

# FCPA: The longer arm of the law

## How to manage heightened compliance risks presented by US enforcement of the Foreign Corrupt Practices Act

The US Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) have dramatically increased enforcement of the Foreign Corrupt Practices Act (FCPA) in recent years. Tellingly, the SEC has filed more FCPA cases since 2006 than it had in all of the prior 28 years since the law was enacted. In the past seven months, the SEC and DOJ set records for financial sanctions in FCPA actions with an US\$800 million settlement with Siemens AG and certain subsidiaries and a settlement with KBR and Halliburton totaling \$579 million. The US authorities also have increasingly focused on conduct in China, having charged multiple companies and individuals for FCPA violations in the country over the last three years.

To the surprise of many non-US companies, the FCPA's jurisdictional reach is very

require certain US-registered companies both to maintain an adequate system of internal accounting controls and to maintain accurate books and records. The SEC and DOJ both have jurisdiction over aspects of the FCPA and often work in parallel on FCPA cases.

### China risks

China's economic structure and culture pose heightened FCPA risks for companies operating there. In particular, many companies in China are state-owned or state-controlled enterprises, or SOEs. US authorities have interpreted the FCPA broadly to apply to any employee of an SOE. Consequently, in China, numerous business relationships potentially implicate the FCPA. The SEC and DOJ have charged companies for improper payments made to Chinese doctors, employ-

and a related website for the same purpose. Under the new initiatives, Chinese citizens who report bribery reportedly can receive up to 10% of the funds recovered by the government.

The SEC and DOJ have recently filed a significant number of FCPA cases that have included improper payments made in China. In the last few years, actions have been brought against a steel company, a manufacturer of airport safety devices, a manufacturer of water pumps for large infrastructure projects, a company building train and voltage transmission lines, software companies, a telecommunications company, and a medical device manufacturer. The SEC and DOJ also have charged individuals involved in improper payments in China. Collectively, the sanctioned conduct pertaining to China has ranged from direct bribes to obtain business, improper payments through intermediaries to achieve the same end, and violative travel and entertainment expenses.

### Managing FCPA risks

There are several measures companies can take to seek to minimize these risks.

It is critical for companies to have specific policies and procedures tailored to address the FCPA risks of business in China. Companies too often rely on generalized codes of conduct that do not provide adequate guidance to employees. Policies addressing FCPA compliance and corporate practices for gifts, charitable donations, travel, and entertainment should be established and should contain clear guidelines and require appropriate corporate approvals.

Train your employees. Establishing an effective compliance program requires periodic and effective training of employees. In-person training is recommended and is considered more effective than alternatives such as web-based training. Effective training enables companies to convey an appropriate "tone at the top" and allows employees the opportunity to obtain practical guidance on company policies.

Because there is no materiality threshold for FCPA violations, it is advisable to con-

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broad and it does not only apply to US companies and citizens. The law also applies to companies with securities registered or listed in the US, even if they are incorporated elsewhere. Non-US companies and individuals can also run afoul of the FCPA if they or their agents cause some act in furtherance of a bribe that has a connection to the US – such as a payment that clears through a US bank.

This aggressive FCPA regulatory climate presents significant compliance challenges for multinational companies doing business in China. We discuss some of the factors presenting unique FCPA risks in China and some practical steps companies can take to manage those risks.

The FCPA, enacted in 1977, prohibits corrupt payments to foreign officials to obtain or retain business. The FCPA also includes accounting provisions, which

ees of industrial companies, and others who did not have typical government roles.

Another factor specific to operating in China is its gift-giving culture. It is traditional in various business contexts, including in connection with certain Chinese holidays and events, to provide gifts. Companies seeking to do business in China may find it challenging to participate in this cultural practice without running afoul of the FCPA. Because there is no materiality threshold for bribe payments under the FCPA, even comparatively small gifts may implicate the anti-bribery provisions if they are provided to an official for an improper purpose.

Finally, the Chinese government has made well-publicized efforts to curb corruption in recent years. In June this year, the Chinese government established a unified 24-hour confidential hotline to enable its citizens to report incidents of corruption

duct specific audit procedures designed to review for FCPA risks. The kinds of issues that may contribute to FCPA problems – such as internal controls weaknesses, procedural failures, and inadequate book-keeping practices may not be captured by typical financial statement audits.

third parties, companies should clearly define the services to be performed and avoid financial arrangements with success fees or high commissions, as these types of compensation structures have been a frequent source of FCPA violations. In addition, companies should obtain

that has previously paid bribes to obtain business may be held liable for those prior violations. Accordingly, pre-acquisition due diligence focused on FCPA issues should be performed. In addition, joint venture structures can present complicated FCPA legal questions, especially when the joint venture partner is an SOE. Companies are well advised to seek legal counsel before entering into such arrangements.

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## FCPA violations commonly result from companies' failure to manage their relationships with third party intermediaries

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### Control your agents

FCPA violations commonly result from companies' failure to manage their relationships with third party intermediaries such as sales agents and distributors. Good procedures require adequate due diligence regarding third parties to establish the business need for utilizing that particular party and require appropriate levels of approval for retaining new agents. In structuring agreements with

appropriate representations and warranties in any contracts or written agreements with third parties that require the third party to acknowledge and comply with the FCPA. Audit rights are recommended as an effective way to enable appropriate insight into third party relationships.

Companies seeking to acquire businesses in China or establish joint ventures also must be cognizant of FCPA concerns. Companies acquiring a business

### Implement a hotline

A compliance hotline provides employees a mechanism to report concerns anonymously outside their chain of command. Companies that are able to identify problems through a hotline can often stop a problem before it becomes more significant. Companies without such a mechanism face an increased risk that employees with a concern will instead report to authorities outside of the company.

*By Walter G Ricciardi (New York), Kevin M Loftus (Washington), Daniel R McCallum, (Washington), Paul Weiss Rifkind Wharton & Garrison*