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Foreign Corrupt Practices Act: A Legal Overview

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Summary

The Foreign Corrupt Practices Act of 1977 was enacted principally to prevent corporate bribery of foreign officials. This act had three major parts: 1. It required the keeping by corporations of accurate books, records, and accounts; 2. It required issuers registered with the Securities and Exchange Commission to maintain a responsible internal accounting control system; and 3. It prohibited bribery by American corporations of foreign officials.

For a number of years after passage of the act, Congress debated amending it in response to numerous criticisms. On August 23, 1988, the President signed into law the Omnibus Trade and Competitiveness Act of 1988, of which Title V is known as the Foreign Corrupt Practices Act Amendments of 1988.

The Amendments maintained the three major parts of the 1977 Act, but significant changes were made. One of these changes enacted a "knowing" standard in order to find violations of the act. This standard was intended to encompass "conscious disregard" and "willful blindness." The amendments provided certain defenses against finding violations of the act, such as that the gift is lawful under the laws of the foreign country and that the gift is a bona fide and reasonable expenditure or for the performance or execution of a contract with the foreign government.

In 1998 the act was further amended in order to implement the Organization of Economic Cooperation and Development Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. These amendments expanded the scope of coverage to include some foreign persons and extended jurisdiction beyond the borders of the United States.

During the mid-1970's investigations and administrative and legal actions against numerous domestic corporations revealed that the practice of making questionable or illegal payments by United States corporations to foreign government officials existed to some extent within the American business community. The legal and regulatory mechanisms for dealing with these payments had involved actions by the Securities and Exchange Commission (SEC) against public corporations for concealing from required

public disclosure substantial payments made by the firm and the potential for an antitrust action for restraints of trade or fraud prosecutions by the Department of Justice.

Government officials and administrators contended that more direct prohibitions on foreign bribery and more detailed requirements concerning corporate recordkeeping and accountability were needed to deal effectively with the problem. The revelations of slush funds and secret payments by American corporations was stated to have affected adversely American foreign policy, damaged abroad the image of American democracy, and impaired public confidence in the financial integrity of American corporations.[1] Congress responded with the passage of the Foreign Corrupt Practices Act of 1977.[2] The principal purpose of the 1977 Act was to prevent corporate bribery of foreign officials. It has three major provisions to attempt to accomplish this purpose.

The first major provision amended section 13(b)[3] of the Securities Exchange Act of 1934[4] to require issuers which must register their securities with the SEC to keep detailed books, records, and accounts which accurately record corporate payments and transactions.

The second major provision required SEC registered issuers to institute and maintain an internal accounting control system to assure management's control, authority, and responsibility over the firm's assets.[5]

The third major provision of the original 1977 Foreign Corrupt Practices Act prohibited domestic corporations, whether or not registered with the SEC, from corruptly bribing a foreign official, a foreign political party, party official, or candidate for the purpose of obtaining or maintaining business. Two provisions of the 1977 Act[6] make it a crime for any American business to use the mails or interstate commerce to offer or pay money or anything of value to a foreign official or to a foreign political party, party official, or candidate for foreign political office in order to influence the person in his decision-making or to use his influence to assist the firm in obtaining or retaining business.

The 1977 Act also prohibits the payment of money to any person by a business if the business knew or had reason to know that the payment was to be used to bribe a foreign official for his influence in obtaining or retaining business. Congressional intent appears to place an affirmative responsibility on the corporation to exercise control over its

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[1] S. REP. NO. 95-114, at 3 (1977).

[2] P.L. 95-213, Title I; 91 Stat. 1494 (1977).

[3] 15 U.S.C. § 78m(b).

[4] 15 U.S.C. §§ 78a *et seq*.

[5] 15 U.S.C. § 78m(b)(2)B).

[6] 15 U.S.C. §§ 78dd-1 and 78dd-2.

officers, directors, and employees and to take steps to assure that its foreign agents are not using corporate assets or payments made to them to bribe foreign officials.[7]

Under the 1977 Act not all payments to employees of foreign governments were intended by Congress to be considered illegal bribes. For example, the definition of "foreign official" excluded employees of a foreign government "whose duties are essentially ministerial or clerical." Also, the legislative history of the act specifically stated that it was not intended to cover "grease payments" to foreign officials, explained as payments for expediting shipments through customs or placing a transatlantic telephone call, securing required permits, or obtaining adequate police protection, transactions which may involve even the proper performance of duties.[8] The legislative history also suggested that extortions of money by foreign officials may be used as a defense against bribery charges by a business if its property or lives of its employees have been threatened. An example used to illustrate acceptable payments was the payment to a foreign official to prevent the dynamiting of an oil rig.[9]

Almost since passage of the 1977 Act, frequent criticism of the operation of the act occurred. Opponents argued that the act had a chilling effect upon United States export trade and that many companies ceased foreign operations rather than face the uncertainties and the burdens of the act.

Critics of the 1977 Act also argued for removal of the "reason to know"standard concerning liability for actions of a firm's agent in a foreign country. This would eliminate the legal responsibility of the management of a domestic firm over the unauthorized and undirected actions of an agent without the necessity of management's also showing that it had no "reason to know" that the agent was using corporate funds, payments, or commissions to bribe foreign officials. These critics argued that American firms should not have to bear the responsibility of playing detective concerning the independent actions of persons that they retained as agents in foreign countries.

Critics also contended that the internal accounting controls required by the 1977 Act were too costly and burdensome upon domestic firms, especially when potential criminal penalties within the act for failure to institute adequate controls arguably made officials of firms overly and unnecessarily cautious in implementing costly accounting controls. The public recordkeeping requirements were also criticized as unduly burdensome. Critics of the act argued for a materiality standard for public recordkeeping in which a firm would be required to report only expenditures and outlays deemed material to the profits and revenues of the firm.

Another frequent criticism of the 1977 Act was that the United States was more interested in exporting its cultural biases than its products. It was argued that, in nations in which acceptance of a fee or payment by a government official from one doing business with the government is customary and not unlawful under the laws of that nation, no violation of a United States law should occur. Critics also argued that an international

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[7] S. REP. NO. 95-114, at 1 (1977).

[8] S. REP. NO. 95-114, at 10 (1977).

[9] S. REP. NO. 95-114, at 10-11 (1977).

agreement among the world's industrialized nations prohibiting businesses of all those countries from bribing foreign officials was necessary to prevent businesses of other countries from gaining an unfair and harmful competitive advantage over American businesses.

In response to these criticisms, Congress for a number of years considered amending the 1977 Foreign Corrupt Practices Act. After considerable debate through at least three Congresses, the Foreign Corrupt Practices Act Amendments of 1988 were signed into law as Title V of the Omnibus Trade and Competitiveness Act of 1988[10] on August 23, 1988. Although the amendments maintained the three major parts of the 1977 Act discussed above, the accounting standards, the requirements of SEC registered issuers, and the anti-bribery provisions, the 1988 amendments made some significant changes to the 1977 Act.

Section 5002 of the Trade Act amended section 13(b) of the Securities Exchange Act to provide that no criminal liability shall be imposed for violation of the accounting standards unless a person knowingly circumvents or knowingly fails to implement a system of accurate and reasonable accounting controls. According to the legislative history, this provision was intended to ensure that criminal penalties would be imposed where acts of commission or omission in keeping books or records or administering accounting controls have the purpose of falsifying books, records, or accounts or of circumventing accounting controls. This was also intended to include the deliberate falsification of books and records and other conduct calculated to evade the internal accounting controls requirement.[11]

Section 5002 of the Trade Act also added to section 13(b) of the Securities Exchange Act a provision that an issuer which holds 50% or less of the voting power of a domestic or foreign firm is required to use its influence only in good faith to cause the domestic or foreign firm to devise and maintain a system of acceptable accounting controls. The House Report stated that this amendment was intended to recognize that it was unrealistic to expect a minority owner to exert a disproportionate degree of influence over the accounting practices of a subsidiary.[12]

For purposes of the accounting standards, "reasonable assurances" and "reasonable detail" mean such level of detail and degree of assurance as would satisfy prudent officials in the conduct of their own affairs. Thus, the prudent man qualification was adopted to clarify that the current standard does not require an unrealistic degree of exactitude or precision.

Section 5003 of the Trade Act amended the provisions of the Foreign Corrupt Practices Act concerning the anti-bribery prohibitions by issuers and domestic concerns. The Foreign Corrupt Practices Act continued to prohibit any issuer having a class of securities registered with the SEC or any officer, director, employee, or agent of the issuer or any stockholder acting on behalf of the issuer or any United States concern to offer, pay, promise to give, or authorize the giving of anything of value to a foreign official, a

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[10] P.L. 100-418, Title V; 102 Stat. 1107 (1988).

[11] H.REPT. NO. 100-576, at 916-917 (1988).

[12] H.REPT. NO. 100-576, at 917 (1988).

foreign political party, party official, candidate, or any person for the purpose of obtaining or maintaining business. Section 5003 amended the 1977 Act to prohibit payments to any foreign official for the purpose of "influencing any act or decision of such foreign official in his official capacity, or inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official." This language was inserted so that the foreign bribery standard would conform to the domestic bribery standard found in 18 U.S.C. section 201.[13]

The "knowing" requirement was retained, and the "recklessly disregarding" standard was abandoned in conference. However, the "knowing" requirement was intended to encompass the "conscious disregard" and "willful blindness" standards, including a conscious purpose to avoid learning the truth.

> [T]he Conferees agreed that "simple negligence" or "mere foolishness" should not be the basis for liability. However, the Conferees also agreed that the so-called "head-in-the-sand" problem — variously described in the pertinent authorities as "conscious disregard," "willful blindness" or "deliberate ignorance" — should be covered so that management officials could not take refuge from the act's prohibitions by their unwarranted obliviousness to any action (or inaction), language or other "signalling device" that should reasonably alert them of the "high probability" of an FCPA violation.[14]

The major changes which section 5003 of the Trade Act made in the 1977 Foreign Corrupt Practices Act had to do with when the bribery provisions apply to an American business or person acting on behalf of an American business. For example, the anti-bribery provisions under the 1988 Amendments did not apply to any facilitating or expediting payment to a foreign official, political party, or party official.

Further, an American business or individual may use one of the "affirmative defenses" in urging that no violation of the FCPA occurred. The first of these enumerated affirmative defenses is that the payment, gift, offer, or promise of anything of value that was made was lawful under the written laws and regulations of the foreign official's, political party's, party official's, or candidate's country. Another affirmative defense is that the payment, gift, offer, or promise of anything of value that was made was a reasonable and bona fide expenditure, such as travel and lodging expenses which were incurred by or on behalf of a foreign official, party, party official, or candidate, and was directly related to the promotion, demonstration, or explanation of products or services or the execution or performance of a contract with a foreign government or agency. This defense does not apply, however, if a payment or gift is corruptly made in return for an official act or omission because it is then not considered a bona fide, good faith payment.

In the definitional sections of the 1988 Amendments the terms "knowing" and "routine governmental action" are especially important. A person's state of mind is "knowing" with respect to conduct, a circumstance, or a result if the person is aware of engaging in the conduct, that the circumstance exists, or that the result is substantially certain to occur or if the person has a firm belief that the circumstance exists or that the

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[13] H.REPT. NO. 100-576, at 918 (1988).

[14] H.REPT. NO. 100-576, at 920.

result is substantially certain to occur. When knowledge of the existence of a particular circumstance is required for an offense, the knowledge is established if a person is aware of a high probability of the existence of the circumstance unless the person actually believes that the circumstance does not exist.

"Routine governmental action" is only ordinarily and commonly performed by a foreign official in obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country; processing governmental papers' providing police protection, mail pick-up and delivery, or scheduling inspections associated with contract performance or inspections related to transit of goods across country; or providing phone service, power and water supply, loading and unloading cargo, or protecting perishable commodities or products from deterioration. The term does not include any decision by a foreign official whether or on what terms to award new business to or to continue business with a particular firm.

Criminal penalties for violations of the Foreign Corrupt Practices Act were increased. The anti-bribery fine for a firm or domestic concern was raised from $1,000,000 to $2,000,000 and for individuals from $10,000 to $100,000. The maximum imprisonment for bribery for an individual remained five years.[15] For willful violations of the accounting provisions the fine for a corporation may not exceed $25,000,000 and for an individual not more than $5,000,000 and/or imprisonment of up to twenty years.[16] The act also provides for civil penalties of up to $10,000 for violations of the bribery provisions.[17]

In 1998 the Foreign Corrupt Practices Act was again amended in order to implement the Organization of Economic Cooperation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.[18] The 1998 Amendments expanded the scope of persons covered to include certain foreign nationals, such as any officer of a public international organization.[19] The 1998 Amendments also extended the act's jurisdiction beyond the borders of the United States.[20]

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[15] 15 U.S.C. § 78dd-2(g).

[16] 15 U.S.C. § 78ff(a).

[17] 15 U.S.C. § 78dd-2(g).

[18] P.L. 105-366; 112 Stat. 3302 (1998).

[19] 15 U.S.C. § 78dd-1(f).

[20] 15 U.S.C. §§ 78dd-1(g) and 78dd-2(i).