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Potential liability under the third-party-payment provision: Due diligence a must do

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Since the Foreign Corrupt Practices Act ("FCPA") was passed into law in 1977, the vast majority of FCPA enforcement actions have involved an allegation concerning the use of a third-party intermediary – usually a consultant, agent, or contractor.[1] Few areas of criminal law involve such a consistent factual predicate, underscoring the fact that third parties pose some of the most vexing and persistent threats of non-compliance for companies doing business overseas. This chapter explores the breadth of the FCPA's third-party-payment provision, reviewing how courts and enforcement authorities have applied it.

A brief overview of the FCPA

The FCPA makes it illegal for U.S.-listed companies or U.S. companies, citizens, nationals, or residents to make, offer, promise, or authorise corrupt payments or transfer anything else of value to foreign officials.[2] Anticipating that companies might try to use third parties to circumvent these legal requirements, the U.S. Congress included language outlawing payments by covered entities or individuals to "any person, while knowing that all or a portion of such… thing of value will be offered, given, or promised directly or indirectly, to any foreign official" to improperly obtain or retain business.[3]

Corporations utilise third-party intermediaries every day in foreign business transactions for a host of legitimate reasons, whether to help navigate unfamiliar environments or to provide other on-the-ground services like market research, sales and after-sales services, logistical arrangement, and legal representation. Intermediaries may also act as a company's local representatives, especially where local laws limit the number of expatriates a company may employ or where local laws require employment of a local agent for business transactions.[4] Although certainly helpful and perfectly legitimate in most circumstances, use of these third-party intermediaries creates room for liability under the FCPA. Even the appearance of stepping over the line can lead to costly and disruptive investigations or challenging questions from transactional counterparties evaluating a prospective business partner's or acquisition target's historical compliance with the FCPA.

Liability for actions of third parties

Given the longstanding focus by U.S. enforcers (and their global compatriots investigating corruption under analogous statutes) on the use of third parties as a basis for the large majority of FCPA enforcement, it is critical to understand how the use of such actors in business opens a company to potential FCPA liability.

A. Liability under common law agency theory

It is clear that companies are liable for authorising corrupt payments by a third party to a foreign official.[5] The FCPA explicitly outlaws this. However, companies may also be

liable for illicit payments made by a third-party intermediary acting as its agent, under traditional agency theory.[6] For example, the Securities and Exchange Commission ("SEC") held Alcoa, Inc., a Pennsylvania company, liable for the actions of its subsidiaries even where the SEC had no evidence that the parent company's officers, directors, or employees authorised or knowingly engaged in bribery schemes themselves.[7] Alcoa's subsidiaries allegedly "knew or consciously disregarded" a consultant's corrupt payments to Bahraini officials for the purpose of obtaining business. Although Alcoa, as the parent company, did not directly or knowingly participate in the bribery of Bahraini officials, the common law of agency allows courts to impute that liability to companies for the actions of their agents. After determining that the foreign subsidiaries were Alcoa's "agents", the SEC concluded that Alcoa "violated Section 30A of the Exchange Act by reason of its agents".[8] Alcoa settled with the SEC, agreeing to disgorge more than $175 million in allegedly ill-gotten gains.[9] This demonstrates a direct application of common law agency theory in an FCPA enforcement action, which is how most U.S. criminal and civil enforcement works. The FCPA's enforcers at the Department of Justice ("DOJ") and the SEC, however, rarely use agency theory in this way to bring FCPA enforcement actions (outside of typical *responeat superior* for employees' behaviour).

B. Liability under the third-party-payment provision

The FCPA's most significant enforcement mechanism for holding corporations liable for the conduct of third parties is its so-called third-party-payment provision. This provision allows enforcers to bypass traditional agency analysis and focus squarely on the *mens rea* that employees of a corporation had when making a payment to a third party. In short, the third-party-payment provision holds companies liable for providing third parties with money or anything else of value while "knowing" that the third party will use it to pay a bribe to a foreign official.[10]

Importantly, the FCPA defines "knowing" more broadly than that word's common usage. The statute defines the requisite level of knowledge as either an awareness that a third party is "engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur" or "a firm belief that such circumstance exists or that such result is substantially certain to occur".[11] However, this knowledge requirement can be established if a company is "aware of a high probability" that the third party is engaged in unlawful conduct, unless the company "actually believes that such circumstance does not exist".[12] Accordingly, companies cannot escape liability by purposefully avoiding knowledge. Indeed, the legislative history of the FCPA indicates that Congress specifically intended the FCPA to reach U.S. companies that "look the other way" so as to be able to raise the defence that they were ignorant of bribes made by a foreign subsidiary.[13] In fact, there is no requirement that the third party actually consummate any improper payment.

In *United States v. Kozeny*, the Second Circuit – consistent with Congress's intent to reach "head-in-the-sand" actors – interpreted the knowledge requirement to include "conscious avoidance" of knowledge. Frederic Bourke, the co-founder of the Dooney & Bourke handbag line, was indicted for FCPA violations based on his $8 million investment in a business venture seeking to gain control of Azerbaijan's state oil company. DOJ alleged that Bourke's business partner, Victor Kozeny, arranged for millions of dollars of corrupt payments to Azeri officials. At his trial in 2009, Bourke claimed that he was unaware of the corrupt payments by Kozeny. The district court instructed the jury that it could convict Bourke if it found that he was aware of a "high probability" that corrupt payments were being paid but had "consciously and intentionally avoided confirming that fact".[14]

The jury voted to convict based on evidence presented.[15] The Second Circuit affirmed the conviction, finding that "a rational juror could conclude that Bourke deliberately avoided confirming his suspicions that Kozeny and his cohorts may be paying bribes".[16] Thus, the knowledge requirement in the third-party-payment provision can be met by a showing of conscious avoidance.

One of the largest-ever FCPA enforcement actions, against Och-Ziff Capital Management Group LLC, illustrates the reach of this low *mens rea* threshold in the corporate context.[17] Och-Ziff entered into a deferred prosecution agreement with DOJ acknowledging responsibility for, among other offences, violating the FCPA's anti-bribery provisions.[18] An SEC investigation found that Och-Ziff violated the FCPA third-party-payment provision by transacting with agents and business partners who "funneled corrupt payments" to high-level officials in multiple African countries.[19]

The SEC identified multiple loans from Och-Ziff to third parties that were used for corrupt purposes. In one instance, "bribes of more than $3 million were paid to Libyan government officials" with the "knowledge of" an employee who was head of Och-Ziff Europe.[20] In other cases, the SEC alleged "willful blindness" in line with *Kozeny*'s "conscious avoidance" standard. For example, Och-Ziff made loans totaling more than $86 million to one of its South African partners to acquire mining rights in Africa. The partner, however, used part of the funds to pay bribes to facilitate the acquisitions.[21] In finding Och-Ziff liable for violating the FCPA, the SEC concluded that the company "failed to conduct any due diligence or investigation into how South African Business Partner spent the loan from Och-Ziff funds...despite suspicion that its business partners were engaged in corrupt transactions and self-dealing".[22] In particular, Och-Ziff allegedly knew that its South African partner was using its funds to pay substantial amounts to "consultants" with no explanation for the work done to justify these payments.[23] The SEC determined that an Och-Ziff employee "was willing to allow South African Business Partner to operate without oversight because he knew or was willfully blind to the high probability that bribes would be paid to acquire assets".[24] Ultimately, Och-Ziff agreed to pay nearly $200 million to the SEC.[25]

Similarly, the SEC reached a deferred prosecution agreement with California-based Bio-Rad Laboratories, Inc., regarding charges that Bio-Rad's foreign agents in Russia paid bribes to secure contracts.[26] The SEC stated that Bio-Rad officers met the third-party-payment *mens rea* requirement by "demonstrat[ing] a conscious disregard for the possibility" that payments to foreign agents were used to bribe foreign officials.[27] The SEC found "conscious disregard" where Bio-Rad ignored red flags: Bio-Rad knew that its Russian agents operated as shell entities, that their commissions were large, and that the Russians agents themselves lacked the resources to perform their contracted-for services.[28]

As the Och-Ziff and Bio-Rad examples demonstrate, the third-party-payment provision's *mens rea* requirement is low, and companies may be held liable for failing to uncover a discoverable risk that third-party payments were used in violation of the FCPA.

Compliance strategies

The broad sweep of the FCPA's third-party-payment provision demonstrates why due diligence on commercial partners became a corporate imperative over the past two decades. Due diligence may help prevent misconduct through the vetting of potential third parties before the company engages their services. By identifying potential bad actors, corporations can steer clear of them in the first instance. Moreover, conducting due diligence creates a record of the company's mental state when engaging with the third party, thereby establishing the facts that the company knew when it entered into the relationship.

The FCPA's enforcers have emphasised the importance of due diligence procedures. In the Bio-Rad case, noted above, the SEC credited Bio-Rad's "significant and extensive remedial actions" in response to the FCPA-violative third-party payments.[29] Specifically, the SEC lauded the following diligence-related actions: "[E]nhancing its internal controls and compliance functions; developing and implementing FCPA compliance procedures, including the further development and implementation of policies and procedures such as the due diligence and contracting procedure for intermediaries and policies concerning hospitality, entertainment, travel, and other business courtesies; and conducting extensive anti-corruption training throughout the organisation world-wide."[30]

While some of the boundaries for what constitutes liability for third-party liability for the acts of agents or consultants has been set forth in judicial opinions, the vast majority of instances where liability has been found arise from settled matters where no court was involved or made a determination about third-party liability, but rather simply approved settlement terms agreed to between the SEC or DOJ and companies. For this reason, the "jurisprudence" of third-party liability largely rests in terms dictated by regulators and accepted by companies as the required terms to settle FCPA investigations and avoid contentious litigation. Accordingly, the guideposts for the reaches of liability are best known by experienced FCPA practitioners, who are aware of what particular arrangements, payments, contractual terms, or due diligence have triggered liability or not.

In part to make more readily transparent those boundaries, the FCPA Resource Guide, published jointly by the SEC and DOJ, lists red flags that an effective compliance programme should watch for. The list includes, among other things, "excessive commissions to third-party agents or consultants", "unreasonably large discounts to third-party distributors", third party associations with foreign officials, and third party requests to have payment in offshore bank accounts.[31] Although not a silver bullet, due diligence can help obviate an inference of "conscious avoidance" or an "aware[ness] of a high probability" of the sort of circumstances that can lead to liability. The FCPA Resource Guide is a reasonably objective recitation of the boundaries found in settled and occasionally in litigated FCPA matters (but as the enforcers drafted it, the document naturally has a bias favoring what the SEC and the DOJ wish the standards to be). Also, the FCPA Resource Guide does not contain the most up-to-date information about what has judicially been found to be or settled to as a basis for third-party agent liability. For that, one must delve deeply into the ever-expanding universe of settled and disputed matters.

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Endnotes

1. *See* Third-Party Intermediaries Disclosed in FCPA-Related Enforcement Actions, Stanford Law School, https://fcpa.stanford.edu/statistics-analytics.html?tab=4. As of November 20, 2022, 281 out of 314 enforcement actions have involved the use of third-party intermediaries.
2. **Prohibition.** It shall be unlawful for any issuer that has a class of securities registered pursuant to section 78*l* of this title or that is required to file reports under section 78*o*(d) of this title, or for any officer, director, employee, or agent of such issuer or any stockholder thereof acting on behalf of such issuer, to make use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorisation of the payment of any money, or offer, gift, promise to give, or authorisation of the giving of anything of value to:

(1) any foreign official for purposes of:
- **(a)** (i) influencing any act or decision of such foreign official in his official capacity, (ii) inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or (iii) securing any improper advantage; or
- **(b)** inducing such foreign official to use his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality, in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person;

(2) any foreign political party or official thereof or any candidate for foreign political office for purposes of:
- **(a)** (i) influencing any act or decision of such party, official, or candidate in its or his official capacity, (ii) inducing such party, official, or candidate to do or omit to do an act in violation of the lawful duty of such party, official, or candidate, or (iii) securing any improper advantage; or
- **(b)** inducing such party, official, or candidate to use its or his influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality,

in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person; or

(3) any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office, for purposes of:
- **(a)** (i) influencing any act or decision of such foreign official, political party, party official, or candidate in his or its official capacity; (ii) inducing such foreign official, political party, party official, or candidate to do or omit to do any act in violation of the lawful duty of such foreign official, political party, party official, or candidate; or (iii) securing any improper advantage; or
- **(b)** inducing such foreign official, political party, party official, or candidate to use his or its influence with a foreign government or instrumentality thereof to affect or influence any act or decision of such government or instrumentality, in order to assist such issuer in obtaining or retaining business for or with, or directing business to, any person. 15 U.S.C.A. § 78dd-1.

3. 15 U.S. Code §§ 78dd–1, 78dd-2, and 78dd-3.
4. *See Typologies on the Role of Intermediaries in International Business* Transactions, Working Group on Bribery in Int'l Transactions (October 2009), https://www.oecd.org/daf/anti-bribery/anti-briberyconvention/43879503.pdf.
5. 15 U.S.C. § 78dd-1(a).
6. 15 U.S.C. § 78dd-1.
7. In re: Alcoa Inc., Admin. Proc. File No. 3-15673 (January 9, 2014).
8. In re: Alcoa Inc., Admin. Proc. File No. 3-15673 (January 9, 2014).
9. In re: Alcoa Inc., Admin. Proc. File No. 3-15673 (January 9, 2014).
10. 15 U.S.C. 78dd-1(a)(3) (prohibiting giving anything of value to "any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly, to any foreign official, to any foreign political party or official thereof, or to any candidate for foreign political office" for any purpose that violates the FCPA).
11. 15 U.S.C. § 78dd-2(f)(2)(A)(i)–(ii).

12. *Id*. at § 78dd-1(f)(2)(B).
13. *See* Foreign Corrupt Practices and Domestic and Foreign Investment Improved Disclosure Acts of 1977, S. Rep. 95-114 at 11 (1977).
14. *United States v. Kozeny*, 664 F. Supp. 2d 369, 389 (S.D.N.Y. 2009).
15. *Id*.
16. *United States v. Kozeny*, 667 F. Supp. 112, 133 (2d Cir. 2011).
17. The authors' law firm, Gibson, Dunn & Crutcher LLP, represented Och-Ziff in the DOJ and SEC investigations.
18. *In the Matter of Och-Ziff Capital Management Group LLC, Oz Management LP, Daniel S. Och, and Joel M. Frank*, Order Instituting Administrative Cease-And-Desist Proceedings, Exchange Act Release No. 78989 (Sept. 29, 2016). Och-Ziff Africa Management GP LLC, the company's wholly-owned subsidiary, also pleaded guilty to a criminal violation of the FCPA in connection with the DOJ settlement.
19. *Id*.
20. *Id*.
21. *Id*.
22. *Id*.
23. *Id*.
24. *Id*.
25. Press Release, DOJ, "Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay $213 Million Criminal Fine" (September 29, 2016), https://www.justice.gov/opa/pr/och-ziff-capital-management-admits-role-africa-bribery-conspiracies-and-agrees-pay-213; Press Release, SEC, "Och-Ziff Hedge Fund Settles FCPA Charges" (September 29, 2016), https://www.sec.gov/news/press-release/2016-203.
26. *In re Bio-Rad Laboratories, Inc.*, Order Instituting a Cease-And-Desist Proceeding, Exchange Act Release No. 73496 (November 3, 2014).
27. *Id*.
28. *Id*.
29. *Id*.
30. *Id*.
31. DOJ and SEC, A Resource Guide to the US Foreign Corrupt Practices Act, at 11 (November 14, 2012).

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In 2022, 2021, 2020, 2019, 2018, and 2017, *Chambers and Partners*' global guide, *Chambers Global*, recognised Mr. Diamant as one of the leading U.S. Foreign Corrupt Practices Act ("FCPA") experts in the United States.

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