SIMPSON THACHER MEMORANDUM

Highlights of the Government's New FCPA Resource Guide

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Last week, the Department of Justice and the Securities and Exchange Commission jointly released a highly anticipated guide about the Foreign Corrupt Practices Act ("FCPA"). The publication, officially titled *A Resource Guide to the U.S. Foreign Corrupt Practices Act* and available here, is an informative resource to the extent it describes the analytical framework used by the government in reviewing issues arising under the FCPA and the government's interpretation of some of the statute's key provisions.

In particular, the guide's discussion about various fact patterns provides insight into what the government views as both problematic and permissible conduct. Hypothetical situations involving gifts and travel and entertainment expenses, for example, reflect the government's view of reasonable, bona fide payments that will not give rise to FCPA liability. And for the first time, the government discloses examples of situations in which it has declined to prosecute. Among the other topics that receive extended treatment are the FCPA's accounting provisions, the potential remedies for FCPA violations, and the different ways that FCPA cases are resolved.

At the same time, the guide is certain to disappoint many practitioners to the extent it does not provide definitive guidance on some of the most difficult questions that arise under the FCPA, including exactly who qualifies as a foreign official under the statute, how much diligence should be done in connection with hiring agents and conducting M&A transactions, when a parent company may be held liable for the acts of its subsidiaries, and how much credit is actually given by the government for self-reporting and other forms of cooperation. Instead of addressing these questions with clear-cut answers, the guide states that these issues must be left to a case-by-case analysis based on the specific facts and circumstances at issue.

Nonetheless, by combining a discussion of legal principles, policy considerations, and hypothetical fact patterns into one official annotated compendium, the guide is an important development in an area that continues to lack extensive judicial precedent or other authoritative practice resources.

"INSTRUMENTALITIES" OF A FOREIGN GOVERNMENT UNDER THE FCPA

One question that has long vexed company counsel and FCPA practitioners alike—and that is being litigated in a number of courts—is who falls within the FCPA's definition of "foreign official." The guide, however, does not provide a definitive answer on this issue. Instead, it reiterates the government's longstanding position that "instrumentalities" of a foreign government can include state-owned or state-controlled entities. The guide then lists the

following non-exclusive factors from a compilation of district court jury instructions to help determine whether a particular entity constitutes an "instrumentality":

- the foreign state's extent of ownership of the entity;
- the foreign state's degree of control over the entity (including whether key officers and directors of the entity are, or are appointed by, government officials);
- the foreign state's characterization of the entity and its employees;
- the circumstances surrounding the entity's creation;
- the purpose of the entity's activities;
- the entity's obligations and privileges under the foreign state's law;
- the exclusive or controlling power vested in the entity to administer its designated functions;
- the level of financial support by the foreign state (including subsidies, special tax treatment, government-mandated fees, and loans);
- the entity's provision of services to the jurisdiction's residents;
- whether the governmental end or purpose sought to be achieved is expressed in the policies of the foreign government; and
- the general perception that the entity is performing official or governmental functions.

The guide states that a company is unlikely to constitute an instrumentality where the government does not own or control a majority of its shares. But the guide is clear that minority ownership is not dispositive where the circumstances reflect that the government exercises substantial control over the company in question. As an example, the guide approvingly recounts a past FCPA settlement in which a telecommunications company was considered an instrumentality of a government for FCPA purposes—notwithstanding the fact that a government finance ministry held only a minority stake in the company—because the finance ministry held the status of "special shareholder," could veto all major expenditures, controlled important operational decisions, and because senior company officers were political appointees.

As a result, without judicial decisions or clarifying legislation, questions about the scope of the FCPA's instrumentality provision will continue to turn on highly fact-specific evaluations of an entity's ownership, control, status, and function, and will likely continue to be subject to the government's broad interpretation of the statute.

MERGER AND ACQUISITION FCPA DILIGENCE

The guide stresses the importance of pre-acquisition diligence by prospective purchasers and describes a series of hypothetical situations to illustrate when an acquirer might face post-acquisition liability for FCPA violations by the acquired company.

The guide states that companies that identify and terminate impermissible payments and then quickly integrate their internal controls into an acquired company's business lines will likely

avoid liability for pre-acquisition FCPA violations. By the same token, companies that fail to terminate misconduct can be held liable for violations that continue after the acquisition. In one of the guide's more interesting passages, the government reveals that while it is more likely to pursue charges against acquired companies in instances of longstanding, egregious corruption, in limited circumstances the government has declined to pursue charges against acquired companies in recognition of the fact that "acquiring companies may bear much of the reputational damage and costs associated with such charges."

The guide does not settle difficult questions regarding successor liability in the M&A context, other than to clarify that successor liability does not "create liability where none existed before." For instance, the mere acquisition by an issuer of an entity not previously subject to the FCPA would not retroactively create FCPA liability over past actions by the acquired entity.

FCPA COMPLIANCE PROGRAMS

The guide describes the following six factors that the DOJ and the SEC consider when evaluating a company's compliance program:

- Tone at the top of the entity;
- Code of conduct and updated and accessible policies and procedures;
- Appointment of senior-level executive and commitment of resources to compliance;
- Allocation of company resources to enforce FCPA compliance in areas of high risk, such as large government bids or questionable payments to third party consultants;
- Clear communication of policies and ongoing training; and
- Self-enforcement of policies and procedures.

DECLINATIONS BY THE DOJ AND THE SEC

One of the more informative sections of the guide provides examples of situations where the government has declined to pursue FCPA charges. Because uncharged cases, of course, are never adjudicated and are not typically described in the public record, it has always been a challenge for practitioners to ascertain how the DOJ and the SEC will decide whether to prosecute a set of facts and to understand the types of cases that will not be of great interest to regulators.

Based on the examples set out in the guide, the following are some factors that appear to have been critical in decisions not to pursue FCPA enforcement actions:

- the amount of the bribe(s) was relatively small;
- the incident was isolated;
- the profits potentially obtained from improper payments were small;
- the company's internal controls identified a potential bribe before it was paid;

- the company voluntarily self-reported to the DOJ and the SEC;
- the company remediated the improper conduct;
- the company immediately conducted an internal investigation;
- the company turned over the results of the internal investigation to the DOJ and the SEC;
- the company fully cooperated with the enforcement agencies; and
- the company took substantial steps to improve its compliance program.

GIFTS AND TRAVEL AND ENTERTAINMENT EXPENSES

Another informative section of the guide concerns gifts and travel and entertainment expenses. The government states that the hallmarks of lawful gift giving under the FCPA are "when the gift is given openly and transparently, properly recorded in the giver's books and records, provided only to reflect esteem or gratitude, and permitted under local law."

The guide provides some examples of permissible gifts—including promotional items, coffee and snacks, and a moderately priced crystal vase as a wedding gift and token of esteem. The guide also reports that expenses such as taxi fare, moderate bar tabs, reasonable meals, and entertainment expenses have not resulted in enforcement actions.

On the other hand, the guide states that lavish and problematic gifts include sports cars, fur coats, and a $12,000 birthday trip. However, paying for business class airline tickets for international travel to inspect a company's facilities is not deemed lavish or problematic, particularly if the paying company would view business class travel as appropriate for its own employees. The guide states that hosting a visiting foreign official at a moderately priced dinner, baseball game, and show is also permissible if these activities are only a small component of the overall trip.

Although any guidance in this area is welcome, the examples of gifts and travel and entertainment expenses provided in the guide are not ones that would be seriously disputed among most FCPA practitioners. As a result, many uncertainties surrounding gifts and travel and entertainment expenses remain even after the publication of the guide.

LOOKING AHEAD

Given the increasingly complex regulatory environment, the guide provides welcome insight into the government's interpretation of the FCPA. Although the publication does not contain many surprises, address some key aspects of the FCPA, or quantify the benefits of self-reporting or cooperation, it is a step forward in helping companies address and avoid FCPA exposure. In the end, the guide reaffirms the value of maintaining a clear FCPA policy and robust FCPA compliance program, conducting due diligence on third party agents, finders, and intermediaries, and conducting FCPA due diligence in connection with corporate transactions.

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