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Evolving FCPA Enforcement Strategy – U.S. Regulators Are Talking; Are You Listening?

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Key Points

- » *The so-called Yates Memorandum directs that a) line prosecutors focus on individuals when investigating allegations of corporate misconduct; b) DOJ's awarding of "cooperation credit" should be based on how companies respond to allegations of wrongdoing.*
- » *SEC will "pursue even the smallest infractions" in order to foster a culture of legal compliance.*
- » *Regulators will continue to push voluntary self-disclosure of FCPA violations*
- » *DOJ will add 10 prosecutors to its FCPA unit (a 50 percent increase) and will establish three International Corruption Squads comprising 23 special agents based in New York, Washington D.C., and Los Angeles.*
- » *DOJ's newly hired corporate compliance expert will advise on prosecution of corporate entities, evaluate compliance programs of accused companies, and help prosecutors develop benchmarks for compliance programs, remediation measures, working with stakeholders in setting those standards.*

Introduction

In 2015, the U.S. Department of Justice (DOJ) and the Securities Exchange Commission (SEC) – the U.S. agencies charged with enforcing the Foreign Corrupt Practices Act (FCPA) – made a number of statements that, collectively, suggest an intention to send several messages to companies subject to the FCPA. We believe these messages are related and signal a shift in the U.S. government’s approach to FCPA enforcement.

DOJ: The Yates Memorandum

The most formal – and potentially most important – pronouncement was in a memorandum issued by Deputy Attorney General (“DAG”) Sally Yates to DOJ prosecutors on September 9, 2015. While the so-called Yates Memo deals generally with DOJ’s policies regarding the prosecution of white collar crime, it has several significant implications for DOJ’s FCPA enforcement program.

• Individuals in the FCPA Crosshairs

One of the most notable aspects of the Yates Memo is its direction that line prosecutors focus on individuals when investigating allegations of corporate misconduct. As DAG Yates summarizes:

“One of the most effective ways to combat corporate misconduct is by seeking accountability from the individuals who perpetrated the wrongdoing. Such accountability is important for several reasons: it deters future illegal activity, it incentivizes changes in corporate behavior, it ensures that the proper parties are held responsible for their actions, and it promotes the public’s confidence in our justice system.”

Accordingly, the Yates Memo emphasizes that both criminal and civil DOJ attorneys should focus on individuals “from the very beginning of any investigation of corporate misconduct.” It goes on to state that, “absent extraordinary circumstances or approved departmental policy ... [DOJ] lawyers should not agree to a corporate resolution that includes an agreement to dismiss charges against, or provide immunity for, individual officers or employees” in either criminal or civil matters. Moreover, if a prosecutor decides not to pursue criminal or civil charges against an individual (in those “extraordinary circumstances”), the Yates Memo instructs that the prosecutor must now obtain written approval from a senior DOJ attorney in advance of any such declination.

The Yates Memo appears to signal a shift from DOJ’s practice of regularly agreeing to decline prosecution of individual employees when resolving corporate criminal investigations. Indeed, in February 2016, the DOJ announced that it will now require companies to certify that they have fully disclosed all information relating to individual wrongdoing before finalizing a corporate settlement agreement.

Consistent with the directives outlined in the Yates Memo, we anticipate that the DOJ will prioritize the review of individual accountability for corporate wrongdoing and, in turn, bring more individual FCPA prosecutions going forward.

- *Investigate for Cooperation Credit*

Another key aspect of the Yates Memo involves the DOJ's awarding of "cooperation credit" based on how companies respond to allegations of wrongdoing. Obtaining such cooperation credit can be extremely valuable for companies, as it can impact whether the company is charged criminally or, if the company is charged, result in a meaningful reduction of the fine range. The Yates Memorandum provides some insight to companies seeking to obtain cooperation credit from DOJ in instances where they are alleged to have engaged in misconduct:

"In order for a company to receive any consideration for cooperation under the Principles of Federal Prosecution of Business Organizations, the company must completely disclose to the Department all relevant facts about individual misconduct. Companies cannot pick and choose what facts to disclose. That is, to be eligible for any credit for cooperation, the company must identify all individuals involved in or responsible for the misconduct at issue, regardless of their position, status or seniority, and provide to the Department all facts relating to that misconduct. (...) This condition of cooperation applies equally to corporations seeking to cooperate in civil matters; a company under civil investigation must provide to the Department all relevant facts about individual misconduct in order to receive any consideration in the negotiation."

It is worth noting that "any" is also underlined in the actual Yates Memo.

We view this statement as a clear mandate to companies: If you want to get cooperation credit from DOJ, you must provide a detailed report of the facts and circumstances surrounding the allegations, including identifying the persons responsible.

In sum, the decision for companies whether to conduct an internal investigation is now made easy. If they hope to get any cooperation credit, an internal investigation is a requirement.

But while the decision to investigate might be easy, the DOJ's renewed focus on individual accountability (and disclosure requirements for cooperation credit) may significantly complicate the investigative process. Companies will now need to be more mindful of potential conflicts in dealing with individual employees, audit committees, and Boards of Directors. Particularly when allegations of wrongdoing reach multiple or high-level employees, companies should consider involving experienced outside investigative counsel.

SEC: “Broken Windows” Enforcement

While it appears as though the DOJ will focus more on prosecuting individuals, the SEC has continued to bring a majority of its enforcement actions against companies. It has done so under what SEC Chairwoman Mary Jo White has referred to as the “broken windows” theory of securities enforcement. That is, the SEC announced, that it will “pursue even the smallest infractions” in order to foster a culture of legal compliance.

In 2015, the SEC put this theory in practice by resolving numerous cases for relatively small amounts. By way of recent example, on the FCPA front, Hyperdynamics Corporation, an oil and gas company with operations in the Republic of Guinea, consented to the entry of an administrative cease-and-desist order and agreed to pay a \$75,000 penalty to the SEC.

The relatively modest penalty (by FCPA standards) issued by the SEC in the Hyperdynamics matter, however, is only part of the story. Even the “smallest infractions” prosecuted by the SEC under its broken windows theory can involve significant investigation and professional costs for companies. In reaching agreement to pay a \$75,000 penalty, for example, Hyperdynamics spent approximately \$12.7 million in professional fees. Prosecution of even minor infractions by the SEC, thus, can still be a very expensive process for the companies involved.

Regulators Continue to Push Voluntary Self-Disclosure of FCPA Violations

FCPA regulators from both DOJ and the SEC have been emphasizing the importance of voluntary self-disclosure for some time. Perhaps most significant was the SEC’s recent announcement that self-reporting will be a pre-condition to a company receiving a deferred prosecution agreement or a non-prosecution agreement.

Other enforcement authorities have made the same point. At the American Conference Institute’s 32nd Annual International Conference on the FCPA, Assistant Attorney General Leslie Caldwell remarked, “we want to encourage self-disclosure by making clear that, when combined with cooperation and remediation, voluntary disclosure does provide a tangible benefit when it comes to making a charging decision.” Similarly, at the American Banking Association and American Bar Association Money Laundering Enforcement Conference, DAG Yates noted that a significant aspect of the Yates Memorandum related to self-disclosure, and she emphasized the significance of self-disclosure to DOJ:

“[O]ne of the changes made to the USAM [US Attorney’s Manual] today separates what used to be a single factor that covered both a corporation’s voluntary disclosure and its willingness to cooperate into two separate factors[.] . . . In recognition of the significant value early reporting holds for us, prompt voluntary disclosure by a company will be treated as an independent factor weighing in the company’s favor.”

The decision whether to self-disclose has historically been one of the most difficult decisions for companies dealing with FCPA violations. This decision was complicated in large part because of the uncertainty surrounding the amount of cooperation credit (if any) a company would receive for effectively turning itself in to the authorities. Through these public statements (and as evidenced by significant credit given in resolving recent FCPA enforcement actions), it appears that the DOJ and SEC are signaling real and tangible benefits to those companies that self-disclose violations.

Strengthening the Bench: Additional FCPA Resources

Another development worth noting is the increase in investigative and prosecutorial resources dedicated to FCPA enforcement. In November 2015, DOJ announced that it will add 10 prosecutors to its FCPA unit, which is, according to DAG Yates, a 50% increase in headcount. This news follows on the heels of the March 2015 announcement that the FBI, acting in conjunction with DOJ's Fraud Section, is establishing three International Corruption Squads comprised of 23 special agents based in New York, Washington D.C., and Los Angeles. These agents will be dedicated to investigating foreign bribery and kleptocracy. This increase in investigators and prosecutors signals the relative importance of FCPA enforcement within the U.S. government, and it will almost certainly lead to more criminal FCPA cases.

Setting Compliance Expectations

In November 2015, the Fraud Section of the DOJ retained Hui Chen as a full-time corporate compliance expert. Chen's role is to provide guidance to DOJ prosecutors concerning the prosecution of corporate entities, to evaluate the existence and effectiveness of compliance programs that companies had in place at the time of alleged misconduct, and to assess whether companies have taken meaningful remedial action, such as implementing new compliance measures, to detect and prevent future wrongdoing. Just as importantly, Chen is also tasked with helping prosecutors develop appropriate benchmarks for evaluating corporate compliance and remediation measures and communicating with stakeholders in setting those benchmarks.

So what are the factors that Ms. Chen will be considering when evaluating corporate compliance programs? The DOJ's Assistant Attorney General Caldwell provided some insight in her November 2015 speech to the Securities Industry and Financial Markets Association. The key questions are as follows:

- » Do company directors and senior managers provide strong, explicit and visible support for its corporate compliance policies?
- » Do the employees responsible for compliance have stature within the company? Do compliance teams get adequate funding and access to necessary resources?
- » Are the company's compliance policies in writing and easily understood by employees? Are the policies translated into the native languages of the employees?
- » Does the company effectively communicate its compliance policies to all employees? Are written policies easy for employees to find? Do employees have regular training, including direction regarding what to do or with whom to consult when issues arise?
- » Does the company update its policies and practices to keep current with evolving risks and circumstances?

- » Are there appropriate mechanisms in place to enforce compliance policies, including incentivizing good compliance practices and disciplining violations. Is discipline applied in an even-handed manner (regardless of the employee's position within the company)?
- » Does the company sensitize third parties – such as vendors, agents, and consultants – to the company's expectation about good corporate compliance practices?

It is worth noting that many of these questions track the “Hallmarks of an Effective Compliance Program” in the DOJ's and SEC's FCPA Guidance. Companies should consider these questions when assessing the adequacy of their compliance programs. As highlighted by several questions, developing a strong compliance program requires continuous improvement. Companies should reevaluate their programs periodically, and particularly after significant events, such as a corporate merger, acquisition, or joint venture.

A New Enforcement Paradigm

It certainly appears that the DOJ and SEC have thought long and hard about their respective missions and visions for FCPA enforcement in the future. The pronouncements described above outline an enforcement program that emphasizes individual prosecutions and demands of companies proactive compliance, investigation and self-disclosure of FCPA violations, and full cooperation with the agencies.