



world compliance

FCPA—Mergers and Acquisitions



**FOREIGN CORRUPT PRACTICES ACT
MERGERS AND ACQUISITIONS**

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Overview

Thirty years after its enactment in 1977, the Foreign Corrupt Practices Act (FCPA)¹ is experiencing the most aggressive enforcement level ever by the Department of Justice (DOJ), and the Securities and Exchange Commission (SEC). A tremendous upswing in enforcement activities in the past several years has been marked by aggressive law enforcement techniques such as search warrants, undercover officers, confidential informants, wiretaps and other strategies typically reserved for investigations of violent gangs and drug trafficking organizations. The government's FCPA enforcement strategy has resulted in large corporate fines and criminal penalties for individuals. The Obama Administration has made it clear to the business community that FCPA enforcement will be a high priority and focused on new industries—pharmaceutical and financial institutions—while additional resources are being assigned to carry out this enhanced effort. As stated in the DOJ's Criminal Division Presidential budget request:

FCPA enforcement is consistent with the Obama Administration's goals of promoting transparency, democracy, sustainable development, and good governance. The global economic crisis presents a real threat to our progress in promoting integrity in international business.²

The FCPA poses crucial challenges, in particular for companies seeking to expand in new markets via mergers and acquisitions, especially when targets are foreign companies and/or have extensive foreign operations. Under the FCPA, an acquiring company may be held liable for any prior unlawful payments made by the acquired company. Prosecutions in the mergers and acquisitions context have been especially high in recent years—almost half of the FCPA prosecutions in the United States arose from pre-acquisition due diligence and disclosure by acquiring companies. It is therefore imperative for acquiring companies to conduct FCPA-specific due diligence to evaluate and resolve any potential FCPA problems before the deal closes, and to enact compliance monitoring programs that persist after the deal is closed.

The FCPA anti-bribery provisions prohibit a domestic concern (a U.S. person or corporate entity) from making corrupt payments or promises to pay foreign officials for the purpose of obtaining or retaining business. Definitions of certain terms, including domestic concern and foreign official, are intentionally expansive to encompass as much business activity as possible. The FCPA's accounting controls provisions include books and records provisions and internal control mechanisms, which apply to corporations whose securities are registered with the SEC or who

¹ Foreign Corrupt Practices Act of 1977, codified as amended at 15 U. S. C. §§ 78m, 78dd, and 78ff .

² Department of Justice, Criminal Division Presidential Budget Request, *available at* <http://www.justice.gov/jmd/2011justification/pdf/fy11-crm-justification.pdf>.



must file regular reports with the SEC. These companies must maintain accurate records to account for certain expenditures and verify use of assets.

FCPA Enforcement Has Dramatically Increased Resulting In Corporate Mega Fines And Increased Scrutiny Of Individuals

The numbers tell the story: year after year, the number of enforcement actions is up. Recent enforcement actions and prosecutions have increased fivefold since 2004; in 2008, DOJ and the SEC assessed fines and penalties of approximately \$2.8 billion against thirty-six corporations and sixty-four individuals for FCPA violations. Of the thirty-six enforcement actions against companies, several have resulted in blockbuster corporate fines:

December 2008: Siemens, AG and three subsidiaries pled guilty to alleged FCPA violations and agreed to pay \$1.6 billion in fines to U.S. and foreign authorities.³

February 2009: Kellogg, Brown and Root pled guilty to a bribery scheme in Nigeria and agreed to pay \$402 million in criminal fines, and \$177 million in disgorged profits.⁴

February 2010: BAE Systems plc ends a ten plus year bribery ring involving mid-East countries and agreed to pay \$400 million in fines.⁵

June 2010: Technip S.A. agreed to pay a \$240 million criminal penalty and agreed to disgorge \$98 million in disgorged profits.⁶

Additional evidence of this growing enforcement trend also exists in the prosecution rates of individuals over just the past two years. In 2009, forty-six individuals were prosecuted for FCPA violations, up from just sixteen in 2008. Lanny A. Breuer, Assistant Attorney General for DOJ's Criminal Division, recently stated:

Put simply, the prospect of significant prison sentences for individuals should make clear to every corporate executive, every board member, and every sales agent that we will seek to hold you personally accountable for FCPA violations. As we undertake these efforts, we hope to do so with enhanced resources. As I imagine most of you have heard, in 2007 the FBI created a squad with agents dedicated to investigating potential FCPA violations. The

3 See <http://www.justice.gov/opa/pr/2008/December/08-crm-1105.html>.

4 See <http://www.justice.gov/opa/pr/2009/February/09-crm-112.html>.

5 See <http://www.justice.gov/opa/pr/2010/March/10-crm-209.html>.

6 See <http://www.justice.gov/opa/pr/2010/June/10-crm-751.html>.



squad has been growing in size and in expertise over the past two years. In addition, we have begun discussions with the Internal Revenue Service's Criminal Investigation Division about partnering with us on FCPA cases around the country. Finally, we are now pursuing strategic partnerships with certain U.S. Attorney's Offices throughout the United States where there are a concentration of FCPA investigations. Our successful efforts thus far in FCPA enforcement have been due in large part to the amazing work of our talented career prosecutors in the Fraud Section and enforcement responsibility, of course, will remain with the Criminal Division's Fraud Section. But these partnerships, we hope, will greatly increase our resources and permit us to capitalize on the skill and expertise of AUSAs in some of the best U.S. Attorney's Offices in the country.⁷

The DOJ is practicing what it preaches. In one recent sting operation conducted over a two year period, the DOJ aggressively employed more traditional law enforcement techniques including undercover agents, wiretaps and search warrants. In January 2010, the sting operation culminated in the arrest of twenty-two arms and weapons dealers in Las Vegas, Nevada. An undercover informant posed as a broker for the Minister of Defense from an African nation.⁸ The undercover informant wore a body wire, recorded hundreds of conversations with the twenty-two individual targets, and worked closely with an undercover FBI agent who posed as a "middle-man" needed to facilitate "commissions" payable to the Minister of Defense. According to the DOJ's press release on the day of the arrest:

In connection with these indictments, approximately 150 FBI agents executed 14 search warrants in locations across the [United States] and seven search warrants were executed by City of London Police in the United Kingdom.⁹

All told, the arrest and indictments stemming from the Las Vegas raid represent the single most expansive investigation and enforcement action by the DOJ, and are a foreshadowing of the enforcement to come.

⁷ Comments by Lanny Breuer to the 22nd National Forum on Foreign Corrupt Practices Act, November 17, 2009. See <http://www.justice.gov/criminal/pr/speechestestimony/documents/11-17-09aagbreuer-remarks-fcpa.pdf>.

⁸ See <http://www.mainjustice.com/2010/04/05/fcpa-sting-case-why-gabon/>; see also http://www.fbi.gov/page2/jan10/fcpa_012610.html.

⁹ See <http://www.justice.gov/opa/pr/2010/January/10-crm-048.html>.



The FCPA's Anti-Bribery Provisions

The Las Vegas raid provides a textbook study of the FCPA in action and enforcement of its anti-bribery provisions. The indicted individuals were part of an alleged conspiracy to pay “commissions” to the Minister of Defense in exchange for securing several arms deals. In FCPA lingo, (1) domestic concerns (the individuals); (2) corruptly paid something of value (cash commissions); (3) to a foreign official (Minister of Defense and his intermediary); (4) for the purpose of obtaining business (military contracts). Below is a thorough explanation of each of the important components.

Who is covered

The FCPA’s anti-bribery provisions apply to three types of individuals and corporate entities:

(1) Issuers. An “issuer” is any company whose security is registered with the SEC or who files regular reports with the SEC.¹⁰ This includes foreign companies whose securities are traded on domestic stock exchanges through the use of ADRs, and extends to subsidiaries of the issuer.

(2) Domestic concerns. Domestic concerns are U.S. citizens, nationals, residents and any business or partnership whose principal place of business is in the United States.¹¹

(3) Any person other than an issuer or domestic concern, including foreign nationals or businesses within the territory of the United States.¹²

“Corrupt payment” must be for purpose of obtaining or retaining business

The payment or promise of payment made by one of the above three subjects must be made “knowingly” that the payment would influence a foreign official “in order to assist . . . in obtaining or retaining business,” i.e. the “conduct.”¹³ For purposes of the statute, “knowing” is either actual knowledge or being aware the conduct is taking place. It is sufficient if the person has a “firm belief” that the circumstances (i.e. a corrupt payment is being made for the purpose of obtaining or retaining business) exist or the result is “substantially certain to occur.”¹⁴ The “firm belief” standard has an expansive, catch-all scope.

10 15 U.S.C. § 78dd-1(a).

11 15 U.S.C. § 78dd-2(h)(1).

12 15 U.S.C. § 78dd-3(f).

13 15 U.S.C. § 78dd-3(f).

14 15 U. S. C. § 78 dd-1(a) and (f).



“Willful blindness” is not sufficient to avoid FCPA liability. As set forth in the Conference Report:

In clarifying the existing foreign anti-bribery standard of liability under the Act as passed in 1977, the Conferees agreed that “simple negligence” or “mere foolishness” should not be the basis for liability. However, the Conferees also agreed that the so called “head-in-the-sand” problem – variously described in the pertinent authorities as “conscious disregard,” “willful blindness” or “deliberate ignorance” – should be covered so that management officials could not take refuge from the act’s prohibition by their unwarranted obliviousness to any action (or inaction), language or other “signaling device” that should reasonably alert them of the “high probability” of an FCPA violation.¹⁵

Conscious disregard or purposefully avoiding learning the truth will be considered sufficient knowledge. If a subject knows or has enough information available to believe circumstances exist for a violation to occur, they must act to stop the potential violation and cannot “look the other way.”

Any payment or offer to pay must be made “corruptly.” One court has defined corruptly as:

[t]he offer, promise to pay, payment or authorization of payment, must be intended to induce the recipient to misuse his official position or to influence someone else to do so . . . an act is “corruptly” done if done voluntarily and intentionally, and with a bad purpose of accomplishing either an unlawful end or result or a lawful end or result by some unlawful method or means.¹⁶

The corrupt payment or offer to pay must be made for the purpose of “influencing,” “inducing” or securing an “improper advantage” in “obtaining or retaining business.”¹⁷ The FCPA applies to more than payments of a “suitcase full of cash” to foreign government leaders to secure a government contract. The term “anything of value” has been broadly construed to include not only cash or a cash equivalent, but also, among other things, discounts; gifts; use of materials, facilities or equipment; entertainment; drinks; meals; transportation; lodging; electronics; insurance benefits; and promise of future employment. There is no de minimis

15 1977 Legislative History – House Report, available at http://10.173.2.10/criminal/fraud/fcpa/history/1988/trade_act.html.

16 15 *United States v. Liebo*, 923 F.2d 1308, 1312 (8th Cir. 1991).

17 15 U. S. C. § 78dd-1(a).



value associated with the “anything of value” element, and the perception of the recipient and the subjective valuation of the thing conveyed is often a key factor considered by the enforcement agencies in determining whether “anything of value” has been given to a foreign official.

For example, a vice-president of a military supplier was convicted of violating the FCPA when he paid for airline tickets for the cousin of a foreign official because, despite the cousin’s testimony that he considered the tickets to be a personal “gift,” the payment was made shortly before a contract was approved and the official had a close relationship with his cousin.¹⁸ Something which might be common practice or custom in a country such as bribes to custom officials, will also run afoul of the FCPA if the stated purpose of the bribe is to assist companies to obtain and retain business.¹⁹ Thus, in *United States v. Kay*, two executives of an American rice exporter were convicted under the FCPA for payments to Haitian custom officials that the Court acknowledged were “the standard practice” and “business as usual” in Haiti.²⁰

Foreign Officials

The recipient of a payment or promise to pay must be a “foreign official,” which is broadly defined to include every possible level of government official; such as a member of a foreign political party or official, candidate for foreign political office, officer or employee of the foreign government and any of its departments, agencies; instrumentalities; or public international organization.²¹ Examples of foreign officials include officials of government owned banks, directors of regional health care funds, physicians and other employees from government owned or controlled hospitals, and officials of government owned financial management services. Of course, the lines between private and government enterprises are often blurred in certain regions of the world (e.g. China).

Instrumentalities, although not clearly delineated in the statute, may include quasi-governmental agencies or business joint ventures between the government and the private sector. Public international organizations are an organization designated as such by Executive Order.²²

18 *Liebo, supra* at 1312.

19 *See United States v. Kay*, 513 F.3d 461, 464-466 (5th Cir. 2007), *aff ’g* 359 F.3d 738 (5th Cir. 2004).

20 *United States v. Kay*, 513 F.3d 432, 439 (5th Cir. 2007).

21 15 U.S.C. § 78dd-1(f)(1)(A).

22 15 U.S.C. § 78dd-1(f)(1)(B)(i)-(ii).



Due to the expansive definitions, the General Manager of a foreign corporation that is partially owned by a government entity is a “foreign official.”²³ Accordingly, even companies seeking to enter into investment opportunities or joint ventures with such persons must consider taking precautions to ensure compliance with the FCPA.²⁴

Third-party Payments

The FCPA also contains broad third-party payments provisions under which the actions of foreign subsidiaries and other third parties such as agents, consultants, distributors, and joint venture partners can result in FCPA liability to a parent company or the entity engaging the third-party. In other words, companies are not immune from FCPA liability by doing business abroad through others because the FCPA prohibits improper payments to “any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to a foreign official.”

Exceptions and Affirmative Defenses

There are very limited and narrow exceptions and affirmative defenses to the statutory violations. Business customs or practices in a foreign country are not enough to escape liability.²⁵ Recognizing that some business customs or practices might influence everyday business decisions, the statute allows, as an exception, payments made to a foreign official for the purpose of facilitating or expediting routine governmental action.²⁶ Examples include payments to obtain permits or licenses or to receive mail, telephone, water, electrical, or cargo handling services.²⁷ Presumably, such payments are not for the purpose of obtaining or retaining a business advantage because they are made for a legitimate purpose. Regardless of the reason, any such payments should be properly accounted for, and recorded to reflect their legitimacy and purpose.

Two affirmative defenses allow consideration for payments or offers which are legally justified or part of a legitimate business activity. First, a payment or offer to pay pursuant to a written law or regulation of the foreign country might be appropriate.²⁸ One example of such a payment would be one made to cover expenses of an administrator appointed by a foreign court in order to proceed with the disposition of an estate.²⁹ A written law, however, does not always protect from FCPA liability.

23 FCPA Op. Proc. Rel. 08-01.

24 *See id.*

25 *See, e.g., Kay*, 513 F.3d at 439.

26 15 U.S.C. § 78dd-2(b).

27 15 U.S.C. § 78dd-1(f)(3)(A); 78dd-2(h)(4)(A); 78dd-3(f)(4)(A).

28 15 U.S.C. § 78dd-2(c)(1).

29 FCPA Op. Proc. Rel. 07-03.



Thus, the DOJ indicated that it would conduct a criminal investigation if a company subject to an otherwise lawful \$50,000 environmental damage fine by the Nigerian government proceeded to make payment of the fine through a “recommended” contractor.³⁰

The second affirmative defense is a bona fide payment or gift—which is a legitimate business expenditure and directly relates to the promotion, demonstration or explanation of a product or service, or to the performance of a contract with a foreign government or agency.³¹ Proper payments under this category may include travel expenses to attend an educational and promotional tour of a company’s U.S. operation sites³² or the provision of product samples for the purpose of testing and evaluation by the appropriate foreign government agency.³³ The DOJ has also indicated that it would not investigate a stipend paid to local journalists employed by media outlets wholly owned by the People’s Republic of China to cover local transportation costs, a meal, and incidental expenses that enabled the journalists to attend a company’s promotional conference in Shanghai.³⁴ The DOJ did, however, prosecute a company that provided two-expense paid trips to various tourist destinations in the U.S. for the chairman (and his wife and children) of an Egyptian instrumentality that awarded the company contracts for the maintenance of wastewater treatment facilities.³⁵

Each of the examples of permissible payments above carries the caveat that the companies at issue undertook several precautions and controls to assure FCPA compliance. Thus, in each instance that the DOJ approved a particular payment or practice through its opinion release process, it further stated that its decision was not binding on any other party nor would it bind the DOJ if the facts as represented were not accurate or complete.

Penalties

Wide ranging civil and criminal penalties for violations add to the potency of the FCPA. On the civil side, the DOJ can avail itself of injunctive relief if it believes an individual or domestic concern is engaged in illegal conduct.³⁶ Although corporations and their executives and employees can be subject to civil fines of up to \$2 million and up to \$100,000, respectively, civil penalties in either case cannot exceed \$10,000.³⁷ On the criminal side, executives and employees may be fined and imprisoned up to five years.³⁸

30 FCPA Op. Proc. Rel. 98-01.

31 15 U.S.C. § 78dd-2(c)(2).

32 FCPA Op. Proc. Rel. 07-01.

33 FCPA Op. Proc. Rel. 09-01.

34 FCPA Op. Proc. Rel. 08-03.

35 *United States v. Metcalf & Eddy, Inc.*, No. 1:99CV12566 (D. Mass. filed Dec. 14, 1999).

36 *See* 15 U.S.C. § 78dd-2(d).

37 *See* 15 U.S.C. § 78dd-2(g).

38 *Id.*



Accounting Provisions—Record Keeping and Internal Controls Intended To Improve Compliance

The rationale behind the record keeping and internal controls provisions is simple: require companies to keep accurate records of their business activity and institute internal controls that will identify and preclude the proscribed activity. Former federal judge Stanley Sporkin, who is often considered to be the father of the FCPA, explains the origin of the accounting provisions as follows:

Most of all, I was amazed that there was no requirement that publicly traded corporations maintain honest books and records. My research of the various laws did reveal that such a “books and records” requirement was included in the laws governing this nation’s financial institutions. It occurred to me that if such a requirement was good enough for this nation’s brokerage and banking institutions, why not for its industrial concerns?

I became convinced that what was necessary was a simple law that would require corporations to keep accurate books and records. In my view, a corporation would think twice before it recorded a bribe for what it was. Since bribery is generally considered a crime, it would be virtually untenable for someone to admit in writing that the corporation is engaging in such activities on an ongoing basis. Bribery needs secrecy in order to flourish. Thus, I theorized that requiring the disclosure of all bribes paid would, in effect, foreclose that activity.³⁹

Together the record keeping and internal controls provisions operate as one of the most effective means for enforcement by governmental agencies. In all practical respects, the accounting provisions are extensions of requirements under the 1934 Securities Act, as amended, requiring companies whose stocks are registered with the SEC or who must file regular reports with the SEC to implement appropriate record keeping and internal accounting controls.

The record-keeping provisions require that books, records and accounts depict (fairly) transactions and use of assets in “reasonable detail.” Reasonable detail means a “level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs.”⁴⁰ The record keeping provision extends to majority

39 Stanley Sporkin, *The Worldwide Banning of Schmiergeld, A Look at the Foreign Corrupt Practices Act on Its Twentieth Birthday*, 18 Nw. J. Int’l Bus. 269, 274 (1998) (citations omitted).

40 15 U. S. C. § 78m(b)(7).



owned (i.e. 50% or more) foreign subsidiaries.⁴¹ However, an issuer that owns 50% or less of a firm and “demonstrates good faith efforts to use such influence shall be conclusively presumed to have complied with the requirements of paragraph (2).”⁴² The FCPA’s internal control provisions closely adhere to and parallel common accounting practices. They require implementation of accounting procedures and controls to “provide reasonable assurance” that company procedure is followed, transactions are recorded, and access to and accountability of assets is controlled and regularly monitored.⁴³ Accordingly, a company that improperly records payments to foreign officials as, for example, “incidental fees” will be subject to liability for violation of the FCPA’s record keeping provisions.⁴⁴

Global Industries Are At The Greatest Risk

The most likely targets of FCPA enforcement actions are multi-national corporations who seek entry into foreign markets where the reward of globalization also poses the greatest risk. Growth of a business on an international level poses inherent compliance challenges because acquisitions, engagement of third-party agents, and intrusive foreign government oversight and regulations may not be thoroughly known or due diligence may be incomplete. Businesses are strictly liable for crimes committed by their employees under the legal doctrine of *respondet superior*.

Certain industries are naturally at greater risk because their businesses are naturally drawn to less developed regions of the world where potential growth is unlimited. But it is these same less developed regions where bribery of government officials is the norm. Between 2002 and 2008, telecommunications, energy, industrial/technology companies, health care and financial services accounted for the vast majority of settlement and penalties.⁴⁵ Certain industries, such as energy, telecommunications and medical devices, are a regular target because these businesses often must work hand in hand with government regulatory divisions. The financial services industry is another at-risk business segment because it commonly interacts with foreign governments on a variety of levels, ranging from providing financial services to setting up new businesses. Global expansion and acquisition of new businesses poses the greatest amount of risk for multi-national corporations.

41 See *SEC v. Int’l Business Machs. Corp.*, SEC Litig. Release No. 16, 839 (Dec. 21, 2000).

42 15 U. S. C. § 78m(b)(6).

43 See 15 U. S. C. § 78m(b)(2).

44 *United States v. O’Hara*, 960 F.2d 11 (2d Cir. 1992); see also *Liebo*, 923 F.2d at 1312 (indicating that the defendant’s classification of airline tickets purchased for a foreign official’s cousin as a “commission payment” was evidence of a violation of the FCPA).

45 Pricewaterhouse Coopers, *Corruption Crackdown*, July 2009 at 15.



MERGERS & ACQUISITIONS

Companies seeking to minimize their FCPA liability risks should pay careful attention to the potential exposure created by merger and acquisition activity. As a number of cases have shown, unwary companies can “purchase” FCPA liability by failing to conduct appropriate due diligence of their intended transaction partner. On the other hand, companies alert to those risks have been able to avoid successor liability altogether or, more frequently, obtain assurance about the scope of potential FCPA liability before the transaction is complete. Indeed, successor liability may attach in a stock transfer or merger because the assets and liabilities of the target company generally transfer to the acquiring company after closing; or the liability may attach in an asset purchase depending on the extent of the purchase and whether the target business is continuing or if the purchase agreement specifies which assets and liabilities transfer.

Since an acquiring company may be held criminally liable for FCPA violations committed by the target company both before and after closing, pre-closing due diligence is critical to assessing risks and avoiding liability. Additionally, the party should request measures for good governance, ask for proof of accurate recordkeeping and anti-bribery efforts, seek audit rights, request anti-corruption representations and written commitments to abide by anti-corruption laws; even if these requests aren’t honored, a record of such requests could help protect against or minimize FCPA exposure for the company. For joint ventures and minority acquisitions, the company can be held liable for the future conduct of the joint venture or majority partner, but it depends on the governance proportion of the JV or majority company (e.g. board members, voting rights). The impact of FCPA liability in the mergers and acquisitions context is wide-ranging. FCPA violations may impact the transaction price and structure and the need for additional warranties/indemnifications. Additionally, it may delay or terminate a proposed deal, and lead to corporate integration issues when a deal is completed. As part of the due diligence process, there may be a need to implement an enhanced FCPA compliance program, voluntarily disclose FCPA violations to the Justice Department to allow for the opportunity to resolve any such potential liabilities, and to halt illegal conduct and even dismiss officers and employees as necessary.

Recent enforcement actions involving FCPA issues identified during pre-acquisition due diligence drive home the need for effective FCPA due diligence, specifically in the context of mergers and acquisitions. For example, in April 2006, the SEC announced that it filed a settled civil injunctive action in district court against Tyco for numerous securities laws violations, including violations of the anti-bribery provisions of the FCPA.⁴⁶ The SEC’s complaint alleged that employees at two Brazilian and South

⁴⁶ See *SEC v. Tyco Int’l Ltd.*, Litig. Rel. No. 19657 (Apr. 17, 2006).



Korean subsidiaries acquired by Tyco in the late 1990s made extensive bribery payments: according to the Complaint, sixty percent of the contracts at the Brazilian subsidiary involved “some form of payment to a government official.”⁴⁷ The SEC’s complaint highlighted that Tyco had made this acquisition, and that these FCPA violations occurred, even though Tyco’s pre-acquisition due diligence revealed that “illicit payments to government officials were common” in Brazil and South Korea, and with respect to the Brazilian acquisition, “were portrayed as necessary in the industries in which [the Brazilian acquisitions] conducted business.”⁴⁸ The SEC’s complaint also alleged that prior to 2003, Tyco did not have a uniform, company-wide FCPA compliance program in place or a system of internal controls sufficient to detect and prevent FCPA misconduct at its globally-dispersed business units. Employees at [the Brazilian and South Korean subsidiaries] did not receive adequate instruction regarding compliance with the FCPA, despite Tyco’s knowledge and awareness that illicit payments to government officials were a common practice in the Brazilian and South Korean construction and contracting industries.⁴⁹ Without admitting or denying the allegations in the complaint, Tyco consented to a permanent injunction against further securities laws violations, \$1 million in disgorgement, and a \$50 million civil penalty.⁵⁰

In addition, in 2004 the proposed merger between Lockheed Martin Corporation and Titan Corporation, a military intelligence and communications company, collapsed following the discovery of FCPA violations during pre-acquisition due diligence. After Lockheed Martin discovered the potential FCPA concerns at Titan during its due diligence, the parties jointly disclosed the matter to the DOJ.⁵¹ Lockheed and Titan pushed back the closing date of the merger two times in order to allow Titan time to settle the matter, but the merger collapsed in June 2004 after Titan was unable to resolve the DOJ’s investigation.⁵² Later, on March 1, 2005, both the DOJ and SEC announced settlement of FCPA enforcement actions filed against Titan.⁵³ Titan pleaded guilty to violating the anti-bribery and books and records provisions of the FCPA, as well as a criminal tax violation arising out of Titan’s decision to employ a third-party agent to assist on a project to build a wireless telephone network in Benin, and agreed to a criminal fine of \$13 million, and a civil disgorgement penalty

47 SEC Civil Complaint, *SEC v. Tyco Int’l Ltd.*, 06 CV 2942 (S.D.N.Y. Apr. 17, 2006), ¶ 49.

48 *Id.* ¶¶ 48, 53.

49 *Id.* ¶ 55.

50 *SEC v. Tyco Int’l Ltd.*, Lit. Rel. No. 19657 (Apr. 17, 2006).

51 *Id.*

52 Renae Merle, *Lockheed Martin Scuttles Titan Acquisition*, *Washington post*, June 27, 2004, available at <http://www.washingtonpost.com/wp-dyn/articles/A8745-2004Jun26.html>.

53 See Press Release, U.S. Att’y, S.D. Cal., News Release Summary (Mar. 1, 2005), available at www.usdoj.gov/criminal/pr/press_releases/2005/03/2005_3859_titancorp030105.pdf; *SEC v. The Titan Corp.*, Litig. Rel. No. 19107 (Mar. 1, 2005).



of \$15.4 million to the SEC.⁵⁴ Titan had hired a consultant who claimed to have close ties to the then-President of Benin without performing adequate due diligence to determine if its agent was complying with the FCPA.⁵⁵ In January 2001, Titan's employees and agents agreed to pay this agent millions of dollars for the purpose of influencing the upcoming presidential election. At Titan's request, the agent submitted over \$2 million in false invoices for these funds to Titan, and Titan used these false invoices to conceal its improper payments.⁵⁶

The GE/InVision case is also illustrative. In December 2004, proposed merger partners General Electric and InVision Technologies, Inc. ("InVision") entered into separate agreements with the Justice Department and the SEC to resolve charges that InVision had violated the FCPA through the actions of its agents in several Asian countries, who had paid or offered to pay money to foreign officials and political parties to secure the purchase of InVision's airport security screening machines.⁵⁷ General Electric's pre-acquisition due diligence was instrumental in uncovering these alleged FCPA violations, which were promptly reported to the Government. InVision ultimately consented to a two-year non-prosecution agreement with the Justice Department in which, *inter alia*, it accepted responsibility for its misconduct and agreed to pay an \$800,000 criminal fine.⁵⁸ General Electric, for its part, entered into an ancillary agreement that obligated it to fully integrate the InVision business into General Electric's FCPA compliance program, retain an independent consultant, oversee InVision's performance of its obligations under the non-prosecution agreement, and to disclose any evidence material to the then-ongoing Government investigation. The merger then closed successfully.⁵⁹

There is evidence that the government may be disinclined to bring direct criminal charges against an acquirer. Johnson Controls, which acquired York International Corp. ("York") in 2005, was not charged with any wrongdoing and was not prosecuted for any of York's actions in connection with York's 2007 settlement of charges stemming from bribes paid to Iraqi officials under the United Nations Oil-for-Food program, as well as kickbacks to government agents in Bahrain, India, Turkey, the United Arab Emirates, and China. Among other sanctions, York paid a \$10 million

54 DOJ Titan Press Release, *supra* note 53.

55 *Id.*

56 *Id.*

57 *SEC v. GE InVision, Inc.*, C 05 0660 (N.D. Cal filed Feb. 14, 2005).

58 *InVision Technologies Inc. Enters into Agreement with the United States*, Dep't of Justice Release No. 04-780 (Dec. 3, 2004). InVision settled a companion SEC case approximately two months later by agreeing to pay \$500,000 in civil penalties and \$617,700 in disgorgement and pre-judgment interest, totaling approximately \$1.2 million. *SEC v. InVision, Inc.*, C 05 0660 (N.D. Cal. filed Feb. 14, 2005).

59 Press Release, Dep't of Justice, *InVision Technologies, Inc. Enters into Agreement with the United States* (Dec. 6, 2004) (discussing InVision's resolution of criminal FCPA liability and General Electric's acquisition of InVision).



criminal penalty pursuant to a deferred prosecution agreement and an additional \$12 million in civil fines and disgorgement.⁶⁰ York also settled with the SEC, agreeing to disgorge about \$10 million in ill-gotten gains and pay \$2 million of civil fines.⁶¹

There is limited authority regarding required due diligence—it is “an art, not a science.” In fact, due diligence is not a legal defense, but can only serve to minimize the risk of successor liability when coupled with the acquiring company’s FCPA compliance commitment. Each transaction requires a different due diligence strategy—a strategy tailored to the transaction that should remain flexible and adaptable to new information and changing circumstances.

Two recent Justice Department opinion releases provide additional guidance about how companies should approach pre-acquisition due diligence. Opinion Release 08-01 was issued in response to an inquiry from an unnamed Fortune 500 company that was preparing to make a major investment in a foreign company.⁶² The foreign company was jointly owned by a private individual (the controlling shareholder) and the government of a foreign country. This circumstance prompted the prospective investor to wonder whether the private individual was a foreign official within the meaning of the FCPA, and to therefore query whether its planned investment could be viewed as violating the FCPA. Acting on an expedited basis, the Justice Department determined that it would not take any enforcement action with respect to the proposed transaction, in prominent part because of the extensive due diligence that had been conducted by the investor, and the resulting transparency surrounding the transaction.⁶³

Opinion Release 08-02 also concerned a complicated acquisition scenario. This

60 *United States v. York Int’l Corp.*, No. 1:07-CR-00253 (D.D.C. filed Oct. 1, 2007).

61 *SEC v. York Int’l Corp.*, No. 1:07-CV-01750 (D.D.C. filed Oct. 1, 2007).

62 Opinion Release 08-01, available at <http://www.usdoj.gov/criminal/fraud/fcpa/opinion/2008/0801.pdf>.

63 This due diligence included the following steps: (i) the requestor commissioned a report on the Foreign Private Company Owner by a reputable international investigative firm; (ii) the requestor retained a business consultant in the foreign municipality who provided advice on possible due diligence procedures in the foreign country; (iii) the requestor commissioned International Company Profiles on the Investment Target and Foreign Private Company from the U.S. Commercial Service of the Commerce Department; (iv) the requestor searched the names of all relevant persons and entities, including the Foreign Private Company Owner, the Investment Target, and Foreign Private Company, through the various services and databases accessible to the requestor’s international trade department – including a private due diligence service – to determine that no relevant parties are included on lists of designated or denied persons, terrorist watches or similar designations; (v) the requestor met with representatives of the U.S. Embassy in the foreign municipality and learned that there were no negative records at the Embassy regarding any party to the proposed transaction; (vi) outside counsel conducted due diligence and issued a preliminary report, with an updated report to be completed prior to the closing date of the proposed transaction; (vii) an outside forensic accounting firm prepared a preliminary due diligence report, with a final report to follow; and (viii) a second law firm reviewed the due diligence.



time, the opinion release was prompted by Halliburton’s efforts to reconcile apparent conflicts between U.S. and U.K. law in conducting FCPA due diligence. A competing firm had submitted a bid for the acquisition target—a British public company. The competing bid, which won a recommendation of approval from the board of the target company, did not include any conditions relating to FCPA due diligence. Under British law, that recommendation meant that the target (1) was not required to provide Halliburton additional information that would enable a full due diligence review prior to placing a bid, and (2) was not required to entertain any offer from Halliburton that contained FCPA-related conditions. Additionally, due to the terms of a confidentiality agreement between Halliburton and the target, Halliburton was restricted from sharing any FCPA violations discovered prior to the proposed acquisition with the DOJ. The upshot was that Halliburton’s hands were substantially tied—Halliburton could not require the target company to disclose all of the information that it would need to conduct comprehensive FCPA due diligence, and in any event, was barred from disclosing any potential violation that it nonetheless managed to uncover before the acquisition was complete. Halliburton responded to this situation by proposing a series of post-acquisition measures that it would take to ensure FCPA compliance. It then posed three questions to the Justice Department: (1) whether the potential acquisition transaction itself would violate the FCPA; (2) whether Halliburton would be liable for the target company’s pre-acquisition conduct; and (3) whether Halliburton would be liable for post-acquisition FCPA violations. In response to the first question, the DOJ stated that it did not intend to take enforcement action against Halliburton purely for engaging in the transaction because the target was a public company listed on a major exchange—with the result that there was a very low probability that shareholders obtained shares in corrupt transactions. The DOJ also indicated that it was unlikely to take any action against Halliburton for any FCPA violations found to have been committed by the target company before or after the transaction, provided that Halliburton adhered to the ambitious post-closing due diligence and disclosure plan that it had proposed in its opinion request.⁶⁴

Importantly, several other cases make clear that a company’s obligation to identify and disclose potential FCPA violations does not end with the closing of a merger or acquisition. In fact, these cases show that the immediate post-acquisition period is critical because the government expects acquirers to quickly harmonize the

⁶⁴ In its opinion request, Halliburton had committed to take the following post-acquisition steps: (1) immediately disclose any violations discovered in pre-closing investigations; (2) within ten days of closing, submit an FCPA due diligence plan to the DOJ to be completed within 180 days of closing, and fully investigate any issues within one year from the closing date; (3) retain outside counsel, third-party consultants, and forensic accountants; (4) sign new contracts that incorporate anti-corruption provisions with all agents and other third parties associated with the target; (5) impose all of its Code of Business Conduct and FCPA anti-corruption policies on the target and conduct anti-corruption training immediately following closing; and (6) disclose all FCPA and related violations discovered during the 180 day due diligence and follow any additional steps requested by the DOJ.



companies' FCPA policies and compliance programs. For example, in a 2001 case involving Baker Hughes, one of the charges leveled by the SEC was that, just two months after its acquisitions by Baker Hughes, employees of an Australian subsidiary made a suspicious payment that was improperly recorded in the Baker Hughes' books and records.⁶⁵ A more recent case involving Con-way International, also serves as a warning that the activities of even a partly-owned subsidiary can lead to FCPA liability for a parent company—Con-way was hit with a \$300,000 civil penalty for FCPA violations committed by a Philippines-based firm in which Con-way indirectly held a 55 percent ownership stake.⁶⁶

Successor liability continues to be a major concern. For example, Snamprogetti, a subsidiary of ENI, engaged in a bribery scheme for 10 years ending in 2004. In 2006, ENI sold Snamprogetti to another company, Saipem. And yet, four years later, in 2010, Snamprogetti was charged with FCPA criminal violations and agreed to a \$240 million fine (ENI and Saipem were jointly liable for the fine).⁶⁷ The DOJ's enforcement in this area has been wide-ranging. In 2005, Dimon Inc. and Standard Commercial Corporation merged to form Alliance One. Five years later, DOJ brought a criminal case against Alliance One for FCPA violations committed by foreign subsidiaries of Dimon and SCC before the merger.⁶⁸ The foreign subsidiaries entered guilty pleas and Alliance One is required to cooperate and retain an independent compliance monitor for three years.

Pre-acquisition due diligence is crucial. In pre-acquisition due diligence, Monsanto discovered improper payments made by Turk Deltapine, a wholly owned U.S.-based subsidiary of Delta & Pine Land Company. Monsanto Company acquired Delta in 2007. Monsanto reported them to the SEC for payments to officials of the Turkish Ministry of Agricultural and Rural Affairs to secure government inspection reports and quality certifications necessary for operations in Turkey.⁶⁹ In June 2002, Cardinal Health sought to acquire Syncor International Corporation, a Delaware corporation providing radio-pharmacy and outpatient medical imaging services in the United States and numerous foreign countries.⁷⁰ A few months later, in conjunction with pre-acquisition due diligence, Cardinal Health discovered improper payments made by several of Syncor's foreign subsidiaries to doctors at state-owned hospitals around the world in order to obtain or retain business. Syncor initiated an investigation and made a voluntary disclosure to the SEC and DOJ, resulting in government investigations and prosecutions. The SEC alleged that the subsidiaries made payments to ensure that

65 SEC Exchange Act Release No. 44784 (September 12, 2001). The case was resolved through a cease-and-desist order that enjoined Baker Hughes from committing future FCPA violations.

66 *SEC v. Con-way Inc.*, Civ. Action No. 08-cv-01478 (EGS) (Aug. 28, 2008).

67 See <http://www.justice.gov/opa/pr/2010/July/10-crm-780.html>.

68 See <http://www.justice.gov/opa/pr/2010/August/10-crm-903.html>.

69 *SEC v. Delta & Pine Land Co.*, No. 1:07-cv-01352 (D.D.C. filed July 25, 2007).

70 *SEC v. Syncor Int'l Corp.*, No. 1:02-cv-02421 (D.D.C. filed Dec. 10, 2002).



the doctors and state-owned hospitals would order Syncor supplies and services and that these payments were made with the knowledge and approval of the subsidiaries' senior executives, and with the occasional knowledge and approval of the parent's founder and board chairman. Syncor settled the charges by paying a fines and penalties, and agreed to engage an independent compliance monitor. Following the investigation and disclosure, Cardinal Health agreed to proceed with the acquisition, but only at a lower price.⁷¹

The proper strategy for addressing FCPA issues in a corporate transaction will depend, in part, on the parties involved in the transaction. For example, when both parties to the transaction are U.S. registrants, enforcement agencies will expect both parties to have existing FCPA policies and to conduct FCPA due diligence in connection with the transaction. If a U.S. registrant seeks to acquire a public company not registered in the United States, diligence should focus on the target's compliance with governing anti-corruption law. And when a U.S. registrant wishes to acquire a private company, due diligence should be particularly focused on whether past practices pose an FCPA risk, as well as on whether future FCPA compliance will impact the target's business model. This is particularly the case when the target is located in a country considered to be high risk from an FCPA compliance standpoint. FCPA issues identified during the course of transactional due diligence may trigger the need for extended due diligence.

Just as with respect to due diligence in connection with the hiring of an agent and with joint ventures, the parties may wish to include representations and warranties in transaction documents. As illustrated in the Commission's Report of Investigation following the failed Lockheed-Titan merger, the parties must be mindful of public representations regarding FCPA compliance in the course of due diligence, and need to continually and carefully assess disclosure issues in connection with these representations, particularly in the event that FCPA concerns are discovered. On the day Titan's FCPA liability was settled, the SEC also released a Report of Investigation cautioning issuers to ensure that disclosures regarding material contractual provisions such as representations regarding FCPA compliance are not misleading.⁷² In this Report of Investigation, the Commission noted that Titan had represented in its merger agreement with Lockheed that it was in compliance with the FCPA.⁷³ Titan then disclosed this representation publicly twice, in a proxy statement and in the parties' merger agreement, which was attached to the proxy statement.⁷⁴ Although the merger

71 See Press Release, *Cardinal Health and Syncor Announce Amended Merger Agreement*, available at http://www.cardinal.com/content/news/1262002_73434.asp.

72 SEC, *Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on Potential Exchange Act Section 10(b) and Section 14(a) Liability*, Exch. Act Rel. No. 51283 (Mar. 1, 2005).

73 *Id.*

74 *Id.*



agreement was amended at various times due to the SEC’s and DOJ’s investigations of potential FCPA violations, Titan’s FCPA representation remained unchanged.⁷⁵ The Commission also asserted that “where specific additional material facts exist that are known to an issuer, or an issuer was reckless in not knowing them, . . . or an issuer was negligent in not knowing them, . . . general disclaimers regarding the material accuracy and completeness of disclosure may not be sufficient disclosure, for example, in situations where an issuer has material information contradictory to representations it has made.”⁷⁶

The scope and depth of FCPA due diligence—which must include an assessment of bribery, books and records, and internal controls risks—will depend on factors such as the nature and location of the company’s business. For example, a business model that involves frequent interaction with government regulators or customers may require more scrutiny than one that does not. In addition, the nature of the business may require scrutiny of specific areas, including, *inter alia*, political contributions, lobbying activities, and payments to customs agents. The FCPA due diligence inquiry is ultimately a risk-based assessment: an assessment of financial controls, business locations, use of third-party agents, prior internal investigations, FCPA compliance culture (e.g. existence of training/employee discipline or hotline reporting system), and the company’s overall compliance structure, including corporate policies, training and audit practices, and scrutiny to determine whether certain expenses—such as travel, gifts, and entertainment—have been used to benefit government officials.

The due diligence assessment is continuous and must evolve as new information becomes available. The due diligence plan should also anticipate a course of action in the event FCPA concerns are identified in the course of due diligence, addressing matters such as preserving privilege over legal strategy and work product, whether to make voluntary disclosures to enforcement agencies, and the parties’ tolerance for delays to the transaction resulting from government investigations.

In addition, there are basic purchase agreement protections against FCPA liability. Specifically, the agreement may include provisions such as warranties and indemnifications against possible FCPA violations, participation in transactions permitted under local law, absence of government owners in company, no corrupt payments were made to foreign officials, and that the books and records are complete and accurate.

75 *Id.*

76 *Id.*



Red Flags

For businesses engaged in global expansion and acquisition of foreign companies, an ounce of prevention is the best medicine. Implementation and execution of preacquisition anti-corruption due diligence is a must before entering strategic alliances, joint ventures or partnerships with new businesses. Any such due diligence should necessarily include the review of business practices, contracts, payment procedures, and accounting procedures. Any number of red flags can arise, which can expose possible FCPA violations:

- Persistent and repeated failure to comply with local law.
- Refusal of agents or third-party representatives to sign FCPA compliance policy.
- Third-party agent or sales representative is a former government official.
- Third-party comes “highly recommended” by government officials.
- Unusual payment methods such as wire transfers or lax accounting or invoicing practices.

In combination or on their own, any one of these red flags should be enough to raise serious concerns about FCPA compliance. In addition to performing this due diligence at the onset of a relationship, organizations need to set up an ongoing due diligence process.

Corporate Self-Assessment

Corporations have begun to institute a proactive approach to compliance. Corporations assess their corporate governance and compliance programs annually. A multinational corporation will take a variety of steps to implement a sustainable anticorruption program, including training and communication programs, transaction testing, and disciplinary mechanisms that are embedded within their business model to help mitigate areas of risk:

- Develop consistent employee recruitment background due diligence and screening procedures.
- Develop third-party acceptance and retention policies and procedures, including compliance contract clauses and maintaining contracts in a central location.
- Implement a robust monitoring, detection, and auditing process for high risk locations, business partners, and activities, including the transactions associated with such relationships.
- Enhance compliance and accounting policies and procedures surrounding government-related activities, implement controls surrounding cash transactions, and delegate appropriate levels of approval requiring pre-approval of high-risk transactions.
- Institute corporate level and company-wide ethics and business conduct policies



and procedures.

- Provide additional compliance resources within high risk locations and training to key employees and third parties.
- Implement a disciplinary mechanism and response plan for instances where potential violations are noted.

Preventing corruption is a sound long-term business strategy, helping to establish that corporations act in a responsible and ethical manner while enhancing shareholder value. Every corporation should become engaged and embrace a proactive compliance strategy, so that it can better manage the risks of operating globally and to demonstrate its strong commitment to stakeholders, business partners, and regulatory agencies.

CONCLUSION

The DOJ and SEC have announced and are pursuing an increased and aggressive level of enforcement activity under the FCPA. Businesses must be particularly careful when engaging in mergers and acquisitions, whether acquiring other companies or being acquired. Due diligence in these situations is critical and must encompass the full range of FCPA compliance issues.



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Experience

Michael Volkov is a former federal prosecutor with almost 30 years' experience in a variety of government positions and private practice. Michael's practice focuses on white collar defense, corporate compliance, internal investigations, regulatory enforcement matters and complex commercial litigation.

Before entering private practice, Michael served for more than 17 years as a federal prosecutor in the US Attorney's Office in the District of Columbia; for 5 years as the Chief Crime and Terrorism Counsel for the Senate Judiciary Committee, and Chief Crime, Terrorism and Homeland Security Counsel for the Senate and House Judiciary Committees; and for 6 years as a Deputy Assistant Attorney General and a Trial Attorney in the Antitrust Division of the US Department of Justice.

Michael has extensive trial experience and has been lead attorney in more than 75 jury trials, including some lasting more than six months. He has handled a number of high-profile criminal cases brought under a wide range of national and international laws, including those covering environmental, antitrust, international traffic in arms (ITAR), money laundering, online gambling, fraud, false claims and other complex crimes as well as the Foreign Corrupt Practices Act (FCPA) and other international bribery laws.

Notable Engagements

- Successfully represented three officers of a multinational company in two separate criminal antitrust investigations.
- Successfully represented pharmaceutical company before the Food and Drug Administration and Congressional committees, and conducted complex internal investigation, regulatory compliance audit and corporate governance review.
- Successfully represented individual in criminal prosecution and secured dismissal of criminal charges and expungement of criminal record.
- Represented company before Congress and Executive Branch in effort to modify Justice Department regulations concerning use of federal funds.
- Advised and assisted World Bank in review of global corruption policies and enforcement matter.

Education

Georgetown University Law Center, JD, Cum laude, 1982 • The Wharton School of the University of Pennsylvania, BS, summa cum laude, 1979 • University of Pennsylvania, BA, History, 1979; Phi Beta Kappa



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