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E-ALERT | Global Anti-Corruption

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ANTI-CORRUPTION MID-YEAR REVIEW

The first half of 2011 has been marked by active anti-corruption enforcement in the United States and around the world, including the resolution of two of the ten largest FCPA enforcement actions in history; the SEC's first deferred prosecution agreement; the DOJ's first criminal conviction of a company; and important legal rulings on the FCPA's definition of "foreign official." In 2011, we also have seen the implementation of significant new anti-corruption legislation in the United Kingdom and the issuance of new SEC whistleblower rules in the United States -- both carrying the potential for increased anti-corruption enforcement.

New Anti-Corruption Laws Around the World Are Affecting the Compliance Landscape

UK Bribery Act. The UK Bribery Act entered into force on July 1, 2011, creating four categories of offenses: (1) bribing another person; (2) taking bribes; (3) bribing foreign public officials; and (4) failure of a commercial organization to prevent bribery. With its expansive scope and jurisdictional reach, the Bribery Act significantly reshapes the UK's anti-corruption regime.

The Bribery Act differs from the FCPA in several important ways:

- *Affirmative defense for adequate procedures*. For the offense of failure of a commercial organization to prevent bribery, the Bribery Act includes an affirmative defense for corporations that have put in place "adequate procedures" to prevent bribery. This defense recognizes -- in a way that the US adherence to the *respondeat superior* doctrine does not -- that robust compliance by companies should insulate the company from criminal liability.
- *Broader scope of conduct covered.* Unlike the FCPA, the Bribery Act reaches commercial bribery -- payments made to induce any person to act "improperly." Additionally, US public officials are considered foreign public officials under the Bribery Act; accordingly, bribing a US government official (or failing to prevent such bribery) could be prosecuted by the Serious Fraud Office ("SFO") when there is a jurisdictional nexus.
- *Broad jurisdiction*. The Bribery Act reaches corporations that conduct some or part of their business in the UK. Guidance on the Bribery Act issued by the Ministry of Justice in March 2011 states that the UK Government will take a "common sense approach" to jurisdiction and "would not expect" a mere listing on the London Stock Exchange or the presence of a subsidiary in the UK to automatically bring a company within the jurisdiction of the UK courts. Nevertheless, the Director of the SFO has stated that he will take a "wide view of jurisdiction" and will not be impressed with "overly technical interpretations" of the Bribery Act crafted to evade the UK's jurisdiction. Ultimately, UK courts will be the final arbiter of whether an organization "carries on a business" in the UK and is thus subject to jurisdiction there. But in the meantime, it is the SFO's exercise of discretion in enforcing the Bribery Act that will determine how broadly the Act will reach in practice.

- *Facilitating payments.* Unlike the FCPA, the Bribery Act does not contain an exception for facilitating payments, although it remains to be seen whether the SFO will prosecute a company when only a facilitating payment has been made.

Other New Anti-Corruption Laws. In addition to the UK, other jurisdictions, including China and Russia, have enacted or are considering enacting their own anti-corruption laws targeting bribery of public officials.

- In February 2011, China broadened its anti-bribery law to criminalize bribery of public officials outside of China and of officials of international organizations. The changes to the law, which apply to entities organized under PRC law and to PRC citizens, were part of a set of amendments to the PRC Criminal Law that became effective May 1, 2011.
- In May 2011, Russia strengthened its anti-bribery law by increasing penalties and expanding the scope to cover bribery by Russian companies and citizens of public officials outside of Russia.
- Brazil, India, and Indonesia are similarly considering changes in their bribery laws that would prohibit their companies and citizens from bribing public officials outside of their countries.

Important Developments in US Law Have the Potential to Significantly Affect Anti-Corruption Enforcement

Final SEC Whistleblower Rules Issued. In May 2011, the SEC adopted final rules implementing its new whistleblower program under the Dodd-Frank Act. As we described in a recent webinar, the SEC must pay cash awards (between 10 and 30 percent of amounts collected in an SEC enforcement action or a "related action" -- e.g., DOJ prosecution) to an individual who "voluntarily" provides "original information" that leads to successful enforcement of the US securities laws, with monetary sanctions obtained by the SEC of more than $1 million. The whistleblower program is likely to increase the number of FCPA-related tips provided to the SEC, and we are aware of plaintiffs' lawyers in emerging markets, such as China, actively seeking to represent whistleblowers. The whistleblower rules may particularly incentivize whistleblowers to report FCPA violations, given the large amounts paid by companies in recent FCPA settlements. Companies considering whether to voluntarily disclose potential anti-corruption problems to the SEC or the DOJ must now factor into their decisionmaking the likelihood that a potential whistleblower will make a disclosure to the government in lieu of, or in addition to, reporting the alleged misconduct to the company. In this regard, the SEC's final whistleblower rules do not require a whistleblower to report internally before disclosing information to the SEC.

Congressional Hearing on the FCPA. In June, the House Judiciary Committee's Subcommittee on Crime, Terrorism, and Homeland Security held a hearing on the FCPA. The hearing considered several FCPA reform proposals -- some sponsored by the US Chamber of Commerce -- intended to clarify the FCPA's definitions of "instrumentality" and "foreign official"; add an affirmative compliance defense; create a "safe harbor" provision to limit the successor liability of companies that undertake thorough post-closing reviews of the business operations of targets and self-disclose any FCPA issues; and raise the intent requirement for companies. After the hearing, Representative Jim Sensenbrenner (R-WI) announced his plan to introduce a bill to reform the FCPA, although he is expected to wait until after the August Congressional recess to introduce the bill.

US Enforcement Authorities Have Initiated and Settled Significant Enforcement Actions

"Top 10" Enforcement Actions. To date, 11 companies have settled enforcement actions with US authorities in 2011. Settlements by JGC and Johnson & Johnson in April joined the list of the ten largest FCPA-related corporate recoveries in the history of the statute.

- JGC, a Japan-based construction company, entered into a two-year deferred prosecution agreement with the DOJ and agreed to pay a $218.8 million criminal penalty to resolve allegations that the company was involved in a decade-long scheme with its joint venture partners to bribe Nigerian government officials in order to obtain contracts to build liquefied natural gas facilities on Bonny Island, Nigeria. US enforcement authorities have now obtained more than $1.5 billion in criminal and civil penalties from the four Bonny Island joint venture partners. JGC's deferred prosecution agreement notes that the company initially declined to cooperate with the DOJ "based on jurisdictional arguments," but ultimately decided to cooperate. Notably, JGC is neither a domestic concern nor an issuer, and the criminal information filed by the DOJ appeared to base jurisdiction on two theories: (1) aiding and abetting a domestic concern in its violation of the FCPA's anti-bribery provisions; and (2) conspiring with issuers and domestic concerns to violate the FCPA. The JGC case again highlights the US enforcement authorities' expansive view of the FCPA's jurisdiction.
- Johnson & Johnson ("J&J") paid $70 million in fines and penalties to the DOJ and the SEC to resolve allegations of bribery in Greece, Poland, Romania, and Iraq as part of a three-year deferred prosecution agreement with the DOJ. According to the deferred prosecution agreement, in the three European countries, J&J subsidiaries made improper payments in order to sell J&J products. The improper payments included bribes funneled through contracts with agents; contracts with health care professionals that did not require services rendered; gifts; and travel sponsorships. The settlements also covered improper payments made in Iraq in connection with the Oil-for-Food Program. The DOJ stated that J&J received a reduced fine "as a result of its cooperation in the ongoing investigation of other companies and individuals." This development -- which appears to differ from the credit a company may receive when it voluntarily discloses, or cooperates in an investigation of, its own conduct -- could reflect an evolution in the DOJ's approach toward cooperation credit. Although the DOJ's Criminal Division has not embraced an amnesty program similar to the program that exists in the Antitrust Division, the Criminal Division may be signaling through the J&J case that providing information on other companies and individuals will result in more lenient treatment than might otherwise be expected.
- In addition to the US settlements, the UK Serious Fraud Office obtained a civil recovery order of £4.829 million plus prosecution costs from a J&J subsidiary in connection with the payments to government officials in Greece. The SFO concluded that criminal prosecution was prevented by double jeopardy because J&J's subsidiary had entered into a deferred prosecution agreement with the DOJ. However, the SFO stated that it worked closely with the DOJ and the SEC in its investigation. The DOJ and SFO settlements were announced on the same day, further evidencing the continuing cooperation between US prosecutors and their counterparts in other jurisdictions.

SEC's First Deferred Prosecution Agreement. In May, the SEC entered into its first-ever deferred prosecution agreement. Tenaris allegedly bribed Uzbekistan government officials while bidding to supply pipelines for transporting oil and gas. Tenaris agreed in May 2011 to pay $5.4 million in disgorgement and prejudgment interest to the SEC. The company also resolved FCPA charges with the DOJ by paying a $3.5 million criminal penalty and entering into a non-prosecution agreement. While the DOJ has used deferred prosecution agreements for many years, the Tenaris deferred prosecution agreement is the SEC's first of any kind, not just in the FCPA context. SEC officials have signaled that they will continue to use deferred prosecution agreements to encourage cooperation from companies and individuals in the future.

DOJ's First Corporate Conviction. Lindsey Manufacturing recently became the first company to be tried and convicted of FCPA violations. Along with its president and chief financial officer, the company was found guilty of FCPA violations stemming from bribes paid to employees of a state-

owned electrical utility company in Mexico. The company made improper payments through inflated commissions to a sales agent, and its executives understood that all or part of the sales agent's commission would be used to pay bribes to certain utility employees in exchange for the award of contracts to Lindsey Manufacturing. (Only one other corporate defendant had ever contested FCPA charges all the way through trial; Harris Corporation was acquitted in 1991.) In a press release after the Lindsay conviction, Assistant Attorney General Lanny A. Breuer characterized the convictions of Lindsay and several of its executives as "an important milestone" in the government's FCPA enforcement efforts. Breuer stated, "Lindsey Manufacturing is the first company to be tried and convicted on FCPA violations, but it will not be the last."

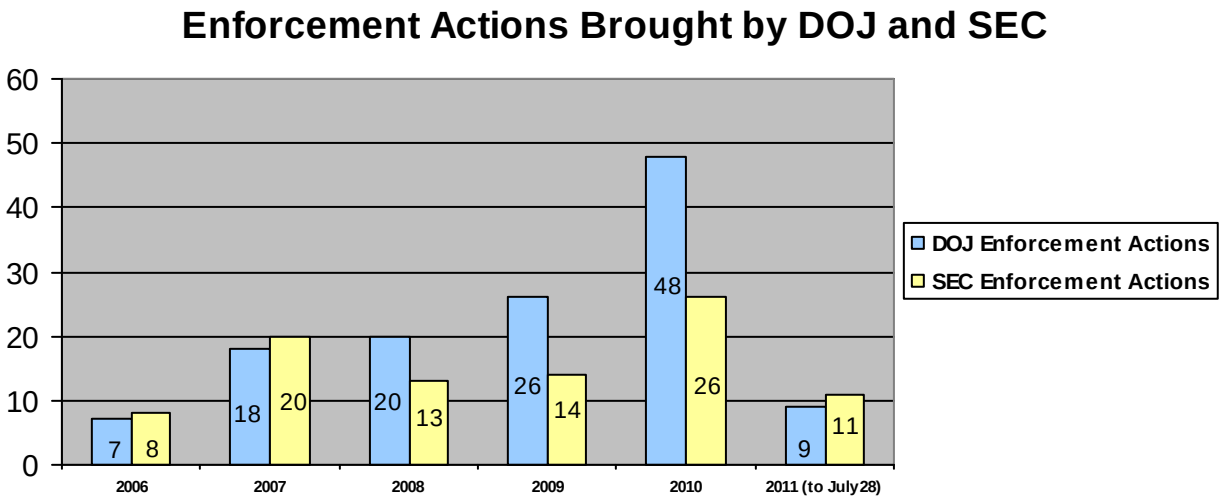
Notable Individual FCPA Prosecutions. In March 2011, Jeffrey Tesler, an agent for the joint venture in Nigeria in which JGC was a partner (see above), pleaded guilty to one count of conspiracy to violate the FCPA and one count of violating the statute after losing his fight against his extradition from the UK. Tesler agreed to forfeit $149 million, the largest forfeiture to date by an individual in an FCPA prosecution. Tesler awaits sentencing in the United States.

Other corporate executives have pleaded guilty or settled civil FCPA charges in 2011, including the former CFO and COO of Latin Node, a Miami-based telecommunications company, and the former CEO and CFO of Innospec.

Some Setbacks for US Enforcement Authorities. Despite the continued steady pace of enforcement in 2011, US enforcement authorities have hit some bumps in the road.

- A district court judge declared a mistrial in the first "shot-show" trial. The trial involved four of the original 22 defendants who were charged with FCPA violations and conspiracy to violate the FCPA following an FBI sting in which an FBI agent posed as an official of an African country. Three defendants have already pleaded guilty. The government has indicated that it intends to retry the four defendants.
- The individual defendants in the Lindsey Manufacturing case have moved to dismiss their convictions, and the judge presiding over the case postponed their sentencing date after discovering that the government had failed to turn over an FBI agent's grand jury testimony in violation of a court order. Judge Matz stated that he was "shocked" by the government's conduct and recited a list of troubling government conduct throughout the prosecution. A hearing on the motions to dismiss is scheduled for September 2011.

Number of Enforcement Actions. Through July 28, 2011, the DOJ and SEC settled nine and eleven enforcement actions, respectively. At this pace, the DOJ and SEC are on track to bring fewer total enforcement actions in 2011 than in 2010, although (1) the number of enforcement actions brought in 2010 was inflated by the 22 individuals charged with FCPA violations after the "shot-show" sting operation; and (2) DOJ officials have indicated that significant prosecutorial resources have been dedicated to staffing the trials described above, leaving fewer resources to prosecute and settle other cases. DOJ officials have publicly stated that over 150 FCPA investigations remain open.



Foreign Enforcement Actions. Notable anti-corruption enforcement actions also have been brought outside the United States during the first part of 2011.

- Niko Resources, a publicly traded oil and gas company based in Calgary, became the first company to plead guilty to a violation of Canada's overseas anti-bribery law, the Corruption of Foreign Public Officials Act. The company agreed to pay a C$9.5 million (US $10.0 million) fine after pleading guilty to bribing a Bangladeshi minister, reportedly with a luxury SUV and a trip to the United States and Canada.
- In May 2011, a district prosecutor's office in Incheon, Korea issued an indictment against several individuals accused of bribing an executive of a Chinese state-owned airline. The indictment is the first enforcement action under Korea's overseas anti-corruption law, the Act on Combating Bribery of Foreign Public Officials in International Business Transactions.
- In addition to the civil recovery order obtained from J&J's subsidiary (see above), the SFO has obtained two other civil recovery orders in 2011 under the Proceeds of Crime Act, a statute that permits prosecutors to target and recover identifiable property that has been acquired through criminal conduct. In February, the SFO secured a civil order requiring M.W. Kellogg Limited (MWKL) to pay £7.028 million. MWKL is a wholly owned subsidiary of KBR, one of the joint venture partners in the Bonny Island project discussed above. In July, the SFO obtained a further civil recovery order requiring Macmillan Publishers Limited to pay £11.263 million plus prosecution costs in recognition of sums the company received through unlawful conducted related to its education division in East and West Africa. The SFO's settlement of three civil recovery orders this year indicates that the agency is making increasing use of this mechanism until such time as it has the power to impose fines on companies or enter into deferred prosecution agreements.

US Courts Have Issued Significant Legal Rulings Rejecting Challenges to the Government's Interpretation of "Foreign Official" Under the FCPA

In several cases this year, individual and corporate defendants have challenged the DOJ's interpretation of the term "foreign official" under the FCPA, arguing that employees of state-owned corporations cannot be considered "foreign officials" under the statute. Thus far, both judges to consider the challenges have held that a government-owned corporation *may* be considered an "instrumentality" of a foreign government – and its employees therefore considered "foreign

officials" -- without going so far as to say that state-owned corporations *always* qualify as instrumentalities under the statute. Because US enforcement authorities frequently file settled enforcement actions and enter into plea agreements, the government's interpretations of the FCPA are rarely tested in court. As a result, the two rulings rejecting challenges to the government's interpretation of "foreign official" will be viewed as significant victories by US enforcement authorities.

- Defendants in the Lindsey Manufacturing case moved to dismiss the charges against them on the grounds that an officer or employee of a state-owned corporation cannot be a foreign official for purposes of the FCPA. A federal district court in California denied the motion. Finding that the legislative history of the FCPA did not demonstrate that Congress definitively intended to include or exclude *all* state-owned corporations from the reach of the FCPA, the court held that a state-owned corporation with the attributes of the utility company at issue could be an instrumentality within the meaning of the statute and its officers could therefore be "foreign officials." The court noted with respect to the utility at issue that (1) the Mexican constitution designates the supply of electricity as exclusively a government function; (2) the utility's website describes it as a government "agency"; (3) the utility was created by statute as a public entity; and (4) the utility's governing board was comprised of high-ranking government officials.
- In *United States v. Carson*, a federal district court in California held that employees of some government-owned companies may be considered "foreign officials" under the FCPA. The judge concluded that the question of whether state-owned companies qualify as instrumentalities under the FCPA is a question of fact. The judge set forth six relevant factors to be considered: (1) the foreign state's characterization of the entity and its employees; (2) the foreign state's degree of control over the entity; (3) the purpose of the entity's activities; (4) the entity's obligations and privileges under the foreign state's law; (5) the circumstances surrounding the entity's creation; and (6) the extent of the foreign state's ownership interest in the entity, including the level of financial support by the state (such as subsidies, special tax treatment, and loans). The judge declined to consider the legislative history of the FCPA, pointing to the statute's clear language and coherent and consistent statutory scheme.
- A third challenge to the "foreign official" definition is pending in a federal district court in Texas.

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Save the Date: Covington & Burling Anti-Corruption Summit 2011

Given the notable developments in the first half of the year, it will be interesting to see how anti-corruption enforcement progresses over the next few months. Covington will be reviewing the year's developments at its Anti-Corruption Summit 2011, featuring Richard Alderman, Director of the UK Serious Fraud Office, as the keynote speaker. Formal invitations will be sent shortly, but we hope you will save the date and join us for the Summit on October 5, 2011 in Washington, DC.

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About Covington & Burling's Global Anti-Corruption Practice

With anti-corruption specialists in our Washington, New York, San Francisco, London and Beijing offices, Covington's Global Anti-Corruption team has global reach. Our team includes more than fifteen experienced lawyers, including partners and of counsel. Our lawyers have held senior positions in the US Department of Justice, UK Serious Fraud Office, US Attorney's Offices, US Solicitor General's Office, White House, Securities and Exchange Commission, and other government

agencies involved in anti-corruption issues and thus understand the approach of the US and UK governments in this area. Associates on the team also have been deeply involved in all facets of our anti-corruption practice, assisting in investigations and devising compliance programs for our clients.

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