



WILMER CUTLER PICKERING HALE AND DORR^{LLP}

Foreign Corrupt Practices Act Update

JULY 27, 2004

ABB Subsidiaries Plead Guilty to FCPA Charges; Swiss Parent Settles With SEC

On July 6, 2004, the Department of Justice (“DOJ”) and the Securities and Exchange Commission (“SEC”) announced results of parallel criminal and civil Foreign Corrupt Practices Act (“FCPA”) enforcement actions against Zurich-based ABB Ltd. (“ABB”) and two of its subsidiaries, Houston-based ABB Vetco Gray, Inc. (“Vetco Gray US”) and Scotland-based ABB Vetco Gray UK, Ltd. (“Vetco Gray UK”).¹ We represented an employee of Vetco Gray UK during the investigation that preceded the settlement.

Vetco Gray US and Vetco Gray UK (collectively, “the subsidiaries”) were part of the Oil, Gas & Petrochemicals division of the Swiss parent ABB, a global provider of power and automation technologies. ABB sold the subsidiaries following the enforcement actions, the conclusion of which was a key contingency in the sale agreement.

In the criminal DOJ case, the subsidiaries pled guilty to violations of the anti-bribery provisions of the FCPA and agreed to pay \$5.25 million each,

for a total of \$10.5 million in criminal penalties. Pursuant to a civil settlement of the SEC case, in which the SEC alleged that the Swiss parent violated the FCPA’s anti-bribery provisions and the FCPA’s accounting provisions as well, ABB agreed to disgorge \$5.9 million in allegedly illicit profits and to pay a \$10.5 million fine, the latter of which was deemed satisfied by the payment of the penalty in the criminal case against the subsidiaries. Thus, the sum of the criminal penalties and the disgorgement was \$16.4 million.

According to the court filings, the fines were less than what they might have been in the absence of “extraordinary” cooperation by the companies involved. The case arose after ABB, which was in the process of selling the subsidiaries, voluntarily disclosed suspicious payments to the DOJ and the SEC in 2003. Following the disclosures, attorneys for the Swiss parent and the purchasers of the subsidiaries agreed to conduct a joint investigation and to disclose the results of that investigation to the DOJ and the SEC. In addition to disclosing the

¹ *SEC v. ABB Ltd.*, Case No. 1:04CV01141 (D.D.C. July 6, 2004); *U.S. v. ABB Vetco Gray, Inc. and ABB Vetco Gray UK Ltd.*, Case No. CR H-04-279 (S.D. Tex. June 22, 2004).

WILMER CUTLER PICKERING HALE AND DORR^{LLP}

investigation results and paying substantial penalties, all of the companies agreed to implement effective FCPA compliance programs. The companies avoided other measures sometimes imposed on companies guilty of criminal violations, such as “organizational probation” and supervision by an outside monitor to ensure future compliance.

The FCPA’s Anti-Bribery and Accounting Provisions

The FCPA anti-bribery provisions make it unlawful for any issuer, domestic concern, or person acting within the United States to make or offer to make a payment of anything of value directly or indirectly to a foreign official, international organization official, political party or party official, or any candidate for public office, for the purpose of influencing that official to assist in obtaining or retaining business. 15 U.S.C. § 78dd-1 to -3. The FCPA’s accounting provisions require companies with securities listed in U.S. trading markets to keep books, records, and accounts, which accurately and fairly reflect any transaction and disposition of assets in reasonable detail, and to maintain an adequate system of internal accounting controls. 15 U.S.C. § 78m(b). A covered company is responsible for ensuring that its subsidiaries, including foreign subsidiaries, comply with the FCPA’s accounting provisions. The parent must ensure that its subsidiaries maintain accurate books and records and establish and implement adequate internal accounting controls. The parent can be held liable for its failure to ensure the accuracy of a subsidiary’s books and records even if the parent company has no knowledge or reason to know of the inadequate recordkeeping.

Stipulated Facts in the DOJ’s Criminal Case

According to the plea agreements and stipulated facts in the DOJ criminal case, the subsidiaries made bribes to Nigerian officials of the National Petroleum Investment Management Services, a Nigerian governmental entity. From 1998 to 2001, the subsidiaries paid bribes and authorized the pay-

ment of bribes to induce the Nigerian officials to: (1) provide confidential and proprietary information regarding its evaluations of competing bids and thereby to provide a competitive advantage to the subsidiaries in bidding for projects; and (2) provide preferential treatment on bids made by the subsidiaries or their affiliates.

The subsidiaries often cooperated to market Vetco Gray services in Nigeria, and the bribes were made by employees of both subsidiaries. In particular, payments amounting to over \$800,000 were made to Nigerian officials pursuant to sham consulting agreements for which no legitimate consulting work was done. In addition, the subsidiaries provided goods and services to the Nigerian officials, including the provision of an automobile, an expense-paid shopping excursion, expenses for a country club membership and limousine service, and expenses related to housing, living, and entertainment. The total value of the bribes paid exceeded \$1 million, and several additional bribes were promised but ultimately not paid. All of the bribes were paid or promised in connection with bids for oil exploration projects and related matters which were expected to generate profits of almost \$12 million.

Of particular interest in the criminal case is the fact that the DOJ charged Vetco Gray UK, a foreign subsidiary of ABB. While Vetco Gray US was charged under the FCPA provision applicable to “domestic concerns,” 15 U.S.C. § 78dd-2, Vetco Gray UK was charged under an FCPA provision added in 1998 to cover any person who, while in the territorial United States, acts in furtherance of a bribe of a foreign official. 15 U.S.C. § 78dd-3. According to the DOJ, the case against Vetco Gray UK is the second case to charge a foreign company under this provision. The plea agreement and stipulated facts do not specify the Vetco Gray UK acts that satisfied the U.S. territorial requirement, but the case nevertheless illustrates the DOJ’s willingness to pursue a criminal case against a foreign company that acts in close concert with a domestic concern to commit violations of the FCPA anti-bribery provisions.

Allegations in the SEC's Civil Case

The parallel SEC enforcement proceeding asserted violations of the FCPA's anti-bribery and accounting provisions by the Swiss parent ABB, acting through its subsidiaries. The SEC asserted jurisdiction over ABB based on the fact that ABB issues American Depository Shares that are registered with the SEC and are traded on the New York Stock Exchange. The SEC also stated that the implicated ABB subsidiaries' financial results were components of consolidated financial statements that ABB filed with the SEC.

The SEC's allegations reiterated many of the stipulated facts in the criminal case against the subsidiaries, added that the Nigerian bribes were improperly recorded as ordinary business expenses, and claimed that ABB also was liable for the subsidiaries' FCPA violations. In addition, the SEC alleged that ABB, through its subsidiaries, made bribes to government officials in Angola and Kazakhstan. These bribes allegedly were made for the purpose of obtaining or retaining business from Sonangol, an Angolan state-owned oil company, and from Kazakh governmental entities.

The payments to the Angolan officials, which occurred between 2000 and 2002, allegedly took the form of cash payments putatively made for three training trips outside Angola. The SEC noted, however, that while Angola's gross annual per capita income was only \$710, the cash payments for one of the trips included \$120 to \$200 per person per day in addition to expenses for travel, meals, lodging, and entertainment; further, the cash payments for another trip amounted to \$4,320 for each Angolan official. Other allegations reflecting the SEC's view that the payments were bribes rather than legitimate travel expenditures included the following: the cash payments generally were funded in circuitous ways designed to conceal the source and nature of the funds; the

payments were made to officials whom Vetco Gray senior management described as "future decision-makers for Sonangol" in "key positions"; at least one of the Angolan officials disclosed confidential competitor information in relation to ABB's bid for a Sonangol contract, and an in-house attorney for one of ABB's U.S. subsidiaries warned that the payments amounted to a "red flag" and a potential "violation of the FCPA." The SEC alleged that two Sonangol contracts were awarded to ABB subsidiaries after the payments, and that the payments were improperly recorded as ordinary business expenses in ABB's books and records. The SEC also alleged that the contracts with Sonangol generated profits of almost \$1.5 million.

With regard to Kazakhstan, the SEC alleged that from 2001 to 2004, ABB's Kazakh subsidiary made six payments to companies owned by an employee of Kazakhstan's state oil and gas companies. The payments allegedly totaled \$125,126 and were made pursuant to sham contracts for consulting services related to the maintenance of drilling equipment. The SEC further alleged that no legitimate services ever were performed, that the payments were documented with phony invoices to mislead auditors, and that the payments were improperly recorded in ABB's books and records. One of the contracts that was obtained or retained through the bribes allegedly generated more than \$1.4 million in profits for ABB.

The SEC's case is yet another reminder of the risks to all parent companies whose shares are traded on U.S. exchanges – whether the companies are foreign or domestic – if they fail to ensure FCPA compliance by their subsidiaries. The SEC has pursued a series of enforcement actions against parent companies for the alleged bribery of foreign officials by subsidiaries, even when the SEC has no indication that the parent companies were involved in any bribe or alleged FCPA violation.² This is another such case - the SEC's complaint

² See, e.g., *SEC v. Schering-Plough Corp.*, Case No. 1:04CV00945 (D.D.C. June 9, 2004); *SEC v. International Business Machines Corp.*, 1:00CV030400 (D.D.C. Dec. 21, 2000); *SEC v. Chiquita Brands International, Inc.*, 1:01CV02079 (D.D.C. October 3, 2001); *SEC v. BellSouth Corporation*, 1:02-CV-0113 (N.D. Ga. Jan. 15, 2002).

against ABB nowhere alleges that the Swiss parent participated in or knew of the alleged bribes, but the complaint nevertheless charges the parent with violating the anti-bribery provisions as well as the accounting provisions.

Practical Advice

Not only U.S. companies but also foreign companies that do business in or whose shares are traded on U.S. exchanges should take care to implement a comprehensive FCPA compliance program and to apply that program equally to all subsidiaries. The minimum components of an effective FCPA compliance regime are:

- Adopting a clear corporate ethics policy prohibiting violations of the FCPA and establishing compliance standards and procedures that are reasonably capable of reducing the prospect of violations;
- Assigning responsibility for the FCPA compliance program to senior managers;
- Training officers, employees, agents, and consultants regularly concerning the requirements of the FCPA;
- Implementing appropriate disciplinary mechanisms for violations or failure to detect violations;
- Establishing a system by which officers, employees, agents, and consultants can report suspected violations without fear of retribution;
- Adopting corporate procedures, including a recorded due diligence inquiry, to ensure that the company forms business relationships with reputable agents, consultants, representatives, and joint venture partners;
- Adopting corporate procedures to ensure that companies do not delegate substantial discretionary authority to individuals with a propensity to engage in illegal activities;

- Including in all contracts with agents, consultants, joint venture partners, and other representatives, warranties that no payments of money or anything of value will be offered, promised or paid, directly or indirectly, to any foreign official, foreign political party, party official, or candidate for foreign public or political office to induce such officials to use their influence with a foreign government or instrumentality to obtain an improper business advantage for the company;
- Including in all contracts with agents, consultants, and other representatives a warranty that the agent, consultant, or representative shall not retain any sub-agent or representative without prior written consent.

In addition, the following lessons emerge from this case:

- Certain African countries and, in particular, Nigeria, continue to present severe challenges for companies with respect to FCPA compliance, and company management and auditors must proactively implement aggressive controls over operations in such countries.
- The amount of the penalties, whether denominated a “fine” or “disgorgement,” being sought for violations of the FCPA by the DOJ and the SEC, even from cooperating companies, has become much higher than in the past. Thus, the risks arising from FCPA violations have become even higher than before.
- In deciding on how to dispose of a case, the DOJ and the SEC continue to give credit to companies that volunteered information and cooperated in the conduct of an internal investigation so as to make that investigation transparent to the government agencies. Just how much credit is “earned” as a result is sometimes uncertain, and

whether the credit given is sufficient is often debated between the government and cooperating companies, and certainly in the defense bar.

- It is also noteworthy that in spelling out what “cooperation” entails, the government agencies are now routinely requiring waiver of lawyer-client and work product privileges and other extraordinary measures.

For a fuller discussion of these and other FCPA issues, see Roger M. Witten, *Complying with the Foreign Corrupt Practices Act* (Matthew Bender, 4th ed. 2003). If you have any questions or need additional information, please contact:

Roger Witten (212) 230-8850
Roger.Witten@wilmerhale.com

Stephen Preston (202) 663-6900
Stephen.Preston@wilmerhale.com

Robert Keefe (617) 526-6334,
Robert.Keefe@wilmerhale.com

Kimberly Parker (202) 663-6987
Kimberly.Parker@wilmerhale.com

Stephen Heifetz (202) 663-6558
Stephen.Heifetz@wilmerhale.com

Alec Scheiner (212) 230-8885
Alec.Scheiner@wilmerhale.com

Jennifer Rockoff (202) 663-6918
Jennifer.Rockoff@wilmerhale.com