually go? Does it go to the government or will it be used for the recouping efforts impacted by the corrupt practices?

The money directly goes to the United States Department of the Treasury. Even though the money is ethically supposed to go back to the victims, the main issue remains how the money can be distributed back accordingly to the victims. For example, in the case of the corruption surrounding the acquisition of the right to drill an oil well in a certain area, it would then be rather complicated to disgorge the money to all people living in that area.

Q: How does the FCPA deal with small-scale American companies?

Contrary to the common assumption, the FCPA actually applies to small companies just as it does to big companies. The notorious example for this is the penalty given to the Green's family in September 2009. With only three people running a family business, the Green's bribed the Tourism Authority of Thailand so they could run the Bangkok International Film Festival for four consecutive years. As decided by the provisions of the FCPA, Mr. Green is now sentenced with 20 years of imprisonment. Another prominent example is the prosecution towards 22 small American companies that bribed the government of Gabon.

Q: I personally think that some assessment to determine the violations of the FCPA cannot be completely understood. It is thus rather confusing for companies to truly realize the violation when their main intention is simply to negotiate with the government. What is the fine line between the violation of the FCPA and a mere negotiation?

The answer is that it all depends on each situation itself. There have been a lot of exceptions where corporate expenses of a reasonable amount are allowed to facilitate business negotiation. The FCPA does not just prosecute people. It prosecutes people who bribe. There is a recent case being investigated right now where Wal-Mart tried to get a permit in Mexico by making a lot of small payments. It would not have been a problem if it was only one or two small payments. But when the frequent payments are used to beat competitors to get the permit, then that is when the violation occurs.

Q: On those bigger payment issues, our company is required to frequently host government officials for the purpose of inspection and auditing and thus pay for all their expenses during their involvement. What kind of legal protection or precaution does our company need to avoid violating the FCPA?

The best precaution for any company is to emphasize the keywords ‘reasonable’ and ‘bona fide’. You can never have a problem for a very small amount of money even if it occasionally includes an entertainment trip. The problem is if the lavish entertainment is more prominent than the main business activities. In a case where a water commissioner from Alexandria, Egypt was brought to New England by a company for the purpose of learning about water-related issues, he brought along his family with first-class tickets and spent most of his time during the scheduled trip in Disneyland. That was an example of a violation of the FCPA. The test is thus very complicated. It is however also important to ensure that all relevant parties are aware of the activities and expenses made. All companies must share information about their business activities, not only with the officials invited, but also with the institution they are affiliated with, so that business transparency can be maintained.

Q: We have a letter from our regulator explaining that for government officials doing business travel you can provide facilities and expenses under the regulation of the Ministry of Finance. How do you see that this kind of letter may provide us with protection from FCPA prosecution?

It is always good when you have talked to the individual employers or regulators. It will also make it easier to prove to the prosecutor that it is not a corrupt payment because there is no misuse of regulations. So it is indeed one way to protect your company from the prosecution. But it is not the only way to ensure the avoidance of investigation because at the end it comes back to the main assessment criteria of ‘reasonable’ and ‘bona fide’.

Q: You mentioned that a company actually has internal control over all of its employees. If we encounter a certain violation of our policies related to the FCPA, would suspending and terminating their employment be a sufficient measure of this internal control?

On the first violation, the employment termination is indeed the right move. However if you encounter more violations after imposing the first measure, then it means that you are not really dealing with the problem. Internal control is not improved by suspending one employee but by addressing the risk. So the measure must depend and adjust to the severity of the problem.

Q: What is the relation between the prosecution of the FCPA with the military force or authority in charge? Can the FCPA cases also be handled by the police or DPS (Department of Public Safety) in charge?

There are hundreds of instances where anti-corruption law intersects with other policies. Sometimes it clouds the analysis of what the real problem is. However it has been obviously stated that the FCPA is about corruption and when it comes down to this, involvement from the police of other parties are irrelevant.

Q: What should the companies from the United States be mostly concerned of with the FCPA related issues as far as representing their country? And what problems do you see with the FCPA as far as its enforcement and accomplishments?

The top concern should be whether your company has a good and realistic compliance program. If your company never really encounters a problem, then you have to wonder if you really have a real program or just a paper program that is never used. To answer your second question, the most prevalent problems with the FCPA are evidence gathering and global cooperation because there are still gawking inconsistencies between the prosecutions of transnational bribery cases in the United States and other parts of the world, especially in Asia. In China, for example, its government only prosecutes domestic briberies but does not extend any support for other cases that involve foreign companies. Similarly, Japan also has a very low incident of prosecution. The challenge would thus be to create a level playing field where all countries share a similar record of prosecution.

Q: How should a company do charity activities so it will not be considered as potential bribery? Should the charity go through an international organization? By directly giving the money to the government to distribute, will it create suspicion of the conduct of bribery from an FCPA point of view?

Charity is a noble action. It does not matter what kind of medium you use to do it. As long as it stays true to the main intention of charitable donation, then you will not have an FCPA problem. It is only when you use the charity as a disguise to get the money into the pockets of the government that you will be penalized with the provisions of the FCPA.

Q: Does the United States intend to assist the Indonesian Corruption Eradication Commission (KPK) to better enforce the FCPA in Indonesia?

Yes, and in fact we have made a schedule to hold a special meeting with them in upcoming days.