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FEATURE COMMENT: DOJ/SEC FCPA Guidance—A 'Must Read' For U.S. Government Contractors Seeking Work Abroad

On November 14, the Department of Justice and Securities and Exchange Commission issued a Resource Guide (the Guide) on their interpretation of and enforcement strategy for the U.S. Foreign Corrupt Practices Act. The Guide does not signal any major shift in DOJ or SEC FCPA enforcement policies, but instead consolidates in one document the authorities' interpretation of the FCPA, as well as what they consider in their exercise of prosecutorial discretion. Given the focus on ethics and compliance by U.S. Government contractors, and the fact that many are turning abroad to foreign customers to diversify their revenue base in light of declines in U.S. federal spending, the Guide is a "must read" for most lawyers and compliance professionals in the industry.

In this Feature Comment, we set forth some of the Guide's more significant points regarding DOJ's and SEC's interpretation of the FCPA's antibribery and accounting provisions, current enforcement policy, and expectations regarding compliance programs.

FCPA Antibribery Elements—The Guide's coverage of the FCPA's antibribery provisions does not provide bright-line definitional guidance regarding "foreign officials" and "instrumentalities," or on the size or amount of payments that will be considered "anything of value." Nonetheless, it sets forth useful insights regarding DOJ's and SEC's interpretation of, and enforcement policy with respect to, these and other elements of the antibribery provisions.

Anything of Value—Gifts, Meals, Entertainment and Travel: The Guide acknowledges that modest gifts, meals, entertainment and promotional expenses can be a legitimate part of conducting business. It suggests that corrupt intent will be the determining factor as to whether hospitality is proper or improper, and notes that travel and entertainment expenses that "occurred in conjunction with other conduct reflecting systemic bribery or other clear indicia of corrupt intent" have been the subject of past enforcement actions. While the Guide resists proposals by some commentators and critics for a de minimis exception for gifts and meals, it does state that "it is difficult to envision any scenario in which the provision of cups of coffee, taxi fare, or company promotion items of nominal value would ever evidence corrupt intent."

In addition, the Guide states that although corrupt intent will likely be evidenced by large, extravagant gifts, smaller gifts will not be viewed as corrupt, except when part of a pattern or practice evidencing a corrupt scheme to improperly influence officials. Appropriate gifts also must be given transparently and in accordance with local law, properly recorded, and provided "only to reflect esteem or gratitude." While the Guide's hypothetical examples typically fall clearly on one side or the other of a sometimes indistinct border dividing proper from improper gifts, meals, entertainment and travel, they nonetheless may serve as helpful reference points when analyzing the more challenging questions that arise in the course of companies' daily operations.

Anything of Value—Charitable Donations: According to the Guide, legitimate charitable giving does not violate the FCPA, but risk-based due diligence and controls are necessary for ensuring that contributions are not "used as a vehicle to conceal" corrupt payments. The Guide also enumerates a list of "questions to consider" when evaluating a proposed donation that relate to its purpose, consistency with internal guidelines, and connection to officials.

Definition of Foreign Officials and Instrumentalities: In its discussion of foreign officials, the Guide notes that the FCPA prohibits payments to foreign officials, rather than to foreign governments, but it cautions that payments to governments—including contributions or donations—should be made with controls ensuring that funds are not diverted for corrupt purposes, "such as the personal benefit of individual foreign officials." The Guide also reflects DOJ's and SEC's position that an "actor need not know the identity of the [bribe] recipient" to commit an offense—a position that has been disclaimed in recent court opinions and is currently contested in individual litigation.

One of the most awaited areas of guidance relates to when an entity is an "instrumentality" under the FCPA, such that its employees are "foreign officials." Those hoping for a bright-line test were left wanting. Instead, the Guide reiterates that the analysis is fact-specific—requiring assessment of an entity's ownership, control, status and function—and consolidates a list of non-exclusive factors approved by courts in several recent cases.

Helpfully, the Guide does suggest that majority ownership or control is a dominating factor: "an entity is unlikely to qualify as an instrumentality if a government does not own or control a majority of its shares." However, the Guide simultaneously cautions that no one factor is dispositive, and that DOJ and SEC may deem as an instrumentality an entity with minority government shareholding or control—for example, where the government controls essential elements of the entity's operations or political appointees hold important positions. Moreover, the Guide highlights the risk that bribes paid to private individuals run the risk of being prosecuted under other provisions of the FCPA or other laws, including the FCPA's accounting provisions, the Travel Act and anti-money laundering laws.

Promotional Expense Affirmative Defense: In addition to the section addressing gifts, meals and entertainment as items of "value" under the antibribery provisions, the Guide separately addresses the FCPA affirmative defense for reasonable and bona fide travel and lodging expenses that are directly related to the promotion, demonstration or explanation of products or services, or to the execution or performance of a contract. The Guide, not surprisingly, states that "trips that are primarily for personal entertainment purposes" are not bona fide. It also compiles a "non-exhaustive list of safeguards" from DOJ opinion procedure releases (OPRs) to guide the analysis of whether certain expenses qualify for the affirmative defense.

Antibribery Provisions Jurisdiction: The Guide reiterates the Government's aggressive stance on FCPA jurisdiction, particularly with respect to non-U.S. persons. For example, DOJ has previously asserted jurisdiction over non-U.S. persons under 15 USCA § 78dd-3 based on isolated meetings in—or telephone calls, e-mails or wire transfers to or from—the U.S. DOJ has also based jurisdiction on the indirect use of "correspondent accounts" that foreign banks maintain at U.S. banks to clear dollar-denominated transactions.

The Guide posits that 15 USCA § 78dd-3 confers jurisdiction whenever a foreign person merely causes an act to be done in the U.S. by an agent. In addition, the Guide advances expansive theories of agency, conspiracy, and aiding and abetting to reach non-U.S. persons "regardless of whether the foreign national or company itself takes any action in the United States." The Guide does not address recent judicial challenges by individual defendants to DOJ's expansive interpretation of the phrase "while in the territory of the United States" under 15 USCA § 78dd-3, or arguments that individual defendants did not have minimum contacts with the U.S. to support personal jurisdiction.

Other Elements: The Guide does not offer any new, significant insights on the interpretation of corrupt intent, willfulness, the business-purpose test, treatment of third parties, facilitating payments or the local law affirmative defense. Instead, in each of those sections, the Guide's treatment essentially restates congressional intent statements, court interpretations or prior settled actions, and does not add any appreciably new information.

Accounting Provisions—*Books and Records*: In its discussion of the FCPA's antibribery provisions, the Guide indicates that improper recording of expenses may be viewed as evidence of corrupt intent. When discussing the accounting provisions, the Guide emphasizes that there is no materiality threshold for books and records violations, but notes that DOJ's and SEC's enforcement generally has involved "misreporting of either large bribe payments or widespread inaccurate recording of smaller payments made as part of a systemic pattern of bribery."

Internal Controls: While the FCPA refers to systems of "internal accounting controls," the Guide, like many DOJ and SEC enforcement actions, considers "an effective compliance program" to be a "critical component of an issuer's internal controls." As originally issued, the Guide incorrectly stated that an issuer must use "best efforts" to cause subsidiaries or affiliates in which it holds "less than 50%" to devise and maintain a system of internal accounting controls. The statutory requirement is actually one of "good faith" and "to the extent reasonable under the issuer's circumstances," and applies with respect to subsidiaries or affiliates in which the issuer holds "50 percentum or less" of the voting power. DOJ recently posted a corrected version of the Guide on its website.

Accounting Provisions Jurisdiction: While noting that the FCPA's accounting provisions apply directly only to issuers, the Guide stresses that others may be liable for aiding and abetting, conspiracy, or causing violations by an issuer, for falsifying an issuer's books and records, or for circumventing internal controls. The Guide also sets forth the various liability risks for certain officers or directors as control persons, for making false statements to auditors, and for providing false certifications under the Sarbanes-Oxley Act of 2002. The Guide also reiterates the risk of criminal liability for companies for knowing violations of the accounting provisions and for individuals for knowing and willful violations.

Parent, Successor and Target Liability—The Guide's discussion of parent, successor and target company liability is noteworthy, as it is the first explicit articulation of DOJ and SEC policies and principles that govern enforcement actions in this area, and because several commentators sought limitations on successor liability as an area of potential FCPA reform. This may be of particular interest to Government contractors that continue to be active in mergers and acquisitions activity in today's uncertain marketplace.

Parent-Subsidiary Liability: The Guide summarizes parent-subsidiary liability generally and reinforces that traditional principles of parent-subsidiary liability—agency and respondeat superior—apply equally to FCPA cases. Consequently, the Guide clarifies the agencies' view that a parent may be held liable for the acts of its subsidiaries, both directly, as a result of its own knowledge of and involvement in the acts of its subsidiary, and indirectly, under traditional agency principles.

Whether the Government will consider a subsidiary as the agent of its parent depends not only on the formal relationship between the parent and subsidiary, but also on the extent of actual control the parent exercises. The Guide makes clear that if an agency relationship exists, DOJ and SEC will apply the respondeat superior doctrine and hold the parent liable for its subsidiary's acts.

Successor Liability v. Liability for Acts of an Acquired Subsidiary: The Guide contains a significant discussion of "successor liability," starting with a general discussion of the risks—both legal and commercial—of entering into corporate transactions without conducting sufficiently robust FCPA-focused due diligence. The Guide emphasizes that DOJ and SEC view successor company liability for the acts of a corporate predecessor as an "integral component of corporate law" and that this is not altered by anything relating to FCPA enforcement. In this discussion, the Guide conflates two related but differentiable scenarios: true successor liability, where a corporate entity has acquired another entity with FCPA liabilities, and subsequently merged or amalgamated with it; and liability of a buyer for the acts of an acquired company that remains a separate legal entity. Notwithstanding this conflation, the Guide's restatement of FCPA enforcement history in this area and treatment of six hypothetical examples highlight the importance in DOJ and SEC charging decisions of pre-acquisition due diligence, post-closing remediation and training, voluntary disclosure, and cooperation with any Government investigations.

Enforcement Guidance—The Guide largely summarizes existing DOJ and SEC guidance on enforcement principles, penalties, sanctions, remedies and resolutions, but provides some additional FCPA-specific information on the application of these topics. It also points to concrete benefits for companies with effective compliance programs, identifies factors for determining whether a monitor is appropriate, and—for the first time—provides examples of matters regulators have declined to pursue by providing anonymized summaries.

Self-Reporting and Cooperation: As expected, the Guide emphasizes that, when determining the appropriate resolution of an FCPA matter, DOJ and SEC place a "high premium" on voluntary and timely self-reporting, cooperation and the implementation of meaningful remedial measures. DOJ specifically explains that these factors may reduce a company's

culpability score under the U.S. Sentencing Guidelines, and thereby lead to fine reductions under the Guidelines. While this is not a guarantee of any specific outcome, it provides some tangible evidence of the benefits that may be afforded to companies who self-report, cooperate and implement meaningful remedial measures. SEC makes similar statements, but—given the operation of its penalty regime—it is not able to say how these factors will affect its penalty determinations in specific quantitative terms.

Role of Compliance Programs: The Guide reaffirms DOJ's and SEC's long-held view that the effectiveness and adequacy of a company's compliance program plays a significant role in the resolution of FCPA matters. The effectiveness and adequacy of such programs may influence whether a deferred prosecution agreement (DPA) or non-prosecution agreement (NPA) is used, the length of any resolution imposed, the penalty amount, and whether a monitor or self-reporting is required. Commentators seeking an affirmative compliance defense were left wanting, but the Guide contains a new recognition that the Government "may decline to pursue charges against a company based on the company's effective compliance program, or may otherwise seek to reward a company for its program, even when that program did not prevent the particular underlying FCPA violation that gave rise to the investigation." While the lack of compliance defense may be a disappointment to some commentators, it should not be surprising.

"Meaningful Credit" for Risk-Based Compliance: The Guide states that DOJ and SEC will give "meaningful credit to a company that implements in good faith a comprehensive, risk-based compliance program, even if that program does not prevent an infraction in a low risk area because greater attention and resources had been devoted to a higher risk area." This statement is quite significant on its face, as all companies have limited resources. How it will be applied in actual cases remains to be seen.

When are Monitors Appropriate?: The Guide reinforces the recent trend of a decreased use of monitors in FCPA resolutions by stating that monitors are "not appropriate in all circumstances." The Guide identifies six factors that DOJ and SEC will consider when determining the appropriateness of a monitor and, in particular, mentions that monitors may be appropriate "where a company does not already have an effective internal compliance program."

Charging Decisions: The Guide compares and contrasts the available dispositions in FCPA matters, such as plea agreements (DOJ), DPAs (DOJ and SEC), NPAs (DOJ and SEC), and civil injunctive and administrative remedies (SEC). The Guide remains silent, however, on the factors that lead to the use of one of these dispositions over another, and on the factors influencing enforcement choices if multiple potential targets are available (e.g., individuals versus companies).

Declinations Data: In response to requests for greater transparency regarding declinations, the Guide states that "in the past two years alone, DOJ has declined several dozen cases against companies where potential FCPA violations were alleged," identifies seven circumstances present in some or all of its recent declinations, and details six recent anonymized examples of declinations involving companies. It is unclear, however, whether the several dozen declinations referred to were declined based on merit, involved tips deemed not credible enough to pursue or were not pursued due to resource issues.

Declination Examples: The declination examples illustrate factors that must be present for DOJ and SEC to consider a declination. Each example appears to have involved a voluntary self-report, an internal investigation, cooperation with the Government and the implementation of remedial measures. Many matters involved relatively small bribes, and some involved the detection and prevention of potential bribes. Although the examples are useful, the Guide is silent on the length of time it took for DOJ or SEC to decline these matters once they were brought to the attention of the Government. In addition, it appears that each company expended considerable resources to investigate and remediate these matters, many of which, as previously noted, involved relatively small improper payments or payments that were never made. Companies are still left to question whether DOJ and SEC would decline these cases if a company chose not to self-report, but undertook a prompt investigation and implemented the aforementioned remedial measures.

Compliance Programs—The Guide's "hallmarks of effective compliance programs" mirror elements set forth in the Organisation for Economic Co-operation and Development's (OECD's) Good Practice Guidance on Internal Controls, Ethics, and Compliance, prior DOJ DPAs, and other existing compliance resources. Compliance professionals are

likely familiar with these elements, although the Guide provides additional detail with respect to Government expectations for anticorruption compliance programs in particular. Set forth below are a few items that may not be embedded in every company's compliance program and therefore may merit further consideration.

Management Commitment: The Guide continues to emphasize the importance of tone at the top; however, it also emphasizes the importance of a "message from the middle" in sustaining a culture of compliance. CEO messages are important, but cascaded reinforcing messages from middle management are also needed.

Policies and Procedures: The Guide reiterates existing guidance that policies and procedures should address payments to officials; use of third parties; gifts, travel and entertainment; charitable and political contributions; and facilitating and expediting payments. The Guide suggests that companies adopt policies and procedures that "outline responsibilities for compliance within the company, detail proper internal controls, auditing practices, and documentation policies, and set forth disciplinary procedures." The Guide also acknowledges that specific policies and procedures will depend on the size and business model of the company. Finally, the Guide recommends that companies "periodically" update their Code of Conduct so that it remains "current and effective."

Risk Assessments: The Guide stresses the importance of risk assessments in designing compliance programs and cautions that "one-size-fits-all" programs are "generally … ineffective." It also warns against spending "a disproportionate amount of time policing modest entertainment and gift-giving" at the expense of paying attention to higher-risk areas like "large government bids, questionable payments to third-party consultants, or excessive discounts to resellers and distributors." While this guidance is welcome, it is unlikely that DOJ or SEC will excuse a pattern of small but improper payments because the company devoted its resources to higher-risk areas.

Communication: The Guide suggests that, to ensure the "effective" communication of compliance policies and procedures, periodic training and certifications should be required for "all" officers, directors, "relevant employees" and, "where appropriate," for agents and business partners. In addition, the Guide recommends providing training and related materials in the local language, tailoring training to specific audiences (such as particular company functions), and implementing measures to provide ethics and compliance advice on an urgent basis. Although these measures represent good practice for larger companies, these steps could impose a significant burden on smaller companies.

Incentives and Discipline: The Guide encourages companies to reward personnel for improving and developing the compliance program and for ethics and compliance leadership. Examples include using a compliance standard of performance as a component of management bonuses, and making ethical and lawful behavior part of the promotion, compensation and evaluation process.

Continuous Improvement: The Guide states that compliance programs should "constantly evolve," and that a company should "regularly review" its compliance program and "periodically" test its internal controls with the goal of "continuous improvement and sustainability" of those areas. The call for "constant" evolution and "regular" reviews appears to go beyond the "periodic" reviews and updates called for in OECD guidance and prior DOJ DPAs.

Third Parties: The Guide also highlights risks related to third-party business partners. The Guide recognizes that appropriate due diligence can vary based on location, industry, nature of the transaction and prior relationships with the third party, but it cautions that certain "guiding principles always apply." These include (1) understanding the third party's qualifications, associations, business reputation and relationship with officials; (2) understanding the business rationale for using the third party and the proposed payment terms, as well as "confirming and documenting" that the third party is "actually performing the work" and that its "compensation is commensurate" with the work provided; and (3) monitoring the relationship on an ongoing basis, including, "where appropriate," by updating due diligence, exercising audit rights, providing periodic training and requesting annual compliance certifications. These steps, particularly in the final category, may be burdensome for low-risk relationships. Also, the Guide does not provide guidance as to how much additional review or diligence should be conducted when red flags arise, or as to the standards DOJ and SEC will apply, in hindsight, to judge the sufficiency and reasonableness of the steps taken in such circumstances.

Conclusion—While the Guide does not represent a stark departure from current DOJ or SEC FCPA enforcement and compliance policy, it is a useful summary of the many issues that companies and individuals face when trying to comply with the law and of the approach DOJ and SEC will follow if their conduct comes to be scrutinized. Given the Guide's heavy reliance on past enforcement actions, combined with the rapid pace at which DOJ and SEC continue to bring enforcement actions, the Guide will remain most helpful if it benefits from periodic updates to reflect any evolution in enforcement policy and practice. Because U.S. Government contractors (particularly those in the aerospace or engineering fields) have lived with the FCPA since its inception, many have had compliance programs and systems for some time. However, FCPA norms continue to evolve, and even mature compliance programs and systems may need to be revisited or refined. And improper acts that occur abroad can still result in Government debarment or suspension at home. The issuance of the DOJ/SEC Guide therefore provides a good opportunity for U.S. Government contractors to take the pulse of their programs.

This Feature Comment was written for The Government Contractor by Rich Battaglia, Tom Best, Chris Conte, Andy Irwin, Sarah Lamoree, Lucinda Low and Brittany Prelogar. The authors are all members of Steptoe & Johnson LLP's FCPA/Anti-Corruption Practice, of which Ms. Low is the head. Mr. Battaglia is in Steptoe's Chicago office. Mr. Irwin, who is also a member of its Government Contracts Practice, is in its Washington and Century City offices. The other co-authors are all in Steptoe's Washington office. Mr. Conte is also a member of its Securities Enforcement Practice, and Ms. Prelogar its Business and Human Rights Practice.

