Fraud Investigation &
Dispute Services

December 2013

Business briefing:

Foreign Corrupt Practices ACT Guidance issued

"The fight against corruption is a law enforcement priority of the United States ... and we will continue to make clear that bribing foreign officials is not an acceptable shortcut."

Lanny A. Breuer – November 14, 2012
Assistant Attorney General – U.S. Department of Justice Criminal Division

"Investors must have faith that the economic performance of public companies reflects lawful considerations of markets, price and product rather than a mirage resulting from bribery and corruption."

Robert Khuzami – November 14, 2012
Director – U.S. Securities and Exchange Commission Division of Enforcement

On November 14, 2012, the US Department of Justice (DOJ) and the US Securities and Exchange Commission (SEC) jointly released A Resource Guide to the U.S. Foreign Corrupt Practices Act, (Guide). The Guide demonstrates their shared commitment to fighting corruption through continued vigorous enforcement of the Foreign Corrupt Practices Act (FCPA).

The interpretations of the FCPA and views of the DOJ and SEC offered within the Guide do not have the force of law. However, given that nearly all FCPA cases against companies are settled outside of court, such views matter greatly to US companies and foreign multinational companies.

The Guide details the approach and priorities of the DOJ and SEC in FCPA enforcement. Topics include global anti-corruption and inter-agency efforts, discussion of key anti-bribery elements and accounting provisions, affirmative defenses, principles of enforcement, and penalties, sanctions and remedies. Fact patterns and hypotheticals illustrate the government's interpretation and application of the FCPA to commonly faced corruption issues.

Perhaps most significantly, the Guide underscores the importance of a company's compliance program to prevent and detect corrupt activity. This view is reinforced through the "hallmarks" of effective corporate compliance, which is a practical framework companies of any size can use to implement risk-based anti-corruption measures.

Corporate compliance programs

The Guide provides "hallmarks" or elements of an effective compliance program. In doing so, it sets forth principles that are perhaps more detailed but very similar to the "Adequate Procedures" guidance issued under the UK Bribery Act, and the Organization for Economic Co-operation and Development's (OECD's) "Good Practice Guidance on Internal Controls, Ethics and Compliance."

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Building a better working world

Many program elements in the Guide are similar to leading practices adopted by many large global companies. The Guide acknowledges that small and medium-size companies will have different compliance programs from large multinationals and in doing so implicitly agrees that cost and size is a factor in measures companies should take to achieve compliance.

It endorses the concept of risk assessment as "fundamental to developing a strong compliance program" stating that "[o]ne-size-fits-all compliance programs are generally ill-conceived and ineffective because resources inevitably are spread too thin, with too much focus on low-risk markets and transactions to the detriment of high-risk areas."

Ten elements of an effective program:

- *Commitment from senior management and a clearly articulated policy against corruption* – often referred to as "tone at the top", senior management and board directors alike are responsible for conveying and adhering to a company-wide anti-corruption policy.
- *Code of conduct and compliance policies and procedures* — a code of conduct provides ethical guidelines for those conducting business on the company's behalf. A company may also have specific anti-corruption policies and procedures that address its most significant risks, outline proper internal controls and monitoring procedures.
- *Oversight, autonomy and resources* — responsibility for the compliance program should be assigned to an appropriate senior individual or group in order to provide the authority and autonomy to oversee the program and report to the company's governing body.
- Risk assessment — a company's compliance program should be designed around and commensurate to its unique risk profile taking into account factors such as its size, structure, industry, geography, interactions with foreign governments, and involvement of business partners. A thorough risk assessment adds both efficiency and credibility to anti-corruption compliance efforts.
- *Training and continuing advice* — a company should take steps to ensure that all employees are aware of the company's anti-corruption policies and procedures which is often accomplished through periodic training. Certain key roles, such as management, sales, finance, and business development personnel, may receive enhanced training.
- *Incentives and disciplinary actions* — to avoid the appearance of a "paper program", the corporate compliance program must be enforced unequivocally throughout the organization with clear disciplinary procedures for violators applied timely and consistently. Also, positive incentives, both financial and other merit based rewards, may reinforce a culture of compliance.
- *Third-party due diligence and payments* — a risk-based due diligence approach identifies and devotes attention to third parties posing the greatest corruption risk. The guidance highlights three areas to govern dealings with third parties from pre-contract due diligence efforts to payment terms and ongoing monitoring of third party relationships.
- *Confidential reporting and internal investigation* — employees and third parties should be encouraged to share 'tips' or suspected violations in a secure and confidential manner. Such reports should ultimately be triaged by qualified individuals who are responsible for investigating corruption allegations.
- *Continuous improvement: periodic testing and review* — companies may perform periodic testing or anti-corruption audits to monitor compliance with the various elements and controls of the program and to uncover existence of potential violations and "red flags" signaling new corruption risks.
- *Pre-acquisition due diligence and post-acquisition integration* — an acquirer is responsible for conducting thorough due diligence of a potential target company which extends to evaluating potential corrupt activity by the target.

Other highlights

The Guide provides useful information and insight into a number of areas, detailed below.

Gifts and entertainment

- Individual gifts and entertainment of reasonable amounts are not likely to face government scrutiny; "DOJ's and SEC's anti-bribery enforcement actions have focused on small payments and gifts only when they comprise part of a systemic or long standing course of conduct that evidences a scheme to corruptly pay foreign officials to obtain or retain business … . The FCPA does not prohibit gift-giving. Rather, just like its domestic bribery counterparts, the FCPA prohibits the payments of bribes, including those disguised as gifts." For example, a small one time gift may be allowable but repeated nominal gifts may indicate corrupt intent.
- Controls over gifts and entertainment of government officials need to be in place: "as part of an effective compliance program, a company should have clear and easily accessible guidelines and processes in place for gift-giving by the company's directors, officers, employees, and agents."

Definition of a government official

- The Guide addresses an area of concern for companies trying to determine who constitutes a government official. In many countries the distinction between a commercial enterprise and a government affiliated entity is unclear. The DOJ and SEC have long advocated a broad interpretation as to the definition of a government "instrumentality" or government affiliated entity. In the Guide, the DOJ and SEC state that they view government control over the entity as the deciding factor: "As a practical

matter, an entity is unlikely to qualify as an instrumentality if a government does not own or control a majority of its shares."

Books and records

- The FCPA's accounting provisions are very broad and not just related to bribery. It states that the accounting provisions of the FCPA cover both books and records and internal controls and are designed to "ensure that all public companies account for all of their assets and liabilities accurately and in reasonable detail, and they form the backbone for most accounting fraud and issuer disclosure cases brought by the DOJ and SEC."

Third Party Due Diligence

More than 90% of reported FCPA cases involved the use of third-party intermediaries such as agents or consultants. Appropriately, this is a central focus of many anti-corruption efforts but the degree of due diligence for each third party should be commensurate with the risks posed by that third party. Notwithstanding the perceived risk associated with a third party, three principles to govern dealings with all third parties are (1) pre-contract due diligence to assess the third party's qualifications, reputation, and connections to foreign officials; (2) understanding the business purpose and services being provided by the third party and ensuring payment terms are in line with the services provided; and (3) monitoring third parties with controls such as periodic due diligence, training to or certifications provided by third parties, and exercising contractual audit rights.

- The Guide draws a link between an FCPA violation and issuers' responsibility under the Sarbanes–Oxley Act of 2002 (SOX), requiring issuers and their auditors to report to the public on the effectiveness of internal controls related to financial reporting. It adds "internal controls include those related to illegal acts and fraud —including acts of bribery — that could result in a material misstatement of the company's financial state¬ments."
- A company's compliance program is called "a critical component of an issuer's internal controls." DOJ and SEC's review of a company's compliance program "is an important part of the government's assessment of whether a violation occurred." Accordingly, the Guide implies that public companies without an effective anti-corruption program will not only have problems obtaining leniency from prosecution, but may in fact be liable for an FCPA violation under the internal controls provision.

Materiality

- Some companies may gain comfort on the issue of materiality and the risk of prosecution for any small payments. While the Guide restates the government's long-held position that there is no materiality threshold for an FCPA violation, it further offers that "[a]s with the anti-bribery provisions, DOJ's and SEC's enforcement of the books and records provision typically involved misreporting of either large bribe payments or widespread inaccurate recording of smaller payments made as part of a systemic pattern of bribery."

Successor liability and FCPA due diligence

- Not surprisingly, the Guide highlights that pre-acquisition FCPA due diligence should be conducted on potential targets. This is particularly important to acquirers given that successor liability "prevents companies from avoiding liability by reorganizing."
- Actions have been taken against successor companies in limited circumstances that generally involve "egregious and sustained violations or where the successor company directly participated in the violations or failed to stop the misconduct from continuing after the acquisition". The Guide points to specific examples where FCPA due diligence and post-acquisition compliance efforts resulted in the government's decision not to prosecute successor companies for pre-acquisition violations.
- When issues surface as a result of an acquisition, the government will evaluate whether the acquiring company conducted pre-acquisition FCPA due diligence as part of its assessment of the acquirer's commitment to compliance and whether the acquiring company promptly integrated the acquired company into its compliance program, including implementing policies, requiring training and performing audits.

Self-reporting

- The Guide reiterates long-standing government support for the concept of self-reporting: "both DOJ and SEC place a high premium on self-reporting, [...] in determining the appropriate resolution of FCPA matters." It also specifies the factors that the government takes into account when conducting an investigation, making a charging position or negotiating a settlement. Little new information is offered to encourage a company to voluntarily report a violation by, for example, more clearly defining the benefits of self-reporting, identifying the boundaries of such cooperation up front and limiting the required level of additional internal investigation.

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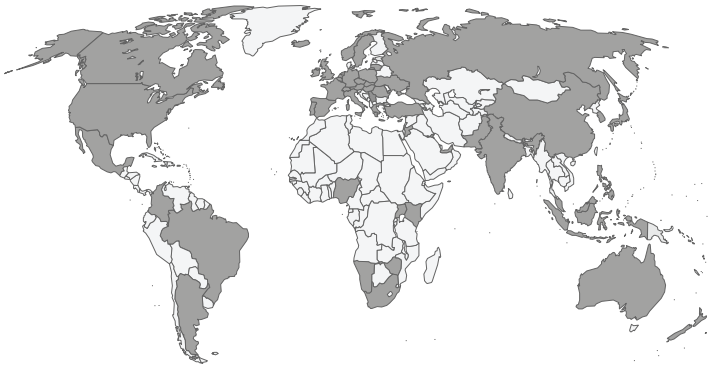

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