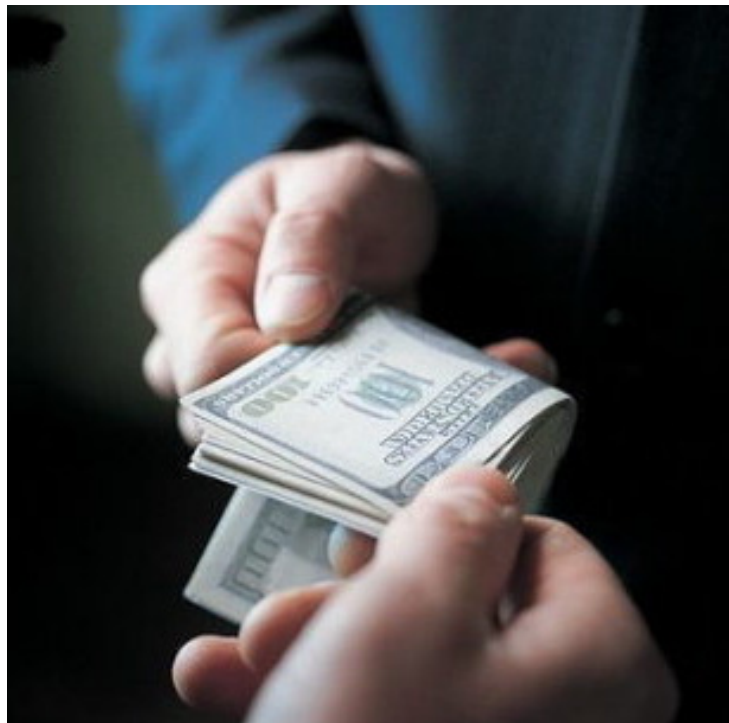


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The Risks of Greasing the Wheel

Effects of Enhanced FCPA Enforcement



Consideration for your troubles. Photo: Stock.

THROUGHOUT the 1990s and early 2000s, Siemens A.G., the German engineering conglomerate, appears to have used bribery as a business tool to secure government contracts throughout the world. Whether it was deals to build power plants in Israel, lay rail lines in Venezuela, or supply hospital equipment in Russia, Siemens won contracts through multi-million dollar payouts to government officials, much to the consternation of competitors and citizens of these countries who overpaid for goods and services.

On December 15, 2008, however, Siemens' dubious business practices came to an abrupt end as the company and three of its subsidiaries admitted to U.S. Foreign Corrupt Practices Act (FCPA) violations. Under the FCPA, it is illegal for any U.S. person, issuer or domestic concern, or any foreign person while in the U.S., to bribe foreign government officials in order to obtain or retain any business advantage. The law also requires companies with securities registered under the

Securities Exchange Act of 1934 to keep accurate records and maintain internal controls so that company books correctly reflect all transactions.

As part of its punishment, Siemens agreed to pay an unprecedented \$800 million to American authorities to settle claims by the United States Securities and Exchange Commission (SEC) and Department of Justice. In sum, Siemens will pay roughly \$1.6 billion in fines and fees to Germany and the United States, and more than \$1 billion for an internal investigation in which lawyers and auditors racked up a staggering 1.5 million billable hours.

To be certain, Siemens use of bribery and the resulting U.S. government fines are atypical. However, it is increasingly common for the SEC and Department of Justice to prosecute business entities and individuals for violating the FCPA. From 1978 to 2000, the SEC and Department of Justice averaged about three FCPA-related prosecutions per year. Since then, FCPA enforcement has tight-

ened dramatically. According to a Shearman & Sterling LLP study, from 2001 to 2006, the SEC alone averaged more than four formal proceedings per year and, in 2007, the SEC brought 16 new proceedings.

Additionally, penalties for FCPA violations can be steep. For instance, under the anti-bribery provisions of the FCPA, officers, directors, stockholders, employees and agents who violate the Act are subject to criminal fines of up to \$100,000 per violation and five years in jail, and companies are subject to criminal fines of up to \$2 million. Further, these penalties may be even higher under the Alternative Fines Act. This is because there is discretion to levy fines that are as much as twice the benefit the defendant sought in making the corrupt payment.

In recent years, extraordinary penalties have been handed down under the FCPA in settlements with companies as diverse as Halliburton/KBR (\$579 million in 2009), Baker Hughes (\$44 million in 2007), ► 26

23 ◀ Chevron (\$30 million in 2007), Titan Corporation (\$28 million in 2005), subsidiaries of Vetco International (\$26 million in 2007) and York International (\$22 million in 2007).

A myriad other actions can be taken against businesses accused of FCPA violations. A mere indictment can lead to a suspension of the right to do business with the U.S. government. Further, the SEC, the Commodity Futures Trading Commission and the Overseas Private Investment Corporation can all take separate action against a company for violating the FCPA. Additionally, if found guilty of conduct that violates the FCPA, private causes of action might be available under the Racketeer Influence and Corrupt Organizations Act (RICO), or under other federal or state laws, and a company may be ineligible to receive export licenses.

On top of larger and more frequent penalties, FCPA enforcement has become broader in scope. Companies and individuals who likely never heard of the FCPA are now being prosecuted under the Act. For instance, Christian Sapsizian, a French citizen, pled guilty to FCPA violations in 2007 for bribing Costa Rican officials in order to obtain a mobile telephone contract on behalf of Alcatel, a French communications company. In other words, a French citizen, working for a French company, was prosecuted in the U.S. for bribing a Costa Rican official. The jurisdictional hook the U.S. court used was that during the time of the alleged bribes (2000 - 2004), Alcatel's American Depository Receipts were traded on the NYSE and the actual payments were made by wire from Europe to Costa Rica through Miami.

Guard Against FCPA Violations.

Companies that seek contracts with

foreign governments must be particularly careful about running afoul of the FCPA. The major risk which these companies face, however, may not be that their American employees will violate the Act, but that foreign consultants and agents they hire will. To ensure FCPA compliance, the U.S. State Department recommends a strategy focused on education, detection and deterrence.

Educate Employees about FCPA.

An effective FCPA compliance program will educate employees about what the FCPA is, the penalties associated with FCPA violations, and how to avoid such violations in the future. To complement such a program, companies should do the following:

Draft an Internal FCPA Code of Conduct.

Companies should draft a clear and concise corporate code of conduct for employees to follow in order to avoid FCPA violations. This code should be a written set of legal and ethical guidelines for employees and agents to abide by which is translated into the languages of countries where the company operates.

Provide Anticorruption Training.

A compliance program's success depends on encouraging FCPA training at every corporate level, with added training in high-risk departments. Ideally, a senior business officer should lead FCPA training seminars in order to convey the importance the organization places on FCPA compliance. If senior officials do not take compliance seriously, neither will employees. This was a problem at Siemens, which created a powerless internal compliance system that looked good on paper, but did nothing to stop the company's

corrupt practices. Internal compliance programs must have teeth. An effective program will educate employees about the FCPA and anticorruption laws in other countries where the company operates.

Detect Violations.

If an FCPA violation occurs, regulators are likely to consider a company's efforts to deter the violation when deciding whether to indict the company or go after corporate officials individually. As a result, companies should be proactive in addressing FCPA violations. Mechanisms should be put in place to detect whether FCPA violations already exist, and in what company departments FCPA violations could arise in the future. Corporate compliance programs should establish standard operating procedures to make certain the company builds business relationships only with trustworthy agents and establishes internal accounting controls governing access to money, travel and other expenses. Such procedures include:

Flagging Dubious Transactions.

Companies should "red flag" transactions in which FCPA violations are most likely to occur. In particular:

- (i) government contracts;
- (ii) political and charitable contributions outside of the United States;
- (iii) payments to offshore holding companies;
- (iv) payments to anonymous accounts;
- (v) payments to accounts with potentially fictitious names;
- (vi) transactions that lack standard invoices;
- (vii) transactions that grant unusually large amounts of credit to customers; and
- (viii) transactions that utilize checks drawn "to cash". ▶ 30

Risks of Greasing the Wheel

26 ◀ Companies should always conduct heightened due diligence when the circumstances above exist to ensure that no FCPA violations occurred. When conducting this due diligence, companies should look for transaction patterns which have no clear economic or lawful purpose.

Conducting Extensive Background Checks on all Employees and Agents.

Prior to hiring individuals to work outside of the United States, companies should also conduct background checks that examine an individual's family and business ties with government officials in the country they are stationed. If the country is one where corruption is particularly rife, the background check should be more in-depth. Transparency International's Corruption Perceptions Index offers a helpful guide in determining which countries are particularly corrupt.

Deter Violations.

An effective FCPA compliance program must threaten punishment for individuals who are in a position to violate the FCPA, and actually punish individuals if FCPA violations are uncovered. To accomplish this, companies should do the following:

Limit Liability Through Contractual Arrangements.

Companies should insert provisions into employment contracts that highlight the FCPA's importance when hiring agents and employees who may encounter FCPA-related situations. A properly drafted provision will state that the individual is aware of the FCPA and will abide by the Act during the term of the professional relationship.

Establish Whistleblower Protections.

An effective FCPA compliance program will include a company helpline, where employees and agents can anonymously report potential FCPA violations, without fear of retaliation.

Implement Disciplinary Mechanisms for Offenders.

When an FCPA violation is uncovered, companies should take decisive disciplinary action ranging from minor sanctions to termination of employment in order to prevent recurrence of this activity in the future.

Enhanced FCPA enforcement is here to stay. With penalties for noncompliance on the rise, companies should take precautionary measures to ensure they are not paying the next record fine under the FCPA. ■

Lessons from Iraq and Afghanistan



Photo: Sgt. Aimee Millham/U.S. Army

22 ◀ payment on this. This is why the long-term answer to security in Afghanistan has to be an Afghan answer provided by Afghan troops.

JIPO: *Do you think this level of commitment is a signal – or can it be construed by the Taliban as a signal – that the U.S. is not really willing to go the distance?*

Nagl: We don't have enough Army to win the wars we are currently fighting. We are not expanding the Army rapidly enough in the wars in Iraq and Afghanistan. We simply do not have enough forces available. So 30,000 is simply all the forces we can afford to send to Afghanistan right now. We need more advisors to build a bigger Afghan army rapidly so that the Afghan forces can provide security in Afghanistan

JIPO: *How long do you think it'll take to build a bigger Afghanistan army?*

Nagl: First we have to decide that's what we are going to do and then we have to do it. Doing it will require more American advisors. We are looking at a five to 10-year process.

JIPO: *Can you describe what "winning" is in Afghanistan, and what that entails in terms of military and political will?*

Nagl: Essentially what we are trying to accomplish is preventing a safe haven for terrorists in Afghanistan and instability from spreading further to Pakistan. In order to accomplish those two objectives, which I believe are the core U.S. objectives in Afghanistan; we have to build an Afghan state which can provide its own security. To do that, we have to build a bigger Afghan army and a bigger Afghan police force. That I believe is the primary focus of the American operations in Afghanistan. ■