New York Law Journal
GC New York
WWW.NYLJ.COM
©2010 ALM An ALM Publication
VOLUME 244—NO. 5
THURSDAY, JULY 8, 2010

FOREIGN CORRUPT PRACTICES ACT

Narrow, Don't Abolish, FCPA Facilitating Payments Exception

By **Joel M. Cohen**

And **Adam P. Wolf**

The Foreign Corrupt Practices Act (FCPA) prohibits, among other things, U.S. companies from paying anything of value to a foreign government official to obtain or retain business. In its early days, the FCPA focused almost exclusively on hard-core payments to senior government officials to secure business, the paradigm "brown-envelope payments." More recently, however, the focus has expanded to include low-value payments that maintain and support existing business directed to, for instance, customs and police officials and low-level functionaries.

The single exception embodied in the statute addresses this latter situation, permitting the offering or paying of small-scale "facilitating payments" (FPs) if they are made to secure "routine governmental action."[1] Examples of such actions are prescribed in the statute, and include obtaining permits, processing visas and procuring police protection.

A growing chorus is calling for the elimination of this exception to the FCPA. The recently enacted UK Bribery Act contains no FP exception. The Organisation for Economic Co-operation and Development (OECD), a group of 31 countries that have each (along with seven other countries) signed an Anti-Bribery Convention and implemented local anti-corruption legislation, issued a statement in late November 2009 recommending that FPs be treated the same as any other improper payments and banned.[2] In the United States, companies increasingly are banning all such payments—according to some estimates, 80 percent now do so.[3]

ISTOCK

Pro-repeal advocates typically focus on the level of ambiguity surrounding FPs, noting that employees operating "in the field" cannot be expected to know the line between legitimate FPs and impermissible bribes. Others contend that the exception gives too much discretion to the regulators charged with enforcing the statute. Many assert an outright ban on all FPs will hasten the demise of global corruption, advocating a "just say no" response to the problem.

While these observations are fair, a solution involving an outright FP ban is not the better course. Aspirationally, it is preferable for companies not to pay FPs. But in the effort to combat corruption, as elsewhere, theory must sometimes accommodate to reality. It is neither commercially practical nor beneficial to defeating corruption to eliminate wholesale the FP exception in the FCPA. Payments are frequently demanded in far-flung locations from employees who must make on-the-spot judgment calls about whether to pay. A refusal to pay for fear of violating an anti-corruption statute containing a ban on all FPs can lead to the denial of basic, required services, or worse.[4] Further, those making payments would be less likely to report their actions.

There is a better solution that balances the need to discourage corrupt payments with the realities of today's global business environment—ban all FPs except those made in response to "requests" whose dominant motivation is extortion by the party demanding payment. This proposed narrowing of the exception would satisfy the core concerns of those advocating a complete FP ban, mandating steps to report and mitigate reoccurrence of such events, while not putting companies operating abroad in unworkable, potentially dangerous situations.

Under this construct, if a foreign government official demands a payment, and the employee believes that he or she is being extorted and has no legitimate choice but to pay, then such a payment will not run afoul of the FCPA, provided the company accurately records the payment and takes affirmative steps to mitigate the

JOEL M. COHEN *is a partner in Gibson, Dunn & Crutcher's New York office. He previously served as an assistant U.S. attorney in the Eastern District of New York and as an advisor to the Organisation for Economic Co-operation and Development.* ADAM P. WOLF *is a litigation associate in Gibson Dunn's New York office.* JOSEPH La PERLA, *an associate in the firm's New York office, contributed to this article.*

likelihood of reoccurrences—including, where appropriate, self-reporting to regulators. This would allow companies to enforce a policy of "no improper payments," but not subject them to liability if a payment is requested or suggested by an unscrupulous foreign official under pressured circumstances.

Mandating such "reporting up" to invoke the exception provides meaningful encouragement to mitigate—rather than hide—payments and the demands for them. Typically, when FPs are made, they are not reported within the company hierarchy and inadequate action is taken to address their root causes because, simply put, employees see no advantage—and, perhaps, employment risk—as the consequence of reporting. Mitigation of corruption is better achieved through encouraging open dialogue within companies about ways to prevent its reoccurrence than by inviting employees facing impossibly difficult choices to pay and hide the circumstances of the payment.

For the purposes of this proposed refinement of the FP exception, extortion can be understood as "the use of threats of injury to person or property to obtain any thing of value from a victim."[5] This definition is consistent with various federal statutes that address extortion, including the Hobbs Act[6] and the Travel Act.[7]

Hypothetical Situations

Let's see how this refined exception would work in practice, by examining two hypothetical situations that seasoned FCPA practitioners will recognize as typical:

1. In Kazakhstan, an employee ("E") driving supplies from a company warehouse to a plant is pulled over by a police officer. The officer tells E that E's truck is too large to be on the highway, and threatens to impound the truck unless E gives him $100 cash. Can E make the payment? Under the current FP exception, such a payment might qualify as an FP, assuming the truck actually is not too large to be on the road. In general, a payment can only qualify as an FP if it is, among other things, made in exchange for something to which the payer is otherwise entitled.

If the truck is actually too large, then E would not be "otherwise entitled" to drive on the highway, and the payment would therefore not be a permissible FP—it would be an improper payment. However, assuming the truck were properly sized, then the payment would likely be considered a permissible FP, as E would be "otherwise entitled" to drive on the highway without being stopped.

This outcome would not change under the proposed reformulation of the FP exception. If the truck is too large, E cannot make the payment because E is not entitled to drive it on the highway.[8] Assuming that the truck is properly sized, however, then E can make the payment. E is entitled to drive on the road, and the officer is threatening E's (or E's employer's) property while demanding the payment—extorting E. If E makes the payment, it should be considered a legitimate FP, assuming of course that E then reports the payment internally and E's company takes appropriate action (more on that later).

What if the officer merely threatens to write E a ticket unless E makes the payment? Under the existing statute, the analysis is the same: if the truck is too large, then E must not make the payment because E is not otherwise entitled to drive on the road; if the truck is properly sized, then the payment would likely be considered a permissible FP. However, under the proposed reformulation, E may not make the payment regardless whether the truck is correctly sized, because there is no longer any threat of injury to the property. Even if the truck is properly sized, the requested payment would not fall within the new exception and E would have to accept the ticket. Of course, if E perceives a threat of violence from the officer—e.g., an implied "you should make this payment because I have a gun"—then E would be allowed to make the payment.[9]

2. In Nigeria, a customs official threatens to hold up a company's shipment of goods—goods that are critical to ensuring that a multimillion-dollar project can proceed—and not allow it to clear customs unless the company's freight forwarder makes a $100 cash payment to the official. Can the freight forwarder make the payment? Under the current exception, such a payment would likely be considered a legitimate FP. It is a de minimus payment made for services to which the payer is otherwise entitled—the payer has a right to its goods being cleared through customs.

Under the proposed reformulation, however, this payment would not be permissible, because there is no threat of injury to person or property. Simply delaying the processing of a shipment would likely not satisfy the "injury to property" prong. Perhaps if the customs official threatened to destroy the shipment, rather than simply delay its clearing customs, then the payment could be made and would qualify as a permissible FP. But absent such a threat, the freight forwarder would have to refrain from making the payment.

Steps to Remediate

This proposed reformulation would not simply permit certain payments if premised on extortion; it would require affirmative steps to remediate and prevent reoccurrences. The payment itself is only half the battle. Under this proposal, to genuinely contribute to the remediation of corruption, companies must also accurately record in their books and records any payments made by employees or agents. This requirement is critically important. Many companies have gotten into trouble not for actually making improper payments, but rather for improperly recording or accounting for (perhaps otherwise legitimate) payments after the fact.[10]

Under the current FP exception, companies might be reluctant to accurately record FPs because they do not want to document bribes, albeit small-scale ones, for fear of opening themselves up to prosecution abroad or in the United States. The proposed reformulation is intended to alleviate this concern—companies should feel more comfortable accurately recording FPs made in response to extortionate demands, because the payments will have been initiated by the government official, rather than by the company.

Combating corruption requires a genuine commitment to fostering a culture where employees feel comfortable reporting any payments made, either to their supervisors or their compliance and/or legal departments. This proposal reinforces this expectation. The compliance and/or legal departments must work with the accounting staff to ensure that any such payments are accurately recorded. Then, they will have to take appropriate steps to remediate the conduct, which may include conducting additional training using either in-house resources or external experts, and finding ways, where feasible, to avoid circumstances where extortionate demands for payments might arise in the future.[11]

Finally, they will have to determine whether external reporting to the Department of Justice or Securities and Exchange Commission is appropriate. None of these steps requires a new way of doing business, and the amount and degree of remediation required as well as the decision whether to report externally will continue to be case-specific inquiries.

Not a Perfect World

Companies increasingly are adapting to today's changed enforcement landscape and

embracing ethical business practices. They are setting a clear "tone from the top" that corruption in any form will not be tolerated, drafting strong anti-corruption policies and procedures, hiring dedicated compliance officers and staffs, and committing to regular, hands-on training of their employees and agents. However, it remains true that in our global environment, companies must do business in many countries where the fight against corruption is still being waged or, in some cases, has hardly begun.

In such places, the unfortunate reality is that foreign officials continue to hold out their hands and solicit bribes, often using pressure amounting to extortion. Well-trained employees and agents will generally refuse to make corrupt payments, accepting that such refusal might very well impact the bottom line. But what are they to do if refusing to pay means that they will not receive services to which they are entitled?

Until now, U.S. companies have been allowed in limited circumstances to make small payments to "grease the skids" and expedite their receipt of routine services to which they are otherwise entitled. There is an escalating push to change this and do away with the FP exception to the FCPA. In a perfect world, such an exception would not be necessary. Unfortunately, we do not live in that world yet. An outright FP ban can be expected, in many regions of the world, to heighten the impulse to "pay and hide."

This proposal—to narrow the FP exception by allowing such small-value "grease payments" only when they are made in response to a demand predominantly motivated by extortion—would provide a measured, commercially practical step toward doing away with all corrupt payments, "facilitating" or otherwise, in a manner that provides concrete business incentives to report payment demands. Limiting the exception in this way will achieve the dual goals of curtailing corrupt payments while still allowing employees in the field flexibility to make payments that they consider absolutely necessary.

1. There are also two rarely successful affirmative defenses available under the statute, which are beyond the scope of this article. Payments that are otherwise prohibited are permitted if they are: (1) "lawful under the written laws and regulations of the [foreign official's] country"; or (2) "reasonable and bona fide" expenditures directly related to the "promotion, demonstration, or explanation of products or services." 15 U.S.C. §§78dd-1(c), 78dd-2(c), 78dd-3(c) (2006).

2. The OECD member countries that currently allow FPs are Australia, Canada, Denmark, New Zealand, Sweden and the U.S. According to Transparency International's most recent release of its widely used Corruption Perceptions Index, which ranks 180 countries according to their perceived levels of corruption, New Zealand is #1, Denmark is #2, Sweden is #3, Australia and Canada are tied for #8, and the U.S. is #19. Certainly, allowing FPs has not resulted in high perceived levels of corruption within these countries. See Transparency Int'l, CORRUPTION PERCEPTIONS INDEX 2009, http://www.transparency.org/policy_research/surveys_indices/cpi/2009/cpi_2009_table (last visited June 12, 2010).

3. See Fulbright & Jaworski LLP, Surveying FCPA Compliance, THE FCPA BLOG (Oct. 14, 2008, 8:04 PM), http://www.fcpablog.com/blog/2008/10/15/surveying-fcpa-compliance.html.

4. A bright-line ban on all FPs also places companies not obliged or inclined to follow such a ban at a competitive advantage in relation to competitors who completely disallow all FPs.

5. Judge Shira Scheindlin, in her 2008 opinion and order in a seminal FCPA decision, *United States v. Bourke*, 05-cr-00518 (SDNY), noted that payments made as a result of "true extortion"—e.g., "to keep an oil rig from being dynamited"—might not violate the FCPA because the payer would lack the "requisite corrupt intent to make a bribe." 582 F.Supp.2d 535, 540 (SDNY 2008). This article focuses on extortionate demands that do not rise to the level of "true extortion" as contemplated by Judge Scheindlin, but that nevertheless carry a threat of injury to person or property.

6. 18 U.S.C. §1951 (2006).

7. 18 U.S.C. §1952 (2006).

8. This example assumes that it is reasonable for the officer to impound oversized vehicles. If not, and the officer is threatening to impound the truck just to extort a payment, then E should be able to make that payment, assuming the payment is then properly recorded and appropriate further steps to mitigate a similar reoccurrence are taken by the company.

9. This would likely rise to the level of "true extortion." See supra note 5.

10. For instance, in January 2010, NATCO Group Inc. settled charges with the SEC relating to payments made by one of its wholly owned subsidiaries, TEST. Kazakh immigration prosecutors had conducted audits and claimed that TEST's expatriate workers were working without proper immigration documentation. They threatened the workers with fines, jail or deportation unless the company made cash payments. TEST, believing the threats to be genuine, authorized the payments and transferred funds to accounts in Kazakhstan to cover the costs; however, TEST inaccurately recorded the payments as salary advances. The SEC acknowledged that the payments were for "extorted immigration fines" but nonetheless fined NATCO because its "system of internal accounting controls failed to ensure that TEST recorded the true purpose of the payments, and NATCO's consolidated books and records did not accurately reflect these payments." *SEC v. NATCO Group Inc.*, Exchange Act Litigation Release No. 21,374, No. 4:10-CV-98 (S.D. Tex. Jan. 11, 2010).

11. It is unrealistic to presume that all corrupt situations can be anticipated and avoided. But businesspeople across myriad sectors note that opportunities to demand payments frequently arise when companies are forced by circumstance to operate under unplanned time pressure. This proposal would encourage companies, where possible, to anticipate and plan properly to avoid such reoccurring events.

Reprinted with permission from the July 8, 2010 edition of GC NEW YORK. © 2010 ALM Media Properties, LLC. All rights reserved. Further duplication without permission is prohibited. For information, contact 877-257-3382 or reprints@alm.com. # 070099-07-10-01