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COVER STORY | BY PAULINE RENAUD

Crackdown on corporate corruption

Introduced in 1977, the US Foreign Corrupt Practices Act (FCPA) has gained in notoriety in recent years following several financial scandals including the bribery of foreign officials by some of the world's largest companies. According to some analysts, the US Department of Justice (DOJ) has brought more prosecutions under the FCPA since 2006 than in the last 20 years. In addition, individuals have faced more severe penalties, such as jail sentences, than in the past. With the financial crisis and increased cooperation between jurisdictions, more prosecutions are expected this year. For companies, this means more challenges in order to achieve compliance with those rules while remaining competitive. However, there are concerns that the current financial crisis has made anti-corruption measures less of a priority than is required.

Enforcement intensified

According to recent reports, the DOJ had nine open investigations into FCPA matters in 2003. By the end of 2008, there were 80, showing the recent accelerated pace in enforcement actions. "FCPA enforcement activity over the last 12-18 months has been prolific, aggressive, jurisdictionally expansive and fearless," notes Sharie A. Brown, a partner at DLA Piper LLP. "No major industry has escaped scrutiny. Targeted industries have included oil and gas, pharmaceuticals, medical equipment, telecommunications, industrial engineering, and technology." High-profile cases include the oilfield services company Baker Hughes, which faced combined civil and criminal penalties of $44m for foreign bribery. But this record fine was eclipsed in 2008 when Siemens and its subsidiaries agreed to pay a total criminal fine of $450m to the DOJ and to disgorge $350m in illicit profits to the SEC. In total, sanctions enforced against Siemens worldwide added up to $1.6bn.

The Siemens case confirmed that foreign companies operating in the US, which once believed that they might be insulated from FCPA enforcement actions, were now open to prosecution, explains Fred Miller, a global co-leader of PricewaterhouseCoopers' FCPA services practice. For him, there has been a "paradigm shift". "The Siemens settlement alone, moving the largest settlement from the $44m mark to the high hundreds of millions, really changes the game for companies regarding these types of risks and exposures. The enforcement activity, though handicapped by a limited amount of dedicated resources at the DOJ and SEC, has truly made a huge impact on the psyche of companies both in the US and abroad." Yet, this awareness of intensified enforcement of the FCPA had already been triggered in 2002 by the Sarbanes-Oxley Act. Following several massive frauds, including the Enron scandal, companies were forced to focus on the adequacy of internal controls and compliance procedures. Furthermore, they had to implement more efficient and stringent fraud controls as the concept of criminal liabilities for top executives started appearing. Training and education of the work force to identify and report potential liabilities also started to become more and more frequent.

Aside from the Siemens and the Baker Hughes cases, other record penalties have illustrated the boom in FCPA violations unearthed recently, especially in some specific sectors traditionally more prone to bribery. "The Willbros Group case was the latest example of the DOJ's continued focus on the oil and gas industry," observes Scott Moritz, an executive director at Daylight Forensic & Advisory. "Indeed, oil and gas is the perfect storm of FCPA risk. Oil exploration almost always involves high corruption risk jurisdictions such as Nigeria, Ecuador, Venezuela, the Middle East, Russia and the CIS; state-owned oil companies and of course billions of dollars of oil revenues." For example, the US-based oilfield services corporation Halliburton has been suspected of bribing Nigerian officials to gain lucrative contracts since 2003. A former senior executive of Halliburton was recently convicted after pleading guilty to the charges. The executive also admitted taking millions of dollars in kickbacks on deals in countries ranging from Malaysia to Yemen.

Violations may occur more frequently in certain countries and sectors, but in reality it can happen almost anywhere. According to its SEC filing, in April 2004, technology company Lucent fired its president, a marketing executive and a finance manager at its China operations for FCPA violations. These violations were uncovered through internal investigations triggered by the DOJ and SEC probe into possible FCPA violations in Saudi Arabia.

While there is evidence to suggest that all this heightened activity can be traced to the inception of the Sarbanes-Oxley Act, some experts argue that it actually began at least a year before Sarbanes-Oxley. Indeed, the co-operation between the US and other countries on anti-terrorism efforts following 9/11 also resulted in increased cooperation on other cross-border issues, including financial fraud. "Since September 2001, there has been an increased awareness of the link between corruption and national security," observes Paul Doxey, a senior managing director at FTI Forensic Accounting. "The Oil-for-Food scandal highlighted the pervasiveness of bribery across a wide range of companies, while earlier scandals such as General Abacha's plundering of Nigeria's assets illustrated the role of western financial institutions in handling stolen funds." Since that time, a number of trends have emerged in connection with the FCPA. Notably, the surge in cross-border M&A deals has created a higher risk of companies being accused of bribery. Several foreign companies that were not subject to the FCPA, for being based outside the US, were suddenly caught in the net by operating on the American territory. In turn, US companies that were complying with the FCPA suddenly faced charges because they had, following a cross-border transaction, started operating in a high-risk jurisdiction. Ultimately, the emergence of new risks at that time encouraged the DOJ to intensify its enforcement of FCPA both in the US and elsewhere.

"Whilst FCPA has obviously been around a long time now, its execution was stifled by a lack of resources and an absence of a coordinated global approach. The US had difficulty in following up issues due to the fact that offences occurred in other jurisdictions may not have been as transparent in the past as they are now," points out John Tudorovic, the executive director of forensic services at Ferrier Hodgson Limited. "The now more global approach, and the fact that more countries have FCPA type legislation, paves the way for more coordinated and strategic investigations." This is illustrated by the increasing acceptance of the OECD Anti-Bribery Convention, which came into effect in February 1999. So far, 37 countries across all five continents have ratified the convention. It is the first widely published and accepted document recognising that bribery of a foreign public official is a global problem, rather than an American one.

The Siemens case was a striking example of the increased collaboration between different jurisdictions, asserts Larry Byrne, a co-managing partner at Linklaters. "One of the most important features in that case, is the extraordinary amount of cooperation between the DOJ, the SEC and the prosecutors in Germany. The monitor that was imposed upon Siemens was not an American official but the former German Minister of Finance, showing how far the DOJ and OECD countries have come in undertaking joint investigations with joint remediation," he says.

In the US, actions taken under the FCPA have, in recent years, benefited from tremendous support from DOJ and SEC officials as well as the US administration, highlights Gary DiBianco, a partner at Skadden Arps, Slate, Meagher & Flom LLP. "Anti-corruption has been a stated political priority of the current US administration, and it is expected that this priority will continue into the next administration." Consequently, the DOJ and SEC are now benefiting from non-traditional tools of investigation, such as FBI resources. But like the chicken and egg scenario, it remains a challenge to determine whether there are more scandals because there are more investigations, or if more scandals have encouraged more prosecutors to intensify their activity. Either way, major financial scandals have rarely been out of the spotlight in the last few years.

Potential trends for 2009

These cases have helped identify several trends in FCPA enforcement that are likely to continue in 2009. First are the escalating corporate financial penalties. "In 2005, the largest FCPA penalty imposed was a $13m criminal fine, and civil disgorgement and prejudgement interest of $15.4m, stemming from alleged bribes and related false entries of approximately $2m. At the end of 2008, combined US enforcement-agency imposed civil and criminal penalties of $800m against Siemens, resulting in $1.6bn in worldwide enforcement sanctions against the company," analyses Ms Brown. This suggests that prosecutors are becoming more proficient and confident in enforcing the Act.

The number of prosecutions is likely to continue to increase in the coming months, as the joint efforts between US and international law enforcement agencies become more effective.

Another major feature is the increasing focus on individual prosecutions. According to DLA Piper, 80 percent of individuals sentenced for FCPA violations received jail terms in the last two years. "In the past, the DOJ used to resolve FCPA violations with some sort of corporate resolution, like in Siemens when a fine was imposed and a disgorgement ordered," recalls Mr Byrne. "But Mark Mendelsohn, deputy chief of the fraud section in the DOJ's criminal division, recently said that in order to really flex the muscle of full deterrent power of the FCPA, the DOJ will now be seeking criminal indictments against individuals. In short, we are going to be seeing more people in jail." For example, a former World Bank employee received a 15-month prison sentence in 2008 after being accused of conspiring to award World Bank contracts to a consultant in exchange for kickbacks. He was also suspected of helping a contractor bribe a foreign official in violation of the FCPA.

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Jail sentences may not follow every prosecution, but companies should be aware of the indirect penalties that can follow a prosecution for bribery. Collateral damages, as described by Mr Miller, will continue to affect companies in 2009, with roughly 100 open investigations said to be in the pipeline. "I find that the even bigger 'penalties' incurred by the companies caught up in FCPA bribery allegations to be the so-called 'collateral penalties'. They include reputational damages, 'transactional costs' of the investigation, costs of dealing with the likely imposition of the compliance monitor or consultant and cost of top management diversion or attention while the investigation is pending."

In addition, the number of prosecutions is likely to continue to increase in the coming months, as the joint efforts between US and international law enforcement agencies become more effective. In its recent review of FCPA enforcement, the law firm Gibson Dunn & Crutcher notes that prosecutors took at least 16 international trips and the DOJ is involved in at least 23 multi-jurisdictional investigations. Furthermore, foreign prosecutors are showing increased interest in pursuing these types of cases and in implementing similar regulations to the FCPA. "Foreign governments are initiating bribery investigations as never before," explains Mr Moritz. "It makes US enforcement actions far more effective when they receive substantive cooperation from foreign law enforcement agencies." This suggests that there will be fewer safe havens for fraudsters in 2009.

Conversely, greater cooperation between jurisdictions also means that there are greater risks and higher complexities involved in operating overseas. With potentially increasing scrutiny in more countries over the course of 2009, some companies might have difficulties in establishing which activity is permitted in one country but illegal in another. For Mr Doxey, the risks particularly affect "acquisitions, joint ventures, supply chain agreements and the use of foreign intermediaries. Another problem for companies involved in foreign M&A activity is the possibility of legacy non-compliance issues within the acquired entity." In addition, it is thought that the combination of increased scrutiny and the financial crisis will make FCPA violations surge throughout 2009.

Closing transactions is getting more difficult in this tough environment, and most companies are focused on cost-cutting measures, which can include slashing internal control resources. "Also, sales forces may resort to sharper business practices to secure contracts. Heightened competition for limited sales may therefore mean an increase in corruption risks," confirms Mr DiBianco. Aware of companies' tendencies to focus on economic imperatives rather than FCPA compliance, Lori A. Richards, director of the SEC, Office of Compliance Inspections and Examinations (OCIE),w sent an open letter to the CEOs of SEC-registered companies, strongly urging them to avoid making cuts in the compliance function area during these difficult times.

However, some analysts believe that the financial crisis will inspire companies and their executives to be more careful with potential bribery liabilities and to reinforce their compliance measures. In this scenario, a jump in FCPA violations and prosecutions in 2009 will be the consequence of past or ongoing non-compliance, as well as reinforced investigations by prosecutors, rather than current mischievous behaviour. "If anything, corruption, fraud and bribery are recession proof. But a potential substantial increase in the number of cases will more likely result from a push by the SEC and DOJ rather a direct result of the financial crisis," insists Mr Tudorovic. In order to counter potential liabilities, at a time when prosecutors are getting more suspicious and have greater tools of investigation, companies are advised to conduct a complete overhaul of their compliance programs.

Getting to know your company

Companies should start the process by evaluating whether the programs and policies implemented within their businesses correspond to regulatory requirements, updating them if necessary. Furthermore, this precaution should be carried out beyond US borders, explains Mr Moritz. "The company should undertake a company-wide risk assessment of the countries where they operate, their business lines, products, vendors and third-party payment recipients and employees to assess the degree of potential FCPA liability that each relationship represents to the organisation." Having a clear understanding of a country's legal landscape and where potential liabilities could hide is essential. In case of problems, an internal investigation should be conducted and the potential breach reported to the regulation authorities concerned with no delay. They can also conduct state-of-the-art controls over monetary transfers, cash accounts and other disbursements.

For non-US companies, the process is very similar. "They should also be mindful that US enforcers will prosecute them even after they delist if misconduct occurred while they were listed on US stock exchanges," specifies Ms Brown. "For example, in December 2008, Italian company Fiat agreed to pay civil and criminal fines and penalties resulting from wire fraud charges and books and records violations of the FCPA. The fraud related to approximately $4.3m in kickback payments under the UN's Oil-for-Food program. Fiat had delisted its American Depositary Receipts from the New York Stock Exchange as of November 2007. Nevertheless, because the improper activity occurred from 2000 through 2003, US prosecutors retained jurisdictions over those acts."

Next, managing risks with agents and employees has indeed been cited as an essential factor in reducing liabilities that may lead to prosecution for bribery of a foreign official. This can be done through training and education of the workforce on relevant anti-corruption laws so they can identify, avoid, or report potential risks. Enhanced codes of conduct are said to be vital. "Like any battle against fraud, one of the best weapons is the people within a company. Setting a cultural tone within the organisation, from the top down, is step one. Policies such as whistleblowing and ethics should not just exist in written documents but should become part of the company's values. Training programs and education should be ongoing in these areas in support of these values," says Mr Tudorovic.

Furthermore, data gathered by Daylight Forensic & Advisory shows that 65 percent of all FCPA cases since 1977 have involved improper payments by third parties. Therefore, analysts recommend a risk score should be assigned to each third party payment recipient. "Thorough and meaningful due diligence on third-party business partners, including consultants, intermediaries, and agents, is essential," confirms Mr DiBianco. Other experts believe there

should be a regular review of main clients as well as a vetting system for new ones to determine whether or not they are trustworthy.

But this can be troublesome in some jurisdictions, where violating the law is common practice. Indeed, FCPA-compliant companies can have difficulties concluding transactions at all, says Mr Doxey. "Compliance by large multinationals is improving. Therefore, the problem of a non-level playing field is more an issue between multinationals from the developed nations and exporters from countries with a weaker approach to fighting corruption. For example, Transparency International has identified emerging economic powers such as China, India and Russia undermining global efforts at tackling corruption." To operate in those jurisdictions and remain competitive while avoiding prosecution, an obvious but efficient solution is to offer the highest quality service or product in an industry.

Ultimately, a company which decides to walk away from a business because it violates the law, can promote its integrity and sense of ethics as one of its core values, which can be a real business asset in the long term. Conversely, reputational damages in case of a fraud have long-lasting consequences. In addition, most fines and penalties under FCPA are now deterrent enough to take the risk of bribing officials. "It is absolutely a cost/benefit analysis. The competitive outlook has to include the risk of having quite a lot of damage done to your bottom line and your future ability to compete," points out Mr Byrne.

All of these measures against potential prosecution might seem very convincing on paper but they need to be put into practice, even if this ultimately reveals some inefficiencies. Mr Miller's main advice is to keep up the monitoring and testing. "There is no substitute for going to high risk locations, interviewing the people who deal with foreign officials directly in these locations and looking at the local books and records. Such testing really lets you know whether you have a well intentioned but toothless paper tiger or a program with some real 'on the ground' traction and 'teeth'," he explains. More importantly though, the example of credibility should come from senior management, who should set up a permanent protocol of FCPA audits. This is vital, but it can be the case that compliant companies can run the risk of becoming less competitive. As such, they need to find a balance between the two goals.

However, some companies might find the costs of fully complying with regulation enforced in a jurisdiction to be too high in the current climate, particularly when compared to the returns that can be made. Many may decide to leave markets where fair competition and compliance is not easily achievable. On the other hand, the FCPA gives American prosecutors strong powers to pursue companies in the US and abroad, and the pace of investigation and prosecution is only likely to accelerate in 2009. As such, many companies are considering regulators' actions from a positive point of view. It is hoped that bribery and corruption will become less frequent with more stringent regulation, ultimately making the global market a more level playing field. ■

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She comes to DLA Piper from Foley & Lardner, where she served as chair of that firm's White Collar Defense & Corporate Compliance practice. While at Foley, Ms. Brown was also a member of the Transactional & Securities and International practices. She was chair of the Litigation department's Diversity Committee and served on the Litigation Program Committee and the Women's Network Steering Committee.

Before joining Foley, Ms. Brown was senior counsel at Mobil Oil Corporation, where she also served as the company's ethics and compliance officer. She developed a worldwide ethics and compliance program, a code of conduct and employee training videos, as well as pamphlets on the FCPA, and Iran, Iraq, Cuba and Libya sanctions compliance. As Mobil's policy advisor in corporate planning and economics, she handled trade, tax and sanctions issues. Previously, Ms. Brown directed Mobil's state government relations in key states.

Prior to Mobil, Ms. Brown was an assistant United States attorney in the Eastern District of Pennsylvania, where she handled tax, bank fraud and securities fraud cases. She was commended by FBI Director William Sessions, for her co-prosecution of a securities fraud RICO, among other enforcement agency commendations. Ms. Brown clerked for the Honorable Richard M. Bilby, United States District Court, District of Arizona.

Ms. Brown's memberships include the National Foreign Trade Council (NFTC), USA*Engage, OFAC Working Group, Iran Working Group, Georgetown Corporate Counsel Institute advisory board, ABA Int'l Anticorruption Committee; ABA Int'l Antimoney Laundering Committee; and the International Bar Association. She speaks at ABA, ACI, Compliance Week, CCI, and D.C. Bar conferences,and has served on ABA and D.C. Bar programming committees.