

Restoring Balance

Proposed Amendments to the Foreign Corrupt Practices Act



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*Proposed Amendments to the
Foreign Corrupt Practices Act*

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I. Executive Summary

Background

This paper presents a series of amendments that would serve to improve the U.S. Foreign Corrupt Practices Act (“FCPA”). That statute was enacted by Congress and signed into law by President Carter in late 1977. Congress’s primary aim in enacting the FCPA was to prohibit U.S. companies and companies operating in the U.S. from paying bribes to foreign government officials, politicians, and political parties for the purpose of obtaining business opportunities abroad. Congress achieved this aim by

making it a crime for U.S. citizens, domestic companies, and certain foreign companies and individuals to make corrupt payments, or offer anything of value, to foreign officials in return for business opportunity, broadly understood. These anti-bribery provisions have always been the centerpiece of the FCPA. But to promote the anti-bribery provisions, Congress further required that corporations with securities listed in the United States keep financial books and records that

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accurately reflect payments and maintain a system of internal accounting controls. The FCPA thus addressed foreign bribery by punishing its occurrence (the anti-bribery provisions) and providing for its detection and prevention (the books-and-records and internal controls provisions).

At the time of enactment, the FCPA was a significant departure from settled expectations in the American business and legal communities. Before the FCPA, no government had made it a crime to bribe officials of a foreign country. Many governments even allowed companies to count bribes paid to foreign officials as ordinary business expenses that the company could ultimately deduct for tax purposes. For approximately two decades, the FCPA stood alone, not only in criminalizing foreign bribery, but in requiring companies to maintain books and records and accounting controls that would help prevent and detect its occurrence.

Recent Enforcement Trends

The last decade has seen a marked increase in FCPA enforcement by both the Department of Justice (“DOJ”) and the Securities and Exchange Commission (“SEC”). Indeed, the last five years has seen nothing short of a boom in FCPA enforcement. More enforcement actions are being brought than ever before, fines and penalties have risen dramatically, and the government has shown

an increased willingness to seek jail terms for individual defendants. Mark Mendelsohn, who spearheaded the recent growth in FCPA enforcement during his tenure in the DOJ’s Fraud Section, made this shift in focus clear in public statements earlier this year: “If you look at who we’re prosecuting, we’re prosecuting mid-level to senior level corporate officers and employees, CEOs, CFOs, heads of international sales.”²

The size of FCPA settlements has also increased dramatically in recent years. The top ten FCPA settlements in terms of overall dollar amount total \$2.8 billion. Five of the top ten FCPA settlements have occurred in 2010 alone. The remaining five have all occurred since 2007. An added sign of increased enforcement is that there are currently more open FCPA investigations pending resolution than at any other time since its inception.³ Both the DOJ and SEC have announced plans to augment their resources dedicated to FCPA enforcement, partly to handle the growing list of pending FCPA matters confronting the enforcement agencies.⁴

In spite of this rise in enforcement and investigatory action, judicial oversight and rulings on the meaning of the provisions of the FCPA is still minimal.⁵ Commercial organizations are rarely positioned to litigate an FCPA enforcement action to its conclusion, and the risk of serious jail time

² Dan Margolies, *Anti-bribery Probes to Target Execs: Official*, REUTERS, Mar. 18, 2010.

³ Zack Harmon, *Confronting the New Challenges of FCPA Compliance: Recent Trends in FCPA Enforcement and Practical Guidance for Meeting These Challenges*, INSIDE THE MINDS (Aspatore Books, 2010); Cary O'Reilly and Justin Blum, *Smith and Wesson Executive Among 22 Accused of Bribery*, BUSINESS WEEK, Jan. 19, 2010 (citing statistics on DOJ investigations reported by Assistant Attorney General Lanny Breuer).

⁴ Fredic D. Firestone & Boris Uphoff, *United States: DOJ and SEC Will Significantly Increase FCPA Enforcement Efforts*, MONDAQ, Mar. 29, 2010.

⁵ James C. Morgan, *Deferred Prosecution Agreements: Recent Justice Department Guidance*, Manufacturers Alliance/MAPI e-Alert E-466, Apr. 2, 2008.

for individual defendants has led most to seek favorable terms from the government rather than face the expense and uncertainty of a trial. Thus, the primary statutory interpretive function is still being performed almost exclusively by the DOJ Fraud Section and the SEC. Notably, these enforcement agencies have been increasingly aggressive in their reading of the law. The DOJ has expressed its approach primarily through its opinion releases, but also in its decisions as to what FCPA enforcement actions to pursue.⁶ Many commentators have expressed concern that the DOJ effectively serves as both prosecutor and judge in the FCPA context, because it both brings FCPA charges and effectively controls the disposition of the FCPA cases it initiates.⁷

The recent prosecution and conviction of Frederic Bourke, a matter currently being reviewed by the U.S. Court of Appeals for the Second Circuit, is just one example of how far the DOJ has pressed the limits of enforcement.⁸ Bourke was convicted of conspiring to violate the FCPA based on certain investments he made with a business partner in Azerbaijan. Although Bourke's business partner had

been the one paying bribes to Azeri officials, and although Bourke denied any knowledge of the illicit payments, the government argued that Bourke had "consciously avoided" knowledge of his partner's dealings, and so could not escape liability under the FCPA, even if he did not himself participate in the bribes. The government introduced circumstantial evidence to demonstrate that Bourke should have known that his business partner was paying bribes in Azerbaijan. The DOJ received a jury instruction that allowed the jury to convict Bourke based not on what he actually knew, but rather on what he "suspects."⁹ This jury instruction reflects the expansive reading the DOJ has been giving to the FCPA's knowledge requirement.

In the corporate setting, the DOJ's aggressive pursuit of BAE Systems PLC is further indication of how far the DOJ is willing to expand the scope of FCPA enforcement.¹⁰ In early 2010, BAE, one of the largest defense contractors in the world, negotiated a global resolution of the U.S. and U.K. governments' investigations into allegations of corruption at BAE.¹¹ To resolve the U.S. inquiry, BAE agreed to plead guilty to a one-count

6 Mike Koehler, *Compliance Lessons from an Active Year in FCPA Enforcement*, 3(4) WHITE COLLAR CRIME REPORT, February 15, 2008.

7 Kevin M. King and William M. Sullivan, *Vigorous FCPA Enforcement Reflects Pursuit of Foreign Bribery*, 5(3) ATLANTIC COAST IN-HOUSE 19, March 2008 (discussing how in 2007, of the 11 enforcement actions the DOJ took against corporations, seven were resolved entirely through either a deferred prosecution agreement or a non-prosecution agreement).

8 See Chad Bray, *Bourke Sentenced to One Year in Azerbaijan Bribery Case*, WALL STREET JOURNAL, Nov. 10, 2009, available at <http://online.wsj.com/article/SB10001424052748704402404574528003117098132.html>; see also Mike Koehler, *Bourke Appeals Ruling in Most Complex, Convoluted Case in FCPA History*, *Corporate Compliance Insights*, Apr. 26, 2010, available at <http://www.corporatecomplianceinsights.com/2010/bourke-appeals-ruling-in-most-complex-convoluted-case-in-fcpa-history/>.

9 Jury Charge at 27, *United States v. Bourke*, S2 05 Cr. 518 (SAS) (S.D.N.Y. Jul. 1, 2009).

10 David Robertson, *US Seeks to Pursue BAE Over Claims Company Paid Bribes*, THE TIMES, May 2, 2007, available at http://business.timesonline.co.uk/tol/business/industry_sectors/engineering/article1733903.ece

11 Press Release, U.S. Department of Justice, *BAE Systems PLC Pleads Guilty and Ordered to Pay \$400 Million Criminal Fine* (March 1, 2010), available at <http://www.justice.gov/opa/pr/2010/March/10-crm-209.html>.

criminal information charging the company with conspiring to make false statements to various U.S. government agencies regarding its anti-corruption undertakings, and with failing to disclose hundreds of millions of dollars in commission payments related to arms sales.¹² BAE also agreed to pay a \$400 million criminal penalty to the U.S. to resolve the investigation.¹³

It is noteworthy that the questionable payments underlying the FCPA allegations appear to have been made almost entirely outside the United States.¹⁴ As a result, the FCPA jurisdictional nexus for the case—which would require acts taken in the United States—was tenuous.¹⁵ The DOJ nevertheless aggressively pursued the BAE investigation as an FCPA matter and ultimately obtained a costly settlement for BAE along with a felony plea.¹⁶ The BAE case further underscores the highly aggressive stance the DOJ is taking to expand the FCPA net beyond its borders.

In addition to increased governmental enforcement, the last five years has seen a marked uptick in the quantity of follow-on civil litigation after an FCPA enforcement action.¹⁷ In most of these cases, claimants assert that mismanagement and poor internal controls allowed the violative conduct to occur. Shareholders in securities class action lawsuits are also increasing their reliance on FCPA enforcement actions to claim they were misled by the directors and officers of the defendant company. Thus, as the frequency of enforcement actions grows, so too should we expect secondary civil litigation to increase.

Unfortunately for the business community, an active FCPA enforcement environment appears likely to continue: current incentives ensure that judicial oversight of FCPA cases will continue to be limited, and both the DOJ and SEC have continued to devote significant new resources to FCPA enforcement actions.¹⁸ In addition, two new legislative developments are likely to reinforce the trend:

12 Press Release, U.S. Department of Justice, BAE Systems PLC Pleads Guilty and Ordered to Pay \$400 Million Criminal Fine (March 1, 2010), *available at* <http://www.justice.gov/opa/pr/2010/March/10-crm-209.html>.

13 *Id.*

14 Steven A. Tyrrell, *DOJ Prosecution of BAE Heralds Continued Aggressive FCPA Enforcement Environment*, Weil Briefing (Feb. 8, 2010), *available at* <http://www.weil.com/news/pubdetail.aspx?pub=9725>.

15 *Id.*

16 Press Release, U.S. Department of Justice, BAE Systems PLC Pleads Guilty and Ordered to Pay \$400 Million Criminal Fine (Mar. 1, 2010), *available at* <http://www.justice.gov/opa/pr/2010/March/10-crm-209.html>.

17 Hanna Hasl-Kelchner, *International Business: How a FCPA Violation Can Morph Criminal Liability into Civil Liability*, ALL BUSINESS, Aug. 28, 2009.

18 See Robert Khuzami, Director, Division of Enforcement, Securities and Exchange Commission, Remarks Before the New York City Bar: My First 100 Days as Director of Enforcement (Aug. 5, 2009), *available at* <http://www.sec.gov/news/speech/2009/spch080509rk.htm> (“The Foreign Corrupt Practices Act unit will focus on new and proactive approaches to identifying violations of the Foreign Corrupt Practice Act ... While we have been active in this area, more needs to be done, including being more proactive in investigations, working more closely with our foreign counterparts, and taking a more global approach to these violations.”); David Hechler, *DOJ UNIT That Prosecutes FCPA to Bulk Up ‘Substantially,’* Corporate Counsel (Feb. 26, 2010), *available at* http://www.law.com/jsp/article.jsp?id=1202444612530&pos=atagance&src=EMCEmail&et=editorial&bu=Law.com&pt=LAWCOM%20Newswire&cn=NW_20100226&kw=DOJ%20Unit%20That%20Prosecutes%20FCPA%20to%20Bulk%20Up%20Substantially%27 (noting that the DOJ’s top anti-corruption prosecutor indicated that the DOJ planned to continue to focus on FCPA enforcement and that the DOJ Fraud Section “could grow by as much as 50%” in 2010 and 2011).

- The new Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”) contains a whistleblower bounty provision that seems likely to produce heightened whistleblower activity in connection with FCPA violations.¹⁹ Under these whistleblower provisions, whistleblowers can receive rewards of up to 30 percent of recoveries over \$1 million.
- The new U.K. Bribery Act received Royal Assent on April 8, 2010. The U.K. Ministry of Justice recently released its timetable for the implementation of the Bribery Act, setting April 2011 as the effective date. The Bribery Act is widely viewed as more “far-reaching” than the FCPA in several key respects, including (i) the creation of a strict liability offense for companies and other commercial organizations that fail to prevent bribery, with the only defense being whether the organization instituted “adequate procedures” to prevent bribery; (ii) the absence of an express exception for facilitation payments; and (iii) the absence of an express affirmative defense for reasonable and bona fide business expenditures or for payments that are lawful in the jurisdiction in which the payment is made.

The existence of a more stringent anti-corruption law in the U.K. has led to speculation that U.S.

enforcement authorities will apply even more pressure to companies through the FCPA so as not to be outdone in this area of traditional U.S. dominance. It will take time to determine whether fears of competitive enforcement policies are prescient or unfounded. And although it is unknown when active implementation of the Bribery Act provisions will commence, there can be no doubt that both the U.K. Bribery Act and the whistleblower provision of the Dodd-Frank Act suggest a more hostile enforcement environment going forward than the U.S. business community has yet seen.

The FCPA’s Impact on Business

The current FCPA enforcement environment has been costly to business. Businesses enmeshed in a full-blown FCPA investigation conducted by the U.S. government have and will continue to spend enormous sums on legal fees, forensic accounting, and other investigative costs before they are even confronted with a fine or penalty, which, as noted, can range into the tens or hundreds of millions.²⁰ In fact, one noteworthy innovation in FCPA enforcement policy has been the effective outsourcing of investigations by the government to the private sector, by having companies suspected of FCPA violations shoulder the cost of uncovering such violations themselves through extensive internal investigations.²¹

19 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 922-4, 124 Stat. 1376, 1841-50 (2010).

20 Melissa Klein Aguilar, *How to Size Up, & Manage, FCPA Investigations*, Compliance Week, Aug. 17, 2010.

21 Assistant Attorney General Lanny Breuer, Prepared Address at the 22nd National Forum on the Foreign Corrupt Practices Act (Nov. 17, 2009), available at <http://www.justice.gov/criminal/pr/speeches-testimony/documents/11-17-09aagbreuer-remarks-fcpa.pdf> (“We recognize the issues of costs to companies to implement robust compliance programs, to hire outside counsel to conduct in-depth internal investigations, and to forego certain business opportunities that are tainted with corruption. Those costs are significant and we are very aware of that fact. The cost of not being FCPA compliant, however, can be far higher.”).

From the government's standpoint, it is the best of both worlds. The costs of investigating FCPA violations are borne by the company and any resulting fines or penalties accrue entirely to the government. For businesses, this arrangement means having to expend significant sums on an investigation based solely on allegations of wrongdoing and, if violations are found, without any guarantee that the business will receive cooperation credit for conducting an investigation.

There is also reason to believe that the FCPA has made U.S. businesses less competitive than their foreign counterparts who do not have significant FCPA exposure.²² For example, a 1999 report to Congress authored by the Congressional Research Service ("CRS"), a division of the Library of Congress that provides nonpartisan analysis on current legislative issues, references an estimate that the FCPA's anti-bribery provisions have cost up to \$1 billion annually in lost U.S. export trade.²³ Critics of the FCPA have also argued that ambiguous areas of the law, where what is permitted may not be clear, have had a chilling effect on U.S. business because many companies

have ceased foreign operations rather than face the uncertainties of FCPA enforcement.²⁴

Of course, the solution to this problem is not to do away with the FCPA and permit American companies to engage in bribery alongside their foreign competitors. Rather, the FCPA should be modified to make clear what is and what is not a violation. The statute should take into account the realities that confront businesses that operate in countries with endemic corruption (e.g., Russia, which is consistently ranked by Transparency International as among the most corrupt in the world) or in countries where many companies are state-owned (e.g., China) and it therefore may not be immediately apparent whether an individual is considered a "foreign official" within the meaning of the act. As the U.S. government has not prohibited U.S. companies from engaging in business in such countries, a company that chooses to engage in such business faces unique hurdles. The FCPA should incentivize the company to establish compliance systems that will actively discourage and detect bribery, but should also permit companies that maintain such effective systems to avail themselves

22 See P. Beck et al., *The Impact of the Foreign Corrupt Practices Act on US Exports*, 12 *MANAGERIAL AND DECISION ECON.* 295 (1991); Scott P. Boylan, *Organized Crime in Russia: Implications for U.S. and International Law*, 19 *FORDHAM INT'L L.J.* 1999, 2015-2022 (1996); John Bray, *International Business Attitudes Toward Corruption*, *GLOBAL CORRUPTION REPORT* 316 (2004).

23 Michael V. Seitzinger, Cong. Research Serv., RL 30079, *Foreign Corrupt Practices Act* (Mar. 3, 1999).

24 *Id.*

of an affirmative defense to charges of FCPA violations. This is so because in such countries even if companies have strong compliance systems in place, a third-party vendor or errant employee may be tempted to engage in acts that violate the business's explicit anti-bribery policies. It is unfair to hold a business criminally liable for behavior that was neither sanctioned by or known to the business. The imposition of criminal liability in such a situation does nothing to further the goals of the FCPA; it merely creates the illusion that the problem of bribery is being addressed, while the parties that actually engaged in bribery often continue on, undeterred and unpunished. The FCPA should instead encourage businesses to be vigilant and compliant.

For this reason, and given the current state of enforcement, the FCPA is ripe for much needed clarification and reform through improvements to the existing statute. Such improvements, which are best

suited for Congressional action, are aimed at providing more certainty to the business community when trying to comply with the FCPA, while promoting efficiency and enhancing public confidence in the integrity of the free market system as well as the underlying principles of our criminal justice system.

Specifically, this paper recommends the following reforms:

- Adding a compliance defense;
- Limiting a company's liability for the prior actions of a company it has acquired;
- Adding a "willfulness" requirement for corporate criminal liability;
- Limiting a company's liability for acts of a subsidiary; and
- Defining a "foreign official" under the statute.

II. FCPA-Overview of the Statute

The Central Provision of the FCPA

The central aim of the FCPA is to prohibit the payment of bribes to foreign officials for the purpose of obtaining or retaining business. *See* 15 U.S.C. §§ 78dd-1, dd-2 and dd-3. The act prohibits all covered companies, as well as their employees, directors, or agents from, among other things, making “use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of” a payment to a foreign official in order to influence a decision or secure business. “Covered” companies include all United States companies and many foreign companies.²⁵

The term “corruptly” in the FCPA has been equated by both courts and the FCPA’s legislative history to the “inten[t] to induce the recipient to misuse his official position.” H.R. Rep. No. 95-640, at 8 (1977). And while a narrow exception exists for payments that merely accelerate the normal operations of government that do not involve discretion, there is no *de minimis* exception in the statute for any payment made corruptly. Further, liability attaches even for corrupt payments that are proposed, but not in fact made. *See* 15 U.S.C. §§ 78dd-1(b); *see*

generally United States v. Kay, 359 F.3d 738, 756 (5th Cir. 2004) (noting the FCPA provides for “narrowly defin[ed] exceptions and affirmative defenses against a backdrop of broad applicability”).

Scope of Application to U.S. and Foreign Companies

The FCPA has extremely broad reach and applicability to American and even foreign organizations. Pursuant to 15 U.S.C. §78dd-2, the so-called “domestic concern” provision of the FCPA, every business entity either organized under United States law or with its primary place of business in the United States is subject to the FCPA.²⁶ U.S. companies and citizens are subject to the FCPA regardless of where the act in furtherance of a “corrupt” payment takes place. *See* 15 U.S.C. § 78dd-1(g); *id.* § 78dd-2(i). In addition to liability for a company’s own actions, the government has interpreted the FCPA to ground liability on a U.S. parent corporation and its employees for “the acts of [a] foreign subsidiar[y] where they authorized, directed, or controlled the activity in question.”²⁷ Of course, a parent corporation may also be liable where the corporate

²⁵ *See infra* Section II.B. and fn 3 for the circumstances under which a foreign company will be subject to the FCPA.

²⁶ Other provisions of the FCPA extend its reach to foreign companies that issue securities within the United States, and any entity or individual that commits an act prohibited by statute on American soil. *See* 15 U.S.C. §§78dd-1, 78dd-3.

²⁷ DEPARTMENT OF JUSTICE, LAYPERSON’S GUIDE TO FCPA, *available at* <http://www.justice.gov/criminal/fraud/fcpa/docs/lay-persons-guide.pdf>. *See infra* Sections III.B. and III.D. for a more in-depth discussion about the government’s imposition of FCPA liability on parent companies for actions taken by foreign subsidiaries.

veil is pierced because the subsidiary is a mere alter ego of the parent. *See generally United States v. BestFoods*, 524 U.S. 51, 62 (1998).

Books-and-Records and Internal Control Provisions

The FCPA also has two additional key provisions that apply to entities that have securities registered pursuant to 15 U.S.C. § 781 and who are required to file reports with the SEC pursuant to 15 U.S.C. § 78o(d). The first provision is known as the “books-and-records” provision, and requires such entities to “make and keep books, records and accounts which in reasonable detail accurately and fairly reflect the transactions and dispositions of the issuer.” 15 U.S.C. § 78m(b)(2)(A).²⁸ The second provision is known as the “internal controls” provision, and requires such entities to “devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that” transactions are executed with proper authorization of management, financial statements are prepared in accordance to proper accounting principles, and that the company “maintain(s) accountability” for assets. 15 U.S.C. § 78m(b)(2)(B).²⁹

These provisions give rise to criminal liability where there are “knowing” violations. *See* 15 U.S.C. § 78m(b)(4) & (5). Because a violation of these provisions does not necessarily require proof of a corrupt payment being made or contemplated, these rules are often invoked by the government to pursue cases where improper payments are suspected, but difficult to prove, or as a means to settle cases for a “lesser” charge. For example, the SEC brought charges for violations of the FCPA books-and-records provision against Oil States International where the company was suspected of having made hundreds of thousands of dollars in improper payments to employees of an energy company owned by the Venezuelan government.³⁰

Applicable Penalties

Violations of the FCPA have led to significant civil and criminal penalties. A company can be criminally fined up to \$2 million per violation of the anti-bribery provisions (which could apply to each illegal payment), and culpable individuals can be subject to a criminal fine of up to \$250,000 per violation (same), as well as imprisonment for up to

28 An “accurate” report is one that “fairly reflect[s] the transactions and dispositions of the assets of the issuer.” 15 U.S.C. § 78m(b)(2). The statute further defines “reasonable detail” as “such level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs.” 15 U.S.C. § 78m(b)(7). Companies must make these accurate reports to the SEC on a periodic basis pursuant to 15 U.S.C. § 78o(d).

29 The statute provides the same definition for “reasonable assurances” as for “reasonable detail.” *See* 15 U.S.C. § 78m(b)(7); *see supra* fn 5.

30 *See* Oil States Int’l., Exchange Act Release No. 53732, 2006 WL 1113519 (Apr. 27, 2006), *available at* <http://www.sec.gov/litigation/admin/2006/34-53732.pdf>. As a practical matter, when the inaccuracy in the companies’ books and records is the mischaracterization of a bribe, then proving the existence of the bribe is required absent a plea or settlement.

five years for each violation.³¹ Violations of the books-and-records and internal control provisions that are deemed “willful” and not just “knowing” can result in a criminal fine of up to \$25 million for a company and a criminal fine up to \$5 million as well as imprisonment for up to 20 years for culpable individuals.³² Further, a defendant—whether a company or individual—can be required to pay twice the gross gains or losses if criminally convicted for an FCPA violation.³³ Where the contract allegedly obtained through a bribe is significant, therefore, this provision can make the potential penalty prohibitive. In addition to these

finances and penalties, the SEC may seek disgorgement of a company’s profits on contracts secured through improper payments.³⁴

It has also become common for the government to require appointment of an independent compliance monitor, at the company’s expense, for a period of time after the settlement (typically two to three years).³⁵ The independent monitor can be charged with giving instructions or making recommendations to the company for FCPA compliance with which the company must comply, and the monitor has reporting duties to the government.

31 See 15 U.S.C. §§78dd-2(g), 78dd-3(e), 78ff.

32 See 15 U.S.C. §§78ff.

33 18 U.S.C. §3571(c)

34 Disgorgement is an equitable concept that has existed in Exchange Act jurisprudence for decades, but the SEC has increasingly relied upon it in the years since the passage of Sarbanes-Oxley. It was first employed by the SEC in an FCPA case in 2004. See David C. Weiss, *The Foreign Corrupt Practices Act, SEC Disgorgement of Profits, and The Evolving International Bribery Regime: Weighing Proportionality, Retribution, And Deterrence*, 30 MICH. J. OF INT’L LAW 471, 474, 485-88 (2009). There is no specific statutory authority for the SEC’s use of disgorgement as a penalty in the FCPA context. See *id.*

35 See *infra* the Alliance One case discussed in Section III.B.1.

III. Potential Reforms

The following are five potential reforms to the FCPA aimed at providing more certainty to the business community while promoting efficiency and enhancing public confidence in the integrity of the free market system as well as the underlying principles of our criminal justice system.

Adding The Compliance Defense Recognized By The United Kingdom

The FCPA does not provide a compliance defense, that is, a defense that would permit companies to fight the imposition of criminal liability for FCPA violations, if the individual employees or agents had circumvented compliance measures that were otherwise reasonable in identifying and preventing such violations. A company can therefore currently be held liable for FCPA violations committed by its employees or subsidiaries even if the company has a first-rate FCPA compliance program. Certain benefits may currently accrue to companies that have strong FCPA compliance programs—the

DOJ or SEC may decide to enter a non-prosecution or deferred prosecution agreement with such companies if violations are uncovered, for example,³⁶ and such compliance systems can be taken into account at sentencing.³⁷ However, such benefits are subject to unlimited prosecutorial discretion, are available only after the liability phase of a FCPA prosecution, or both.

By contrast, the comprehensive Bribery Act of 2010 recently passed by the British Parliament—Section 6 of which addresses bribes of foreign officials and closely tracks the FCPA—provides a specific defense to liability if a corporate entity can show that it has “adequate procedures” in place to detect and deter improper conduct.³⁸ In September 2010, U.K.’s Ministry of Justice provided initial guidance on what may constitute such “adequate procedures.”³⁹ The proposed guidance consists of the following six principles:

1. Risk Assessment (regular and comprehensive assessment of bribery-related risks to an organization).

36 See Principles of Federal Prosecution of Business Organizations, Title 9, Chapter 9-28.000, UNITED STATES ATTORNEY’S MANUAL, *available at* http://www.justice.gov/usao/eousa/foia_reading_room/usam/title9/28mcrm.htm (decision whether to charge). While evidence of a strong compliance program may help a corporation reach a non-prosecution or deferred prosecution agreement in connection with FCPA charges, the government has complete discretion as to how much credit to give for such a program. Thus, a corporation may still find that it is pressured to give up certain rights or to accept certain punishments in order to achieve what is not only a desired, but a fair, outcome. See, e.g., Gerald E. Lynch, *The Role of Criminal Law in Policing Corporate Misconduct*, 60 LAW & CONTEMP. PROBS. 23, 59 (1997).

37 See U.S.S.G. § 8B2.1.

38 See Bribery Act of 2010, ch. 23, § 7(2) (U.K.).

39 Section 9 of the Act requires the Secretary of State to publish and then solicit comments on such guidance. Bribery Act of 2010, ch. 23 § 9 (U.K.). The comment period runs until November 8, 2010.

2. Top-Level Commitment (a commitment to preventing bribery clearly communicated by top-level management).
3. Due Diligence (due diligence policies and procedures covering all parties to a business relationship).
4. Clear, Practical and Accessible Policies and Procedures (ensuring that policies and procedures are readily accessible and enforceable throughout the organization).
5. Effective Implementation (ensuring that the policies and procedures are embedded throughout the organization).
6. Monitoring and Review (mechanisms to ensure compliance with relevant policies and procedures, and implementation of improvements where appropriate).

In 2001, the Italian government also passed a statute that proscribes foreign bribery.⁴⁰ Like the UK Anti-Bribery bill, it contains a compliance defense. Articles 6 and 7 of the statute permit a company to avoid liability if it can demonstrate

that, before employees of the company engaged in a specific crime (e.g., bribery), it (1) adopted and implemented a model of organization, management and control (the “Organizational Model”) designed to prevent that crime, (2) engaged an autonomous body to supervise and approve the model, and (3) the autonomous body adequately exercised its duties.⁴¹ To determine whether the model was effectively designed, the law requires consideration of the following factors:

1. Management of Resources (whether financial resources were managed in a way that discouraged crime).
2. Provision of Information to Management (whether the model required officers and employees to supply the supervisory body responsible for monitoring the model with the necessary information to ensure their compliance with it).
3. Disciplinary Measures (whether such measures necessary to sanction non-compliance were included in the model).⁴²

⁴⁰ Legislative Decree no. 231 of 8 June 2001; *see also Italian Law No. 231/2001: Avoiding Liability for Crimes Committed by a Company's Representatives*, McDermott, Will & Emery, April 27, 2009, available at <http://www.mwe.com/info/news/wp0409f.pdf>. The statute proscribes a variety of criminal activity, including foreign bribery.

⁴¹ *See id.*

⁴² *See id.*

The principles embodied in the British and Italian laws closely track the factors currently taken into consideration by courts in the United States only at a very different phase of the criminal process, namely when considering whether a corporation should have a slight reduction in its culpability score when sentencing it for FCPA or other violations.⁴³ These principles—which Congress and the Sentencing Commission have already identified as key indicators of a strong and effective compliance program—should be considered instead during the liability phase of an FCPA prosecution.⁴⁴ The adoption of such a compliance defense will not only increase compliance with the FCPA by providing businesses with an incentive to deter, identify, and self-report potential and existing violations, but will also protect corporations from employees who commit crimes despite a corporation’s diligence. And, it will give corporations some measure of protection from aggressive or misinformed prosecutors, who can exploit the power imbalance inherent in the current FCPA statute—which permits indictment of a corporation even for the acts of a single, low-level rogue employee—to force corporations into deferred prosecution agreements.⁴⁵

In addition, institution of a compliance defense will bring enforcement of the FCPA in line with Supreme Court precedent, which has recognized that it is appropriate and fair to limit *respondeat superior* liability where a company can demonstrate that it took specific steps to prevent the offending employee’s actions. See, e.g., *Kolstad v. American Dental Ass’n*, 527 U.S. 526 (1999). The Court concluded in *Kolstad* that, in the punitive damages context, “an employer may not be vicariously liable for the discriminatory employment decisions of managerial agents where these decisions are contrary to the employer’s ‘good-faith efforts to comply with Title VII.’” *Id.* at 545. This holding was motivated by a concern that the existing standard was “dissuading employers from implementing programs or policies to” comply with Title VII for fear that such programs would bring to light violations for which a company would ultimately be liable, no matter what steps it had undertaken to prevent such violations. *Id.* at 544-45. Here, companies may similarly be dissuaded from instituting a rigorous FCPA compliance program for fear that the return on such an investment will be only to expose the company to increased

43 See U.S.S.G. § 8B2.1.

44 There is evidence that Congress may be open to such a proposal. In 1988, the United States House of Representatives proposed adding a similar “safe harbor” to the FCPA, which would have shielded companies that established procedures that were “reasonabl[y] expected to prevent and detect” FCPA violations from vicarious liability for FCPA violations of employees. See H.R. Conf. Rep. on H.R. 3, 100th Cong., 2d Sess. 916, 922 (1988).

45 See Andrew Weissmann, Richard Ziegler, Luke McLoughlin & Joseph McFadden, *Reforming Corporate Criminal Liability to Promote Responsible Corporate Behavior*, U.S. CHAMBER INSTITUTE FOR LEGAL REFORM (Oct. 2008), available at http://www.instituteforlegalreform.com/component/ilm_issues/29.html.

liability and will do little to actually protect the company. An FCPA compliance defense will help blunt some of these existing “perverse incentives.” *Id.* at 545.⁴⁶

Limiting a Company’s Successor Criminal FCPA Liability for Prior Acts of a Company it Has Acquired

Under the current enforcement regime, a company may be held criminally liable under the FCPA not

only for its own actions, but for the actions of a company that it acquires or becomes associated with via a merger—even if those acts took place prior to the acquisition or merger and were entirely unknown to the acquiring company.⁴⁷ Such a standard of criminal liability is generally antithetical to the goals of the criminal law, including punishing culpable conduct or deterring offending behavior. While a company may mitigate its risk by conducting due diligence prior to an acquisition or merger (or, in certain circumstances,

46 See also Weissmann with Newman, 82 *Ind. L.J.* at 432-33 (describing the lack of incentive for corporations “to implement effective compliance programs” given that “[u]nder the current legal regime, a corporation is given no benefit at all under the law for even the best internal compliance program if such crime nevertheless occurs”). Numerous judges, former and current prosecutors, and legislative counsel have criticized the current system. See, e.g., Preet Bharara, *Corporations Cry Uncle and their Employees Cry Foul: Rethinking Prosecutorial Pressure on Corporate Defendants*, 44 *AM. CRIM. L. REV.* 53 (2007); Edwin Meese III, *Closing Commentary on Corporate Criminal Liability: Legal, Ethical, and Managerial Implications*, *AM. CRIM. L. REV.* 1545 (2007); George J. Terwilliger III, *Under-Breaded Shrimp and Other High-Crimes: Addressing the Over-Criminalization of Commercial Regulation*, 44 *AM. CRIM. L. REV.* 1417 (2007); Dick Thornburgh, *The Dangers of Over-Criminalization and the Need for Real Reform: The Dilemma of Artificial Entities and Artificial Crimes*, *AM. CRIM. L. REV.* 1279 (2007); Andrew Weissmann, *A New Approach to Corporate Criminal Liability*, 44 *AM. CRIM. L. REV.* 1319 (2007); Gerard E. Lynch, *The Role of Criminal Law in Policing Corporate Misconduct*, 60 *LAW & CONTEMP. PROBS.* 23 (1997); Hon. Lewis A. Kaplan, Remarks to the New York State Bar Association: Should We Reconsider Corporate Criminal Liability? (Jan. 24, 2007), available at http://nysbar.com/blogs/comfed/2007/06/should_we_reconsider_corporate.html.

The critique from scholars and practitioners has also been persistent and compelling. See, e.g., Jennifer Arlen, *The Potentially Perverse Effects of Corporate Criminal Liability*, 23 *J. LEGAL STUD.* 833 (1994); Kathleen F. Brickey, *Rethinking Corporate Liability Under the Model Penal Code*, 19 *RUTGERS L.J.* 593 (1988); H. Lowell Brown, *Vicarious Criminal Liability of Corporations for the Acts of Their Employees and Agents*, 41 *LOV. L. REV.* 279, 324 (1995); Pamela H. Bucy, *Corporate Ethos: A Standard for Imposing Criminal Liability*, 75 *MINN. L. REV.* 1095 (1991); Pamela H. Bucy, *Trends in Corporate Criminal Prosecutions*, 44 *AM. CRIM. L. REV.* 1287 (2007); John C. Coffee, Jr., “No Soul To Damn: No Body To Kick”: *An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 *MICH. L. REV.* 386 (1981); John C. Coffee, Jr., *Does “Unlawful” Mean “Criminal”?: Reflections on the Disappearing Tort/Crime Distinction in American Law*, 71 *B.U. L. REV.* 193 (1991); Daniel R. Fischel & Alan O. Sykes, *Corporate Crime*, 25 *J. LEGAL STUD.* 319 (1996); Brent Fisse & John Braithwaite, *The Allocation of Responsibility for Corporate Crime: Individualism, Collectivism and Accountability*, 11 *SYDNEY L. REV.* 468 (1988); Richard S. Gruner & Louis M. Brown, *Organizational Justice: Recognizing and Rewarding the Good Citizen Corporation*, 21 *J. CORP. L.* 731 (1996); V.S. Khanna, *Corporate Criminal Liability: What Purpose Does It Serve?*, 109 *HARV. L. REV.* 1477 (1996); V.S. Khanna, *Is the Notion of Corporate Fault a Faulty Notion?: The Case of Corporate Mens Rea*, 79 *B.U. L. REV.* 355 (1999); Bruce H. Kobayashi, *Antitrust, Agency, and Amnesty: An Economic Analysis of the Criminal Enforcement of the Antitrust Laws Against Corporations*, 69 *GEO. WASH. L. REV.* 715 (2001); William S. Laufer & Alan Strudler, *Corporate Crime and Making Amends*, *AM. CRIM. L. REV.* 1307 (2007); Craig S. Lerner & Moin A. Yahya, *Left Behind After Sarbanes-Oxley*, 44 *AM. CRIM. L. REV.* 1383 (2007); Geraldine Szott Moohr, *Of Bad Apples and Bad Trees: Considering Fault-Based Liability for the Complicit Corporation*, 44 *AM. CRIM. L. REV.* 1343 (2007); Ellen S. Podgor, *A New Corporate World Mandates a “Good Faith” Affirmative Defense*, *AM. CRIM. L. REV.* 1537 (2007); Paul H. Robinson, *The Practice of Restorative Justice: The Virtues of Restorative Process, the Vices of “Restorative Justice,”* 2003 *UTAH L. REV.* 375, 384-85; Charles J. Walsh & Alissa Pyrich, *Corporate Compliance Programs as a Shield to Criminal Liability: Can a Corporation Save Its Soul?*, 47 *RUTGERS L. REV.* 605, 689 (1995); Bruce Coleman, *Comment, Is Corporate Criminal Liability Really Necessary?*, 29 *SW. L.J.* 908, 927 (1975); *Developments in the Law—Corporate Crime: Regulating Corporate Behavior Through Criminal Sanction*, 92 *HARV. L. REV.* 1227 (1979); John Baker, *Corporations Aren’t Criminals*, *WALL ST. J.*, Apr. 22, 2002, at A3.

47 See, e.g., Department of Justice FCPA Opinion Procedure Release No. 03-01 (Jan. 15, 2003), available at <http://www.justice.gov/criminal/fraud/fcpa/opinion/2003/0301.pdf> (advising that a company that conducted due diligence on a target company and self-reported any violations that took place pre-acquisition may be able to escape criminal and/or civil successor liability, thereby suggesting that successor liability was a viable theory of liability under the FCPA).

immediately following an acquisition or merger),⁴⁸ that does not constitute a legal defense if a matter nevertheless arises that was not detected. Thus, even when an acquiring company has conducted exhaustive due diligence and immediately self-reported the suspected violations of the target company, it is still currently legally susceptible to criminal prosecution and severe penalties.

1. The Problem of Successor Liability

The DOJ appears to have first stated its position that a company can be subject to criminal successor liability under the FCPA in an opinion published in 2003.⁴⁹ In that opinion, the DOJ provided advice to a company that was seeking to acquire a target company. In the course of pre-acquisition due diligence, the company discovered potential FCPA violations that had been previously committed by the target. The DOJ outlined a series of steps that the company could take to avoid successor liability for the target's violations, including cooperation with DOJ and SEC investigations, disclosure of any additional violations, and institution of an FCPA compliance program at the target.

- In the years since, the government has continually reiterated that the one way companies can appeal to the government to

exercise its discretion not to seek to impose criminal successor FCPA liability for pre-acquisition or pre-merger actions by a target company is rigorous due diligence accompanied by disclosure of any violations. For instance, a 2006 speech given by then-Assistant Attorney General Alice Fisher, the head of the Criminal Division at the DOJ, underscored this philosophy: Fisher stressed that any company seeking to acquire a target company with overseas dealings should include as a component of its due diligence a search for indicators of FCPA violations, and that disregard of such indicators could lead to “successor liability” for the prior conduct of a target's actions.⁵⁰

- The uncertainty about how much due diligence is sufficient, coupled with the threat of successor liability even if thorough due diligence is undertaken, have in recent years had a significant chilling effect on mergers and acquisitions. For example, Lockheed Martin terminated its acquisition of Titan Corporation when it learned about certain bribes paid by Titan's African subsidiary that were uncovered during pre-closing due diligence; Lockheed Martin was simply unwilling to take on the risk of FCPA successor liability for those bribes.⁵¹

48 See Department of Justice FCPA Opinion Procedure Release No. 08-02 (Jun. 13, 2008), *available at* <http://www.usdoj.gov/criminal/fraud/fcpa/opinion/2008/0802.html> (providing advice on proper post-acquisition due diligence in the rare situation where it was impossible for the acquiring company to perform due diligence on the target prior to acquisition).

49 See Department of Justice FCPA Opinion Procedure Release No. 03-01 (Jan. 15, 2003).

50 Alice S. Fisher, Assistant Attorney General, United States Department of Justice, Prepared Remarks at the American Bar Association National Institute on the Foreign Corrupt Practices Act (October 16, 2006), *available at* <http://www.justice.gov/criminal/fraud/pr/speech/2006/10-16-06AAGFCPASpeech.pdf>.

51 See Margaret M. Ayres and Bethany K. Hipp, *FCPA Considerations in Mergers and Acquisitions*, 1619 PLL/CORP 241, 249 (Sept. 17, 2007); see also SEC Litig. Rel. No. 19107, 2005 WL 474238 (Mar. 1, 2005), *available at* <http://404.gov/litigation/litreleases/lr19107.htm>.

Recent FCPA enforcement actions indicate that the government has moved beyond simply asking companies to look for FCPA violations of a target company during due diligence if those companies want to escape successor liability. For proof, one need only look to the DOJ's Opinion Procedure Release No. 08-02 ("Opinion 08-02"), in which the DOJ provided advice to a company inquiring about the necessary amount of post-acquisition due diligence on a target company required in a situation where pre-acquisition due diligence could not be undertaken. The DOJ required the company to conduct due diligence on a scale equivalent to a vast internal investigation in order to avoid prosecution by the DOJ for any FCPA violations previously committed by the target company.⁵²

This investigation required the company to "retain external counsel and third-party consultants, including forensic accountants, as well as utilize internal resources, as appropriate, to conduct the FCPA and anti-corruption due diligence."⁵³ The company was also compelled to conduct an "examination of relevant [target company] records, including e-mail review and review of company financial and accounting records, as well as interviews of relevant [the target company's] personnel and other individuals."⁵⁴ The opinion also set forth a rigid disclosure schedule: The company was required to meet with the DOJ

within ten business days of closing to discuss the problematic documents from the data room and to investigate high-risk issues and report findings to the DOJ within 90 days of closing, followed by medium-risk issues (with disclosure within 120 days of closing) and low-risk issues (with disclosure within 180 days of closing).⁵⁵ And the DOJ warned that even if the company took all of these steps and made all of the required disclosures, the DOJ would still hold the company liable for ongoing violations by the target company not uncovered during the first 180 days of due diligence, as well as prior violations by the target company disclosed to the DOJ to the extent that such violations were not "investigated to conclusion within one year of closing."⁵⁶

The DOJ has thus leveraged the threat of successor liability into a means to achieve expansive internal controls. Opinion 08-02 is a harbinger of the increased threat posed by the FCPA to businesses contemplating mergers and acquisitions with companies that have foreign subsidiaries or offices. The dominant take-aways are that (1) to even qualify for such a "grace period" for successor liability an acquiring company must expend enormous resources on a complex and far-reaching internal investigation, and (2) even if a company expends such resources and honestly and diligently seeks to identify prior FCPA violations,

52 See Department of Justice FCPA Opinion Procedure Release No. 08-02 (Jun. 13, 2008), *available at* <http://www.justice.gov/criminal/fraud/fcpa/opinion/2008/0802.pdf>.

53 *Id.*

54 *Id.*

55 See *id.*

56 *Id.*

it may ultimately still be held liable for those violations. The DOJ also added a footnote in its opinion discouraging companies who would seek a release of liability from the DOJ from entering into confidentiality agreements for pre-closing documents, suggesting that companies may be penalized for their inability to provide the DOJ with a full accounting of their concerns.

That potential for so-called criminal successor liability which animated Opinion 08-02 is real. The following are two recent examples:

- Alliance One—Alliance One is an American tobacco company that was formed in 2005 with the merger of Dimon Incorporated (“Dimon”) and Standard Commercial Corporation (“SCC”). Employees and agents of two foreign subsidiaries of Dimon and SCC committed FCPA violations before the merger.⁵⁷ In 2010, the DOJ brought a criminal case against Alliance One on a successor liability theory; that is, subsidiaries of Dimon and SCC engaged in FCPA violations, subsequent to which the two parent companies formed Alliance One, and thus Alliance One is now liable for the prior actions of the Dimon and SCC subsidiaries.⁵⁸ The DOJ ultimately entered a non-prosecution agreement with Alliance One, after the foreign subsidiaries of each pled guilty to multiple-count criminal informations; the agreement requires Alliance One to cooperate with the DOJ’s ongoing investigation and to retain an independent compliance monitor for a minimum of three years to oversee the implementation of a compliance program and to report back to the DOJ on its progress. (Alliance One also settled a related civil complaint brought by the SEC, and agreed to disgorge approximately \$10 million in profits).
- Snamprogetti—Snamprogetti was a wholly-owned Dutch subsidiary of a company called ENI S.p.A. From approximately 1994 to 2004, Snamprogetti participated in a complex and far-reaching bribery scheme.⁵⁹ In 2006, after the then-completed conduct was under investigation, ENI sold Snamprogetti to another company, Saipem S.p.A. Snamprogetti was charged with criminal violations of the FCPA in connection with the scheme in July 2010.⁶⁰ The DOJ ultimately reached a deferred prosecution agreement in connection with these charges; that agreement was between the DOJ, Snamprogetti, ENI and Saipem.⁶¹ The

57 See Press Release, Department of Justice, Alliance One International Inc. and Universal Corporation Resolve Related FCPA Matters Involving Bribes Paid to Foreign Government Officials (Aug. 6, 2010), *available at* <http://www.justice.gov/opa/pr/2010/August/10-crm-903.html>; see Press Release, Securities and Exchange Commission, SEC Files Anti-Bribery Charges Against Two Global Tobacco Companies (Aug. 6, 2010), *available at* <http://www.sec.gov/litigation/litreleases/2010/lr21618.htm>.

58 See, e.g., Complaint, *Securities and Exchange Commission v. Alliance One International, Inc.*, Civil Action No. 01:10-cv-01319 (RMU) (D.D.C. Aug. 6, 2010), *available at* <http://www.sec.gov/litigation/complaints/2010/comp21618-alliance-one.pdf> (describing the merger in ¶ 1 of the Complaint, and then detailing the actions taken by the Dimon and SCC subsidiaries, which formed the basis for the charges against Alliance One).

59 See Criminal Information, *United States v. Snamprogetti Netherlands B.V.*, Crim. No. H-10-460, (S.D. Tex. Jul. 7, 2010), ECF No. 1.

60 See *id.*

61 See Deferred Prosecution Agreement, *United States v. Snamprogetti Netherlands B.V.*, Crim. No. H-10-460, (S.D. Tex. Jul. 7, 2010), ECF No. 3.

agreement provides that Snamprogetti pay a \$240 million fine, for which ENI and Saipem are jointly and severally liable; that ENI, Snamprogetti and Saipem institute a corporate compliance program; and that the statute of limitations for any action against Snamprogetti, ENI and Saipem connected to the underlying facts in the matter will be tolled for the duration of the agreement. Saipem's inclusion in the deferred prosecution agreement clearly indicates that it is being held criminally liable for Snamprogetti's actions on a theory of successor liability.

These cases illustrate the purest form of FCPA successor liability, where the conduct that constituted an FCPA violation or violations was complete *prior* to a merger or acquisition that connected that conduct to the corporate entity that was ultimately charged or held liable for that conduct. The conduct underlying the violations in the Alliance One case predated the very existence of the corporate entity that was charged with the violations; the conduct in the Saipem case predated the company's acquisition of the subsidiary that had committed the violations. Regardless, both companies were held accountable as if they themselves had engaged in the improper conduct.

2. Federal Successor Liability Law

Successor liability law in the United States is a complex, multi-factor matter. The usual rationale

for such liability was to avoid a company evading liability by simply reconstituting itself as another company. Thus, successor liability for corporations originated in state law as "an equitable remedy against formalistic attempts to circumvent contractual or statutory liability rules."⁶² Though it varies from state to state, the question of whether successor liability can be imposed generally requires a complex analysis of various factors, including whether the successor company expressly agreed to assume the liability, or if a merger or acquisition was fraudulently entered into to escape liability.⁶³ Courts may also look to whether it is in the public interest to impose such liability. *See, e.g., United States v. Cigarette Merchandisers Ass'n, Inc.*, 136 F. Supp. 214 (S.D.N.Y. 1955) (determining that criminal successor liability was appropriate because the public policy of the state was that a corporation remain suable for its debts and obligations after dissolution).

A federal court considering a question of successor liability in the context of a state law claim will clearly look to the law of the relevant state for the proper analysis. But, as there is no relevant federal corporate law, there is no clear avenue for determining whether corporate criminal successor liability is appropriate in a federal action brought by the government. Thus federal courts have had to make the determination of whether to impose successor liability on a case-by-case, statute-by-statute basis. In the majority of cases where a

62 Aaron Xavier Fellmeth, *Cure Without A Disease: The Emerging Doctrine Of Successor Liability In International Trade Regulation*, 31 YALE J. INT'L L. 127, 136 (2006).

63 See Carolyn Lindsay, *More Than You Bargained For: Successor Liability Under the U.S. Foreign Corrupt Practices Act*, 35 OHIO N.U.L. REV. 959, 965-68 (2009).

federal court has imposed successor liability, the enforcement action has involved civil penalties and has arisen in connection with regulatory laws, such as environmental remediation statutes (particularly the Comprehensive Environmental Response, Compensation and Liability Act, or CERCLA) and labor statutes (particularly the National Labor Relations Act, or NLRA).⁶⁴

There are few cases in which a federal court has had to consider the question of whether a corporation should be held criminally liable under a theory of successor liability. However, in most of these cases, courts have declined to permit criminal successor liability for a corporation with no knowledge of the prior bad acts. For example, in *Rodriguez v. Banco Central*, 777 F. Supp. 1043, 1064 (D.P.R. 1991), *aff'd*, 990 F.2d 7 (1st Cir. 1993), the court declined to permit successor liability in connection with a RICO action, finding that “successor liability should be found only sparingly and in extreme cases due to the requirement that RICO liability only attaches to knowing affirmatively willing participants.” Similarly, in *R.C.M. Executive Gallery Corp. v. Rols Capital Co.*, 901 F. Supp. 630, 635 (S.D.N.Y. 1995), the court concluded that it is possible for a corporation to be found liable as a successor only if there is a showing that the purchaser had knowledge of the RICO Act violation at the time of purchase.

There are some exceptions, however. In *United States v. Alamo Bank of Texas*, 880 F.2d 828 (5th Cir. 1989), Alamo Bank (“Alamo”) was prosecuted

for violations of the Bank Secrecy Act that had been committed by a company called Central National Bank (“CNB”), three or four years prior to its merger with Alamo Bank. The court concluded that Alamo could be charged with the criminal violations because “CNB continues to exist, albeit now as part of Alamo...Thus, Alamo is CNB, and it is CNB now named Alamo which is responsible for CNB’s actions and liabilities. This includes criminal responsibility.” *Id.* at 830. Alamo’s ignorance of the acts committed by CNB did not persuade the court that it should escape successor liability. *Id.*

Because the issue of criminal successor liability under the FCPA has never been raised in court, no corporation charged on the basis of such a theory of liability has ever put the government to a test of whether such liability is appropriate for that specific corporation; nor has it considered the broader question of whether criminal successor liability is appropriate for the FCPA as a general matter. We contend that it is not.

3. The Legislative Fix

Clear parameters need to be placed on successor liability in the FCPA context. At a minimum, a corporation, irrespective of whether or not it conducts reasonable due diligence prior to and/or immediately after an acquisition or merger, should not be held criminally liable for such historical violations. Under the criminal law, a company (just like a person) should not be held liable for the

⁶⁴ Fellmeth, 31 YALE J. INT’L L. at 142; *see, e.g. Smith Land & Improvement Corp. v. Celotex Corp.*, 851 F.2d 86, 92 (3d Cir. 1988) (finding successor liability in connection with a CERCLA enforcement action); *Golden State Bottling Co. v. Nat’l Labor Relations Bd.*, 414 U.S. 168, 176 (1973) (finding successor liability in connection with a NLRA enforcement action).

actions of another company with which it did not act in concert. Yet in the FCPA context that is just what is happening. Of course, if the successor company inherits employees who continue to commit an FCPA violation, that new conduct can rightfully be imputed to the new company, but that is not a limitation that the government is currently applying. Simply put, the DOJ should not be able to impute criminal actions of employees of another company, to a current company. That would extend *respondeat superior* (imputation of current employee conduct to an employer) beyond its already vast bounds. Certainly, if a company does conduct reasonable due diligence, the company should not as a matter of law (not as a matter of mere DOJ or SEC discretion) be subject to liability, for much the same reason that a compliance defense is a shield to corporate liability in the U.K. and Italy.

In addition, it is important to more clearly delineate what constitutes “sufficient due diligence.” Obviously, what is considered “sufficient” diligence will vary depending on the inherent risks in a given merger or acquisition—e.g., whether the target company does significant business in regions that are known for corruption—and the size and complexity of the deal. But it is important to dispel the notion that adequate due diligence requires a full-blown

internal investigation and the expenditure of extraordinary resources. Instead, guidance could be created, akin to Section 8 of the United States Sentencing Guidelines, that spells out the general due diligence steps that are warranted.

Adding a “Willfulness” Requirement for Corporate Criminal Liability

There is an anomaly in the current FCPA statute: although the language of the FCPA limits an individual’s liability for violations of the anti-bribery provisions to situations in which she has violated the act “willfully,” it does not contain any similar limitation for corporations.⁶⁵ This omission substantially extends the scope of corporate criminal liability—as opposed to individual liability—since it means that a company can face criminal penalties for a violation of the FCPA even if it (and its employees) did not know that its conduct was unlawful or even wrong. *See, e.g., Bryan v. United States*, 524 U.S. 184, 191-92 (1998) (under a “willfulness” standard, the government must “prove that the defendant acted with knowledge that his conduct was unlawful”) (internal citation and quotation omitted). In other words, the absence of a “willful” requirement opens the door for the government to threaten corporations—but not individuals through whom

65 15 U.S.C. §78dd-3(a)(2). The anti-bribery provisions do contain a requirement that conduct in furtherance of an improper payment must be “corrupt” in order to constitute an FCPA violation, and this requirement applies to both corporate entities and to individuals. *See* 15 U.S.C. §§ 78dd-1(a), 78dd-2(a), 78dd-3(a). The statute does not define the word “corruptly,” but courts have consistently interpreted it to mean an act that is done “voluntarily and intentionally, and with a bad purpose.” *See, e.g., United States v. Kay*, 513 F.3d 461, 463 (5th Cir. 2008). However, the requirement that an individual’s conduct be “willful” in addition to “corrupt” adds another layer of intent; namely, it requires a showing that not only was the act in question made with a bad purpose, but with the knowledge that conduct was unlawful. *Id.* at 449-50; *see also* Jenner FCPA Treatise at 1-20.

they act—with what is tantamount to strict liability for improper payments under the anti-bribery provisions of the act. Given that corporations are by their very nature at least one more step removed from conduct that runs afoul of the anti-bribery provisions than the individuals who actually commit improper acts, it is only fair to—at the very least—hold the corporate entity to the same level of *mens rea* as individuals for such acts. Indeed, since the corporation can only be liable if an individual for whom the corporation is liable (typically an employee) has committed the criminal act, it should not be possible to convict a corporation unless the employee is liable. Such individual liability requires willful conduct; so should corporate liability.

Adding a willfulness requirement will also ameliorate another unfairness in the FCPA statute. Permitting a corporation to be criminally punished for improper acts of its subsidiaries that it has no knowledge of runs counter to the intent of the drafters of the FCPA. Nothing in the legislative history suggests that the statute was intended to allow a parent corporation to be charged with criminal violations of the anti-bribery provisions by another company, even a subsidiary, if it had no

knowledge of improper payments. At most, the drafters indicated that if a parent company's ignorance of the actions of a foreign subsidiary was a result of conscious avoidance, or "looking the other way," that such parent "could be in violation of section 102 requiring companies to devise and maintain adequate accounting controls."⁶⁶

Furthermore, because the federal government has construed its FCPA jurisdiction to cover acts that have nothing more than a tangential connection to the United States,⁶⁷ the lack of a "willful" requirement means that corporations can potentially be held criminally liable for anti-bribery violations in situations where they not only do not have knowledge of the improper payments, but also do not even know that American law is applicable to the actions in question. In such a case, the parent corporation could be charged with violations of the anti-bribery provisions, even if it was unaware that the FCPA could reach such payments. For example, in connection with the Siemens case, the DOJ separately charged a Siemens subsidiary in Bangladesh with conspiracy to violate the FCPA, predicated in part on bribes that occurred outside of the United States and that solely involved foreign entities; the DOJ's

⁶⁶ See S. Rep. No. 95-114, at 11 (1977).

⁶⁷ The government's increasingly broad interpretation of the jurisdictional reach of the FCPA is another example of how the DOJ and SEC have aggressively pushed enforcement of the FCPA. In addition to the Siemens case discussed *supra*, the government charged BAE Systems, a British company, with FCPA violations based on the possible use of U.S. bank accounts to make improper payments; against DPC Tianjin, a Chinese subsidiary of an American company, because certain improper payments were reflected in a budget that was at one point emailed to the American parent; and against SSI International Far East ("SSIFE"), a Korean subsidiary of an American company, and individual employees of SSIFE who were foreign citizens, because requests related to certain improper payments were "transmitted" to people located in the United States. See Press Release, Department of Justice, BAE Systems PLC Pleads Guilty and Ordered to Pay \$400 Million Criminal Fine (Mar. 1, 2010), *available at* <http://www.justice.gov/opa/pr/2010/March/10-crm-209.html>; Press Release, Department of Justice, DPC (Tianjin) Ltd. Charged With Violating the Foreign Corrupt Practices Act (May 20, 2005), *available at* http://www.justice.gov/opa/pr/2005/May/05_crm_282.htm; and Press Release, Department of Justice, Former Senior Officer of Schnitzer Steel Industries Inc. Subsidiary Pleads Guilty to Foreign Bribes (Jun. 29, 2007), *available at* http://www.justice.gov/opa/pr/2007/June/07_crm_474.html.

jurisdictional hook for those bribes was that some of the money connected to the transactions had passed at some point through American bank accounts.⁶⁸ But given that any back-office wire that crosses into the United States can be cited by the United States as a basis for application of the FCPA, a defendant can be convicted although completely unaware that her conduct would or could violate American law.⁶⁹

For all these reasons, the “willfulness” requirement should be extended to corporate liability, at the very least to the anti-bribery provisions. This statutory modification would significantly reduce the potential for American companies to be criminally sanctioned for anti-bribery violations, particularly those of which the company had no direct knowledge or for which the company could not have anticipated that American law would apply. The statute should also preclude unknowing *de minimis* contact with the United States as a predicate for jurisdiction: the defendant should either have to know of such contact or the contact, if unknown, should have to be substantial and meaningful to the bribery charged (and thus foreseeable).

Limiting a Parent Company’s Civil Liability for the Acts of a Subsidiary

While the DOJ has not yet taken such action, the SEC routinely charges parent companies with civil violations of the anti-bribery provisions based on actions taken by foreign subsidiaries of which the parent is entirely ignorant. This approach is contrary to the statutory language of the anti-bribery provisions, which—even if they do not require evidence of “willfulness”—do require evidence of knowledge and intent for liability.⁷⁰ It is contrary to the position taken by the drafters of the FCPA, who recognized the “inherent jurisdictional, enforcement and diplomatic difficulties raised by the inclusion of foreign subsidiaries of U.S. companies in the direct prohibitions of the bill” and who made clear that an issuer or domestic concern should only be liable for the actions of a foreign subsidiary if the issuer or domestic concern engaged in bribery by acting “through” the subsidiary.⁷¹ And, it appears to be out of step with the government’s stated position that a parent corporation “may be held liable for the acts of [a] foreign subsidiary[y] [only] where they authorized, directed, or controlled the activity in question.”⁷²

68 See Criminal Information, *United States v. Siemens Bangladesh Limited*, Cr. No. 08-369-RJL (D.D.C Dec. 12, 2008), available at <http://www.justice.gov/criminal/fraud/fcpa/cases/docs/siemensbangla-info.pdf>.

69 This is problematic because it is another way a corporation may be held liable without the government needing to prove that the corporation acted with the requisite criminal intent. See, e.g., Brian Walsh and Tiffany Joslyn, *Without Intent: How Congress is Eroding the Criminal Intent Requirement in Federal Law*, THE HERITAGE FOUNDATION AND THE NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS (May 5, 2010), available at http://s3.amazonaws.com/thf_media/2010/pdf/WithoutIntent_lo-res.pdf (advocating for meaningful *mens rea* requirements as an essential protection against unjust convictions).

70 See *infra* footnote 65.

71 See H.R. Conf. Rep. 95-831, at 14 (1977). See also *supra* fn 66 and accompanying text (the drafters intended that actions of a foreign subsidiary unknown to a parent company could constitute FCPA liability only under the books-and-records and internal controls provisions, and not under the anti-bribery provisions).

72 See DEPARTMENT OF JUSTICE, LAYPERSON’S GUIDE TO FCPA, available at <http://www.justice.gov/criminal/fraud/fcpa/docs/lay-persons-guide.pdf>.

The SEC has provided no explanation for how it can hold a parent company liable for a subsidiary's violations of the anti-bribery provisions—as distinct from the books-and-records and internal controls provisions—where the activity was not “authorized, directed or controlled” by the parent or where the parent did not itself act “through” the subsidiary, but, to the contrary, where the subsidiary's improper acts were undertaken without the parent's knowledge, consent, assistance or approval.

The following are two recent examples:

- United Industrial Corporation (“UIC”)—The SEC charged UIC, an American aerospace and defense systems contractor, with violations of the FCPA's anti-bribery provisions based on allegations that a UIC subsidiary—ACL Technologies, Inc.—made more than \$100,000 in payments to a third-party.⁷³ The SEC further alleged that the agent subsequently passed portions of those payments to Egyptian Air Force officials in order to increase ACL's chances to secure a contract to build a military depot in Cairo. The SEC did not, however, allege that UIC had any direct knowledge of the fact that its subsidiary violated the anti-bribery provisions of the FCPA by making these payments.⁷⁴ Thus the SEC's unspoken theory

was that UIC could be held liable for violating the anti-bribery provisions of the FCPA—separate and apart from UIC's failure to institute proper controls over its employees and subsidiaries and from related violations of the books-and-records provisions (for which strict liability does attach pursuant to the statute)—even if it had no knowledge of the improper payments or therefore their unlawfulness. The complaint was silent as to whether the subsidiary's employees knew the payments were either illegal or wrongful under the local law.

- Diagnostics Product Company (“DPC”)—In 2005, the SEC alleged that a Chinese subsidiary of Diagnostics Products Company (“DPC”), an American company, had violated the anti-bribery provisions of the FCPA by routinely making improper commission payments to doctors at state-controlled hospitals between 1991 and 2002.⁷⁵ The SEC charged that “as a result” of the payments made by the subsidiary, DPC itself could be charged with a violation of the anti-bribery provisions.⁷⁶ There was no allegation that DPC had any knowledge of these payments; in fact, the SEC's Complaint clearly stated that DPC only learned of the payments in November 2002. It

⁷³ See United Industrial Corp., Exchange Act Release No. 60005, 2009 WL 1507586 (May 29, 2009), *available at* <http://www.sec.gov/litigation/admin/2009/34-60005.pdf>; SEC Litig. Rel. No. 21063, 2009 WL 1507590 (May 29, 2009), *available at* <http://www.sec.gov/litigation/litreleases/2009/lr21063.htm>.

⁷⁴ See *id.*

⁷⁵ See Diagnostics Products Corp., Exchange Act Release No. 51724, 2005 WL 1211548 (May 20, 2005), *available at* <http://www.sec.gov/litigation/admin/34-51724.pdf>.

⁷⁶ *Id.*

also acknowledged that DPC put a halt to the payments immediately upon learning of them.⁷⁷

The theory espoused in these cases—that a parent company can be held civilly liable for violations of the anti-bribery provisions as if they themselves committed those violations—has not been put to the test in court. Instead, both companies reached settlements with the SEC. UIC’s settlement required the company to pay disgorgement and prejudgment interest totaling almost \$350,000. DPC’s settlement agreement required DPC to retain an independent monitor for a period of three years, to disgorge approximately \$2 million, and to make an additional payment of prejudgment interest of \$750,000.⁷⁸

As the scope of this potential liability is not definitively established, it is a source of significant concern for American companies with foreign subsidiaries. A parent’s control of the corporate actions of a foreign subsidiary should not expose the company to liability under the anti-bribery provisions where it neither directed, authorized nor even knew about the improper payments in question.

Clarifying Definition of “Foreign Official”

Another ambiguity in the FCPA that requires clarity is the definition of “foreign official” in the anti-bribery provisions. The statute defines—unhelpfully—a “foreign official” as “any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization,⁷⁹ or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.”⁸⁰ The text of the statute does not, however, define “instrumentality”; it is therefore unclear what types of entities are “instrumentalit[ies]” of a foreign government such that their employees will be considered “foreign officials” for purposes of the FCPA.

Consider this: is a payment to a professor to speak at a client conference an FCPA violation if the professor works at a university that receives public grants or is state run? What if the speaker works for a Chinese company that is owned in whole or part by the state? Since the FCPA statute on its face does not indicate that these situations are beyond its reach, and there is no requirement that

⁷⁷ See *id.*

⁷⁸ See *id.*

⁷⁹ A “public international organization” is “(i) an organization that has been designated by Executive Order pursuant to Section 1 of the International Organizations Immunities Act (22 U.S.C. § 288), or (ii) any other international organization that is designated by the President by Executive order for the purposes of this section, effective as of the date of publication of such order in the Federal Register.” 15 U.S.C. §§ 78dd-1(f)(1)(B), 2(h)(2)(B), 3(f)(2).

⁸⁰ 15 U.S.C. §§ 78dd-1(f)(1), 78dd-2(h)(2)(A), 78dd-3(f)(2).

the company know it is violating the FCPA or even acting wrongly, the DOJ or the SEC could prosecute a company for engaging in such actions. Are these far-fetched examples? The real life examples below suggest not.

The DOJ and SEC have provided no specific guidance on what sorts of entities they believe qualify as “instrumentalities” under the FCPA. However, their enforcement of the statute makes it clear that they interpret the term extremely broadly and that this interpretation sweeps in payments to companies that are state-owned or state-controlled. And once an entity is defined as an instrumentality, all employees of the entity—regardless of rank, title or position—are considered “foreign officials.” The government’s expansive interpretation of “instrumentality” has not yet been tested in the courts and is unlikely to be tested in the near future.

The following are a few examples of instances where the government has pursued FCPA violations predicated on an expansive reading of what sorts of entities are “instrumentalities” of a foreign government:

- **Control Components, Inc.**—In 2009, the DOJ and SEC brought actions against Control Components, Inc. for payments totaling approximately \$4.9 million over four years to a variety of entities in China, Malaysia, South

Korea and the United Arab Emirates. Among those entities were companies that the government defined as Chinese “state-owned customers.”⁸¹ In the criminal information filed against Control Components, the DOJ stated summarily that “[t]he officers and employees of these entities, including but not limited to the Vice-Presidents, Engineering Managers, General Managers, Procurement Managers, and Purchasing Officers, were ‘foreign officials’ within the meaning of the FCPA.”⁸²

- **Baker Hughes**—In 2007, the SEC and DOJ brought actions against Baker Hughes and its subsidiaries for, *inter alia*, payments made to a company called Kazakhoil. The government claimed that the payments constituted violations of the FCPA because Kazakhoil was an “instrumentality” of a foreign government as it was “controlled by officials of the Government of Kazakhstan,” making its officers and employees “foreign officials.”⁸³ Baker ultimately settled with the SEC and the DOJ for \$44.1 million; at the time, it was the largest FCPA-related settlement ever.⁸⁴
- **Lucent Technologies**—In 2007, the SEC charged Lucent with violations of the books-and-records and internal control provisions of the FCPA in connection with hundreds of trips that Lucent had financed for employees of

81 Criminal Information, *United States v. Control Components Inc.*, No. SACR09-00162 (C.D. Cal. Jul. 28, 2009), available at http://www.justice.gov/criminal/pr/press_releases/2009/07/07-31-09control-guilty-information.pdf.

82 *Id.*

83 Criminal Information, *United States v. Baker Hughes Inc.*, No. H-07-129 (S.D. Tex. Apr. 11, 2007).

84 See Press Release, Securities and Exchange Commission, SEC Charges Baker Hughes With Foreign Bribery and With Violating 2001 Commission Cease-and-Desist Order (Apr. 26, 2007), available at <http://www.sec.gov/litigation/litreleases/2007/lr20094.htm>.

some of its Chinese customers between 2000 and 2003.⁸⁵ The SEC alleged that financing the trips constituted improper conduct under the FCPA because “many of Lucent’s Chinese customers were state-owned or state-controlled companies that constituted instrumentalities of the government of China and whose employees, consequently, were foreign officials under the FCPA.”⁸⁶ The companies in question were Chinese state-owned telecommunications entities. Lucent settled the action, agreeing to pay \$1.5 million in fines and it also entered a non-prosecution agreement with the DOJ for the same conduct.⁸⁷

- KBR—In an action against American construction company KBR (formerly Kellogg, Brown & Root), the SEC and DOJ claimed that among the improper payments made by KBR were payments made to officers and employees of Nigeria LNG Limited. The government claimed that these officers and

employees were “foreign officials” for purposes of the FCPA, despite the fact that 51% of Nigeria LNG Limited is owned by a consortium of private multinational oil companies, including Shell, Total, and Eni.⁸⁸

Given the potentially vast number of companies that may be categorized as “instrumentalities” of foreign governments due to the government’s expansive interpretation of the phrase, it should be no surprise that in recent years the DOJ and SEC have increasingly brought FCPA actions based on dealings with “foreign officials” at such companies. By one estimate, fully two-thirds of enforcement actions brought against corporations in 2009 involved the enforcement agencies’ interpretation of the “foreign official” element to include employees of state-owned entities.⁸⁹

As these examples illustrate, the government has interpreted “instrumentality” in the FCPA to encompass entities that are directly owned by a

⁸⁵ See *Complaint, S.E.C. v. Lucent Technologies*, C.A. No. 07-2301, (D.D.C. Dec. 21, 2007), available at <http://www.sec.gov/litigation/complaints/2007/comp20414.pdf>.

⁸⁶ *Id.*

⁸⁷ See Press Release, Department of Justice, Lucent Technologies Inc. Agrees to Pay \$1 Million Fine to Resolve FCPA Allegations (Dec. 21, 2007), available at http://www.justice.gov/opa/pr/2007/December/07_crm_1028.html.

⁸⁸ See Koehler, 43 IND. L. REV. at 412.

⁸⁹ *Id.* at 411-13.

foreign government (the Control Components and Lucent Technologies cases), entities that are directly controlled by a foreign government (the Lucent Technologies case), entities that are controlled by members of a foreign government (the Baker Hughes case), and entities that are only partially owned by a foreign government (the KBR case). The latter effectively sweeps in entities that are only tangentially related to a foreign government, with sometimes absurd results. Taken to its logical conclusion, the government's position means that employees of General Motors or AIG could be considered "foreign officials" of the United States government, because the government owns portions of the company. So too could employees of Bloomberg Media, 85% of which is owned by a government official (the Mayor of New York City, Mike Bloomberg).

The government's approach to what companies qualify as "instrumentalities" of foreign governments is detrimental to American business

interests. Without a clear understanding of what companies are considered "instrumentalities," companies have no way of knowing whether the FCPA applies to a particular transaction or business relationship, particularly in countries like China where most if not all companies are either partially or entirely owned or controlled by the state.

For this reason, the FCPA should be modified to include a clear definition of "instrumentality." Such a definition could indicate the percentage ownership by a foreign government that will qualify a corporation as an "instrumentality"; whether ownership by a foreign official necessarily qualifies a company as an instrumentality and, if so, whether the foreign official must be of a particular rank or the ownership must reach a certain percentage threshold; and to what extent "control" by a foreign government or official will qualify a company as an "instrumentality."

IV. Conclusion

In recent years, concerns about the effects of the U.S. regulatory framework on American companies have been widely voiced in Congress, as has the concern about the lack of sufficient *mens rea* requirements in criminal statutes. Legal reforms in other countries, such as the new limitation on corporate liability for bribery in Britain and new corporate statutes in Italy, may help remove

obstacles that currently hamper the competitiveness of American businesses and make Congress realize that such reforms are neither unprecedented nor pro business. They are simply appropriate. The time is ripe to amend the FCPA so as to make the statute more equitable, its criminal strictures clearer, and its effect on American business no more onerous than warranted.



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