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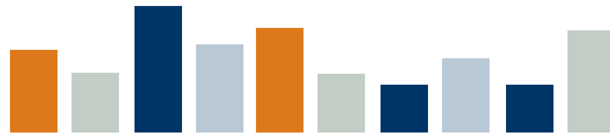

Investment Management Hot Topics

The Foreign Corrupt Practices Act: How Funds Can Mitigate Risks

May 8, 2012

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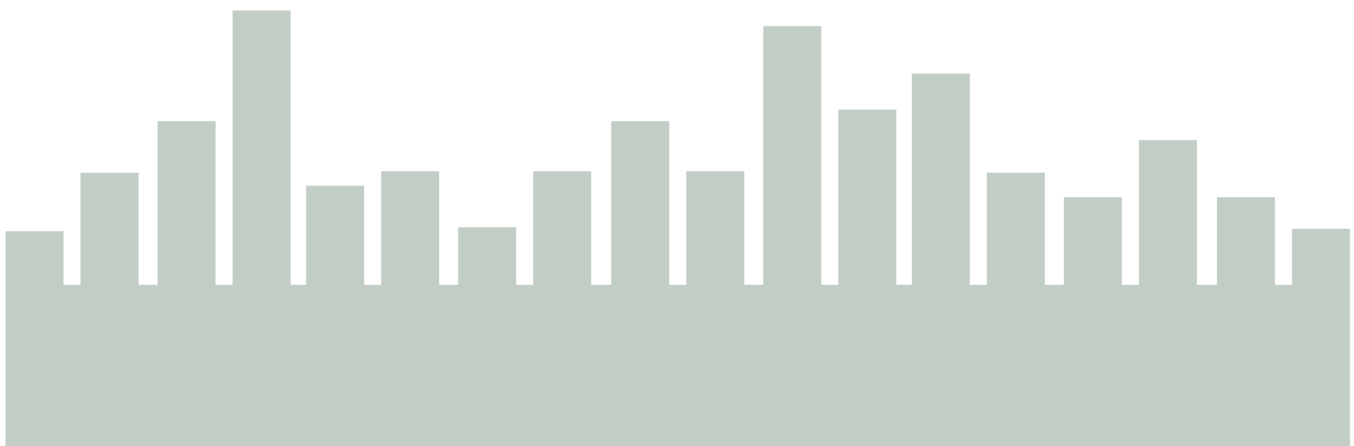

1. About the Speakers

Stephanie R. Breslow
919 Third Avenue
New York, NY 10022
+1 212.756.2542 | stephanie.breslow@srz.com

Stephanie R. Breslow is a partner in the New York office of Schulte Roth & Zabel, where she is also co-head of the Investment Management Group and a member of the Executive Committee. Her practice includes investment management, partnerships and securities, with a focus on the formation of liquid-securities funds (hedge funds, hybrid funds) and private equity funds (LBO, mezzanine, distressed, real estate, venture), as well as providing regulatory advice to investment managers and broker-dealers. She also represents fund sponsors and institutional investors in connection with seed capital investments in fund managers and acquisitions of interests in investment management businesses, and represents funds of funds and other institutional investors in connection with their investment activities.

Stephanie is currently Vice-Chair of the Private Investment Funds Subcommittee of the International Bar Association and is also a founding member and former chair of the Private Investment Fund Forum, a member of the Advisory Board of Third Way Capital Markets Initiative, a former member of the Steering Committee of the Wall Street Fund Forum and a member of the Board of Directors of 100 Women in Hedge Funds. She was named one of *The Hedge Fund Journal*'s 50 Leading Women in Hedge Funds and is listed in *Chambers USA*, *Chambers Global*, *The Legal 500 United States*, *Best Lawyers in America*, *America's Leading Lawyers*, *Who's Who Legal: The International Who's Who of Business Lawyers* (which ranked her one of the world's "Top Ten Private Equity Lawyers"), *IFLR Best of the Best USA* (Investment Funds), *IFLR Guide to the World's Leading Investment Funds Lawyers*, *IFLR Guide to the World's Leading Women in Business Law* (Investment Funds), *IFLR Guide to the World's Leading Private Equity Lawyers*, and *PLC Cross-border Private Equity Handbook*, among other leading directories.

Stephanie is a sought-after speaker on fund formation and operation and compliance issues, and also publishes books and articles on the latest trends in these areas. She co-authored *Private Equity Funds: Formation and Operation* published by Practising Law Institute, contributed a chapter on "Hedge Funds in Private Equity" for inclusion in Private Equity 2005-2006 (PLC Cross-border Handbooks) and co-wrote *New York and Delaware Business Entities: Choice, Formation, Operation, Financing and Acquisitions* and *New York Limited Liability Companies: A Guide to Law and Practice*, both published by West Publishing Co. Stephanie earned her J.D. from Columbia University School of Law, where she was a Harlan Fiske Stone Scholar, and her B.A., *cum laude*, from Harvard University.

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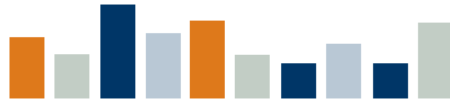

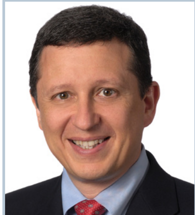

Gary Stein
919 Third Avenue
New York, NY 10022
+1 212.756.2441 | gary.stein@srz.com

Gary Stein is a partner in the New York office of Schulte Roth & Zabel, where he focuses on white-collar criminal defense and securities regulatory matters, complex commercial litigation, internal investigations, anti-money laundering issues, civil and criminal forfeiture proceedings and appellate litigation. He represents public companies, financial institutions, hedge funds, other entities and individuals as subjects, victims and witnesses in federal and state criminal investigations and regulatory investigations by the SEC, SROs and state attorneys general. He has conducted numerous internal investigations involving potential violations of the Foreign Corrupt Practices Act, financial statement fraud, money laundering and other matters, and advises companies on compliance with the FCPA and anti-money laundering and OFAC regulations.

As a former assistant U.S. attorney and chief appellate attorney in the Southern District of New York, Gary investigated, prosecuted, tried and represented the government on appeal in numerous white-collar criminal cases involving money laundering, fraudulent investment schemes, bank fraud, insider trading, art theft, illegal kickbacks, terrorist financing and other financial crimes. His civil litigation experience includes claims of fraud and breach of contract, securities class actions and derivative actions, contests over corporate control and disputes arising from the sale of businesses. He has handled more than 150 appeals in federal and state courts involving issues of both criminal law and procedure and complex commercial law and has successfully argued 15 appeals in the U.S. Court of Appeals for the Second Circuit.

An accomplished public speaker and writer, Gary has presented on risk management and crisis management issues at global conferences and seminars. He co-authored the "Scienter/Trading 'on the Basis of'" chapter in the *Insider Trading Law and Compliance Answer Book*, which was published by Practising Law Institute. In 2008, he won a Burton Award for Achievement in Legal Writing for co-authoring "The Foreign Corrupt Practices Act: Recent Cases and Enforcement Trends," which appeared in the *Journal of Investment Compliance*. Gary obtained his J.D. from New York University School of Law, where he was senior articles editor of the *New York University Law Review*, and his B.A. from New York University.

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Sung-Hee Suh
919 Third Avenue
New York, NY 10022
+1 212.756.2418 | sung-hee.suh@srz.com

Sung-Hee Suh, a partner in the New York office of Schulte Roth & Zabel, practices in the areas of white-collar criminal defense, securities regulatory enforcement, internal investigations, anti-money laundering ("AML") compliance and complex commercial litigation. Her recent white-collar criminal and regulatory matters include representing the subject of an SEC investigation into alleged insider trading in the stock of a pharmaceutical company; conducting an internal review of a global financial institution's AML program in the aftermath of a Ponzi scheme involving numerous bank and brokerage accounts; defending a foreign bank against the U.S. Department of Justice's seizure of assets from the bank's interbank accounts; representing a fund manager in pension fund-related "pay-to-play" investigations by the New York Attorney General's Office and the SEC; conducting an internal investigation for a global telecommunications company into possible Foreign Corrupt Practices Act ("FCPA") violations; representing an interdealer brokerage firm in a FINRA investigation into certain brokerage practices; and defending a former in-house attorney at Hollinger International Inc. against federal criminal fraud charges based on an "honest services" theory that was ultimately rejected by the U.S. Supreme Court.

A frequent speaker and writer, Sung-Hee authored the chapter on the "Use of Paid Consultants" in the *Insider Trading Law and Compliance Answer Book* published by Practising Law Institute and co-authored "Recent FCPA Developments Highlight Risk of Individual Liability" and "Government Launches FCPA Inquiry into Investments by Sovereign Wealth Funds in U.S. Banks and Private Equity Firms," both of which appeared in the *Financial Fraud Law Report*. She also speaks regularly at PLI's annual "Financial Services Industry Regulatory Compliance & Ethics Forum" and PLI's annual program on "Bet the Company Litigation."

Prior to joining SRZ, Sung-Hee served as an assistant U.S. attorney in the Eastern District of New York, including as Deputy Chief of the Organized Crime and Racketeering Section. She currently serves on the Federal Bar Council's Program Committee and on the New York City Bar Association's Judiciary Committee and is also a member of the New York Council of Defense Lawyers. In 2011, the New York chapter of the National Organization for Women honored Sung-Hee with its annual Women of Power & Influence Award. Sung-Hee received her A.B., *cum laude*, from Harvard/Radcliffe College and her A.M. from Harvard Graduate School of Arts and Sciences. She received her J.D., *cum laude*, from Harvard Law School, after which she was a law clerk to the Honorable Robert L. Carter, U.S. District Judge of the Southern District of New York.

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Peter H. White
1152 Fifteenth Street, NW, Suite 850
Washington, DC 20005
+1 202.729.7476 | pete.white@srz.com

Peter H. White, a partner in the Washington, D.C. office of Schulte Roth & Zabel, concentrates his practice on representing corporations and executives in criminal and related civil and administrative matters, including grand jury investigations, internal investigations, SEC enforcement proceedings, False Claims Act and qui tam lawsuits, and shareholder class actions. Pete has litigated disputes involving accounting and securities fraud, Foreign Corrupt Practices Act violations, government program fraud, false claims and statements, antitrust violations, public corruption, tax evasion, insider trading, environmental violations and other claims. A former assistant U.S. attorney for the Eastern District of Virginia and the District of Columbia, Pete has served as lead counsel in over 80 federal and local jury trials and many more bench trials.

A recipient of the Department of Justice Director's Award for Superior Performance as an Assistant U.S. Attorney, Pete has performed with comparable skill as a private practitioner. Among the many publications that have recognized him as a leading litigator are: *The Best Lawyers in America* (white collar criminal defense, corporate governance and compliance law); *Ethisphere: Attorneys Who Matter*; *Washington, D.C. Super Lawyers*; *Washingtonian Magazine* (white collar defense) and *The Washington Post* ("Their Own Defense," June 18, 2007).

Pete regularly speaks and writes, recently authoring the chapter on "Civil and Criminal Enforcement" in the *Insider Trading Law and Compliance Answer Book*, which was published by Practising Law Institute, and co-authoring "Recent FCPA Developments Highlight Risk of Individual Liability" for the *Financial Fraud Law Report*. He also spoke on "Retaining Counsel, the Search, and Investigating the Case" and "Handling the Search" at the National Association of Criminal Defense Lawyers White Collar Criminal Defense College and participated in an SRZ webinar titled "Recent Developments in U.S. Insider Trading Law and FCPA Enforcement." Pete obtained his B.A., with high honors, from the University of Notre Dame and his J.D. from The University of Virginia School of Law, where he was Order of the Coif and on the Management Board of the *Virginia Law Review*. Upon graduation, he had the distinction of serving as a law clerk to The Honorable Richard L. Williams of the Eastern District of Virginia.

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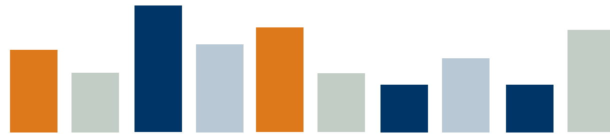

Investment Management Hot Topics

2. PowerPoint Presentation

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Investment Management Hot Topics

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What Is the FCPA?

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Notes:

To Whom Does the FCPA Apply?

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Elements of an FCPA Violation

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FCPA Risks for Investment Funds

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Ways to Mitigate FCPA Risk

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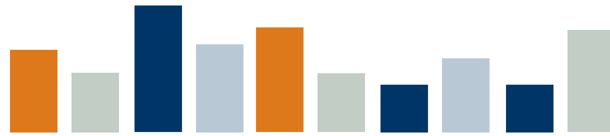

Investment Management Hot Topics

3. Outline

The Foreign Corrupt Practices Act: How Funds Can Mitigate Risks

I. Why investment funds should care about the FCPA

A. Most funds have some FCPA risk; some funds have a lot of FCPA risk

B. The FCPA has broad extraterritorial reach

C. The U.S. Government has been very aggressive in this area

D. The consequences of an FCPA violation — or merely an allegation of an FCPA violation — are serious

E. Counterparties care about the FCPA

F. Anti-corruption efforts have now gone global — other countries and international organizations have already passed and will continue to pass similarly aggressive anti-bribery laws (e.g., UK Anti-Bribery Act; EU; OAS; World Bank; IMF; OECD Convention on Combating Bribery of Foreign Officials in International Business Transactions)

II. What is the FCPA?

A. Federal statute passed by post-Watergate Congress in 1977

B. Two prongs

1. Anti-Bribery Provisions: prohibit bribery of foreign government officials for the purpose of obtaining or retaining business

   Apply to bribes paid directly and bribes paid indirectly through third-party intermediaries (e.g., agents, placement agents, sub-agents, consultants, representatives, distributors, resellers, introducers/finders, joint venture partners, brokers, contractors, lawyers, accountants, lobbyists)

2. Accounting Provisions: require Issuers to maintain accurate books and records and establish a system of internal controls

   (a) The Accounting Provisions only apply to Issuers

   (b) They do *not* apply merely because a fund is registered with the SEC, so they are usually not an issue for private investment funds. However, they do apply to portfolio companies that are publicly traded, whether in equity or debt markets

C. Enforced by DOJ and SEC

1. Penalties are harsh

2. Criminal penalties for violating the Anti-Bribery Provisions: entities can be fined up to $2MM for each violation

   (a) Officers/directors/employees/agents can be fined up to $250K and imprisoned up to five years for each violation

   Note: Fines on individuals cannot be paid by the firm

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(b) Fines can also be up to twice the profit gained from the illegal activity or twice the loss resulting from the illegal activity

(c) In addition, FCPA violations can be the basis for forfeiture of assets

3. Criminal penalties for violating the Accounting Provisions: corporate fine up to $25MM and individuals up to $5MM and/or 20 years in prison

4. Civil Penalties may include: DOJ and/or SEC obtaining injunctive relief and fines up to $10K for each violation of the Anti-Bribery Provisions

(a) SEC may impose hefty fines

(b) SEC may also obtain disgorgement of illegal profits

5. Other penalties include suspension or disbarment from the securities industry or doing business with the U.S. federal government, plus other collateral consequences

III. To whom does the FCPA apply?

Anti-Bribery Provisions make it illegal for an “issuer,” a “domestic concern” or any “other” person to make corrupt payments, directly or indirectly, to a foreign government official in order to obtain, retain or direct business. 15 U.S.C. §§ 78dd-1, 2 and 3

A. “Issuer”

1. Issuers with a class of securities registered under the Securities Exchange Act of 1934

2. Includes foreign companies with U.S. ADRs

B. “Domestic concern”

1. U.S. citizens, nationals and residents

2. Companies that have their principal place of business in the U.S. or are organized under U.S. law

C. Any “other” person (i.e., non-U.S. persons)

May be liable if they commit any act in furtherance of unlawful payment while in the U.S., including (according to the DOJ) “causing” an act in the U.S., directly or through agents

D. Foreign subsidiaries

U.S. parents may be held liable for acts of foreign subsidiaries if they authorized, directed or controlled the activity in question

E. Related persons (i.e., officers, directors, employees, or agents of a U.S. issuer or domestic concern or a covered non-U.S. company, or any stockholder acting on their behalf)

F. SEC’s “control person” theory of liability

Nature’s Sunshine: SEC charged two top executives in their capacity as control persons with books and records and internal control violations

Note: A private investment fund that controlled a U.S. issuer that engaged in FCPA violations could face liability under this theory

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IV. Elements of an FCPA violation

A. Payment or offer

1. Of money or "anything of value"

2. Offer, promise, or authorization of a payment is enough to violate the FCPA, even if no payment has yet been made

B. Prohibited recipient

1. "Foreign official" (i.e., "[a]ny officer or employee of a foreign government or any department, agency or instrumentality thereof, or any person acting in an official capacity for or on behalf of any such government or department, agency or instrumentality")

2. Officials of a "public international organization" (e.g., UN, World Bank)

3. Foreign political parties, officials of foreign political parties and candidates for foreign political office

4. Any person acting as a conduit for payments to any of the above

C. Corrupt intent

Payment must be for the purpose of:

1. Influencing any act or decision of a foreign official in his or her official capacity;

2. Inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official;

3. Securing any improper advantage; or

4. Inducing such foreign official to use his or her influence with a foreign government or instrumentality to affect or influence any act or decision of such government or instrumentality

D. Business purpose requirement

1. Payment must be made for the purpose of assisting the violating party in obtaining or retaining business for or with, or directing business to, any person

2. Such business does not need to be with a foreign government or foreign government instrumentality

E. Jurisdiction

1. U.S. issuers, U.S. companies and U.S. individuals liable for prohibited acts committed anywhere in the world, regardless if there is a nexus to the U.S.

2. Non-U.S. persons liable (as noted above) for prohibited acts committed while in the U.S., including (according to the DOJ) "causing" an act in the U.S.

V. Common misconceptions about the FCPA

A. The FCPA only applies if the recipient of the bribe is a high-ranking foreign official (e.g., a minister)

Wrong: The FCPA defines a foreign official as "*any officer or employee* of any government or agency, department or instrumentality." US officials take the position that this includes low-level officials and all employees of state-owned companies. *United States v. Aguilar*, 783 F. Supp. 2d 1108 (C.D. Cal. 2011) (holding that FCPA's definition of foreign official can include employees of state-owned business enterprises)

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B. If I don't actually know that a bribe is being paid, I haven't violated the FCPA

Wrong: Prosecutors can and frequently do pursue FCPA cases on a "conscious avoidance" or "willful blindness" theory. That theory permits the imposition of liability even where the defendant did not have actual knowledge that a bribe was being paid, if he or she was aware of a "high probability" that a bribe was being paid, and consciously avoided trying to confirm whether that was the case. This often becomes a key issue when dealing with agents, consultants and other third-party intermediaries. *United States v. Kozeny*, 667 F.3d 122 (2d Cir. 2011) (upholding conviction of investor in Azerbaijan privatization venture on conscious avoidance theory)

C. It is a defense under the FCPA that the defendant didn't propose the bribe and only paid it after the foreign official solicited the bribe

Wrong: It doesn't matter who solicited or first suggested the bribe. The scheme does not have to originate with the person making the payment; rather, the Anti-Bribery Provision "cover[s] payments and gifts intended to influence the recipient, regardless of who first suggested the payment or gift." S. Rep. No. 114, 95th Cong., 1st Sess., at 11 (1977)

D. It is a defense under the FCPA that bribery is part of the culture in a foreign country

Wrong: It is no defense that bribery is customary or pervasive in the country in question. It doesn't matter if this is the way "people do business"

VI. FCPA risks for investment funds

A. Risks in raising money

1. Foreign government investors (e.g., sovereign wealth funds, state-owned pension plans, private pension plans requiring government approval, any other investor owned or controlled by a foreign government)

2. Placement agents and other third-party marketers and intermediaries who help solicit foreign money, especially from foreign government investors

3. Gifts/entertainment of foreign government investors

   Note: What a hedge fund considers "reasonable" in New York may be viewed as "lavish" by the U.S. government

4. Foreign officials, political leaders, or candidates as investors

   Note: Beware of "private" parties who are acting on behalf of foreign officials

B. Risks in making investments

1. Portfolio companies (both U.S. companies that do business overseas and foreign companies)

2. Overseas investments

3. Privatization deals

4. Joint ventures with state-owned entities

C. Risks in foreign offices/operations

1. Obtaining licenses and permits

2. Regulatory inspections and audits

3. Foreign tax issues

VII. Recent enforcement activity/trends

A. The DOJ and SEC have dramatically stepped up FCPA enforcement in recent years

B. More cases are being brought

1. 32 DOJ enforcement actions in 2005-2007
2. 92 DOJ enforcement actions in 2008-2010

C. Higher penalties are being imposed

1. In the FCPA's first 25 years, only four fines > $1MM
2. Now, eight-digit and nine-digit fines are common

D. Focus on prosecuting individuals

1. Assistant Attorney General Lanny Breuer (March 2010): "[C]ornerstone of our FCPA enforcement policy: the aggressive prosecution of individuals. Put simply, the prospect of significant prison sentences for individuals should make clear to every corporate executive, every board member, and every sales agent that we will seek to hold you personally accountable for FCPA violations."

E. The trend toward increased FCPA enforcement shows no sign of abating

1. Expansion of FCPA enforcement resources
2. Additional FCPA prosecutors at DOJ
3. New FCPA Unit at SEC
4. More than 150 open FCPA investigations (as of April 2012)

F. Aggressive law enforcement techniques

1. Sting operations
2. Sector-wide probes/sweeps
3. Wiretaps?

VIII. Recent enforcement actions focusing on investment funds

A. SEC sovereign wealth funds investigation

1. In January 2011, the SEC sent letters to a number of firms to determine whether banks and private equity firms violated the FCPA in their dealings with sovereign wealth funds and state-owned pension plans
2. No charges announced to date

B. Azerbaijan privatization case

1. Scheme to bribe senior government officials in Azerbaijan with several hundred million dollars in shares of stock, cash and other gifts

   Intended to influence privatization of State Oil Company

2. Omega Advisors, Inc.

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(a) One of the investment funds that invested in the Azerbaijan privatization program entered into a Non-Prosecution Agreement in July 2007

(b) Agreed to civil forfeiture of $500K

(c) Acknowledged that its former employee had learned, prior to its investment, that some Azeri officials had been given a financial interest in the privatization by Victor Kozeny, the organizer of the investment consortium

3. *U.S. v. Bourke* (Frederic A. Bourke Jr.)

(a) Investor in same Azerbaijan privatization program, convicted after a jury trial in July 2009 of conspiracy to violate the FCPA and the Travel Act and of making false statements to the FBI

(b) Sentenced in November 2009 to one year and one day in prison; case now on appeal

(c) Bourke did not pay bribes directly and lost $8MM on deal

(d) Jury instructed on "conscious avoidance" theory

(e) "We thought [Bourke] knew [about the bribery] and definitely could have known. He's an investor. It's his job to know." (Jury Foreman, *U.S. v. Bourke*)

(f) Bourke's conviction affirmed on appeal in December 2011. Court of Appeals held that evidence was sufficient to establish that Bourke "deliberately avoided confirming his suspicions that Kozeny and his cohorts may be paying bribes."

(g) Court of Appeals also held that it was proper for prosecutors to argue that "Bourke refrained from asking his attorneys to undertake the same due diligence done by [representatives of another investor, who would up deciding not to invest] because Bourke was consciously avoiding learning about the bribes."

C. There is very little case law, so risks often have to be evaluated on the basis of DOJ's and SEC's one-sided and often expansive interpretations of the FCPA

IX. Ways to mitigate FCPA risk

Each fund's FCPA compliance program should be commensurate with the nature and extent of its interaction with foreign government officials and its level of FCPA risk

A. Fund level

1. Written policies and procedures (should address: gifts, entertainment, hospitality, travel; retention of and dealings with agents/third-party intermediaries; facilitation payments; political and charitable contributions)

2. Designation of FCPA compliance officer

3. Training of relevant personnel

4. Employee certifications

5. Due diligence on/contractual representations by third-party intermediaries

(a) Full compliance (no materiality threshold)

(b) No financial interest on part of government official

(c) Termination rights

B. Acquisition/investment due diligence

1. Risk assessment (key factors include: extent of the company's interaction with foreign governments; use of agents/third-party intermediaries; operating in high-risk jurisdictions)

2. Review of target's FCPA/anti-bribery compliance program (if it has one)

3. Examination of agent/consultant relationships (vetting third-party intermediaries via: due diligence, approval requirements, documentation)

4. Background checks on principals

5. Questions regarding any FCPA/anti-bribery issues, investigations, etc.

6. FCPA contractual representations and warranties

C. Ongoing FCPA Compliance for Portfolio Companies

1. Establish compliance program if one doesn't exist

2. Ensure that the program has elements appropriate for the nature of business (e.g., written policies and procedures, FCPA compliance officer, training of employees, employee certifications, due diligence on third-party intermediaries, periodic testing)

D. FCPA opinion procedure

1. Can request DOJ opinion as to whether certain prospective conduct, such as proposed business ventures involving foreign officials, violates the FCPA

2. DOJ reviews and must issue an opinion within 30 days after a request is deemed complete.

3. Infrequently used

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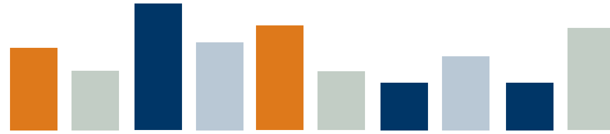

Investment Management Hot Topics

4. Additional Materials

Recent FCPA Developments Highlight Risk of Individual Liability

BETTY SANTANGELO, GARY STEIN, SUNG-HEE SUH, AND PETER H. WHITE

Two recent developments underscore the extensive reach of the U.S. Foreign Corrupt Practices Act, which can extend criminal liability to U.S. and non-U.S. citizens alike and to circumstances where an individual does not have actual knowledge that a bribe was paid. The authors of this article describe these developments.

Two recent developments bring the potential for individual criminal liability under the U.S. Foreign Corrupt Practices Act ("FCPA") back into the spotlight. These developments underscore the extensive reach of the FCPA, which can extend criminal liability to U.S. and non-U.S. citizens alike and to circumstances where an individual does not have actual knowledge that a bribe was paid.

- In *United States v. Kozeny*,[1] the U.S. Court of Appeals for the Second Circuit last December affirmed the FCPA conviction of Frederic Bourke based on his participation as an investor in a bribery scheme involving a privatization venture in Azerbaijan. Of particular importance is the court's ruling that Bourke could properly have been convicted on a theory that he "consciously avoided" knowing that bribes

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Betty Santangelo, Gary Stein, Sung-Hee Suh, and Peter H. White are partners at Schulte Roth & Zabel LLP. Katherine Earnest and Michael Sanocki, associates at the firm, contributed to the article. The authors may be contacted at betty.santangelo@srz.com, gary.stein@srz.com, sung-hee.suh@srz.com, and pete.white@srz.com, respectively.

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were being paid, even if he lacked actual knowledge of the bribery scheme. The court's ruling highlights the importance of conducting due diligence — and, if necessary, declining to participate in a transaction — if and when there are red flags indicating that a bribery scheme may be afoot.

- Also in December 2011, the U.S. Department of Justice ("DOJ") indicted several former executives and agents of Siemens AG and its subsidiaries.[2] Even though none of the defendants is a U.S. citizen, and even though the alleged bribery scheme related to efforts by the Argentine subsidiary of a German company to win a contract with the Argentine government, the defendants now find themselves accused of violating U.S. law and facing the prospect of extradition, prosecution and possible imprisonment in the United States. This case thus illustrates the long jurisdictional reach of the FCPA.

UNITED STATES v. KOZENY: THE IMPORTANCE OF DUE DILIGENCE ON FOREIGN INVESTMENTS

The Bourke prosecution arises from an alleged scheme to bribe senior government officials in Azerbaijan in the 1990s in connection with the planned privatization of the state-owned oil company, SOCAR. The alleged architect of the bribery scheme was Viktor Kozeny, an international businessman whose involvement in prior shady dealings had earned him the nickname the "Pirate of Prague." Kozeny organized an investment consortium — which included Bourke, the co-founder of the handbag maker Dooney & Bourke — that invested hundreds of millions of dollars to purchase vouchers issued by the Azerbaijani government that could be used to bid at auction for shares of SOCAR and other state-owned companies. Kozeny allegedly engineered the payment of tens of millions of dollars and vouchers to various Azerbaijani officials, including the president, that were intended to encourage the president to approve SOCAR's privatization. Nevertheless, SOCAR was not privatized, and by the end of 1998 Kozeny lost all hope in the venture, resulting in large losses to the investors.

The government indicted Bourke in 2005 for participating in Kozeny's scheme to bribe Azerbaijani officials. Following a trial, Bourke was

convicted in 2009 of conspiring to violate the FCPA, despite his assertion that he lacked knowledge of the bribery scheme, and was sentenced to one year in prison. Although the government's primary theory at trial was that Bourke had actual knowledge of the bribery scheme, the jury was also instructed that it could convict Bourke on a "conscious avoidance" theory. In other words, the jury was allowed to find that Bourke possessed the requisite guilty knowledge if he was aware of a "high probability" that bribes were being paid to Azerbaijani officials but "consciously and intentionally avoided confirming that fact."[3]

On appeal, Bourke argued, among other things, that the conscious avoidance instruction was improper because there was no factual predicate for such a theory in the evidence at trial. The Court of Appeals rejected that argument, citing the following evidence to support the conscious avoidance charge:

- Bourke was aware of pervasive corruption in Azerbaijan;
- Bourke knew of Kozeny's reputation as the "Pirate of Prague;"
- Bourke created corporations to shield himself and other American investors from potential liability from payments made in violation of the FCPA, and joined the boards of the American companies instead of the main company;
- Bourke, in a taped conference call with a fellow investor and attorneys, voiced concerns that Kozeny and his associates were bribing officials;
- Bourke's attorney advised him that if he thought there might be bribes paid, he could not look the other way.

Viewing this evidence in its totality, the court found that a "rational juror could conclude Bourke deliberately avoided confirming his suspicions that Kozeny and his cohorts may be paying bribes."[4]

The court also rejected Bourke's argument that the conscious avoidance charge improperly allowed the jury to convict him based on mere negligence. The court pointed to evidence that other prospective investors "with access to the same sources of information available to Bourke

were able to figure out Kozeny's scheme and avoid participating." Specifically, another prospective investor's representatives, after conducting due diligence on the transaction and Kozeny's past reputation, had advised their client not to invest because there could be an FCPA issue. The court held that "[i]t was entirely proper for the government to argue that Bourke refrained from asking his attorneys to undertake the same due diligence done by [the representatives of the other investor] because Bourke was consciously avoiding learning about the bribes."[5]

The *Kozeny* ruling thus highlights the importance of conducting FCPA due diligence, particularly in transactions in high-risk jurisdictions. Bourke's failure to conduct due diligence, in the face of highly suspicious circumstances suggesting that Kozeny was involved in a corrupt scheme, was viewed by the court as affirmative evidence of Bourke's guilty knowledge. While each case will depend on its own facts and circumstances (and while there was additional evidence introduced at Bourke's trial suggesting that he had actual knowledge of Kozeny's scheme), the message of the *Kozeny* decision seems clear. Conducting appropriate due diligence is an essential risk mitigation strategy for both companies and individuals to avoid potentially crushing liability, including criminal penalties, under the FCPA.

THE SIEMENS INDICTMENT: THE LONG ARM OF THE FCPA

In December 2008, Siemens AG and three of its subsidiaries, including its Argentine subsidiary, pled guilty to criminal violations of the FCPA as well as civil charges brought by the Securities and Exchange Commission ("SEC"). Siemens paid a record-breaking $800 million in criminal fines and civil penalties to the DOJ and SEC, on top of an additional $800 million to settle charges brought by Munich prosecutors.[6] Yet, as the December 2011 indictment shows, the Siemens corporate settlement does not mean the case is over as far as individual Siemens employees are concerned.

A total of eight individuals, including six former Siemens employees and two alleged former agents, were named in the indictment, which was filed in federal district court in Manhattan.[7] All of the defendants are citizens of Germany, Israel, or Argentina. The scheme detailed in the indictment involved paying Argentine government officials $60 million in

bribes to win a $1 billion contract to produce Argentine national identity cards. The defendants allegedly disguised the various bribes given to Argentine government officials to secure the project by entering into consulting "contracts" with at least 17 conduit entities controlled by intermediaries and Argentine government officials. These entities were located in off-shore locations, such as the Bahamas; the British Virgin Islands; Guernsey in the Channel Islands; the Cayman Islands; Panama; Switzerland; and Uruguay. While these entities appeared to provide legitimate business consulting services, in reality they provided no such services.[8]

According to the indictment, when the project stalled in 2001, the defendants continued to pay additional bribes in an attempt to kick-start it, using the bribes to secure additional favor with Argentine officials for future projects. When it became evident that the project would not be restarted, the defendants allegedly commenced a fraudulent arbitration proceeding in Washington, D.C. demanding nearly $500 million from the Argentine government, all the while concealing the fraudulent activity in connection with the project. In 2007, Siemens was awarded $218 million in the arbitration.[9]

The defendants are alleged to have utilized various methods to promote or conceal the conspiracy, which included:

- Using cash and withdrawals of funds from general purpose accounts to make bribe payments;
- Using deceptive accounting maneuvers to conceal the bribes;
- Characterizing bribes in corporate books and records as "consulting fees;"
- Using off-books accounts and transferring funds through accounts held by conduit entities, as well as U.S. bank accounts, to conceal corrupt payments;
- Using accounts controlled by Siemens AG business divisions and subsidiaries having no connection to the identity card project as a way to conceal the payments;
- Issuing false invoices to Siemens that requested payment for services and authorizing reimbursement for those services;

- Circumventing Siemens AG's compliance and ethics program, including internal and external audits aimed at detecting criminal conduct;
- Disguising bribe payments as funds used to settle an arbitration proceeding;
- Paying off witnesses.[10]

The jurisdictional basis for the FCPA anti-bribery charges is two-fold. First, the indictment relies on the part of the FCPA that applies to U.S. issuers.[11] The indictment alleges that the defendants were "officers, directors, employees and agents of an issuer," namely, Siemens AG, whose ADRs began trading on the New York Stock Exchange in 2001, and hence fall within the scope of the statute.[12] Yet it appears from the indictment that, with the exception of one defendant, who was a director of Siemens AG, the defendants were officers, directors, employees, or agents of Siemens' Argentine subsidiary or another Siemens subsidiary, not of Siemens AG. The government's theory may be that, even though not directly employed by an issuer, the defendants nevertheless should be viewed as agents of an issuer for purposes of the FCPA.

Second, the indictment relies on the prong of the FCPA that applies to non-U.S. persons,[13] alleging that the defendants fall within the scope of this provision because they agreed to commit acts in furtherance of the bribery scheme "while in the territory of the United States."[14] While the vast majority of the alleged wrongful conduct took place in Argentina and Germany, certain acts are alleged to have occurred in the United States, including the use of U.S. bank accounts to funnel at least $25 million of the bribe payments to Argentine officials. The indictment also alleges that a meeting in New York between two of the defendants, and the fraudulent arbitration proceedings in Washington, were additional acts in furtherance of the conspiracy that took place in the United States.[15]

As the indictment against these individuals reflects, U.S. officials take a very broad view of the jurisdictional reach of the FCPA. There is a dearth of judicial decisions on the subject. Corporations that have been the subject of FCPA investigations generally have chosen to enter into settlements with the DOJ and have not contested the DOJ's assertion of jurisdiction. Now that the DOJ has been more actively pursuing prosecutions of indi-

viduals, we may see more litigation and more court rulings clarifying just how far the territorial reach of the FCPA does extend.

CONCLUSION

In recent years, DOJ officials have emphasized the importance of criminal prosecution of individuals who violate the FCPA, describing it as a "critical part" and a "cornerstone" of their FCPA enforcement strategy. Warning that the DOJ "vigorously prosecut[es] individual defendants who violate the FCPA," these officials have added that "we do not hesitate to seek jail terms for these offenders when appropriate."[16] The Bourke and Siemens prosecutions illustrate that policy and highlight the critical importance of conducting effective due diligence whenever an investment or transaction involves a risk of bribery of foreign officials.

NOTES

[1] *United States v. Kozeny*, No. 09-4704-cr(L), 2011 WL 6184494 (2d Cir. Dec. 14, 2011).

[2] Indictment, *United States v. Uriel Sharef, et al.*, No. 11 Cr. 1056 (DLC) (S.D.N.Y. Dec. 12, 2011).

[3] *Kozeny*, 2011 WL 6184494, at *6-7.

[4] *Id.* at *7-8.

[5] *Id.* at *9.

[6] DOJ Press Release, Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations and Agree to Pay $450 Million in Combined Criminal Fines (Dec. 15, 2008) *(available at* http://www.justice.gov/opa/pr/2008/December/08-crm-1105.html).

[7] The following day, the SEC filed a related civil complaint against six of the same defendants and another formers Siemens executive, charging them with FCPA violations. Complaint, *SEC v. Uriel Sharef, et al.*, No. 11 Civ. 9073 (SAS) (S.D.N.Y. Dec. 13, 2011).

[8] Indictment, *United States v. Uriel Sharef, et al.*, ¶¶ 18-21; Edward Wyatt, *Former Siemens Executives Are Charged With Bribery*, N.Y. Times, Dec. 13, 2011.

[9] Indictment, *Uriel Sharef, et al.*, No. 11 Cr. 1056, ¶¶ 19, 49-52.

[10] *Id.* ¶ 21.
[11] 15 U.S.C. § 78dd-1.
[12] Indictment, *Uriel Sharef, et al.*, No. 11 Cr. 1056, ¶¶ 10-11, 54.
[13] 15 U.S.C. § 78dd-3.
[14] Indictment, *Uriel Sharef, et al.*, No. 11 Cr. 1056, ¶ 55.
[15] *Id.* ¶¶ 38, 41, 49, 59.
[16] DOJ News, Statement of Acting Deputy Assistant Attorney General Greg Andres Before Senate Judiciary Subcommittee on Crime and Drugs, Nov. 30, 2010 (*available at* http://www.justice.gov/criminal/pr/testimony/2010/crm-testimony-101130.html); DOJ Press Release, Remarks by Lanny A. Breuer, Assistant Attorney General for the Criminal Division, at the American Bar Association National Institute on White Collar Crime, (Feb. 25, 2010) (*available at* http://www.justice.gov/criminal/pr/speeches-testimony/2010/02-25-10aag-AmericanBarAssosiation.pdf).

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The FCPA and AML Statutes

The Prosecutor's Combined Weapon of Choice

Part One of a Two-Part Article

By Betty Santangelo and Eric Brin

Although criminal prosecutions under the Foreign Corrupt Practices Act of 1977, as amended, 15 U.S.C. §§ 78dd-1, *et seq*. (FCPA) and the U.S. anti-money laundering (AML) laws have developed differently over the years, a review of recent enforcement actions reveals that prosecutions under these criminal schemes have started to converge. It is no secret that the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) have placed increased emphasis on prosecutions for FCPA and AML violations. What *is* new, however, is that the DOJ has started to use the statutes in tandem to ensure the success of its criminal prosecutions. Some of the more recent cases over the past 12 to 18 months demonstrate that the dual use of these statutes has been successful in meeting this goal.

Betty Santangelo is a partner practicing in the New York office of Schulte Roth & Zabel LLP. She is a former assistant U.S. attorney for the Southern District of New York who currently concentrates her practice on white-collar criminal defense and securities enforcement. **Eric Brin** is an associate with the firm.

In proclaiming the DOJ's firm commitment to investigating and prosecuting foreign bribery, Assistant Attorney General Lanny A. Breuer declared, at the 24th National FCPA Conference, that "FCPA enforcement is stronger than it's ever been … [and] we are in a new era of FCPA enforcement." Consistent with that approach, 2010 witnessed an 85% increase in FCPA enforcement actions over 2009, which was itself a record year. The DOJ brought 48 enforcement actions in 2010, compared with 26 actions in 2009. *See* FINRA Annual Conference, FCPA Compliance, May 24, 2011. The same is true for AML enforcement. In 2010, the number of federal banking fines for AML violations in the United States, according to MoneyLaundering.com, rose by nearly fourfold, while the total dollar amount of the monetary penalties rose to over $660 million. Moreover, the DOJ's combined focus on FCPA and AML is exemplified by its 2010 Kleptocracy Asset Recovery Initiative, which targets the proceeds of foreign official corruption that have been laundered into or through the United States.

While the government has clearly stepped up enforcement of both the FCPA and AML regulations independently, notably, prosecutors appear to be using these provisions concurrently in an increasing number of enforcement actions. An understanding of how these two sets of criminal statutes work together can help a defense lawyer in approaching the handling of these cases. In analyzing the "why" behind this emerging trend, it is best to begin with some background of the FCPA and AML provisions.

Legislative Background

The FCPA was enacted in 1977 as a result of SEC investigations into over 400 U.S. companies admittedly making questionable payments to foreign officials, as well as Congress' concern with foreign bribery and its desire to restore public confidence in the integrity of the American business system. It was amended by the International Anti-Bribery and Fair Competition Act of 1998, which was designed to implement the anti-bribery conventions of the Organization for Economic Cooperation and Development. In general, the FCPA prohibits corrupt payments to foreign officials for the purpose of obtaining or keeping business. The anti-bribery provisions of the FCPA make it unlawful for U.S. persons or companies, and foreign issuers of U.S.-registered securities, to make a corrupt payment to a foreign official for the purpose of obtaining or retaining business.

The Bank Secrecy Act, 31 U.S.C. §§ 5311 *et seq.*, which was enacted in 1970 as a result of the need to prevent illegally obtained funds from being deposited into the U.S. financial system, established a number of transaction reporting requirements to assist government agencies in detecting and preventing money laundering. More relevantly, Title 18 U.S.C. sections 1956 and 1967 (the criminal money laundering statutes) were enacted in 1986, making money laundering a crime in and of itself for the first time. Section 1956 prohibits conducting or attempting to conduct a financial transaction involving the proceeds of specified unlawful activity (SUA) for the purpose of promoting or concealing an SUA. Section 1957 prohibits engaging or attempting to engage in a monetary transaction of more than $10,000 in proceeds of specified unlawful activity. The Bank Secrecy Act and the criminal money laundering statutes have been amended several times over the years, but most significantly by the USA PATRIOT Act in 2001, after the events of 9/11. *See* Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Pub. L. No. 107-56, 115 Stat. 296 (2001).

In 1992, the FCPA was added as an SUA under the criminal money laundering statutes and, in 2011, the PATRIOT Act specifically added to the list of SUAs, among others, offenses against a foreign nation, with respect to a financial transaction occurring in whole or in part in the United States, involving the bribery of a public official, or the misappropriation, theft, or embezzlement of public funds by or for the benefit of a public official.

Moreover, conspiracy charges pursuant to 18 U.S.C section 371 have also historically been used in FCPA and AML enforcement actions. The DOJ uses this law, among other things, to prosecute individuals for conspiring to commit FCPA or AML violations in cases where two or more persons conspire to commit the underlying offense, and one or more such persons commit an act in furtherance of the conspiracy. As discussed below, prosecutors also frequently combine the FCPA and AML laws as objects of the conspiracy.

AML and FCPA Legislation: The Convergence

The first significant instance of the government's concurrent use of FCPA and AML laws occurred in 2003 when prosecutors charged Hans Bodmer, a Swiss lawyer, with conspiracy to launder money and to violate the FCPA's anti-bribery provisions for participating in a scheme to bribe Azerbaijan government officials to secure a controlling interest in the State Oil Company of Azerbaijan (SOCAR). *See United States v. Bodmer*, 342 F. Supp. 2d 176 (S.D.N.Y. 2004). U.S. District Court Judge Shira Scheindlin dismissed the FCPA charges against Bodmer because the pre-1998 version of the FCPA had not given him fair notice that its criminal penalties applied to the conduct of a non-resident foreign national who acted as an agent for a U.S. concern. But the district court refused to dismiss the money laundering charge, finding that the alleged conduct was sufficient to substantiate the necessary criminal intent and noting that "if immunity from the FCPA's criminal penalties automatically conferred non-resident foreign nationals with immunity from the money laundering statute, these non-resident foreign nationals could openly serve as professional money launderers of proceeds derived from violations of the FCPA, without repercussion." The outcome of this case involved nuances such as the effect of FCPA amendments on foreign nationals and his extradition from South Korea. Yet, the government's joint use of these two statutes proved successful. Bodmer subsequently pleaded guilty to conspiracy to launder money, and facing the potential of a 10-year prison sentence, he cooperated with the government. Two years later Frederic Bourke and Viktor Kozeny, two alleged co-conspirators, were charged with FCPA and AML violations relating to their participation in the same investment consortium allegedly designed to bribe Azerbaijan officials. Bourke was acquitted of conspiracy to commit money laundering, but found guilty of conspiracy to violate the FCPA following a six-week trial. Kozeny is fighting extradition proceedings. *See United States v. Viktor Kozeny, et al.*, 05-CR-518 (S.D.N.Y. 2005).

Since 2003, AML charges have rapidly become a mainstay of FCPA enforcement actions. Some of the reasons a prosecutor may choose to bring AML charges in an FCPA-type enforcement action include: 1) extending the jurisdictional reach so as to include foreign bribe recipients who are not covered under the FCPA; and 2) bolstering settlement leverage by increasing the potential for higher sentences and fines.

Next month, we will discuss jurisdictional and sentencing factors that arise in FCPA/AML cases, along with specific cases in which both FCPA and AML charges were brought.

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Schulte Roth&Zabel

Schulte Roth & Zabel LLP
919 Third Avenue, New York, NY 10022
212.756.2000 tel | 212.593.5955 fax | www.srz.com
New York | Washington DC | London

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The FCPA and AML Statutes

Prosecutors Increasingly Combining Charges, to Great Effect

Part Two of a Two-Part Article

By Betty Santangelo and Eric Brin

Last month, we began to discuss how federal prosecutors are increasingly combining charges under the Foreign Corrupt Practices Act of 1977, as amended, 15 U.S.C. §§ 78dd-1, *et seq.* ("FCPA") and the U.S. anti-money laundering ("AML") laws to reach more defendants and achieve greater success in their criminal prosecutions. We continue herein.

Jurisdictional Reach

Amendments made to the FCPA in 1998 expanded its reach so that territorial jurisdiction could be asserted over foreign companies and nationals. *See* 15 U.S.C. § 78dd-3. Since 1998, a foreign company or person has been subject to the FCPA for taking any act in furtherance of the corrupt payment while within the territory of the United States. However, foreign officials who do no more than receive bribes from a covered person or entity are beyond the reach of the FCPA.

Notwithstanding this limitation, an example of the DOJ's aggressive effort to combat foreign corruption, even when FCPA charges are inapplicable, is the prosecution of Juthamas Siriwan in the Central District of California. *United States v. Siriwan*, No. 09-CR-0081 (C.D.Cal. 2009). Siriwan, a senior official of the Tourism Authority of Thailand ("TAT"), was charged with money laundering and conspiracy to launder money in violation of 18 U.S.C. §§ 1956(a)(2)(A) and (h). The charges stem from bribes paid to her in violation of the FCPA, as well as the anti-corruption laws of Thailand. Film producers Gerald and Patricia Green were convicted of substantive FCPA violations for paying Siriwan $1.8 million in bribes to influence the granting of $14 million of TAT funds relating to the Bangkok International Film Festival. Under the FCPA, Siriwan is not prohibited from receiving bribes, yet the Department of Justice ("DOJ") creatively decided to bring AML charges in order to extend its otherwise insufficient jurisdictional reach. It will not be known for some time whether the money-laundering theory will be sustained in court. Additionally, in the Haiti Teleco case (09-CR-201010 (S.D.Fl. 2009)), involving bribes to two Haitian public officials, Robert Antoine and Jean Rene Duperval, the foreign officials were charged with conspiring to commit money laundering, essentially enabling the prosecutor to avoid the fact that foreign officials who are recipients of bribes cannot be charged under the FCPA.

Likewise, in *United States v. Lazarenko*, CR 00-0284-MJJ (N.D.Cal. 2001) prosecutors in the Northern District of California used money-laundering charges to reach a foreign national to fight foreign bribery and corruption without charging an FCPA violation. In that case, the government charged Pavlo Lazarenko, a former Ukrainian prime minister who was extradited to the United States, with engaging in a series of corrupt business transactions that defrauded the Ukrainian people of millions of dollars. Although his corruption was the root of the criminal charges against him, Lazarenko was charged with money laundering as a result of transferring funds from one foreign bank account to another, including bank accounts in the United States. A federal jury in San Francisco found Lazarenko guilty, and he was sentenced to nine years in federal prison.

These cases demonstrate the government's creativity in using AML statutes when it cannot pursue FCPA charges.

Increased Sentences and Fines

The criminal penalties for money laundering are severe, often exceeding the penalties under the FCPA and foreign anti-bribery laws. A violation of the FCPA carries a five-year prison term, as well as a criminal fine of up to $100,000 for each FCPA violation. By contrast, an AML violation carries a maximum term of imprisonment of 20 years and a fine of up to $500,000, or twice the value of the property involved in the transaction, whichever is greater. In addition, the Alternative Fines Act, 18 U.S.C. § 3571(d), which authorizes a fine of up to twice the gain from an unlawful activity, applies to both FCPA and AML offenses. Moreover, although the Federal Sentencing Guidelines are no longer mandatory, recommended FCPA and AML sentences are determined pursuant to a sentencing table that uses offense level and criminal history. AML sentences are additionally governed by § 2S1.1 of the U.S. Sentencing Guidelines, which tends to lengthen a prescribed sentence. Accordingly, in charging FCPA

Betty Santangelo is a partner practicing in the New York office of Schulte Roth & Zabel LLP. She is a former assistant U.S. attorney for the Southern District of New York who currently concentrates her practice on white-collar criminal defense and securities enforcement. **Eric Brin** is an associate with the firm.

violations, the government's inclusion of AML charges serves to increase the potential penalties applicable to the defendant.

Present and Future: The Cases and Predictions

From the *Bodmer* indictment in 2003 until a few years ago, prosecutors' concurrent use of the FCPA and AML provisions was limited and sporadic. There were only a few prosecutions that included charges for both AML and FCPA violations. Since 2007, there have been at least 17 such prosecutions, the majority coming within the last 18 to 24 months. In addition to those cases discussed above, recent notable enforcement actions charging violations of both AML and FCPA provisions include:

- James Tillery and Paul Novak, 08-CR-022 (S.D.Tx. 2008) — Wilbros International executive and consultant accused of making corrupt payments to Nigerian and Ecuadorian officials were charged with FCPA violations, conspiracy to violate the FCPA and conspiracy to commit money laundering. Novak pleaded guilty to one count of conspiracy to violate the FCPA and one substantive count of violating the FCPA, and was sentenced to three years' probation. Tillery is a fugitive.
- Gerald and Patricia Green, 08-CR-59 (C.D.Ca. 2009) — The Greens were involved in a bribery scheme that enabled them to obtain a series of Thai government contracts, including valuable contracts to manage and operate Thailand's annual film festival. Both were charged with FCPA violations, conspiracy to violate the FCPA, money laundering and conspiracy to commit money laundering. A jury found the Greens guilty on all four counts, and both were sentenced to six months' imprisonment and six months' home confinement.
- Nexus Technologies, Inc. (Nguyens), 08-CR-522 (E.D.P. 2009) — The Nguyens conspired to bribe officials of the Vietnamese government in exchange for lucrative contracts to supply equipment and technology to Vietnamese government agencies. Charges included FCPA violations, conspiracy to violate the FCPA, money laundering and conspiracy to commit money laundering. Three former employees and a partner of Nexus Technologies pleaded guilty to both FCPA and AML charges and were sentenced to imprisonment and/or probation.
- John O'Shea, 09-CR-629 (S.D.Tx. 2009) — The general manager of a Texas business, who approved payments to sales representatives in a scheme to bribe Mexican government officials to secure contracts with CFE (Mexico Electric), was charged with FCPA violations, conspiracy to violate the FCPA and conspiracy to commit money laundering. O'Shea's case is currently being litigated.
- Enrique and Angela Aguilar, 10-CR-1031 (C.D.Ca. 2010) — Directors of a Mexican company (Grupo), which allegedly secured contracts with CFE for U.S.-based companies in return for a commission of the proceeds, were charged with FCPA violations, conspiracy to violate the FCPA, money laundering and conspiracy to commit money laundering. Angela Aguilar was convicted of conspiracy to launder money and sentenced to time served (nine months in custody), while Enrique Aguilar remains a fugitive.
- Haiti Teleco Case, 09-CR- 201010 (S.D.Fl. 2009) — Several individuals involved with a Florida-based telecommunications company collectively paid more than $800,000 in bribes to officials of Haiti's state-owned national telecommunications company. Charges against the individuals included FCPA violations, conspiracy to violate the FCPA, money laundering and conspiracy to commit money laundering. A jury found two former top executives guilty of substantive FCPA and AML violations, as well as the corresponding conspiracy charges. These convictions followed guilty pleas by four other defendants; six additional defendants charged with a related scheme are awaiting trial.
- Jorge Granados and Manuel Caceres, 10-CR-20881 (S.D.Fl. 2010) — The CEO and the VP of Miami-based Latin Node, who paid more than $500,000 in bribes to government officials in Honduras to secure telecommunications contracts with Hondutel, were charged with FCPA violations, conspiracy to violate the FCPA, money laundering and conspiracy to commit money laundering. Granados pleaded guilty to one count of conspiracy to violate the FCPA and was sentenced to 46 months in prison. Caceres also pleaded guilty, testified as a cooperating witness in the Granados sentencing, and is to be sentenced on Jan 30, 2012.
- *U.S. v. Goncalves*, 09-CR-00335 (D.D.C. 2010) — This was an undercover operation involving the military and law enforcement products industry, where individuals were indicted for engaging in schemes to bribe African government officials. They were charged with FCPA violations, conspiracy to violate the FCPA and conspiracy to commit money laundering. This case is currently being litigated.

In all of these actions, prosecutors used a combination of the FCPA, the AML laws and charges of conspiracy to violate one or the other statute. Moreover, in seven of the eight enforcement actions described above, the indictment alleged the "specified unlawful activity" under 18 U.S.C. § 1956 as the bribery of a foreign public official.

Conclusion

Whether prosecutors are using FCPA and AML charges together for efficiency purposes, or as a negotiating tactic in furtherance of the government's heightened commitment to rooting out foreign bribery, their convergence is unmistakable.

The effect of this emerging trend on practitioners is important because all signs point to an ever-increasing number of enforcement actions involving both FCPA and AML charges. Most notably, understanding how and why the government is using these statutes may alter one's defense strategy and a defense counsel's approach in plea negotiations.

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Schulte Roth&Zabel

Schulte Roth & Zabel LLP
919 Third Avenue, New York, NY 10022
212.756.2000 tel | 212.593.5955 fax | www.srz.com
New York | Washington DC | London

Government Launches FCPA Inquiry into Investments by Sovereign Wealth Funds in U.S. Banks and Private Equity Firms

BETTY SANTANGELO, GARY STEIN, SUNG-HEE SUH, AND PETER H. WHITE

In this article, the authors explain the Foreign Corrupt Practices Act, its anti-bribery provisions, and the legal risks arising from investments by sovereign wealth funds in U.S. banks and private investment funds. The article also describes actions firms should take to mitigate those risks and avoid potential legal liability and reputational harm.

In recent years, the U.S. Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") have stepped up their enforcement of the anti-bribery provisions of the U.S. Foreign Corrupt Practices Act of 1977 ("FCPA"), imposing record criminal fines and civil penalties, such as the $800 million fine in 2008 against Siemens, the German conglomerate. The DOJ and SEC have declared FCPA enforcement a high priority, bulked up their enforcement teams, and shown a readiness to apply the statute in increasingly expansive and creative ways. Earlier this year, in a development that should be of particular interest to the private investment fund community, the *Wall Street Journal* reported that the SEC is investigating whether banks and private equity firms may have violated the FCPA in their dealings with sovereign wealth funds ("SWFs").[1]

The authors are partners at Schulte Roth & Zabel LLP. They may be contacted at betty.santangelo@srz.com, gary.stein@srz.com, sung-hee.suh@srz.com, and pete.white@srz.com, respectively. The authors wish to thank William I. Friedman, an associate at the firm, for his contributions to this article.

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SWFs have become an increasingly common source of investment capital for private investment funds in recent years, and have also acquired large stakes in major U.S. financial institutions.[2] Private investment funds that raise money from SWFs, or interact in other ways with foreign government agencies or government-owned entities, should be mindful of the legal risks arising from the FCPA and take steps to mitigate those risks and avoid potential legal liability and reputational harm.

THE FCPA AND ITS ANTI-BRIBERY PROVISIONS

The FCPA's anti-bribery provisions broadly apply to any U.S. citizen, U.S. company or U.S. issuer, and even to non-U.S. persons under certain circumstances.[3] The FCPA prohibits bribes offered or paid to any foreign official, foreign political party, official or candidate, or official of a public international organization, in order to assist in obtaining, retaining or directing business.[4] The official who receives the bribe need not be a governmental official in the classic sense, such as the head of a government ministry or agency; the statute broadly defines the term "foreign official" to encompass any officer or employee of any foreign government agency or instrumentality, including government-owned or operated business enterprises.[5]

The FCPA also includes a prohibition on indirect bribery covering any payment made to a third party with knowledge that all or a portion of the payment will be transmitted to a foreign official or any other prohibited party in order to assist in obtaining, retaining or directing business.[6] Under the statute's definition of "knowing" conduct, the entity or individual may be held liable based on awareness of a "high probability" that a payment was being made to a foreign official, even if the entity or individual did not have actual knowledge of that fact.[7] This provision allows the government to prosecute, on a "willful blindness" or "conscious avoidance" theory: use of third party intermediaries such as an agent retained to help the U.S. company obtain business in that country or a foreign joint venture partner.[8] In practice, many unlawful payments prosecuted under the FCPA are made through such third party intermediaries.

The government must also show corrupt intent under the anti-bribery provisions of the FCPA, in that the payment was intended to induce the

recipient to misuse his or her official position or to secure an improper advantage.[9] A person who makes such a payment may be held liable under the FCPA, even if the person did not know the payment violated the statute and even if the payment was solicited by the foreign official.[10] Nor is it a defense that corruption is "how business is done" in the foreign country or that it would have been impossible to obtain a contract with the foreign government unless the payment was made. Moreover, the statute prohibits not only an actual improper payment, but also an offer, promise or authorization of such a payment.[11]

The anti-bribery provisions explicitly carve out payments for the purpose of expediting or securing the performance of a "routine governmental action," such as processing visas or providing phone service or water supply.[12] The FCPA also provides two affirmative defenses to alleged violations of the anti-bribery provisions, which are available for: (1) payments that are lawful under the written laws and regulations of the foreign official's country; or (2) reasonable and bona fide expenditures, such as travel and lodging expenses, incurred by or on behalf of the foreign official, foreign party, party official or candidate and directly related to the promotion, demonstration or explanation of products or services, or to the execution or performance of a contract with a foreign government or agency.[13] These exceptions and defenses are narrowly construed by the DOJ and SEC and their use should therefore be carefully controlled.

PRIVATE INVESTMENT FUNDS ARE EXPOSED TO FCPA RISK

Private investment funds that seek investments from foreign government-owned entities, such as SWFs or state-owned pension plans, are exposed to the risk of violating the FCPA's anti-bribery laws. Because SWFs are owned and operated by foreign governments, all of their directors, officers and employees qualify as foreign officials under the FCPA. Therefore, a private investment fund that makes payments, or offers gifts or entertainment, to insiders at an SWF for the purpose of inducing the SWF to invest in the fund, could face criminal prosecution or civil enforcement liability under the FCPA, as could individual employees of the fund.

Likewise, a private investment fund's use of placement agents or third

party marketers to solicit investments on the fund's behalf from SWFs or other foreign government entities also raises an FCPA risk for the fund and its employees. If the third party intermediary makes an unlawful payment to an insider at the SWF in soliciting an investment for the private investment fund, the fund can face liability if there is evidence that the fund knew about the payments or was aware of "red flags" indicating that such a payment would be made but failed to take steps to stop the activity or investigate further.

There are FCPA risks for private investment funds not only in raising capital, but also in making investments. For example, a private investment fund that acquires a controlling interest in a portfolio company that engages in business overseas with foreign governments, or that enters into a joint venture with a foreign government entity, has exposure to FCPA risk. For a private investment fund acquiring an interest in an overseas business, or in a U.S. company that does business abroad, FCPA violations associated with the target company can be "a little like asbestos," in that the acquiring private investment fund will inherit financial responsibility for any FCPA violations committed prior to the acquisition by the target company.[14] In addition, if the acquired business continues to engage in FCPA violations following the change in ownership, the acquirer not only could face financial repercussions but could also find its own knowledge and conduct questioned in a government investigation. Accordingly, it is essential to conduct appropriate FCPA due diligence on target companies that engage in business with foreign governments.

WAYS TO REDUCE FCPA RISK

The contours of a private investment fund's FCPA compliance program should be commensurate with the fund's potential exposure under the FCPA, which will depend on the nature and extent of its interactions with foreign government entities, the jurisdictions in which the fund operates, the fund's use of placement agents and other third party intermediaries, and other factors. As a general matter, private investment funds should consider undertaking certain measures to reduce the fund's exposure to FCPA risk, such as:

- The promotion of an organizational culture among the private investment fund's employees, agents and business partners that encourages ethical conduct and a commitment to compliance with the law;
- The adoption of a written FCPA compliance policy and procedures that prohibit bribery and require relevant employees to certify, on an annual or other periodic basis, their compliance with the fund's FCPA policy and procedures;
- The delegation of operational responsibility for the private investment fund's FCPA compliance policy and procedures to one or more designated personnel, who should report periodically to management on the effectiveness of the program;
- FCPA training on a periodic basis for management and all personnel who have been identified by the fund as likely to face FCPA-related issues in order to ensure that such persons are aware of the FCPA and its restrictions and the fund's FCPA compliance policy and procedures; and
- The maintenance of accurate books and records of all transactions that, directly or indirectly, involve gifts or payments to foreign officials.

Private investment funds that use placement agents, third party marketers or other intermediaries in dealing with SWFs and other foreign government entities should consider taking certain additional steps, as set forth below, to mitigate the fund's FCPA risk:

- Provisions in the firm's FCPA policy and procedures that set forth a process for vetting third party intermediaries, and that require the approval of designated senior business executives and/or in-house legal or compliance personnel, before the intermediary is retained by the fund;
- Pre-retention due diligence of third party intermediaries to ensure that the intermediary is legitimate and reputable and that there are no red flags indicating that the intermediary would be prepared to pay bribes to foreign officials;

- Appropriate contractual representations with third party intermediaries relating to compliance with the FCPA and relevant foreign anti-corruption laws; confirming that no foreign official is an owner of or otherwise has a financial interest in the intermediary; and providing for termination as a result of any breach of applicable anti-corruption laws; and
- Periodic certifications from the third party intermediary attesting to the intermediary's compliance with the FCPA and all other relevant foreign anti-corruption laws.

A firm's FCPA policy and procedures should also address the subject of gifts and business entertainment. There is no dollar threshold or other formula for distinguishing permissible from impermissible gifts and entertainment under the FCPA. Providing a small, non-cash gift of nominal value, or paying for a business-related lunch or dinner, should be permissible so long as it is not designed to influence the foreign official's action or to obtain an improper advantage. To mitigate risk in this area, a firm's policy should set forth objective guidelines and pre-approval requirements. The gift or expenditure should also be permissible under both the foreign country's law and the guidelines of the employer of the foreign governmental official or employee.

While every private investment fund's FCPA compliance needs will differ, these basic measures should help substantially to reduce the likelihood that the private investment fund or its employees will become the target of an investigation or action by the DOJ or the SEC.

NOTES

[1] *See* Dionne Searcey & Randall Smith, "SEC Probes Banks, Buyout Shops Over Dealings With Sovereign Funds," *Wall Street Journal*, Jan. 14, 2011.
[2] *See* "Sovereign Wealth Funds Investing in Hedge Funds," June 1, 2010, www.hedgefundmarketing.org; Mina Kimes, "Sovereign Wealth Funds on the Hunt," *Fortune*, Dec. 23, 2009.
[3] The FCPA's anti-bribery provisions include three separate prongs, applicable to (1) U.S. issuers, *see* 15 U.S.C. § 78dd-1, (2) "domestic concerns" (U.S.

citizens and companies), *see* 15 U.S.C. § 78dd-2, and (3) any person other than U.S. issuers and domestic concerns, see 15 U.S.C. § 78dd-3. Under the last prong, the FCPA applies to non-U.S. individuals and entities who commit an act in furtherance of an unlawful bribe while in the territory of the United States. *See* 15 U.S.C. § 78dd-3(a). The DOJ broadly interprets the statute to reach foreign persons who, while never entering the United States, cause an act in furtherance of the bribe to take place within the United States.

[4] 15 U.S.C. § 78dd-1(a); 15 U.S.C. § 78dd-2(a); 15 U.S.C. § 78dd-3(a).

[5] 15 U.S.C. § 78dd-1(f)(1)(A); 15 U.S.C. § 78dd-2(h)(1)(2)(A); 15 U.S.C. § 78dd-3(f)(2)(A). *See United States v. Aguilar*, __ F. Supp. 2d ___ , 2011 WL 1792564 (C.D. Cal. Apr. 20, 2011) (rejecting defense argument that Congress did not intend employees of state-owned companies to be covered by the FCPA).

[6] 15 U.S.C. § 78dd-1(a)(3); 15 U.S.C. § 78dd-2(a)(3); 15 U.S.C. § 78dd-3(a)(3).

[7] 15 U.S.C. § 78dd-1(f)(2); 15 U.S.C. § 78dd-2(h)(3); 15 U.S.C. § 78dd-3(f)(3).

[8] *See United States v. Kozeny*, 664 F. Supp. 2d 369, 385 n.130 (S.D.N.Y. 2009).

[9] 15 U.S.C. § 78dd-1(a); 15 U.S.C. § 78dd-2(a); 15 U.S.C. § 78dd-3(a).

[10] *See United States v. Kay*, 513 F.3d 432, 447-48 (5th Cir. 2007); *Stichting Ter Behartiging v. Schreiber*, 327 F.3d 173, 183 (2d Cir. 2003); S. Rep. No. 114, 95th Cong., 1st Sess., at 11 (1977).

[11] 15 U.S.C. § 78dd-1(a); 15 U.S.C. § 78dd-2(a); 15 U.S.C. § 78dd-3(a).

[12] 15 U.S.C. § 78dd-1(b),(f)(3); 15 U.S.C. § 78dd-2(b),(h)(4); 15 U.S.C. § 78dd-3(b)(f)(4).

[13] 15 U.S.C. § 78dd-1(c); 15 U.S.C. § 78dd-2(c); 15 U.S.C. § 78dd-3(c).

[14] *See* Mark Brzezinski, "That Bribe Could Be Costly," *New York Times*, Nov. 10, 2010.

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Sentencing of Individuals in FCPA Cases

By Gary Stein

As part of their stepped-up enforcement of the Foreign Corrupt Practices Act (FCPA) in recent years, Justice Department officials have emphasized the importance of prosecuting — and sending to prison — individual executives who violate the statute. Calling "aggressive prosecution of individuals" a "cornerstone of our FCPA enforcement policy" in a speech last year, Assistant Attorney General Lanny Breuer warned that "the prospect of significant prison sentences for individuals" should "make clear to every corporate executive" that they will be held "personally accountable for FCPA violations."

The DOJ exercises virtually unlimited discretion in deciding who gets charged in FCPA cases and, for all practical purposes, in deciding the amount of the financial penalty imposed against corporate violators. But sentencing of individual defendants, particularly after *United States v. Booker*, 543 U.S. 220 (2005), is ultimately a matter of judicial, not prosecutorial, discretion. And it has become apparent that there is a wide and growing rift between the views of the DOJ and the courts as to the appropriate sentences for individual violators in FCPA cases.

Cases in Point

Over the past year or so, the courts have delivered a series of stunning rebukes to federal prosecutors' efforts to obtain lengthy prison sentences for FCPA violators:

- Prosecutors in the Southern District of New York sought a ten-year sentence for Frederic Bourke, who was convicted after a hard-fought trial involving a privatization venture in Azerbijan. The court sentenced Bourke to one year and one day in prison.
- Prosecutors in the Central District of Los Angeles were equally disappointed in the six-month sentences meted out to Gerald and Patricia Green after another high-profile FCPA trial. Prosecutors had asked that each receive 10 years for bribing Thai officials in order to secure rights to produce the annual Bangkok Film Festival.
- A district judge in the Eastern District of Pennsylvania rejected the 168–210 month Guidelines sentence prosecutors recommended for Nam Nguyen, the lead defendant in a Vietnam bribery case. Nguyen was instead sentenced to 16 months. His co-defendant, Am Nguyen, received a nine-month sentence, likewise well below the 87-108 months recommended by prosecutors.

At each of these five sentencings, the government argued emphatically that a lengthy sentence was necessary to punish the defendant's conduct and deter others in the business community from violating the FCPA. And in each case, the court imposed a sentence dramatically below the applicable Guidelines range amounting to roughly 10%, or less, of the government's recommended sentence.

A similar pattern can be seen in recent sentencings of cooperators in FCPA cases. While moving for a downward departure under Section 5K1.1, prosecutors have nonetheless urged courts to sentence cooperators to substantial jail terms. Still, in five separate sentencings over the past year, the courts have refused to do so:

- The two cooperators in the Vietnamese bribery case, Kim Nguyen and Joseph Lukas, were both sentenced to probation, even though the government sought jail time for both.
- Two former executives of the Wilbros Group who cooperated with the government, Jason Edward Steph and Jim Bob Brown, were sentenced in the Southern District of Texas to 15 months and one year and one day in prison, respectively, despite government recommendations that they be sentenced to 45 months and 30 months, respectively.
- Bobby Jay Elkin, a cooperator in a case involving the Alliance One tobacco company, was sentenced to probation in the Western District of West Virginia, notwithstanding the prosecution's request for a 38-month sentence.

The Statistics

The evidence of judicial reluctance to impose harsh sentences in FCPA cases is more than anecdotal; it is statistical as well. Over the past four years, approximately 58% of all federal sentences were within the Guidelines range and 40% were below the range, according to U.S. Sentencing Commission data. *See* U.S. Sentencing Comm'n, Sourcebook of Federal Sentencing Statistics, FY 2007-2010. In FCPA cases, however, the opposite is true: a Guidelines sentence is the exception rather than the norm. Since 1998, a total of 36 individuals have been sentenced in FCPA cases. Only nine of the 36 defendants, or 25%, received sentences within the Guidelines range. The remaining 27 defendants — a remarkable 75% of the total — were sentenced below the range. Post-*Booker*, the percentage of below-Guidelines sentences is even higher: 81%. (Moreover, two of the seven defendants sentenced within the Guidelines, Juan Diaz and Charles Jumet, may yet receive a lower sentence, as they have been cooperating with the government in hopes of obtaining a Rule 35 post-sentencing motion.)

The unusually high percentage of below-Guidelines sentences in FCPA cases reflects, to some extent, the disproportionate number of FCPA cooperators. Half of the FCPA defendants received the benefit of a 5K1.1 departure motion from

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Gary Stein, a member of this newsletter's Board of Editors, is a partner in the New York office of Schulte Roth & Zabel LLP. **Eric Brin**, an associate at the firm, assisted in the preparation of this article.

the government. This compares with 13% of federal criminal defendants overall. Yet even non-cooperating defendants are sentenced more leniently in FCPA cases. Nine of the 18 non-cooperators, (eight of 13 post-*Booker*) received a below-Guidelines sentence.

The prevalence of below-Guidelines sentences in FCPA cases also reflects the nature of the crime: bribery. In federal bribery offenses of all types (not just FCPA prosecutions), courts have imposed below-Guidelines sentences 61% of the time. Bribery, it seems, is viewed by the courts as less deserving of Guidelines-level punishment than other federal crimes. The only offense categories that consistently see similar or greater levels of below-Guidelines sentences are tax (58%), money laundering (58%), national defense (61%) and antitrust (88%). These white-collar crimes frequently led to non-incarceratory sentences prior to the enactment of the Sentencing Guidelines in 1987, and it may be that we are seeing a return to pre-Guidelines sentencing practices in white-collar cases across-the-board, including in bribery cases.

The median and mean (average) sentences imposed in FCPA cases are also revealing. Notwithstanding the DOJ's demands for severity, the median sentence in the 36 FCPA cases is only 12 months; the average is 17.8 months. In all bribery cases over the past four years, the median sentence has been the same — 12 months — and the average has been slightly higher, ranging from 19.4 to 22.9 months. Yet FCPA prosecutions typically involve much greater dollar amounts — a key determinant of the Guidelines offense level — than run-of-the-mill bribery cases. *See* U.S.S.G. § 2C1.1(b)(2). Only a small fraction (about 15%-30% per year) of bribery sentences under § 2C1.1 involve amounts in excess of $200,000. *See* U.S. Sentencing Comm'n, Use of Guidelines and Specific Offense Characteristics, FY 2006-2009. By contrast, the vast majority of FCPA cases (more than 70%) have involved bribe payments in excess of that amount, often in the millions of dollars. Nevertheless, the average FCPA sentence is below the average sentence in a bribery case.

Why the Gap?

What accounts for the predominance of relatively low, below-Guidelines sentences in FCPA cases? While each sentence may be significantly influenced by the defendant's unique characteristics (*e.g.*, age, health, family situation), there are some common mitigating circumstances found in FCPA cases that appear to be playing a role in the courts' reluctance to dance to the DOJ's tune in sentencing individual defendants.

First, FCPA violators often, if not typically, do not set out to break the law. Rather, operating in countries in which corruption is a way of life, they may accede to an official's solicitation of a bribe, or turn a blind eye to an intermediary's misconduct, in the belief that there is no other way to obtain the sought-after government contract. None of this may be a defense to an FCPA charge, but sentencing courts understandably view these circumstances as mitigating. At the Bourke sentencing, for instance, the court expressly noted that "this defendant was in no way the originator of this scheme," but rather "went along with" it. The judge who sentenced Elkin similarly noted that the defendant was confronted with a choice of "either you do this or you lose your job," and compared Elkin's actions with the CIA's payments to warlords in Afghanistan, saying that "it sort of goes to the morality of the situation."

Second, FCPA defendants often do not directly benefit from their crimes. Rather, most are sales representatives or business executives attempting to secure contracts for their companies. This fact has not been lost on sentencing courts, such as the judge who, in sentencing Brown, expressly noted that "he did not personally profit from the scheme." The loss in FCPA cases is also often abstract at best; the judge in the Green case reportedly did not view Thailand as a victim of the Greens' offenses since the Bangkok Film Festival generated substantial revenues for the Thai economy.

Third, FCPA defendants typically are first-time offenders who have led otherwise honest, law-abiding and often exemplary lives. Incarceration will not be necessary to achieve specific deterrence. For example, the judge who sentenced Bourke, a prominent businessman active in charitable causes, described him as "an asset to the public" whose incarceration "will only impede his efforts to improve the environment and the society in which he lives."

Many judges have failed to see the wisdom of imprisoning such individuals for many years in order to "send a message" to the business community that violations of the FCPA will not be tolerated. Instead, courts seem to be sending a message of their own to the DOJ.

FCPA Sentences: Cooperators (with year of sentence)

Darrold Crites, 6 months' home confinement (1999); Albert Reitz, 6 months' home confinement (2002); Richard Halford, probation (2002); Richard Pitchford, 12 months (2002); Faheem Mousa Salam, 36 months (2007); Yaw Osei Amoako, 18 months (2007); Steve Head, 6 months (2007); Gautam Sengupta, 2 months (2008); Steven Ott, 6 months' home confinement, 6 months' community center (2008); Roger Michael Young, 3 months' home confinement, 3 months' community center (2008); Christian Sapsizian, 30 months (2008); Richard Novak, probation (2008); Misao Hioki, 24 months (2008); Jim Bob Brown, 12 months (2010); Jason Steph, 15 months (2010); Kim Nguyen, probation (2010); Joseph Lukas, probation (2010); Bobby Jay Elkin, probation (2010)

FCPA Sentences: Non-Cooperators (with year of sentence)

David Mead, 4 months plus 4 months' home confinement (1999); Herbert Tannenbaum, 12 months (1999); Thomas Qualey, 4 months' home confinement (1999); Daniel Rothrock, probation (2001); Robert Richard King, 30 months (2003); David Kay, 37 months (2005); Douglas Murphy, 63 months (2005); Ramendra Basu, 15 months (2008); Martin Self, probation (2008); Shu Quan-Sheng, 51 months (2009); Frederic Bourke, 12 months (2009); Charles Jumet, 87 months (2010); John Warwick, 37 months (2010); Juan Diaz, 57 months (2010); Gerald Green, 6 months (2010); Patricia Green, 6 months (2010); Nam Nguyen, 16 months (2010); Am Nguyen, 9 months (2010)

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Schulte Roth&Zabel

Schulte Roth & Zabel LLP
919 Third Avenue, New York, NY 10022
212.756.2000 tel | 212.593.5955 fax | www.srz.com
New York | Washington DC | London

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Schulte Roth & Zabel

Schulte Roth & Zabel LLP
New York
919 Third Avenue
New York, NY 10022
+1 212.756.2000
+1 212.593.5955 fax

Schulte Roth & Zabel LLP
Washington, DC
1152 Fifteenth Street, NW, Suite 850
Washington, DC 20005
+1 202.729.7470
+1 202.730.4520 fax

Schulte Roth & Zabel International LLP
London
Heathcoat House, 20 Savile Row
London W1S 3PR
+44 (0) 20 7081 8000
+44 (0) 20 7081 8010 fax

www.srz.com