FCPA Lessons for the Middle Market

January 23, 2015

Several Foreign Corrupt Practices Act (FCPA) cases involving both domestic and foreign-based Fortune 500 companies have been in the headlines recently due to the large fines and settlement provisions. These FCPA cases against large multinational companies also provide guidance for middle-market companies, private equity firms and their employees.

Lesson 1: The SEC and DOJ are refocusing on middle-market companies.

The government has announced that it will increase its FCPA enforcement review for mid-sized companies and private equity firms. In announcing the settlement with Smith & Wesson, the U.S. Securities and Exchange Commission (SEC)'s FCPA Unit chief, Kara Brockmeyer, warned: "This is a wake-up call for small and medium-size businesses that want to enter into high-risk markets and expand their international sales." Brockmeyer added that companies expanding into overseas markets, which would include middle-market companies, must ensure that "the right internal controls are in place and operating." (SEC Press Release, "SEC Charges Smith & Wesson With FCPA Violations," July 28, 2014). The SEC's whistleblower program, authorized under the Dodd-Frank Act, allows individuals to help uncover FCPA violations.

Lesson 2: The number of FCPA cases brought annually may have declined, but penalties continue to increase.

While the U.S. Department of Justice (DOJ) had fewer enforcement actions in 2014, penalties assessed have increased dramatically in recent years. In 2010, the average monetary penalty in an FCPA action was approximately $82 million, which amount dropped to $22 million by 2012. The trend reversed in 2013 when French oil and gas company, Total S.A., settled FCPA charges for $398 million. Between 2012 to 2014, the average penalty increased seven-fold, reaching $157 million in 2014. Last month, the DOJ imposed its largest-ever FCPA fine -- $772 million -- against French power company, Alstom S. A. Companies should expect the trend toward larger fines to continue in 2015.

In December 2014, the DOJ fined Dallas Airmotive, Inc., a Texas-based aircraft service provider, $14 million for bribing foreign officials in Argentina, Brazil, and Peru. The same month, Avon Products, the large multinational corporation, agreed to pay $135 million to settle FCPA charges by both the SEC and DOJ. Avon's fine was nearly 10 times that of Dallas Airmotive. Both companies entered into three-year deferred prosecution agreements that required on-going compliance monitoring, remediation, and reporting to the government.

Lesson 3: Failure to detect and stop misconduct will trigger more severe penalties.

Another important lesson from recent FCPA cases is that merely having a compliance program is not enough. More than ever, the DOJ looks behind the "paper" compliance program to determine how it is being implemented and monitored by senior management. In announcing Alstom's record-breaking fine, the DOJ stressed that it expects companies to "eradicate misconduct when it is detected" and the DOJ "will not wait for companies to act responsibly." Newly-created FBI squads focused on foreign corruption and stationed in several major U.S. cities are a signal that the DOJ will be looking for FCPA violations.

Middle-market companies and private equity firms, either voluntarily or as part of an agreement with the government, may find that they need to change their business structure in addition to paying monetary fines. In July 2014, for example, Smith & Wesson agreed to pay $2 million to settle allegations of FPCA violations in several different countries, including Bangladesh and Pakistan. It took remedial actions (which the SEC considered in imposing its fine), that included eliminating its entire international sales staff and canceling all pending international sales transactions.

Lesson 4: The government continues to focus on individuals.

In 2014, the DOJ announced its intention to re-emphasize individual accountability. Newly-appointed DOJ Assistant Attorney General for the Criminal Division, Leslie Caldwell, announced that "[t]he prosecution of culpable individuals—including corporate executives—for their criminal wrongdoing continues to be a high priority for the [DOJ]." (Caldwell Speech, October 1, 2014, Atlanta, GA). In Fall 2014, Deputy Attorney General Marshall L. Miller echoed Caldwell's statements, stressing that the DOJ intends to prosecute individuals, "whether they're sitting on a sales desk or in a corporate suite." (Miller Speech, September 17, 2014, New York).

In FCPA cases, AAG Caldwell has explained the DOJ's strategy in focusing on individuals: "Stripping individuals of the proceeds of their conduct—and thus depriving them of the very profits that are driving the corrupt conduct in the first place—is one technique that we are using increasingly in our fight against foreign bribery." (Caldwell Speech, November 19, 2014, National Harbor, MD).

The SEC similarly focused on individuals in 2014, settling charges of FCPA violations against two former employees of defense contractor, FLIR Systems, through an SEC administrative proceeding. The SEC has increased the use of administrative proceedings for enforcement actions involving the FCPA.

In 2015, the government is likely to continue its focus in FCPA enforcement on individuals. In January 2015, the president of a privately-held consulting company in Pennsylvania was indicted under the FCPA and Travel Act for paying $3.5 million in bribes to a European banking official. The SEC also brought charges against a former officer of a construction company for FCPA violations involving Qatari contracts. He paid a $50,000 fine while the company entered into a deferred prosecution agreement and paid a $3.4 million penalty.

Conclusion

Mid-size companies and private equity firms may not have large compliance departments or budgets, as some of the Fortune 500 companies do. Nonetheless, a careful assessment of potential FCPA exposure and compliance is critical. Like other companies, private equity firms must ensure that proper due diligence is done before using agents in foreign countries, and before completing a merger or acquisition. Robust compliance procedures, training, and internal controls are essential to identify "red flags" and address problems.

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