May 28, 2015

SEC Extends Application of FCPA Accounting Provisions in BHP Billiton Enforcement Action

Executive Summary

On May 20, 2015, the U.S. Securities and Exchange Commission ("SEC") announced a settled enforcement action against Anglo-Australian global resources firm BHP Billiton Ltd. and BHP Billiton Plc (collectively, "BHPB"), alleging violations of the internal accounting controls and books and records provisions of the Foreign Corrupt Practices Act ("FCPA"). The SEC did not allege any violation of the FCPA's anti-bribery provisions, and BHPB did not admit or deny the SEC's findings.[1]

Under the SEC's Cease and Desist Order, BHPB agreed to pay a civil monetary penalty of $25 million, and to provide the SEC with voluntary reporting on its FCPA compliance for one year. This settlement appears to be the largest-ever civil fine imposed by the SEC in an FCPA enforcement action.[2]

In addition to the record-setting civil fine, *BHPB* is notable as a significant expansion of the SEC's use of the FCPA's accounting provisions in cases where the SEC believes an issuer's compliance program creates the *potential* for bribery, even if bribery has not actually occurred or cannot be established. *BHPB* raises the very real prospect that issuers may face charges under the FCPA's accounting provisions—even when there is no evidence of a *quid pro quo*, corrupt intent, or any improperly awarded business or government action—if the SEC is not satisfied that the issuer's internal accounting controls and anti-corruption compliance program are sufficient to adequately manage corruption risks.

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1 *See* BHP Billiton Ltd. and BHP Billiton Plc, Exchange Act Release No. 74998, 2015 WL 2393657, at *1 (May 20, 2015).

2 Of course, the SEC has assessed much larger overall penalties in FCPA enforcement actions through the use of its disgorgement of profits remedy. *See generally, e.g.*, Siemens Aktiengesellschaft, Accounting and Auditing Enforcement Act Release No. 2911, 94 SEC Docket 2869 (Dec. 15, 2008) (assessing $350 million in disgorgement).

Moreover, in *SEC* v. *Tyco International Ltd.*—a case that alleged bribery by a Brazilian subsidiary—the SEC imposed a $50 million civil fine. However, the focus of that enforcement action was Tyco's allegedly improper acquisition accounting and scheme to overstate financial results by one billion dollars. It is unclear what, if any, portion of Tyco's civil penalty was attributed to the FCPA charge. *See generally* Tyco Int'l Ltd., Accounting and Auditing Enforcement Release No. 2414, 87 SEC Docket 2449 (Apr. 17, 2006).

Factual Allegations

According to the SEC's Cease and Desist Order, BHPB invited approximately 176 foreign government officials to attend the 2008 Beijing Summer Olympic Games in connection with BHPB's sponsorship of the Games, and as part of a related global hospitality program intended "to reinforce and develop relationships with key stakeholders." A number of these officials were allegedly "involved in, or in a position to influence, pending contract negotiations, efforts to obtain access rights, regulatory actions, or business dealings affecting BHPB in multiple countries."

Specifically, BHPB offered three-to-four day hospitality packages consisting of free event tickets, luxury hotel rooms, meals, and sightseeing tours—each with a package price of approximately $12,000 to $16,000. In addition, BHPB executives approved the offer of round-trip business class airfare to 51 government officials, as well as airfare for 35 of their spouses or guests. Most of the invited officials were from African and Asian countries with "well-known histories of corruption." Ultimately, 60 of the invited government officials and 24 of their spouses or guests attended the Beijing Olympic Games at BHPB's expense.

In an effort to address the potential corruption risk associated with inviting government officials to the Games, BHPB devised a hospitality application form that business managers were required to submit for any individual they proposed to invite. The form included multiple questions designed to elicit whether the invitation could create even the appearance of an improper nexus with any BHPB business being negotiated, considered, or conducted. BHPB required the forms to be completed by an employee with knowledge of the invitee's relationship to the company, and approved in writing by either the President of the relevant BHPB business division or the relevant country head. The form was also accompanied by a cover sheet that described the anti-bribery provisions set forth in BHPB's Guide to Business Conduct, and directed employees to re-read the sections of the Guide concerning travel, entertainment, and gifts.

A. The SEC's Internal Accounting Controls Charge

The SEC alleged that BHPB violated Section 13(b)(2)(B) of the Securities Exchange Act, 15 U.S.C. § 78m(b)(2)(B), because BHPB's internal accounting controls over its Olympic hospitality program allegedly did not "provide reasonable assurances that access to assets and transactions were . . . executed in accordance with management's authorization." The SEC alleged that the following facts supported finding such a violation:

- BHPB did not require independent legal or compliance review of the hospitality applications overseen by business managers, and did not clearly communicate to employees that the company's Global Ethics Panel would not review each individual invitation to a government official.

- Some of BHPB's hospitality application forms were not accurate or complete.

- Although BHPB had an annual Guide to Business Conduct review and certification process, as well as generalized training, it did not provide its personnel with specialized training on how to fill out the hospitality forms or how to evaluate whether an invitation to a government official complied with the Guide.

- While the application form asked whether any business was "expected to develop" with the invitee, BHPB did not institute a process for updating the applications or reassessing invitations that had been extended in the event that circumstances changed.

- Even though the list of invitees was circulated among senior BHPB business managers, BHPB lacked a process to determine whether the invited government official had relationships with business divisions other than the particular one that submitted the application.

As a result, BHPB invited a number of government officials to the Games who were in a position to influence pending business matters. In particular, the SEC Order cited hospitality invitations made in 2007 to officials from four countries: the Republic of Barundi, the Republic of the Philippines, the Democratic Republic of the Congo, and the Republic of Guinea. The Order emphasized that BHPB had informed its employees that one of the core objectives of the Olympic sponsorship was to "maximize the commercial investment made in the Games through assisting [BHPB] to strengthen relationships with key local and global stakeholders, e.g.: Government Ministers, Suppliers and Customers," and that the hospitality program was "a primary vehicle to ensure this goal is achieved."

B. The SEC's Books and Records Charge

The SEC alleged that BHPB violated Section 13(b)(2)(A) of the Exchange Act, 15 U.S.C. § 78m(b)(2)(A), because "certain Olympic hospitality applications[] did not, in reasonable detail, accurately and fairly reflect pending negotiations or business dealings between BHPB and government officials invited to the Olympics." For example, many applications identified an employee of a state-owned enterprise as a "Customer," rather than a "Representative of Government." Other applications incorrectly stated that BHPB did not have pending negotiations, efforts to obtain access rights, regulatory actions, or other business dealings over which an invited government official had influence. And still other applications did not describe the specific facts and circumstances concerning invited government officials who were in a position of influence, as called for in one of the questions on the hospitality application form.

C. BHPB's Cooperation and Remedial Efforts

The SEC credited BHPB with providing "significant cooperation" in the government's investigation. BHPB retained outside counsel to conduct an extensive internal investigation, produced voluminous documents from around the world, voluntarily provided translations of key documents, and offered

regular reports to the Staff on outside counsel's findings following witness interviews. The SEC's Order also identified "significant remedial actions" taken by BHPB, such as creating an independent compliance group that reports directly to BHPB's General Counsel and Audit Committee, embedding independent anti-corruption managers into its business lines, and enhancing internal policies and procedures, financial controls, and training with respect to anti-corruption issues. Exactly how BHPB's "significant cooperation" and "significant remedial actions" affected the resolution of this case, including the $25 million record civil fine, is not explained in the SEC's Order or Press Release.

Key Takeaways and Analysis

The SEC's enforcement action against BHPB is significant for at least four reasons.

First, this settlement represents a rare example of the SEC bringing internal accounting controls and books and records charges in a case where it neither alleges actual bribery of a foreign official, nor suggests that such bribery took place but could not be charged for jurisdictional or other reasons.

Historically, the SEC has tended to charge issuers with violating the accounting provisions of the FCPA as a supplement to—rather than a substitute for—a bribery charge. In the exceptional cases where the accounting provisions alone have been charged, there is ordinarily some indication that improper payments were offered in exchange for a business benefit—in other words, that bribery had in fact occurred even if not charged.[3] SEC precedent for bringing charges under the accounting provisions without an indication of actual underlying bribery seems to have its roots in a 2012 settled enforcement action against Oracle Corporation ("Oracle").[4] In *Oracle*, the SEC alleged that employees of an Oracle subsidiary in India secretly "parked" proceeds from sales to the Indian government for potential future use. The SEC did not claim that the Oracle subsidiary made corrupt payments to government officials, but did allege that the parked proceeds created "the potential for bribery or embezzlement," and that Oracle lacked proper internal controls in light of that potential.

Here, it appears that the SEC was unable to show that BHPB's business hospitality entertainment program was accompanied by any corrupt motive or involved a *quid pro quo*. This outcome is consistent with the proposition—well established in the domestic bribery context—that giving things of value to government officials for the purpose of building relationships or buying generalized goodwill is

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3 *See generally, e.g.,* Compl., *SEC* v. *Schering-Plough Corp.,* 1:04-cv-00945-PLF (D.D.C. June 9, 2004).

4 *See* Compl., *SEC* v. *Oracle Corp*., No. 12-cv-4310 (N.D. Cal. Aug. 16, 2012); Press Release, SEC Charges Oracle Corporation With FCPA Violations Related to Secret Side Funds in India (Aug. 16, 2012), *available at* http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171483848.

permissible.[5] The *BHPB* enforcement action thus suggests that the *Oracle* case may not be an outlier in charging FCPA violations in the absence of an allegation of actual bribery, as some expert commentators have suggested, but perhaps the beginning of a new frontier in FCPA enforcement.

Second, even if it is tenable as a general legal matter to charge a standalone internal accounting controls violation based solely on the SEC's subjective assessment of the adequacy of an issuer's anti-corruption compliance program, the *BHPB* settlement represents an expansive application of the accounting provisions.[6] Indeed, the SEC's Order acknowledges that BHPB devised and maintained multiple internal controls to prevent corruption. For example, BHPB adopted a written Guide to Business Conduct; the President of each business line was given responsibility for ensuring compliance with that Guide; all business line Presidents certified annually that they had read and understood the Guide, confirmed that their direct reports did the same, and discussed compliance with their direct reports; BHPB established a Global Ethics Panel whose remit involved advising business leaders on compliance with the Guide and other business ethics issues; and BHPB's compliance was overseen by a centralized Legal Department. In addition, BHPB instituted internal controls intended to address the particular corruption risks arising from the Olympics Hospitality Program, including creating detailed internal application forms aimed at addressing corruption risk, a senior business manager approval process, and a role for the Global Ethics Panel in assessing the invitation process that included reviewing a sample of the hospitality application forms.

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5 *See, e.g., United States* v. *Sun-Diamond Growers of California*, 526 U.S. 398, 404–06 (1999) (holding that offering gifts to government officials for the mere purpose of relationship building may be permissible); *United States* v. *Siegelman*, 640 F.3d 1159, 1171 (11th Cir. 2011) (holding that generalized giving for relationship purposes, even with an expectation of future favorable action, is not punishable under anti-bribery laws); *United States* v. *Ganim*, 510 F.3d 134, 149 (2d Cir. 2007) (holding that "buy[ing] favor or generalized goodwill from a public official" who is "in a position to act favorably on the giver's interests" is "legal lobbying," not bribery); *United States* v. *Kemp*, 500 F.3d 257, 281 (3d Cir. 2007) ("[B]ribery may not be founded on a mere intent to curry favor. . . . [T]here is a critical difference between bribery and generalized gifts provided in an attempt to build goodwill."); *United States* v. *Jennings,* 160 F.3d 1006, 1013 (4th Cir. 1998) ("[A] good will gift to an official to foster a favorable business climate . . . does not constitute a bribe.").

These cases are instructive because, as the courts, the SEC, and the Justice Department have all recognized, U.S. domestic bribery law—principally criminalized under 18 U.S.C. §§ 201(b) and 666—provides a close interpretive analogue to the FCPA. *See, e.g., Stichting ter Behartiging van de Belangen van Oudaandeelhouders in het Kapitaal van Saybolt Int'l B.V.* v. *Schreiber*, 327 F.3d 173, 182 (2d Cir. 2003) (noting that Congress intended to incorporate within the FCPA certain elements of domestic bribery law); Criminal Division of the U.S. Dep't of Justice & Enforcement Division of the U.S. Sec. & Exch. Comm'n, *A Resource Guide to the U.S. Foreign Corruption Practices Act*, at 16 (2012) [hereinafter "FCPA Resource Guide"].

6 It is controversial whether the requirement that an issuer maintain adequate internal accounting controls includes a requirement to maintain an anti-corruption compliance program. That subject matter is beyond the scope of this article.

To be sure, the SEC's Order notes the absence of a centralized compliance group, and BHPB confirmed that it had "no independent compliance function" in its release announcing the end of the U.S. government investigations.[7] However, more than any objective deficiency with BHPB's compliance structure, the SEC's internal accounting controls charge appears to rest on highly specific criticisms of the internal forms used to evaluate individual hospitality applications and the related compliance process. While giving things of value for purposes of relationship building is permissible and does not constitute bribery, it appears that the SEC may intend to use the FCPA's internal accounting controls provisions to penalize any perceived shortcomings in companies' efforts to scrutinize such activities.

Third, the SEC's books and records charge reflects an aggressive, but not necessarily new, interpretation of Section 13(b)(2)(A), which requires issuers to make and keep books and records that "accurately and fairly reflect the transactions and dispositions of the assets of the issuer." The SEC's position raises important questions of statutory interpretation and public policy. There is nothing in the language of the books and records provision to suggest that it encompasses purely internal application forms completed for the purpose of approving gifts and entertainment expenditures.[8] If the SEC can charge a books and records violation for any alleged inaccuracy in any internal paperwork, it will impose an enormous compliance burden that even the most sophisticated and well-resourced companies may struggle to satisfy.

Finally, the imposition of a $25 million civil fine and year of compliance reporting to the SEC is remarkable for a case in which there was no actual bribery, much less a bribery charge, no allegation of any *quid pro quo* or improper business benefit, and complete cooperation and full remediation. It is also noteworthy that the SEC has consistently reaffirmed its authority to seek disgorgement in enforcement actions brought under the internal controls or books and records provisions, but did not seek any disgorgement here. And despite the record-setting fine against BHPB, the SEC's Order sheds no light on how such a fine was calculated. Moreover, although the SEC's press release acknowledged the assistance of the Department of Justice's Fraud Section, the Federal Bureau of Investigation, and the Australian Federal Police, no criminal charges to date have been brought.

Implications for Corporate Compliance Programs

The U.S. government's FCPA Resource Guide makes clear that "[e]ffective compliance programs are tailored to the company's specific business and to the risks associated with that business. They are

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7 *See* Press Release, BHP Billiton, BHP Billiton Announces End of US Investigations (May 20, 2015), *available at* http://www.bhpbilliton.com/home/investors/news/Pages/Articles/BHP-Billiton-Announces-End-of-US-Investigations.aspx.

8 *See* ABA Comm. On Corporate Law & Accounting, *A Guide to the New Section 13(b)(2) Accounting Requirements of the Securities Exchange Act of 1934*, 34 Bus. Law. 307, 313 (1978) ("[T]he books, records and accounts with which subsection (A) is concerned are those that are relevant to the preparation of financial statements.").

dynamic and evolve as the business and the markets change." Moreover, the government disclaims any "formulaic requirements regarding compliance programs," and promises to "employ a common-sense and pragmatic approach to evaluating compliance programs, making inquiries related to three basic questions:

- Is the company's compliance program well-designed?
- Is it being applied in good faith?
- Does it work?"[9]

The SEC's approach to settling this case nonetheless suggests that unanticipated gaps or shortcomings in the implementation of a compliance program may become fodder for an SEC investigation or enforcement action, even where there was no actual (or even alleged) bribery. Companies subject to the SEC's jurisdiction will therefore want to read closely the SEC's Order in this case and reflect on whether their own internal controls and anti-corruption compliance programs would pass muster under the kind of scrutiny the SEC appears to have applied to BHPB. Specifically, companies that engage in organized business entertainment, gift-giving, marketing, sponsorships, or even community development projects would be well-advised to take a second look at their controls, processes, communication, and training with respect to each of those activities. In addition to conducting a one-time reassessment and addressing any identified deficiencies, ongoing monitoring and auditing of such activities may well prove to be the best approach to satisfying enforcement expectations.

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It is unclear whether the BHPB case represents a new frontier for SEC enforcement of the FCPA's accounting provisions, or a negotiated resolution that is a creature of its own facts. In either case, this settlement provides further evidence of the SEC's determination to make full use of its substantial enforcement powers under the FCPA, and underscores the importance of continuous attention to corruption risks and the adequacy of the approach taken to mitigate those risks.

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[9] *FCPA Resource Guide*, at 6.

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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