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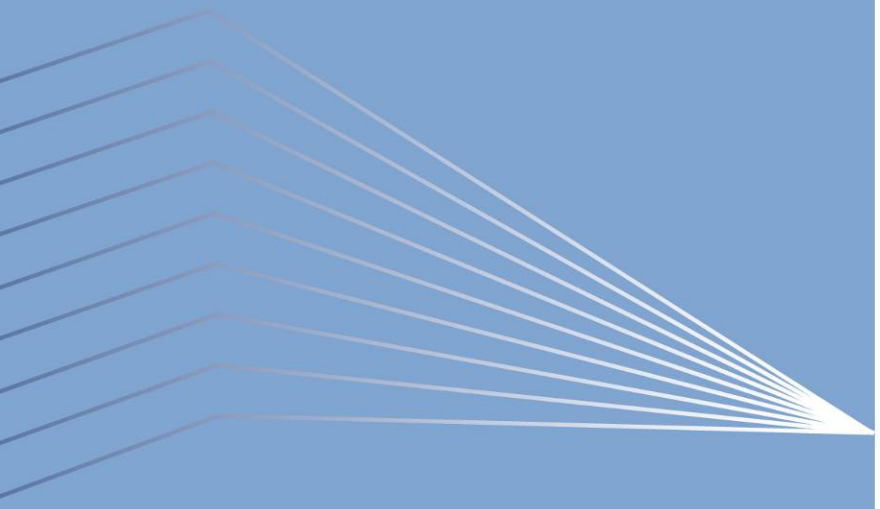

FCPA Digest

Recent Trends and Patterns in the Enforcement of the Foreign Corrupt Practices Act

JANUARY 2012

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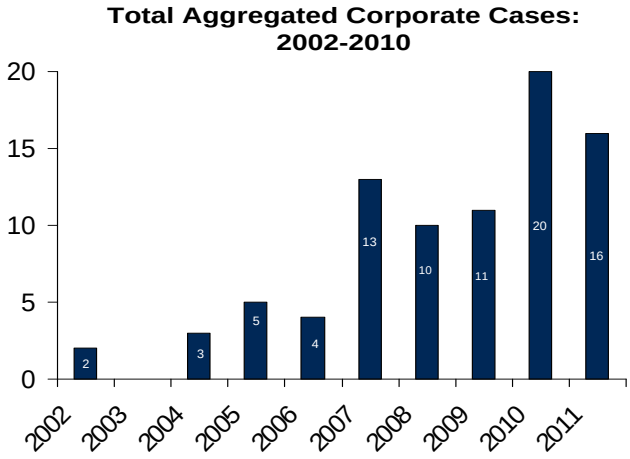
Recent Trends and Patterns in FCPA Enforcement

Although the pace of new FCPA enforcement actions was somewhat off in 2011 – o*nly* sixteen corporate cases and eighteen new individual defendants – 2011 was nevertheless an eventful year for FCPA enforcement and indeed for enforcement of other countries' similar laws. Among the highlights:

- Defendants took the government to trial in a number of FCPA matters, with mixed results reflecting the difficulty and uncertainty of proving foreign bribery beyond a reasonable doubt;
- Judges in multiple districts largely adopted the government's expansive interpretation of what constitutes an "instrumentality" of a foreign government, including state-owned entities indirectly controlled by a foreign government;
- The DOJ and the SEC continued their focus on prosecution of individuals;
- The U.S. enforcement authorities brought fewer cases in 2011 against non-U.S. companies;
- Despite claims that the government extracted exorbitant fines in FCPA matters, the average penalty continued to be less than $25 million;
- The DOJ and the SEC almost completely withdrew from their prior practice of routinely requiring an independent monitor in all cases and demonstrated a willingness to accept various forms of self-monitoring;
- With the advent of the U.K.'s Bribery Act, the British government offered considerable guidance on compliance and began exploring ways of encouraging voluntary disclosures and cooperation by emulating the U.S. system of deferred prosecution agreements.

Enforcement Actions

The first half of the year started off with the U.S. authorities continuing their record pace of the previous years, bringing nine actions. In the latter half of the year, the pace dropped somewhat, perhaps because the DOJ was pre-occupied with the trials in the *Lindsay Manufacturing*, *Haiti Telecom*, and *SHOT Show* cases and in preparing for additional *SHOT Show* trials as well as upcoming trials in *O'Shea* and *CCI*. Nonetheless, the final total was a respectable sixteen corporate cases, including the last corporate case involving the TSKJ consortium and the first FCPA case against a major pharmaceutical company, *Johnson & Johnson*.



Non-U.S. Companies and Individuals

In previous years, we have noted that the U.S. authorities appeared to be targeting non-U.S. companies, particularly those in jurisdictions that did not appear to be bringing sufficient energy and commitment to enforcing their own laws implementing the OECD Anti-Bribery Convention. Thus, for example, in 2010, eleven of the twenty corporate cases involved non-U.S. parent companies. In contrast, in 2011, only five of the sixteen corporate cases did so.

On the other hand, as discussed below, the U.S. authorities have repeatedly stated that individuals, as well as corporations, need to be held accountable, a position echoed (or sometimes led) by politicians and commentators. This year saw a record number of non-U.S. individuals charged in the United States, with twelve of the eighteen individuals charged being non-U.S. citizens and three more holding dual U.S./foreign citizenship. Of course, those twelve individuals were all charged in just two cases, *Siemens* and *Magyar Telekom*, and the three dual-nationality citizens were officers or agents of U.S.-based companies, so it is too early to say whether these cases represent a trend.

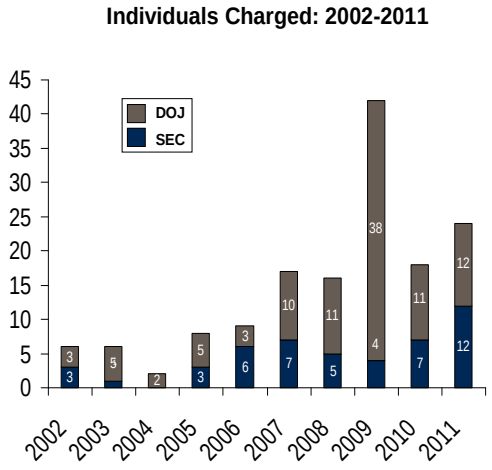
Still, the same underlying policy interests likely hold true for individuals as for corporations – the U.S. authorities want to see enforcement actions by their foreign counterparts and, until they do, they will likely continue bringing actions against non-U.S. individuals. However, in contrast to foreign corporations, over which they may have leverage due to the corporation's ties to the United States or their concern that their business partners will shy away from doing business with them if they are charged with a bribery offense, the U.S. authorities have considerably less leverage over foreign individuals. Thus, over the next few years, we will have to see whether the countries whose nationals have been indicted – Germany, Argentina, Switzerland, Israel, and Hungary, all of whom are signatories to the OECD Convention – will extradite these individuals to stand trial in the U.S., will bring their own enforcement actions against them, or will do nothing. As we have noted in the past, the record on extradition of individuals in FCPA cases is mixed, with some notable extraditions – *Naaman, Chodan,* and *Tesler* having been extradited, while others – *Pluimers* – living openly and without fear in the Netherlands and yet others – *Kozeny* – tying the matter up in endless litigation in foreign courts.

Individuals

Most of the news concerning individuals involves the trials that took place in 2011 and that are discussed below. Nevertheless, the eighteen additional individuals charged in 2011 represents the second highest total in FCPA history, eclipsed only by 2009 in which the government charged the 22 individuals in the *SHOT Show* case and seven of the eight defendants in *CCI*.

Half of this number is attributable to the indictment of the *Siemens* executives and agents. For us, the most interesting aspect of this case is that it comes almost three years to the day after the original *Siemens* settlement in 2008. The obvious question this raises, apart from why the U.S. government felt it necessary to charge such

a large number of German, Argentine, and Israeli nationals (and why it took three years to do so), is what this bodes for individuals associated with other large-profile cases. For example, in the *TSKJ* cases, the government has thus far charged only two executives of *KBR* and one of the *TSKJ* agents; the new case against the *Siemens* executives obviously raises the question as to whether the executives of the other *TSKJ* partners are similarly at risk.



The case against the *Siemens* individuals may also reflect the pressure from commentators, the courts, and the Congress to see that individuals are held accountable for corporate crimes. To date worldwide, only one individual has been brought to trial for the allegations relating to the bribery at Siemens. The German authorities initiated court proceedings in January 2011 against Thomas Ganswindt, a former member of Siemens AG's management board, in a Munich regional court alleging that he had inadequately supervised the company by failing to halt the corrupt payments and tax evasion, the case was dropped in May 2011 due to insufficient evidence to support the charges. However, Ganswindt was ordered to pay $250,000 as a condition to have the case dropped. Authorities in several countries, including Bangladesh, Greece, Turkey, Brazil, Russia, and Austria, have also brought investigations against Siemens, but none have brought actions against individual defendants. Given the lack of individual prosecutions worldwide, the current action may serve as a not-so-subtle push to authorities of other countries to hold the individual actors accountable for the actions that, until now, have only been attributed to the corporate entities.

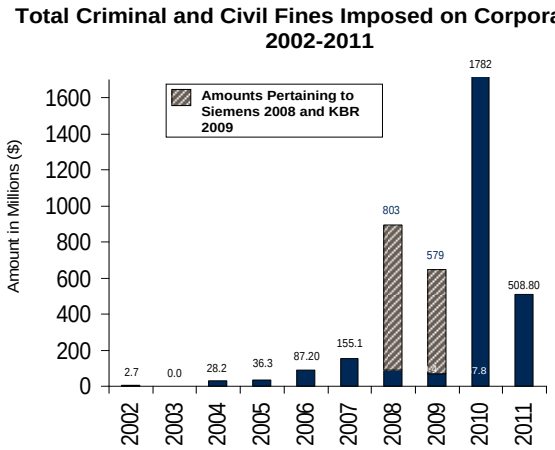
Finally, of the numerous cases awaiting trial or sentencing, five defendants were sentenced in 2011. Among them, in October, *Joel Esquenazi* was sentenced to 15 years, the longest FCPA-related sentence thus far, for his involvement in the *Haiti Telecom* case. Two other *Haiti Telecom* defendants also received significant, albeit shorter sentences: *Antonio Perez* was sentenced to 24 months and two years supervised release and *Carlos Rodriguez* was sentenced to 84 months. In addition, *Jorge Granados* of *Latin Node* was sentenced to 46 months, and the year wrapped up with *Innospec*'s *Ousama Naaman* being sentenced to 30 months.

Sanctions

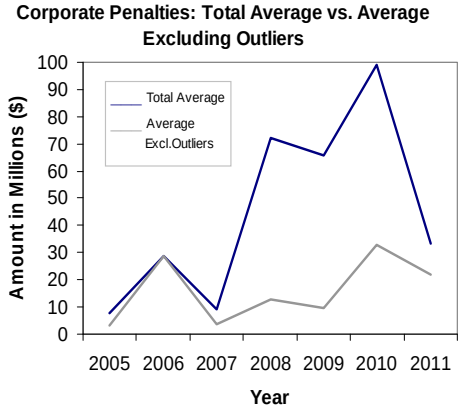
Before we get to the corporate numbers, we have to mention the highest financial sanctions ever assessed against individuals in an FCPA case, which, naturally, came in a *TSKJ* case relating to the bribes paid for contracts in Bonny Island, Nigeria. Earlier this year, the courts ordered forfeiture of $148,964,569 in *Geoffrey Tesler*'s Swiss bank accounts and of $726,885 from *Wjodek Chodan*, the former *KBR* employee. The pleadings simply alleged these funds were the proceeds of their illicit activity, but the amounts invite the question – what

was Tesler doing with so much of TSKJ's money if he was supposed to have paid his commissions over as bribes?

Setting aside the Tesler/Chodan forfeitures, the total amount of sanctions imposed in FCPA cases in 2011 was $509,123,840, of which $508,829,803, was imposed against corporations and $294,037 against individuals ($229,037 against *Paul Jennings*, an *Innospec* executive, $40,000 against *Bernd Regendantz*, a *Siemens* executive, and $25,000 against *Leesen Chang*, a *Watts Water* executive).[1]



The total corporate sanctions imposed this year are obviously down somewhat from the record of $1.7 billion from 2011. This reduction, however, reflects that the enforcement actions this year included only one *TSKJ* case (*JGC*) and very few big-ticket cases such as *BAE* and *Alcatel*. Indeed, *JGC* was the only FCPA case this year to exceed $100 million in fines, and only two cases exceeded $20 million: *Johnson & Johnson* with combined penalties of $70 million, and *Magyar Telekom* with combined penalties of $95 million. (*Bridgestone*, with fines of $28 million, is a special case since that amount also includes an antitrust component.)



The penalties this year thus confirm the trend we have previously noted that the fines in FCPA cases are rarely as enormous as portrayed by the Chamber of Commerce and certain congressmen. Indeed, the average FCPA sanction this year, including criminal fines, SEC penalties, disgorgement, and interest, is $33.8 million. If the high (*JGC* $218.8 million) and low (*Ball Corp.* $300,000) outliers are removed, the average falls to $22.1 million.[2]

Moreover, this average is consistent with the fines in previous years. Since the record-holding $800 million penalty for Siemens in 2008, each subsequent year has seen at least one corporate FCPA case with a penalty of several hundred million dollars. As we have noted in our previous *Trends and Patterns*, however, these headline-grabbing high penalties and

[1] This figure also excludes the $3.09 million forfeiture ordered against Carlos Rodriguez and Joel Esquenazi, jointly and severally, as a part of their sentencing.

[2] This graph compares the total average penalty for each year with the average excluding the high and low outliers, which are, in turn, specified in the chart.

resulting high annual totals tend to obscure the reality of what companies, on average, pay for FCPA violations. When the highest and lowest "outlier" cases are excluded, the averages-per-year are lower still. Thus, over the past several years, when the outliers are excluded, the averages have ranged from $3 million to $33 million – not inconsequential, but certainly not as severe and extreme as the annual total penalties might suggest.

YEAR	HIGH OUTLIER(S) ($)	LOW OUTLIER(S) ($)
2005	28,479,195 (*Titan*)	450,000 (*Micrus*)
2006	n/a (only three cases, 15, 21 and 50 million respectively)	n/a
2007	30,000,000 (*Chevron*) 26,000,000 (*Vetco*) 22,032,880 (*York*)	 300,000 (*DeltaPine*) 325,000 (*Dow*)
2008	800,000,000 (*Siemens*)	11,200 (*Nexus*)
2009	579,000,000 (*Halliburton/KBR*)	337,679 (*United Industrial Corp.*)
2010	365,000,000 (*Snamprogetti*) 338,000,000 (*Technip*) 264,576,998 (*Noble*)	1,700,000 (*Rae*)
2011	218,800,000 (*JGC Corp.*)	300,000 (*Ball Corp.*)[3]

As another historical note, the government has long argued that companies that make voluntary disclosures and cooperate with the government receive a tangible benefit. Our analysis of penalties over the past five years indicates that the DOJ has often, but not always, granted discounts ranging from 3% to 67% in cases involving voluntary disclosures and negotiated resolutions. The following chart provides some examples.

COMPANY	PERCENTAGE REDUCTION	YEAR
Siemens[4]	67%	2008
Innospec[5]	60%	2010
Pride International	55%	2010
Latin Node	52%	2009

3 These averages are based on fifteen enforcement actions because one of the corporations charged in 2011, *Cinergy Telecommunications*, is pending trial and has not been convicted or sentenced.

4 *Siemens* paid huge fines in Germany and also to the SEC. When combined with the DOJ fine, Siemens's total payments exceeded the minimum Sentencing Guidelines fine. The large reduction to the DOJ fine was thus necessary to bring Siemens's total payments in line with the Guidelines.

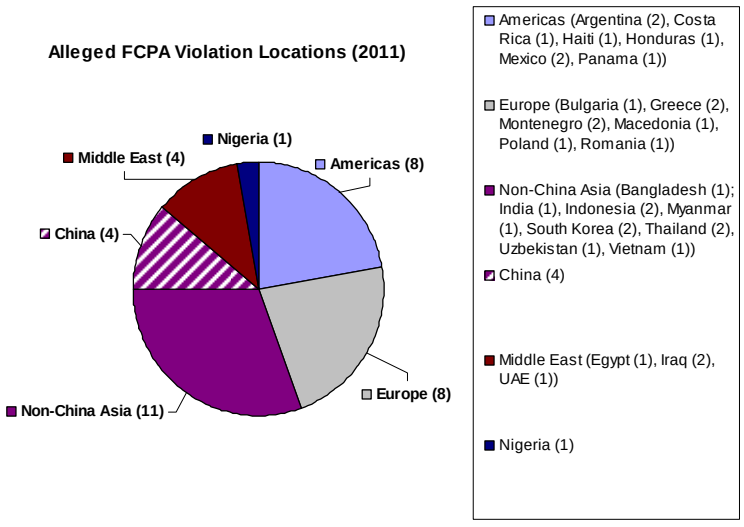
5 This reduction was based on Innospec's inability to pay a larger fine. Thus, this departure is of a different type than the others.

COMPANY	PERCENTAGE REDUCTION	YEAR
Control Components	35%	2009
Tidewater Marine	30%	2010
Universal Corp.	30%	2010
JGC Corporation	30%	2011
Technip	25%	2010
Johnson & Johnson	25%	2011
Maxwell Technologies	25%	2011
Daimler	20%	2010
Snamprogetti	20%	2010
Transocean	20%	2010
Tyson Foods	20%	2011
Royal Dutch Shell	12%	2010
Panalpina	3%	2010

The court filings in a number of these cases list the reasons for the DOJ's decision to depart, including: voluntary and thorough disclosure; nature and extent of cooperation; penalties imposed or to be imposed by other U.S. and foreign enforcement agencies and international organizations; and "extraordinary" remediation, including self- and independent-monitoring.

Country Distribution

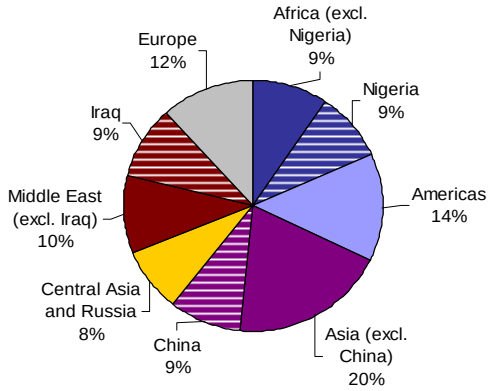
An analysis of the countries where improper conduct was alleged to have occurred in this year's enforcement actions shows, perhaps unsurprisingly, that companies are most prone to FCPA violations when doing business in markets where major industries are dominated by state-owned or state-controlled business.



Recent Trends and Patterns in FCPA Enforcement

According to the allegations brought by U.S. authorities this year, the incidence of FCPA violations in 2011 was highest in countries in Asia and the Americas, a trend that is consistent with previous years.

Alleged FCPA Violation Locations (2006-2010)



As the adjacent graph demonstrates, China has been the most significant demand-side country for the last five years, and continues to hold the top spot. One explanation for this result is the combination of increased investment by U.S. and other foreign companies and the prevalence of state-run enterprises. All four actions involving Chinese officials this year (*IBM*, *Watts Water Technologies*, *Maxwell*, and *Rockwell*) alleged payments to employees of state-owned entities. Similarly, in the Americas, a majority of the alleged bribery schemes involved payments to officials at state-run companies (*Latin Node*, *Haiti Telecom*, *Aon*, and *Bridgestone*). Eastern Europe and the former Soviet Republics were also in the spotlight this year, with actions involving officials in Bulgaria, Montenegro, Poland, Romania, Uzbekistan, and Macedonia. Notably, only one enforcement action implicated officials in Africa this year (*JGC*), and that action pertained to the Bonny Island Project in Nigeria, for which the other companies who participated in the *TSKJ* consortium and several individuals have been charged in previous years.

Types of Resolutions

Department of Justice

In 2011, the Department brought only one contested action against a corporation – the superseding indictment in the *Haiti Telecom* case that included charges against *Cinergy Telecommunications*. In addition, of course, it went to trial on the 2010 indictment against *Lindsey Manufacturing* and its executives as discussed below.

Of the remaining ten criminal cases involving corporations, one was resolved through a plea (*Bridgestone*), four were resolved through non-prosecution agreements (*Aon*, *Armor Holdings*, *Comverse Technology*, *Tenaris*) and four were resolved through deferred prosecution agreements (*Johnson & Johnson/DePuy*, *JGC*, *Maxwell Technologies*, and *Tyson*). In *Magyar Telekom*, however, the DOJ entered into a deferred prosecution agreement with *Magyar Telekom*, and a separate Non-Prosecution Agreement with *Magyar Telekom*'s parent, *Deutsche Telekom*.

For the most part, the NPAs and DPAs are similar in scope and requirements to those of previous years. However, we can see the emergence of two trends and patterns. First, although most previous NPAs/DPAs had terms of three years, in 2011 only *JGC* and *Maxwell Technologies* had three-year terms, while the remainder were for only two years.

Second, of the ten criminal settlements, only in *JGC* did the government, consistent with the treatment of other corporate defendants in the *TSKJ* case, require the company to retain an independent compliance monitor. In the remainder, the company was allowed to "self-monitor" by filing periodic reports on the implementation of their remedial compliance programs with the Department or, in the cases of *Tenaris* and *Aon*, only reporting violations or investigations. This represents a substantial reversal from previous practice in which virtually every case involved a monitor, a trend we began seeing last year.

SEC

Of the thirteen corporate enforcement actions brought by the SEC in 2011, eight were resolved through consent judgments (*Aon, Armor Holdings, Comverse Technology, IBM, Johnson & Johnson, Magyar Telekom, Maxwell Technologies,* and *Tyson*), four were resolved through administrative cease & desist orders (*Ball Corporation, Diageo, Rockwell Automation,* and *Watts Water Technologies*), and, for the first time, one was resolved through the SEC's first-ever deferred prosecution agreement (*Tenaris*).

At the end of the year, the SEC's enforcement strategy was thrown into disarray by Judge Rakoff's rejection of its settlement with Citibank, a non-FCPA case, making a wholesale attack on its longstanding practice of allowing companies to settle enforcement actions without admitting or denying any of the SEC's factual allegations (other than jurisdiction). Apart from objecting to the amount of the settlement, Judge Rakoff objected to the "neither admit nor deny" practice, finding that the public interest required accountability and assessment of responsibility in a public enforcement action. In response, the SEC, which may appeal the Citi decision, argues, probably correctly, that companies will be less likely to settle if they have to admit to the facts (although, of course, this is precisely what they have to do in DOJ DPAs and NPAs), that the courts (and the SEC) will be swamped by trials, and that the public interest is better served by quick and certain settlements. As demonstrated by the settlement with *Aon* and *Magyar Telekom* in December, the SEC has not given up on its practice, but it is clearly concerned that Judge Rakoff's position might be taken up, in an unpredictable way, by other courts.

Even before the Citi decision, however, the SEC was beginning to take advantage of its new authority under Dodd-Frank to collect financial penalties in administrative actions. The SEC had brought administrative actions in FCPA cases in the past, with occasional disgorgement. In 2011, however, the SEC brought four administrative actions in which it collected financial penalties under its newfound authority: *Watts Water and Leesen Chang* ($225,000), *Ball Corp.* ($300,000), *Rockwell* ($400,000), and *Diageo* ($3 million), for a total of $3,925,000. Following the Citi decision, we may see more administrative actions, with perhaps steeper financial penalties, in the coming year.

In addition, the SEC has begun to explore other alternatives, such as adopting the DPA model routinely used in DOJ actions. In 2011, the SEC entered into a DPA for the first time, in *Tenaris*. The language, however, is slightly weaker than a typical DOJ DPA and rather muddled. Instead of admitting, accepting, and acknowledging that the alleged facts in the DPA are true, the *Tenaris* DPA says only that the company has "offered to accept responsibility for its conduct and to not contest or contradict the factual statements . . . in any future Commission enforcement action in the event it breaches this agreement." As we have commented in the past, however, it is not altogether clear what advantages a company gains from a SEC DPA as opposed to a traditional enforcement action, and, indeed, a company may even be at a disadvantage given the SEC's insistence that the company agree not to deduct the fine on its taxes – a fairly unexceptional restriction – but also that it not deduct the disgorgement amount.[6] Moreover, while corporations may welcome this alternative disposition, there has been some concern that the SEC's use of DPAs will further remove SEC enforcement actions from judicial scrutiny.

Although the SEC will undoubtedly continue to settle cases using the "neither admit nor deny" formulation where they are confident that the local district court will not create issues, it is clearly prepared to proceed with alternatives that do not involve the courts, such as DPAs or administrative orders.

Industry Initiatives

It is hard to keep track, but there appear to be several industry initiatives in progress at the DOJ and the SEC. The first such initiative involved oil & gas companies dealing with freight forwarders and customs brokers, which was followed by one targeting medical device companies (a spin-off from a domestic kickback investigation). In late 2009, Assistant Attorney General Lanny Breuer announced the long-expected initiative targeting pharmaceutical companies. In addition, there appears to be a SEC initiative targeting financial companies marketing to sovereign wealth funds.

The freight forwarders initiative culminated in the prosecution of *Panalpina* and five oil & gas companies and oil field services companies in November 2010. Although it is possible there may be some lingering investigations of individuals and entities, the DOJ and SEC appear to have largely closed this project down and have notified several companies, including *Cameron International, ExxonMobil, ENSCO, Team Inc.*, and *Global Industries*, that they have closed their respective investigations of them.

None of the other initiatives have yet resulted in enforcement actions. In 2011, *Johnson & Johnson* and its subsidiary, *DePuy*, settled an investigation, and *Pfizer* has announced that it has reached a settlement in principle with the DOJ, but both of these investigations predated the inception of the pharma initiative.

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[6] For a further discussion of these issues, you may wish to refer to our prior client publication, available at Shearman & Sterling, *A New Tool and a Twist? The SEC's First Deferred Prosecution Agreement and a Novel Punitive Measure* (May 24, 2011).

Trials

SHOT Show

The much-anticipated trials in the *SHOT Show* case began in 2011, and the year ended in a surprising twist, with the judge throwing out the conspiracy counts for six of the defendants on trial, thus completely exonerating one, *Stephen Giordanella*. The 22 defendants, caught in the government's largest FCPA-related undercover sting operation, had been divided into four groups to make the trial more manageable. The first group of defendants went to trial on May 16, 2011, but, after the jury deliberated for five days without reaching a verdict, the court declared a mistrial on July 7, 2011. The second group of defendants began their trial on September 28, 2011, but District Judge Richard Leon dismissed the conspiracy counts on December 22, after twelve weeks of trial, citing lack of evidence to justify sending the charges for the jury to decide.

The crowing about the government's failure to obtain a verdict in these two trials by some commentators and defense counsel is probably as misplaced as was the government's overblown announcements at the time of takedown in January 2010. The problems the government encountered have very little to do with FCPA legal theories or the appropriateness of a vigorous FCPA enforcement regime. Instead, the verdicts more likely reflect the two significant obstacles inherent to the government's case in this unique matter. The first is the risk that the jury may perceive the government to have overreached and entrapped the defendants into committing a crime. Sting trials are notoriously difficult to prosecute, and the *SHOT Show* case seems to be no exception. After the first trial's hung jury, one jury member reportedly said that the jurors distrusted the FBI's methods, arguing, "[The defendants] wouldn't be there unless it were a sting." Although three of the 22 defendants pleaded guilty this year to conspiring to violate the FCPA (*Daniel Alvirez* on March 11, *Jonathan Spiller* on March 29, and *Haim Geri* on April 28), it is unclear whether these pleas, apart from providing cooperating witnesses for trial, validate the government's case. For example, Alvirez pleaded to a separate criminal information that alleged, in addition to the undercover sting, a separate and independent bribery scheme involving payments to Ministry of Defense officials of the Republic of Georgia. Similarly, Spiller, the former CEO of *Armor Holdings*, was the former boss of Richard Bistrong, who helped orchestrate the *SHOT Show* sting after being implicated in unrelated violations of the FCPA involving payments to a U.N. procurement official. This year, *Armor Holdings* settled related allegations of corrupt payments to a U.N. procurement officer and agreed to pay the DOJ and the SEC a total of $15,980,744.

Second, although the government initially charged the 22 defendants in 16 separate indictments, with groups of defendants charged in separate conspiracies, it later sought to avoid separate trials by bringing a superseding indictment charging *all* of the defendants with having joined a *single* conspiracy. The evidence of such a single conspiracy, however, has never been viewed as strong, and the government's choice to proceed on that theory exposed it to a risk that the jury, or the court, would find the conspiracy to consist only of the proverbial hub (Bistrong) and spokes (the 22 defendants) without a unifying rim. This may have influenced the mistrial in the first trial, and seems to have been the basis of the judge's decision in the second trial. This, as well as the

ultimate outcome of the second trial and the results of the retrial in 2012, will likely influence the government's strategy in using novel methods of FCPA enforcement. In the meantime, the retrial and the two trials for the remaining groups of defendants should give the prosecution a chance to apply any lessons learned from the first two runs.

Lindsey Manufacturing

The government experienced several landmark successes this year in the trial of *Lindsey Manufacturing*, followed by a late-stage victory for defendants. First, defendants moved to dismiss the indictment on the grounds that officials at the Mexican Comisión Federal de Electricidad ("CFE"), whom defendants were charged with bribing, were not "foreign officials." Defendants argued that a state-owned entity ("SOE") such as CFE did not qualify as an instrumentality under the FCPA. The court disagreed.

Based on several factors, the court found that CFE could be considered an instrumentality of a foreign government within the meaning of the FCPA, and its employees accordingly government officials. This was the first opinion to substantively confront the question of whether the definitions of "foreign official" under the FCPA include employees of SOEs. Although the decision was narrowly drawn – the Court declined to find *no* corporation could qualify as an "instrumentality" and based its ruling on facts specific to CFE – it marked a definitive victory in favor of the DOJ's expansive definition of "foreign official" and could set the stage for how other courts interpret the term.

The *Lindsey Manufacturing* case proceeded to trial, and, on May 10, 2011, the jury issued guilty verdicts on all counts against the defendants. Lindsey Manufacturing was the first company to be convicted on FCPA violations after trial, and the guilty verdict was heralded by the DOJ as an "important milestone" in FCPA enforcement. The victory, however, was short-lived. Following trial, defendants filed a motion to dismiss the indictment based on alleged prosecutorial misconduct. The defendants claimed that the government allowed an FBI agent to make false statements to the grand jury, obtained search and seizure warrants using affidavits containing false statements, and failed to disclose exculpatory evidence as required under *Brady v. Maryland*. On December 1, 2011, the court granted defendants' motion with prejudice, citing multiple instances of misconduct by the government.

Although the *Lindsey* dismissal was not based on any factual or legal issues related to the FCPA itself, the ruling may have some legacy for future FCPA trials. In a footnote to the opinion, the court appears to require the government to trace funds paid to an intermediary to specific bribes or specific officials. This ruling may result from the fact that the government relied on trial exhibits that appeared to trace the flow of funds from the company to the bribes, although it later tried to walk away from this theory. The court's suggestion that the government must prove that defendants' money was used for particular payments to an official has no support in the statute, which makes clear that intent and authorization to bribe are the keys. And in fact, the judge in the *O'Shea* case – involving bribes through the same agent to the same officials at the same government agency – has rejected the defendant's argument there that the government must be able to trace funds to specific

payments to an official and that therefore the government cannot attribute the same bribes to both Lindsey Manufacturing and to his employer (*ABB*) (although O'Shea has once again raised this argument in light of the *Lindsey* ruling).

The DOJ filed a notice of appeal to the Ninth Circuit immediately following the dismissal of the *Lindsey* indictment. If defendants file a cross-appeal, as they likely will, the "foreign official" question could be decided for the first time at the appellate level.

CCI

In April 2011, Flavio Riccoti, a former *Control Components* executive, who had been an FCPA fugitive, was captured in Germany, extradited to the United States, and pleaded guilty to conspiring to violate the FCPA. However, consistent with recent trends, the remaining five former *Control Components* executives (out of the eight originally charged with violating the FCPA and the Travel Act) have refused to plead and will proceed to trial in June 2012.[7]

Similar to the defendants in the *Lindsey Manufacturing* case, the defendants in this matter also sought to have the court rule that an SOE was not an instrumentality of a foreign government within the meaning of the FCPA. Here, again, the argument failed, and in May 2011, the court denied their motion to dismiss. The court pointed to other U.S. statutes' definitions of instrumentality as support for the FCPA applying to SOEs and thus determined that review of the legislative history was unnecessary. The court stated that no single factor was dispositive as to whether an SOE was an instrumentality, but rather involved a case-by-case factual determination based on factors similar to those stated in *Lindsey Manufacturing* (below).

As a result of the court's decision, the DOJ stipulated in September to jury instructions that will require it to prove that the *Control Components* defendants *knew* that the bribe recipients were government officials. While this stipulation makes the DOJ's case against the *Control Components* executives potentially more difficult, it has also had a spillover effect in other cases. In appeal briefs seeking to dismiss the trial verdict in his case, *Carlos Rodriguez* cited the stipulation as evidence that the government failed to establish that he knew that government officials were bribed.

Bourke

Earlier this year, *Frederic Bourke* moved for a new trial based on newly discovered evidence, claiming that statements made by the prosecution at oral argument in the Second Circuit demonstrated that the prosecution knew that co-defendant Hans Bodmer lied at Bourke's original trial. However, on December 14, 2011, the Second Circuit affirmed the jury verdict against Bourke in his previously filed appeal, and the trial court denied

[7] Earlier this year, the DOJ dismissed Count 16 of the Indictment, an obstruction of justice charge against Rose Carson arising from allegations that she destroyed documents by flushing them down a toilet after she learned that *Control Components* hired outside counsel to investigate corrupt payments made by the company.

Bourke's motion for a new trial the next day, rejecting Bourke's contention that the government knowingly permitted the introduction of false testimony.

Bourke was convicted for his role in paying bribes to Azeri officials in connection with investing with the privatization of a state-owned company in Azerbaijan. His trial was complex and fraught with uncertainty, and even his sentencing judge had stated, "After years of supervising this case, it's still not entirely clear to me whether Mr. Bourke is a victim or a crook or a little bit of both." At the government's request, the district court had instructed the jury on both "actual knowledge" and "conscious avoidance" and had argued both theories to the jury. This became one of the critical issues on appeal.

Conscious avoidance is defined in the FCPA as: "when knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is *aware of a high probability of the existence of such circumstance*, unless he actually believes the circumstance does not exist" (emphasis added). In Bourke's appeal, he argued that the conscious avoidance charge lacked a factual predicate. The Second Circuit, however, rejected this notion, finding that while the government's primary theory at trial was that he had actual knowledge of the bribery scheme, there was ample evidence to support a conviction even based on the alternate theory of conscious avoidance. Bourke also argued that the government had to elect a theory and that by going forward on both theories it invited the jury to return a verdict based on negligence rather than knowledge. Again, the Second Circuit disagreed, noting the difficulty of proving conscious avoidance and stating that the evidence adduced by the government (in support of its theory that Bourke actually knew about the crimes) was sufficient to support the conscious avoidance charge. Thus, the court held that the district court correctly permitted the government to proceed on both theories.

Siriwan

The case against Gerald and Patricia Green reached an end in 2011, when the government dismissed its appeal of the low sentences imposed on the Greens by the trial court.

The action has now turned to the government's case against the mother-daughter team of Juthamas and Jittisopa Siriwan, the Thai officials alleged to have received the bribes from the Greens. The FCPA itself applies only to the bribe payers and long-standing precedent has held that the government not only may not charge the officials with FCPA bribery but cannot charge them with conspiracy to violate the FCPA either. Thus, in a number of recent cases, including both this case and the *Haiti Telecom* case, the government has tried a new theory – charging the allegedly corrupt officials with laundering, or conspiring to launder, the proceeds of the FCPA bribery. In this case, the Siriwans have challenged this approach directly, and in an August 19, 2011 motion to dismiss, argued that the government's theory is an attempt to evade the limits of the FCPA and thus improperly usurps the congressional authority that had intentionally created those limitations. In addition, they have asserted that the U.S. lacks jurisdiction, as Thailand's penal code gives Thailand exclusive jurisdiction over extraterritorial crimes of misconduct committed by its public officials. The hearing on the motion is currently set for January 2012.

One of the more curious aspects of this case is that the district court has allowed the Siriwans to litigate this issue without coming to the United States or otherwise submitting to the court's general jurisdiction. In doing so, the judge determined that the fugitive disentitlement doctrine does not apply to this case, and an American prosecution necessarily implicates issues of Thai sovereignty. While such a ruling may not prevent the ultimate extradition of the Siriwans, it has allowed them to challenge the charges brought against them without leaving Thailand.

Legal Issues

Business Nexus

The "obtain or retain business" element is recognized as a critical factor in narrowing the scope of the FCPA. The extent to which it does, however, has been a recurring topic of debate. As we have previously discussed, the line as to what constitutes "obtain or retain business" was blurred in the *Panalpina* cases. While some of the bribes paid in the 2010 *Panalpina* cases were made to obtain contracts and other specific business advantages, most of the payments were made to customs or tax officials to reduce duties and taxes, to expedite customs clearances, or to evade import regulations.[8]

None of the cases in 2011 went as far beyond the scope of the FCPA as delineated in *United States v. Kay*. In the past year, the government has alleged a variety of business advantages to satisfy the FCPA's business nexus. For example, the SEC has alleged that reduction of costs, influencing inspectors, importing and exporting goods, and sabotaging competitor's tests, and obtaining regulatory benefits satisfy the FCPA's "obtain or retain business" element.

In one case, the DOJ claimed that the reduction of operating costs constituted "obtaining or retaining business" under the FCPA. In January 2011, Manuel Salvoch, the former Chief Financial Officer of *Latin Node*, pleaded guilty to conspiracy to violate the FCPA. The alleged purpose of the conspiracy was to pay bribes to Honduran officials, with the goal of obtaining business advantages with Hondutel, a wholly state-owned telecommunications authority in Honduras. These business advantages included preferred telecommunications rates, retention of an interconnection agreement, and continued operations in Honduras, despite late payments to Hondutel.

Influencing inspectors has also come into the realm of "obtaining or retaining business." On February 10, 2011, the SEC alleged that Tyson de Mexico, a wholly-owned subsidiary of *Tyson Foods*, paid more than $100,000 to two Mexican veterinarians who were responsible for certifying Tyson de Mexico meat products for export. As a result of the payments, the government claims that Tyson Foods realized net profits of more than $880,000

[8] For a further discussion of these issues, you may wish to refer to our prior client publication, available at Shearman & Sterling, *Recent Trends and Patterns in FCPA Enforcement* (Jan. 20, 2011).

from export sales from its Tyson de Mexico facilities from 2004-2006. Thus, unlike in some of the *Panalpina* cases, the allegations in this case tie the payments to the inspectors directly to specific business opportunities.

Similarly, in the *Ball Corporation* matter, the SEC claimed that allowing the importation of prohibited items and exporting materials at reduced tariffs constituted "obtaining or retaining business." Ball Corporation acquired Fornamental, an Argentinean company, in 2006, and the conduct at issue dealt with importation and exportation of used equipment and parts by Fornamental from July 2006 to October 2007. According to the SEC's complaint against Ball Corporation, Fornamental paid over $100,000 in bribes to circumvent Argentinean law prohibiting the importation of used equipment and parts. These bribes were disguised as customs fees which were eventually booked to an "other expenses" account or to accounts associated with the related equipment. Similarly, Fornamental allegedly authorized the payment of bribes in order to secure government approval to export scrap metal at reduced tariffs.

The SEC's case against *Paul Jennings* filed in January 2011 argued that sabotaging a competitor's tests, with the ultimate result of lower costs and higher revenues to a company, can also satisfy the "obtain or retain business" element. Jennings was CFO and later became CEO of Innospec Inc. It was through these payments that Innospec was allegedly able to obtain additional fuel additive orders and favorable exchange rates against its competitors.

Finally, *Magyar Telekom* also involved eliminating competition, but in that case, the bribes were allegedly paid to delay or preclude the effects of a new Macedonian law that called for the issuance of a third mobile phone license that would cut into Magyar Telekom's existing business. The new law also imposed increased frequency fees and other regulatory burdens. Magyar Telekom entered into a secret agreement with the Macedonian authorities to make the payments, and in return, the Macedonian government delayed the introduction of a mobile phone competitor by two years, and unlawfully reduced the tariffs imposed on Magyar Telekom.

Travel, Entertainment, & Gifts

As we have observed previously, the limits of what may be considered reasonable travel and entertainment-related expenses are often difficult to discern. The SEC provided another layer of guidance in 2011, and it made clear that companies must maintain sufficient internal mechanisms for tracking and evaluating expenses not only for the company itself but also for any subsidiaries. For example, in *Diageo*, the SEC charged Diageo with violations of the FCPA for the actions of its Korean subsidiary. The Korean subsidiary paid for the travel expenses of customs officials and other government officials to Scotland, ostensibly to inspect production facilities, but also paid for purely recreational side trips to Prague and Budapest.

Similarly, in *IBM*, the SEC charged the company for the actions of its Chinese and Korean subsidiaries, which had paid for unapproved sightseeing trips that involved little or no business context while also giving free notebooks and computers. In *Rockwell*, the company was charged when its former Chinese subsidiary was discovered to have funded non-business trips for employees of state-owned companies, and held meetings in

places such as New York – where it did not have offices. Finally, in *Aon*, the company's U.K. subsidiary improperly used training and education funds to provide travel to tourist destinations. These cases demonstrate the difficulty large and complex multinational companies face, as they will need to pay closer attention to the internal controls they have in place for their culturally-diverse subsidiaries.

Entertainment is also a focus on the U.K. Ministry of Justice's Guidance on the scope of the statute and of its adequate procedures defense. The government there embraced a rule of reason and sought to assure the U.K. business community that the law was not intended to restrict traditional British hospitality. Significantly, the Guidance anticipated the upcoming London Olympics and included, as examples of what might be legitimate entertainment, taking customers and clients to tennis matches at Wimbledon or rugby games at Twickenham.

Books and Records

Typically, the books and records offenses in the FCPA context referred to the financial records of a company. However, the government recently demonstrated its more expansive approach. In *Magyar Telekom*, a secret agreement was signed between Magyar Telekom and Macedonian government officials, by which payments were promised in exchange for illegal benefits for Magyar Telekom's business. The SEC alleged that the agreement was placed in the hands of a Greek intermediary, and thus kept out of Magyar Telekom's books and records. This tends to solidify the notion that books and records under the FCPA can refer to *any* records, and not just financial records.

Instrumentalities / State-owned Entities

As we reported in our previous *Trends & Patterns*, defendants have raised the issue of when – or if – a government-owned company is an "instrumentality" of a foreign government, without success, in several recent cases. The government has consistently argued that "instrumentality" includes state-owned enterprises and SOEs; defendants, in turn, have tried to argue that the term is simply another word for "agency." This argument was previously summarily rejected by the court in *Nexus Technologies* and, in 2011, by the courts in the *Lindsey Manufacturing*, *Control Components*, and *Haiti Telecom* cases, with each court determining that an entity's instrumentality status requires a fact-specific assessment suitable for a jury.

As discussed above, in April 2011, the *Lindsey Manufacturing* court denied defendants' motion to dismiss on the grounds that CFE, a Mexican SOE, was an instrumentality of the government and its two officers were foreign officials. The Court found legislative history on this issue inconclusive because it failed to demonstrate Congress's intent to include *all* SOEs, but neither did it exclude *all* such corporations. The court, however, noted that Congress had amended the FCPA in 1998 in conformity with the international OECD Anti-Bribery Convention, which defines "public enterprises" as "any enterprise . . . over which the government . . . may directly or indirectly, exercise a dominant influence." The court identified the following list of non-exclusive factors that make an entity a government instrumentality:

- The entity provides a service to the citizens of the jurisdiction;
- The key officers and directors of the entity are, or are appointed by, government officials;
- The entity is financed, at least in large measure, through governmental appropriations or through revenues obtained as a result of government-mandated taxes, licenses, fees, or royalties;
- The entity is vested with and exercises exclusive or controlling power to administer its designated functions; and
- The entity is widely perceived and understood to be performing official (*i.e.*, governmental) functions.

In *Control Components,* defendants similarly challenged whether officials of foreign, state-owned companies in China, Korea, Malaysia, and United Arab Emirates qualified as "foreign officials." The government emphasized the foreign government's control power as the test for finding whether a company was an instrumentality. Here again, the court found that the question of whether a particular SOE could qualify as an instrumentality under FCPA was a question of fact and set forth a multifactor analysis that included not only the foreign state's degree of control, but also the entity's functions or objectives.

In *Haiti Telecom,* the defendants took a somewhat different tact, but came to the same disappointing result. In an unusual post-conviction (pre-sentencing) twist, defendants submitted a declaration from a former Haitian Minister stating Haiti Telecom had never been a state enterprise and remained a company under common law. Based on this new evidence, the defendants moved for a judgment of acquittal or a new trial. The next day, however, the DOJ submitted a clarifying declaration written by the Haitian Minister, claiming that he did not know that his prior statement was going to be used in criminal legal proceedings in the United States or that it was going to be used to support the argument that Haiti Telecom is not part of the Public Administration of Haiti. He said that the prior statement, while truthful, could be "confusing" and he gave several examples of government involvement in Haiti Telecom. Unpersuaded by the defendants' motion, the court, on October 12, 2011, rejected the defense's motion and pointed to its jury instruction providing non-exclusive factors to assess when deciding whether Haiti Telecom constituted an instrumentality of the government of Haiti.

It remains a question how the government will meet its burden to prove that a SOE is an instrumentality and whether the competing affidavits of government and non-government officials will become the norm. This, in turn, raises a future evidentiary issue with respect to how much weight may be afforded a foreign government's assertion that it controls (or does not control) an alleged SOE, particularly given the government's consistent position that the FCPA's definition of government official is "autonomous," *i.e.*, that it does not depend on the foreign government's classification of particular individuals as officials. Guidance on the recently passed U.K. Bribery Act is illuminating in its anticipation of this challenge, stating plainly that "because the exact nature of the functions of persons regarded as foreign public officials is often very difficult to ascertain with any accuracy . . . the securing of evidence will often be reliant on the co-operation of the state any such officials serve." As we noted in previous *Trends & Patterns*, it remains to be seen just what facts could result in a SOE not being deemed an instrumentality.

This issue will again be put to the court and the jury in the upcoming *O'Shea* trial. In that case, the defendant's proposed jury instructions stress that an entity is not an instrumentality of a foreign government merely because it is government-owned; the entity must be "created, owned, or controlled by a foreign government to achieve a governmental purpose or function." The defense attempted to draw a distinction by citing to the OECD Convention to support its proposition that if an enterprise operates on a basis "substantially equivalent to that of a private enterprise," an employee of that enterprise is not performing a governmental purpose or function. Recall that the *Lindsey Manufacturing* court already found the government's position on foreign officials persuasive in part because of the OECD Convention. Undeterred, O'Shea is hoping to fare better despite relying on the same Convention.

If anything, prosecutors appear to have been encouraged by this year's many challenges to the definition of "foreign official" and corporations do not appear to have been encouraged to challenge them. Indeed, in 2011, six settlements, plea agreements, and deferred prosecutions involved SOEs (*Comverse, Maxwell, Rockwell, Watts, IBM* and *Bridgestone*). Four of these cases (*Maxwell, Rockwell, Watts, IBM*) involved Chinese officials or employees of SOEs. Two of these firms—Watts and Rockwell—allegedly made illegal payments to state-owned design institutes.

Foreign companies are bound by Chinese regulations that effectively compel foreign companies to partner with design institutes, which make product recommendations to SOEs. In *Watts* and previously in *Rockwell*, the companies are alleged to have made improper payments to employees of such institutes. The exact nature of these design institutes is not clear, nor are they always state-owned. In *Watts*, the SEC expressly stated that payments were made to "state-owned" design institutes; in *Rockwell*, the SEC said that design institutes are "typically state-owned." Previously, in *ITT Corporation* (2009), the SEC had alleged payments to employees of Design Institutes, "some of which were SOEs." This progression towards clarity may indicate the SEC's increasing wariness of public scrutiny towards what constitutes an instrumentality of a foreign government.

Territorial Jurisdiction over Non-U.S. Companies

Territorial jurisdiction over foreign persons was added to the FCPA in the 1998 amendments, which were intended to implement the OECD Convention's requirement that transnational bribery laws apply to "any person." The new language provided for jurisdiction over non-U.S. persons who "*while in the territory of the United States* . . . make use of the mails or any means or instrumentality of interstate commerce or . . . do any other act." Significantly, the statute does *not* say "*cause* any act in the United States," and it has been a quiet debate whether it covers a person who, while *outside* the territory of the United States, causes an act to be performed in the United States, such as executing a bank transfer.

The year ended with an entirely new expansion of what constitutes territorial acts. In *Magyar Telekom*, the DOJ's sole claim to anti-bribery jurisdiction (but not to books and records jurisdiction) was based on a foreign official's "U.S.-based email address," whereby email was "passed through, stored on, and transmitted from servers located in the U.S." This is a particularly weak jurisdictional basis, given that this one count resulted in

a Sentencing Guidelines calculation of eight times what the company would have had to pay under just the books and records provisions. Interestingly, although the DOJ's criminal information and the SEC's complaints both reference a sham consulting contract that "purported to require a New York, NY-based counterparty to provide vaguely-identified assistance" in connection with a *Magyar Telekom* acquisition, neither the DOJ nor the SEC allege any territorial act in connection with this sham contract.

Meanwhile, the U.S. authorities have often stated that their jurisdiction under the FCPA extended to foreign funds transfers that passed through correspondent accounts, a concept that we have previously referred to as "correspondent" bank account jurisdiction theory. Pursuant to "correspondent" bank account jurisdiction theory, a sufficient U.S. connection exists where a transfer is denominated in U.S. dollars and transferred via a "correspondent" bank in the U.S. These correspondent banks are maintained by banks to clear U.S. dollar transactions; their use is not controlled or even apparent to the parties to a funds transfer. The U.S. authorities have taken the position that such fleeting contact with U.S. territory is sufficient to satisfy the FCPA's jurisdictional requirement that non-U.S. persons "while in the territory of the United States, [the defendant] corruptly [made] use of the mails or any means or instrumentality of interstate commerce or [did] any other act in furtherance" of the bribery scheme.

This expansive theory of jurisdiction first surfaced in the 2008 *Siemens* matter and has been applied in the *TSKJ* cases, most recently in 2011 in the *JGC* case. JGC is the first Japanese company ever charged under the FCPA, and it is notable that, unlike its partners in the infamous *TSKJ* joint venture who were issuers or subsidiaries of issuers, JGC had no apparent commercial connection with the United States whatsoever. Instead, jurisdiction was based on territorial acts by KBR, its joint venture partner and co-conspirator and, for the substantive count, which involved a transfer between two foreign banks, on correspondent account liability.

The government may also have applied correspondent account liability in the *Tenaris* matter. In *Tenaris*, both the SEC and DOJ alleged that the Luxembourg company "made use of the means and instrumentalities of interstate commerce" in making a "same day transfer of approximately $32,140.67 through an intermediary bank" in New York to an agent acting on Tenaris's behalf. Neither the SEC nor DOJ chose to define "intermediary," and it remains unclear whether Tenaris owned or controlled the U.S. bank account or whether the account was merely a correspondent account for a foreign bank.[9]

The use of "correspondent" account liability, which has not yet been challenged or litigated by any defendant, is a powerful tool for the U.S. authorities. In the past, although the U.S. authorities had jurisdiction over a foreign issuer's books and records and internal controls by virtue of the issuer having filed periodic reports with the SEC, the U.S. authorities' ability to reach conduct by foreign companies under the FCPA's anti-bribery provisions had been circumscribed by the implicit requirement that the government prove that the foreign

[9] For a further discussion of these issues, you may wish to refer to our prior client publication, available at Shearman & Sterling, *A New Tool and a Twist? The SEC's First Deferred Prosecution Agreement and a Novel Punitive Measure* (May 24, 2011).

company had knowingly and deliberately taken some action in the United States in furtherance of a bribe to a foreign official.

However, this expanding scope of jurisdiction has not been left entirely unchecked. In June 2011, in the first of the *SHOT Show* trials, the court dismissed one of the substantive counts against defendant Pankesh Patel on the ground that the government could not establish territorial jurisdiction where Patel caused a DHL package containing a purchase agreement to be sent from the U.K. to a government informant in the U.S. The ruling represents the first successful challenge to the government's expansive interpretation of the FCPA's territorial jurisdiction. However, it is not clear whether the fatal weakness of the dismissed count was that Patel had acted in the U.K. or whether the acts "caused" in the U.S. were those of a government informant and thus arguably an act in furtherance of a bribery scheme. It therefore remains to be seen whether this will establish a strong enough precedent to influence future cases. If the sole jurisdictional hook were to be a package sent to the U.S., courts could be wary of entirely exonerating a defendant based on a yet unclear theory of jurisdiction.

Compliance Guidance

M&A

Several actions this year highlighted the importance of post-closing due diligence in M&A transactions where the target company poses potential corruption risks. In *Watts Water*, *Diageo*, and *Ball Corporation*, the SEC entered settlements with companies for violations of the books and records and internal controls provisions of the FCPA arising out of misconduct by recently-acquired subsidiaries. In *Watts Water*, the SEC alleged that Watts failed to implement adequate internal controls to address the potential FCPA problems posed by its ownership of a subsidiary that sold its products almost exclusively to state-owned entities. *Diageo* involved improper payments made by subsidiaries in India, Thailand, and South Korea that Diageo allegedly recognized had weak compliance policies and controls, but which Diageo failed to remedy in part due to its rapid multinational expansion through mergers and acquisitions. In *Ball Corporation*, the SEC specifically alleged that accounting personnel at Ball Corporation learned soon after acquiring an Argentine subsidiary that employees of the subsidiary may have made questionable payments before the acquisition, but failed to take sufficient action to ensure they did not continue. Taken together, these actions seem to send a strong message that the SEC expects acquirers to conduct due diligence and undertake measures to address existing FCPA issues in the aftermath of a merger.

The need to conduct appropriate due diligence even extends to non-issuers that cannot themselves be held liable by the SEC. This year, the DOJ and SEC brought enforcement actions against *Armor Holdings Inc.*, a recently-acquired subsidiary of BAE Systems PLC ("BAE"). Prior to its acquisition by BAE, Armor Holdings was a free-standing issuer. In 2011, it entered a non-prosecution agreement with the DOJ and entered a settlement with the SEC related to payments to U.N. officials before it was acquired by BAE, a non-issuer. Notably, despite the fact that Armor Holdings was no longer an issuer at the time of the action, the SEC

asserted jurisdiction over its books and records. The case thus demonstrates that acquisition by a non-issuer does not shield a former issuer from SEC liability, and accordingly even a non-issuer should take care to conduct adequate pre- and post-acquisition due diligence of any acquisition that poses a corruption risk or risk having to deal with (and pay for) an internal investigation, settle an enforcement action, and, in effect, pay a fine on behalf of its newly acquired property.

Role of Subsidiaries

A few cases this year illustrated the different ways the government might pursue an FCPA case when a subsidiary is primarily at fault. In *Bridgestone*, the DOJ charged Bridgestone, a Japanese manufacturer of tires and rubber products, with making corrupt payments from 1999 to 2007 to foreign officials in Latin America. The payments were made by local sales agents employed by Bridgestone's U.S. subsidiary, Bridgestone International Products of America, Inc. ("BIPA"). However, Bridgestone, the parent company, was alleged to have conspired with BIPA to facilitate these corrupt payments. Of note, the DOJ's Antitrust Division has separately charged Bridgestone for antitrust violations in connection with allegations that it had conspired to rig bids.

In the *DePuy/Johnson & Johnson* matter, the DOJ and SEC brought separate actions against the two companies: the DOJ filed a criminal information against DePuy, and the SEC filed a civil complaint against Johnson & Johnson ("J&J"). DePuy, a supplier of orthopedic medical devices, is a wholly-owned subsidiary of J&J. In its criminal information against DePuy, the DOJ alleged improper payments to doctors at publicly-owned hospitals in Greece. The DOJ also alleged that J&J was aware of, and became complicit in, the scheme after its acquisition of DePuy. The SEC's complaint against J&J related to a wider scope, including allegations of bribery in Romania and Poland. Furthermore, in addition to the facts laid out in *DePuy*, the SEC alleged that J&J not only failed to conduct due diligence in its acquisition of DePuy, but also that J&J allowed the *DePuy* bribery scheme to flourish by, *inter alia*, creating sham businesses to facilitate the bribery and paying its consultant outside of Greece to avoid its detection. In contrast to *DePuy*, however, the SEC did not allege that parent company J&J became directly involved in the improper conduct of its Polish and Romanian subsidiaries.

The filings alone do not tell the whole story, however, because the DOJ in fact entered into a deferred prosecution agreement with J&J, in which J&J accepted and acknowledged that the criminal information would be filed against DePuy. Attached to the DPA is a statement of facts that J&J acknowledged as true, which describes instances of wrongdoing not only in Greece, but also in Poland, Romania, and in connection with the Oil-for-Food program in Iraq.

In *Magyar Telekom*, a criminal information was filed only for *Magyar Telekom* (the subsidiary), but the parent (*Deutsche Telekom*, "DT") and Magyar Telekom entered into separate resolutions with the DOJ: DT entered into a non-prosecution agreement, while Magyar Telekom entered into a deferred prosecution agreement. DT, as a majority owner of Magyar Telekom and "issuer" under the FCPA, was charged only with books and records

and was not alleged to have been involved in the bribery allegations. Magyar Telekom, also an "issuer" under the FCPA, was charged not only for its improper conduct, but also for the conduct of its own subsidiaries. The SEC brought charges against both companies and settled with both, but obtained disgorgement from Magyar Telekom only. No other penalties were imposed on either entity.

"Reform" Efforts

Congressional Hearings

Various proposals to improve – or narrow – the FCPA continue to be bandied about by legislators this year, with very little result. As reported in the mid-year *Trends & Patterns*, the House of Representatives Judiciary Committee, Subcommittee on Crime, Terrorism, and Homeland Security held a hearing on FCPA enforcement and reform proposals in June. The hearing was convened as a response to an October 2010 U.S. Chamber of Commerce report on alleged shortcomings in the statute, and concerns of the business community about the lack of certainty in FCPA law. The issues raised by this report guided much of the debate about FCPA reform throughout 2011.

As previously reported, the House Committee hearing focused on alleged overreaching by federal prosecutors in FCPA enforcement actions, and included testimony in favor of FCPA reform from former U.S. Attorney General Michael Mukasey and former Deputy Attorney General George Terwilliger. Mukasey, representing the Chamber of Commerce, called for amendments that would create a compliance defense and for clarification of the definition of "foreign official." Greg Andres, acting Deputy Assistant Attorney General in the Justice Department's Criminal Division, responded that companies are already given credit for having robust compliance programs at sentence determination. Andres further argued that additional clarification of the definition of "foreign official" is impracticable in light of the various forms of governments around the world – a view that the DOJ has expressed in the past.

Although the hearing failed to produce any evidence of the overly aggressive FCPA enforcement complained of by the Chamber of Commerce, the Committee was generally receptive to the notion of reform, with Representative James Sensenbrenner (R-Wis.), the chair of the Committee, promising to introduce legislation to revise the Act to address the issue identified at the hearing. Staffers for Senators Amy Klobuchar (D-Minn.) and Chris Coons (D-Del.) are also reportedly considering FCPA reform legislation that would include a corporate leniency program for companies under which the DOJ would reward companies that disclose violations of the FCPA. Although a new bill was expected to be introduced in the fall of 2010, as of the date of publication, no reform legislation designed to curb the FCPA has been proposed.

In November, the DOJ publicly responded to the reform discussion and indicated that it would issue guidance that may render at least some of the proposed amendments moot. In a speech before an FCPA audience, Assistant Attorney General Larry Breuer announced that the DOJ is preparing "detailed new guidance on the [FCPA's] criminal and civil enforcement provisions" to be released next year. Breuer observed, however, that

over the past year, the trend across the globe is toward criminalization of foreign bribery – citing the new U.K. Bribery Act and anti-bribery laws recently passed in China and Russia – and that some of the reforms proposed at the House hearing, such as elimination of successor liability, would send the wrong message about the U.S. government's stance on corruption at a crucial moment in the global anti-corruption movement.

The SEC has similarly defended the need for strong enforcement of the FCPA in response to calls for reform by Congress. In response to a June 30th letter by Senator Mike Crapo (R-Id.) questioning the SEC's stance on a possible compliance defense and additional clarity with respect to the definition of "foreign official," SEC Chairman Mary Schapiro stated that the SEC already considers compliance programs as a mitigating factor in FCPA enforcement actions and explained that a compliance defense would only disincentivize companies from adopting rigorous anti-corruption programs by potentially allowing them to retain ill-gotten gains. Chairman Schapiro, echoing Breuer, expressed concern that an affirmative defense would significantly dilute the deterrence message sent by strong enforcement of the FCPA. Consistent with the DOJ's position at the June hearing, Chairman Schapiro took the view that the FCPA, along with SEC and DOJ guidance, sufficiently defines the term "foreign official" and explained the need to be flexible to accommodate various forms of government in foreign countries.

Legislation

While no legislation curtailing FCPA enforcement has materialized this year, members of Congress did propose several bills related to FCPA enforcement in the second half of 2011 that would, at least on their face, bolster the statute. In December, Representative Peter Welch (D-Vt.) introduced the "Overseas Contractor Reform Act," under which federal contractors convicted of violating the FCPA would be debarred from contracting with the federal government. Critics of the bill argue that it is unlikely to have any impact on FCPA enforcement because few FCPA actions result in findings of FCPA violations, and the proposed bill would only trigger debarment for violations of the FCPA's anti-bribery provisions. Earlier in December, Congressmen Ed Perlmutter (D-Co.) introduced a bill that would authorize private rights of action for violations of the anti-bribery provisions of the FCPA that damage domestic business, provided that the violation is caused by a "foreign concern." This legislation, too, has been criticized as unlikely to have much force because a "foreign concern" can only violate the FCPA "while in the territory of the U.S."

Undoubtedly, the most significant legislative change this year was the adoption of the SEC's Dodd-Frank whistleblower regulations, which went into effect on August 12, 2011. These regulations provide financial awards to individuals who report potential violations of federal securities laws, including the FCPA. These incentives only apply when the whistleblower provides information against an issuer and, to be eligible for an award, the information provided must lead to a successful SEC enforcement action resulting in monetary sanctions of over $1 million. Despite the eligibility requirements, however, these regulations are expected to significantly increase the flow of information to the SEC and result in more civil – and criminal – enforcement

actions. Under Dodd-Frank, FCPA whistleblowers can receive between 10%-30% of monetary sanctions imposed in *all* resulting enforcement actions *worldwide*.

According to the first progress report from the new program, released in mid-November, whistleblowers are coming forward at a rate of about seven per day. In addition to an increase in the number of tips received, the SEC had indicated that the quality of the tips and referrals has also improved. Data from 334 tips received during the first seven weeks indicate that the most common complaint categories were market manipulation (16.2%), corporate disclosures and financial statements (15.3%), and offering fraud (15.6%). Whistleblower submissions were received from individuals in 37 states and several foreign countries. The most foreign tips came from countries including China (10), the United Kingdom (9) and Australia (3). No awards were paid during the 2011 fiscal year.

In addition to providing the SEC with more and higher quality information under the whistleblower regulations, Dodd-Frank reform also enables the agency to bring actions against individuals, which is expected to substantially enhance FCPA enforcement. Sections of the Act clarify the SEC's legal authority to bring actions against "control persons." Although the SEC brought a settlement enforcement action premised on "control person" liability against executives of *Nature's Sunshine Products Inc.* in 2009, it was not clear until the passage of Dodd-Frank that the SEC had the power to sue individuals under this theory.

To the extent that the SEC increases it focus on individuals as a result of its new authority to target control persons, it will also be aided in its Section 9290 of the Dodd-Frank Act, which lowers the legal state of mind required to trigger liability for aiding and abetting a violation of the Exchange Act. Previously, a person had to "knowingly" provide substantial assistance to another person in violation of a provision of the Exchange Act. Now, a person has to "knowingly or recklessly" provide substantial assistance. Given these new changes in law, the coming year is likely to see a significant increase in the number of SEC enforcement against individuals in foreign bribery investigations.

The U.K. Bribery Act 2010

Official Guidance

After some delays, the U.K. Bribery Act 2010 (the "Act") finally came into force on July 1, 2011, following the publication of guidance by the U.K. Ministry of Justice in March 2011 on the "adequate procedures" defense to the corporate offense of failure to prevent bribery. The MoJ guidance provides six principles of bribery prevention,[10] along with eleven case studies which are designed to demonstrate how the six principles should be applied.

[10] The six principles are: (1) proportionate procedures; (2) top-level commitment; (3) risk assessment; (4) due diligence; (5) communication (including training); and (6) monitoring and review.

The MoJ guidance provides valuable insight into the U.K. government's view of how certain provisions of the Act should be interpreted concerning such matters as corporate hospitality, the meaning of "associated persons," and the jurisdictional reach of the Act. However, it is not clear to what extent the courts will share the same view on the Act's interpretation as that set out in the MoJ guidance. The MoJ also published a "Quick Start Guide" to assist small and medium-sized companies in complying with the Act.

The Director of the Serious Fraud Office ("SFO") and the Director of Public Prosecutions in the U.K., who have joint responsibility for prosecutions under the Act, have also published joint guidance setting out the approach to prosecutorial decision-making with respect to the Act. This guidance confirms that before bringing a prosecution they must, as with other offenses, be satisfied that (among other things) it is in the public interest to prosecute. It is difficult to predict at this stage how that concept will be applied in the context of the Act.

Separately, the Financial Services Authority ("FSA") has recently published a financial crime guide which now forms part of the FSA Handbook. The FSA is currently the main regulator for firms operating in the financial sector in the U.K.. Although the FSA is not an enforcement authority for the Bribery Act, the firms that it regulates are required to have in place effective systems and controls to monitor and manage legal risks, which includes the mitigation of legal risks relating to financial crime. The FSA's financial crime guide outlines steps that regulated firms can take to reduce their financial crime risk, and provides practice indications for firms on anti-bribery systems and controls. The FSA guidance does not seek to establish guidance or a particular interpretation on the Bribery Act. However, it would be used by the FSA in assessing and enforcing any systems and controls breaches by regulated firms.

Industry Guidance

Industry specific guidance has also been published by leading bodies. Most recently, the British Bankers' Association ("BBA") published a comprehensive guide for financial institutions on steps that the banking sector can take to comply with the Act. The guidance gives an overview of the six principles under the MoJ guidance and how they may apply to financial institutions. Chapter 2 of the BBA guidance provides a useful comparison of the Act with the FCPA and also compares financial institutions' obligations under other industry rules with their obligations under the Act. The BBA has indicated that in 2012 it will undertake separate work in relation to wider bribery and corruption risks, including managing third-party bribery risks and the issue surrounding corrupt politically exposed persons.

Of particular note are the "red flags" sections of the BBA guidance. These set out a number of red flags which may be identified by a financial institution, and the appropriate response. In the context of undertaking due diligence on an associated person, the BBA notes that "[w]here a red flag is identified it should be documented and there should be a clear audit trail detailing any further investigation undertaken, how any issues have been resolved and the decision of whether to proceed." Examples of red flags in this area set out by the BBA include: "the associated person insists on operating in anonymity"; "there are persons involved in the transaction who have no substantive commercial role"; and "the associated person does not reside or have a significant business

presence in the country where the customer or project is located." Examples of red flags in the context of the MoJ's sixth principle (monitoring and review) are: "excessive or disproportionate gifts and hospitality, offered, received and declined"; "relocation of third party/supplier/contractor/agents to countries with higher bribery risk"; and "large/frequent fourth-quarter adjustments to contractual payments by associated persons."

The Act's treatment of gifts, corporate hospitality and promotional expenditure are issues of concern to many companies and the BBA guidance deals specifically with these topics. For example, its guidance states, "The best protection for banks, to ensure they do not infringe the Bribery Act, is to have in place clear written policies detailing the principles for giving and or receiving gifts, entertainment and hospitality."

Focus on Non-U.K. Companies?

As we have noted in previous *Trends & Patterns*, the U.S. authorities, after years of focusing on U.S. companies, have recently targeted non-U.S. companies as part of an apparent effort to spur non-U.S. enforcement agencies to be more active in this area. It is interesting, therefore, to note the repeated statements by the SFO's Director, Richard Alderman, that the SFO will focus from the outset on prosecuting non-U.K. companies with a business presence in the U.K. Mr. Alderman has stated that this will be an SFO priority to help ensure that U.K. companies which behave properly are not subject to unfair competition from non-U.K. companies which do not.

U.K. Prosecutions

Although the Act only came into force in July 2011, the first prosecution and sentencing for an offense under the Act has already taken place. Many thought the first such prosecution would be brought against a company, but it was in fact a clerk from Redbridge Magistrates Court who was convicted of an offense under section 2(1) of the Act. He was sentenced to three years' imprisonment for the offense under the Act (as well as six years for misconduct in public office, with the two sentences to run concurrently).

In terms of foreign bribery cases, it will likely be some time before we see a prosecution, given that the Act only applies to events after July 1, 2011 and the time required to investigate such cases. In the meantime, the previous hodgepodge of various laws will continue to apply to conduct prior to that date. These provisions include regulatory oversight of financial companies by the FSA and the possibility of civil actions by the SFO.

Willis Limited

On July 21, 2011 the FSA published its Final Notice to Willis Limited, a leading insurance broker. Willis was found to have failings in its anti-bribery systems and controls in relation to payments made to overseas third parties. It was fined nearly £7 million for breaches of the FSA's Principles for Business and the FSA Handbook. This is the biggest fine imposed by the FSA to date in this area, but it would have been nearly £10 million if it

were not for a number of mitigating circumstances, including the fact that Willis settled at an early stage of the investigation.

The FSA determined that between January 14, 2005 and December 31, 2009, Willis failed to take reasonable care to establish and maintain effective systems and controls to counter the risks of bribery and corruption associated with making payments to overseas third parties. These third parties had helped Willis win and retain business from overseas clients, and it was found that Willis had a weak control environment in relation to the making of such payments. As a result, there was an unacceptable risk that the payments made by Willis could be used for corrupt purposes (including the payment of bribes). A number of payments made by Willis during the course of the FSA's investigation were identified as suspicious and were reported to the Serious Organised Crime Agency in the U.K.

While Willis had amended its policies and guidance following a letter circulated by the FSA in November 2007 to all wholesale insurance broker firms (including Willis) and the publication of the Final Notice to Aon Limited by the FSA in January 2009, the FSA determined that Willis had failed to implement these policies properly. The Final Notice to Willis also criticizes the limited information given to senior management on financial crime issues.

Macmillan Publishers

On July 22, 2011, the High Court granted a civil recovery order against Macmillan Publishers Ltd in the sum of £11.2 million. The order was imposed following an agreement between the SFO and the company, and recovers sums received by Macmillan through illegal payments which it had made to secure business contracts in Africa. Separately, Macmillan has also been debarred from participating in World Bank funded tender business for a period of at least three years, and a compliance monitor will be in place for a 12-month period (who will report to both the SFO and the World Bank).

Macmillan has also agreed to undertake an independent investigation into publicly tendered contracts which it had won elsewhere in Africa between 2002 and 2009. The SFO stated, "It was impossible to be sure that the awards of tenders to the Company . . . were not accompanied by a corrupt relationship." Therefore, Macmillan may have received revenue which had been derived from unlawful conduct.

The SFO's decision to proceed by a civil recovery action rather than a criminal prosecution appears to reflect a number of factors, including the fact that Macmillan approached the SFO with a view to cooperation and agreed to undertake an internal investigation. Although the Macmillan action is only the fifth time that the SFO has entered into such a civil settlement with a company, it was the third such settlement in 2011 alone. The other civil recovery actions in 2011 related to (1) proceedings against DePuy International Limited, the U.K. subsidiary of Johnson & Johnson, which was ordered to pay almost £5 million, and (2) M W Kellogg Limited, the U.K. subsidiary of Kellogg Brown and Root LLC, which was ordered to pay just over £7 million.

Deferred Prosecution Agreements

The SFO does not currently have the power to enter into a DPA. However, the U.K. authorities have indicated a strong interest in adding DPAs to the prosecutorial toolbox, and there is now increasing expectation that the U.K. will introduce a similar concept in the near future. Richard Alderman, the current Director of the SFO, is very keen on obtaining the power to enter into such agreements and the Attorney-General, speaking in September 2011, stated that the "crucial question for any comparable U.K. process would be the degree of judicial oversight and the mechanism for achieving that….if the U.K. can learn from the U.S. experience and avoid some of the pitfalls the Americans have encountered then deferred prosecution agreements may offer a new way for the U.K. to deal with corporate crime in appropriate cases." Indeed, DPAs may be particularly helpful in the U.K. given the recent experience in cases such as *Innospec* which highlighted the difficult interface between negotiated settlements and the sentencing power of the English courts.

DPAs are still some way off in England and it currently remains to be seen whether there will be sufficient Parliamentary and judicial support for them.[11] Many practical issues are still to be resolved around how they would work. For example, what would be the legal treatment of discussions which did not ultimately lead to a DPA being concluded? If those discussions could later be used against the company in that situation, that would likely have a significant effect on the level of defendant cooperation with this process.

If the SFO was granted the power to proceed with DPAs, it is likely that such agreements would include both a financial penalty and remedial measures that could be tailored to suit the company in question and the particular harm done. Similar measures in the U.S. have included disgorgement of profits and the removal of directors. DPAs in the U.K. might also include a court-appointed monitor to oversee DPA compliance, if adequate anti-corruption procedures are not already in place.

[11] Unlike the current initiative in the U.K., DPAs and their non-judicial counterparts (NPAs) were developed and implemented in the United States without any particular statutory authority.

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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