Recent Trends in FCPA Enforcement:
Third-Party Agents

Contributed by: Zachary Harmon and Ehren Halse, King & Spalding

Introduction

Imagine or perhaps recall this common scenario – your company has identified an exciting and promising emerging market for your products or services. In the current global economy, the added revenue predicted from this market would go a long way toward improving your company's balance sheet. Your sales, marketing and other business personnel are eager to seize the opportunity, so they map out a plan to begin operations quickly. However, the emerging market is not short on challenges, including a pronounced language barrier and a complicated and insular business culture. To address these challenges quickly, your company reaches out to a variety of local entities: consultants, distributors, brokers and other agents offering to help you establish the necessary local footholds by obtaining permits and licenses, making important introductions, responding to tenders or negotiating contracts on your company's behalf, and otherwise navigating the cultural and business barriers encountered by every expanding multinational company. These local entities promise your company rapid and meaningful results, and the costs for their services – while somewhat higher than you might have expected – seem like a good investment. Agreements are signed, marketing dollars begin to flow and sales follow soon thereafter. In many ways, this scenario appears close to perfect. Not so fast. Expanding into emerging markets and, in particular, pairing with third-party agents in order to do so can be risky. Obviously, the foregoing business approach is a common one, but companies expanding into new markets should be aware that their interactions with local agents may draw the attention of U.S. authorities enforcing the Foreign Corrupt Practices Act (FCPA).1

How Common Are Enforcement Actions Based On the Conduct of Third Parties?

During the American Conference Institute's yearly FCPA conference held November 17-18, 2009, in Washington, D.C., panelists observed that 10 of the 11 corporate FCPA investigations initiated by U.S. authorities to that point in 2009 involved payments made by third parties. In his remarks at this conference, Mark Mendelsohn, the prosecutor who at the time oversaw FCPA enforcement at the Department of Justice (DOJ), highlighted that there has been a rise in the number of foreign intermediaries charged with FCPA violations while working on behalf of U.S. companies and individuals. Obviously, U.S. authorities are focusing intently on the activities and relationships of U.S. companies operating abroad.
Three recent cases illustrate the extent to which relationships with third parties can expose U.S. companies to FCPA liability. On April 1, 2010, Daimler AG announced a $185 million dollar criminal and civil settlement stemming from FCPA violations. The criminal information filed against Daimler AG details years of widespread payments and gifts channeled through third parties, many of them shell companies, to state-owned customers and government officials around the world in order to win business and increase revenue. In June 2010, Technip, S.A., a French engineering and construction firm, paid a $240 million criminal penalty for FCPA bribery violations concerning payments made to Nigerian government officials. Technip, along with other parties in a joint venture to procure government contracts related to the Bonny Island Liquified Natural Gas facility, used a variety of third parties and agents to serve as conduits for the payments of bribes.

Another recent case demonstrating the importance of agent vetting and oversight involved AGCO, a Georgia-based agricultural machinery supplier. In the civil settlement with AGCO involving FCPA violations, the Securities and Exchange Commission (SEC) detailed the company's internal control failures, highlighting the absence of adequate oversight by finance personnel of payments to a Jordanian agent and the company legal department's inattention to third-party due diligence and contractual irregularities. AGCO paid $16 million in civil penalties and agreed to a deferred prosecution agreement with the DOJ.

DOJ and the SEC continue to trumpet the twin perils of engaging third parties in the absence of meaningful due diligence, and allowing those agents to operate with inadequate oversight. To drive this point home, the authorities have stepped up individual prosecutions based on FCPA violations, targeting individuals and their corporate employers simultaneously. In a dramatic recent development, DOJ indicted and arrested 22 individuals for allegedly attempting to bribe an African government official through intermediaries. The purported intermediaries were actually undercover FBI officials, and DOJ is heralding this FCPA "sting" operation as a warning to companies and their officers and employees that they should be very wary of engaging in illegal conduct through third parties.

How Does the FCPA Apply in the Context of Third-Party Relationships?

The FCPA was enacted in 1977 with the objective of combating corporate bribery of foreign government officials for the purpose of obtaining or retaining business. The FCPA has two basic provisions. At the risk of oversimplification, the first provision prohibits companies and individuals based or operating in the U.S. from bribing foreign government officials to retain or grow business. The second provision of the FCPA requires companies that are publicly traded on U.S. exchanges to maintain accurate, complete and transparent books and records, and to devise internal controls adequate to maintain such records.

Unlike the bribery statute on which it is based, the FCPA expressly states that a company or individual may be held directly liable for bribes paid by a third party if the principal has knowledge of the third party's misconduct. Specifically, the FCPA criminalizes payments made to "any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for political office..."
Taking an expansive view of this language, U.S. authorities have brought enforcement actions based on constructive, rather than actual knowledge of third-party conduct. They have applied "willful blindness," "deliberate ignorance," and similar knowledge standards in the FCPA context. Their position is that companies and individuals can run afoul of the FCPA when they learn of suspicious conduct on the part of their agents and fail to investigate the conduct. Even more unnerving, the authorities have taken the position that, under certain circumstances, companies and individuals can violate the FCPA by failing to conduct adequate due diligence or monitor sufficiently the activities of third parties.

In addition to the AGCO case noted above, two recent FCPA settlements have focused in part on failures to perform adequate due diligence and monitoring of agents. Halliburton's FCPA settlement involving natural gas contracts in Nigeria included findings by the SEC that the company failed to perform adequate due diligence on agents who paid illegal bribes. Similarly, United Industrial Corporation's settlement, predicated on payments made by an agent to secure contracts with the Egyptian Air Force, faulted the company for failing to document its due diligence and implement agreements obligating the agent to follow corporate policy.

Companies are seldom surprised to hear that they cannot engage third parties to make payments which the companies are prohibited from making directly. However, they are often surprised to learn that they may face enforcement proceedings even when they have no actual knowledge of an agent's misconduct.

What Should My Company Do to Guard Against the Risks of Engaging Third-Parties?

Speaking at the 2009 FCPA conference noted above, then-DOJ lead FCPA prosecutor Mark Mendelsohn stated that, "Third-party due diligence must be robust, thorough, impeccably documented, and preserved." Further, Assistant Attorney General Lanny Breuer stated at the 2010 Compliance Week Conference that one benchmark of an effective corporate compliance program is "extension of anti-corruption policies to third-party agents and business partners." While the expectations of U.S. authorities are clearly high, unfortunately the enforcement community has not defined specific protocols that companies should follow when vetting, monitoring and compensating third parties. Nonetheless, widespread practices have emerged with the implicit – and occasionally express – blessing of the authorities. For purposes of this short article, we will only identify and summarize some of the more notable practice trends.

Common Components of a Third-Party Due Diligence Program

In order to collect adequate information concerning prospective third-party representatives and business partners, many companies are now employing a variety of increasingly common tools, for example: (1) forms requiring that internal corporate stakeholders elicit basic information prior to contracting with third parties, such as the reasons for engagement, the specific services required, how prospective third-party individuals or companies were selected for possible service, relevant experience and capabilities of the prospective third party, whether the prospective third-party would need to interact with government officials, how much and in what manner the third party should be compensated, etc.; (2) forms used to elicit similar information from the prospective agent; and (3) some method of vetting the
reputation and background of the prospective third-party representative or business partner. These basic tools continue to evolve as the authorities shed additional light on their expectations and as more effective ways of obtaining the requisite information are developed. The tools are also becoming more sophisticated, reflecting a widespread recognition that one size does not fit all when it comes to agent due diligence. Decisions about scope and cost of due diligence should reflect assessments of risk.

Oversight of Third Parties

U.S. authorities clearly expect companies to exercise reasonable oversight of business partners and third parties acting on the companies' behalf. This oversight should begin with sensible contract provisions. While these provisions are not yet "standardized," FCPA contract language has become relatively consistent and widespread. For example, the provisions may start with language obligating the third party not to violate applicable laws (including the FCPA), but the contract language should provide sufficient clarity about what is prohibited and that the third parties understand their obligations. Other contract provisions, such as annual certifications, termination clauses and audit rights, are favored by the authorities in many situations. Like due diligence, contract provisions can and should vary depending on the nature and location of the services provided. For example, a contract with a small, local agent engaged to "develop business opportunities" in a high-risk country can reasonably differ from a contract governing the work of a Big Four accounting firm in a low-risk country. Finally, if a company elects to include contract language obligating the third party to notify the company — or even obtain the company's approval — prior to or in conjunction with actions in certain situations (e.g., payments to government officials), then the company must exercise this oversight role diligently.

Compensation, Finance & Accounting Controls

In the FCPA context, concerns may arise when third parties receive excessive compensation; specifically, a common suspicion is that excessive compensation paid to an agent may include some amount intended ultimately for bribes. Accordingly, companies are well-served by careful, up-front evaluation of compensation arrangements. Moreover, companies should document their rationale for any decision to pay a third party more than fair market value for a service. Finally, companies should institute strong finance and accounting controls in their interactions with third parties. For example, companies should be wary of accepting invoices from agents describing services in broad and ambiguous terms. This is particularly true if the agent is being paid (or seeking reimbursement) for expenses incurred by the agent in transactions with foreign government officials.

Conclusion

Business consultants, brokers, advisors, local partners, and agents of every variety serve critical and valid roles in the international marketplace. Obviously, companies must rely on these third parties for innumerable services, and particularly when they are entering unfamiliar markets. The purpose of this short article is simply to note that these relationships are under increasing scrutiny by government authorities, and that companies face risks – and attendant obligations – that are in many ways not intuitive. While these compliance obligations are very real, they can be managed.
with relative ease when incorporated into effective compliance and oversight practices and programs.

Zachary Harmon is a partner and Ehren Halse an associate with King & Spalding in Washington, D.C.

8 Id.