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Foreign Corrupt Practices Act Updates

Department of Justice Issues Opinion on U.S. Company Liability for Corrupt Payments Made by Joint-Venture Partners Before the Formation of the Venture

The Department of Justice (DOJ) issued Opinion Release 2001-01 on May 24, 2001. It gives considerable guidance on what arrangements may be necessary and appropriate when a U.S. company enters into a joint venture with a foreign company contributing contracts to the venture that may have been procured through questionable means. DOJ, in essence, permitted the U.S. company to enter into the joint venture and to enjoy the fruits of the questionable contracts through the joint venture so long as (1) no funds from the U.S. company or the joint venture were, or could be, used to make payments to the foreign company's sales agents, and (2) the joint venture adopted a suitable compliance program. The Opinion Release appears to endorse the idea that a foreign company contemplating a transaction that would subject it to FCPA, such as listing in the United States, may make "winding up" payments to terminate sales agents whose prior activities may have raised "red flags."

BACKGROUND

The FCPA's Antibribery Provisions

The FCPA's antibribery provisions make it unlawful for any issuer, domestic concern, or person acting within the United States corruptly 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 any official act to assist in obtaining or retaining business. 15 U.S.C. § 78m(b). Indirect payments include payments that are made by foreign agents on behalf of a company if the company knowingly participates in or authorizes the payments.

The FCPA's antibribery provisions do not apply directly to foreign joint ventures in which U.S. companies are partners so long as the joint venture itself is not an issuer or a U.S. company and so long as no acts in furtherance of any corrupt payment take place in the United States. A U.S. company is not liable for corrupt payments made by a foreign joint venture or joint venture partner unless the U.S. company knowingly participates in or authorizes the corrupt payment. If a U.S. company knows that a foreign joint venture in which it has an interest is making corrupt payments, the U.S. company must use reasonable efforts to halt the payments and prevent corrupt practices in the future.

The DOJ Opinion Request Procedure

The DOJ's opinion request procedure allows companies to describe a set of facts to DOJ and to obtain an opinion whether DOJ will seek enforcement action against the company based on the representations in the request. If DOJ states that it does not intend to seek enforcement action, the company may proceed with the transaction described in the letter with no risk of DOJ prosecution, provided that the facts described in the request accurately depict the transaction.

OPINION RELEASE 2001-01

A U.S. company advised DOJ that it had plans to enter into a 50-50 joint venture with a French company ("FRENCHCO"). The U.S. company and FRENCHCO each planned to contribute pre-existing contracts to the joint venture. Some of the contracts to be contributed by FRENCHCO predated enactment of the French law prohibiting corrupt payments to foreign government officials. *See* French Law No. 2000-595 Against Corrupt Practices (FLAC). FRENCHCO had used foreign sales agents to procure some of these contracts. Although not stated in the Opinion Release, it can be assumed that the arrangements with at least some of the agents raised red flags. The joint venture, and derivatively the U.S. company, would enjoy the benefits of the contracts assigned by FRENCHCO to the joint venture.

The U.S. company sought an opinion on its FCPA liability should it later become known that FRENCHCO had engaged in corrupt practices to obtain any of the pre-existing contracts that it was contributing to the joint venture. The U.S. company made the following representations in its request:

- FRENCHCO had represented to the U.S. company that none of the contracts FRENCHCO was contributing to the joint venture were procured "in violation of applicable antibribery or other laws," and the U.S. company was not aware of any facts that cast doubt on FRENCHCO's representation.

- In the event FRENCHCO in the future were convicted of, or admitted to, violating the FLAC, or the U.S. company were to receive evidence of a FRENCHCO violation of antibribery laws that had a "material adverse impact" on the joint venture, the U.S. company would have the right to terminate the joint venture or to refuse to satisfy certain obligations under the agreement.

- FRENCHCO had terminated all agent agreements entered into before January 1, 2000, relating to contracts that it would contribute to the joint venture; all payment obligations under those agent agreements had been liquidated; and the funds for the liquidation payments would come solely from FRENCHCO — not the joint venture or the U.S. company.

- FRENCHCO would continue to pay commissions and other compensation due under its agent agreements entered into after January 1, 2000 relating to contracts contributed to the joint venture, but these payments would not be obligations of the joint venture, and no funds of the joint venture or the U.S. company would be used to satisfy them.

- When entering into new agent agreements the joint venture would follow a rigorous compliance program that would prohibit the parties from recommending an agent known to have engaged in illegal or unethical conduct and would give each party the right to veto any agent believed to have engaged in illegal conduct.

Based on these representations, DOJ responded that it did not intend to take any enforcement action against the U.S. company as a result of its participation in the joint venture. DOJ made clear, however, that its position was subject to three important caveats:

- DOJ construed FRENCHCO's representation that none of the contracts it planned to contribute to the joint venture was procured "in violation of applicable antibribery or other laws" as a representation relating both to French law and any other applicable antibribery law, including the laws of the countries in which FRENCHCO procured the contracts in question. In DOJ's view, if FRENCHCO had intended to limit its representation to French law, then the U.S. company would be subject to FCPA prosecution if it knowingly took any act in furtherance of a payment made to procure to a pre-existing contract that had been procured in violation of any other relevant country's antibribery law.

- DOJ declined to endorse the "material adverse effect" standard for terminating the joint venture

agreement. In its view, if the U.S. company's inability to extricate itself from the joint venture results in it taking any acts in furtherance of previous acts of bribery by FRENCHCO, the U.S. company could be prosecuted under the FCPA.

- Although DOJ emphasized that the joint venture's proposed compliance program for hiring new agents would be significant, it declined to endorse any specific aspect of the program.

SIGNIFICANCE OF DOJ OPINION

Opinion Release 2001-01 provides valuable guidance on structuring joint ventures and mergers between U.S. companies and non-U.S. companies that have not historically been subject to strict anticorruption laws like the FCPA. It suggests that U.S. companies may, in certain circumstances, acquire, or participate in ventures that acquire, contracts their partner obtained in ways that were legal under the laws of the foreign company's jurisdiction but may have violated the FCPA had it applied. The Release makes clear that neither the U.S. entity nor the joint venture may directly or indirectly fund any future payments that may still be owed to foreign a company's sales agents in connection with such contracts if the U.S. company knows of any past corrupt acts by the foreign company in obtaining the contracts. It is not sufficient protection for the U.S. partner that the foreign company ostensibly complied with its own country's anticorruption laws, if any. It must also have complied with the laws of the countries in which it procured the contracts. In forming joint ventures or engaging in mergers or acquisitions, U.S. companies must obtain reliable representations and warranties from their foreign partners that the contracts that will be part of the joint venture or the merged entity were not procured in violation of the laws of any applicable jurisdiction. Even if foreign partners make such representations and warranties, it is advisable, as a prophylactic measure, for the U.S. company to structure the joint venture so that neither the U.S. company's nor the joint venture's funds are used to pay any remaining obligations owed to the foreign company's sales agents.

The Release is also significant because it appears to endorse the conclusion that U.S. companies can sufficiently separate the joint venture or the merged entity from questionable pre-existing contracts if the foreign company "winds up" all remaining financial obligations to agents related to the contracts that it plans to contribute to the venture. The Release cautions, however, that if the U.S. company later discovers that these contracts were procured through corrupt means and the U.S. company itself performs acts in furtherance of the original bribery, it may be liable under the FCPA.

In rejecting the "material adverse effect" standard, the Release suggests that a U.S. company must disassociate itself from a foreign company or joint venture if it discovers evidence of corruption concerning a contract entered into before the U.S. company's participation, even if the violation does not have a material effect on the joint venture. While DOJ has always taken the position informally that U.S. companies should disassociate themselves from foreign ventures when they are unable to prevent ongoing corruption, this Release appears to take a somewhat more aggressive position.

PRACTICAL ADVICE

U.S. companies should take care in entering into joint ventures or mergers where pre-existing contracts will constitute part of the assets of the new entity. At a minimum, U.S. companies should:

- Perform due diligence on their foreign partners to identify agents and contracts of potential concern and, to the extent possible, obtain reliable representations and warranties that none of the pre-existing contracts was obtained in violation of any applicable antibribery laws.

- Regarding contracts that raise potential corruption issues: either structure the venture to exclude those contracts or take prophylactic steps before creating the joint

venture or consummating the merger to insure that neither the venture's funds nor the U.S. company's funds can be used to pay agents who may have made or may be making corrupt payment to foreign governance officials.

- Regarding questionable agents of the foreign partner: avoid having the joint venture or merged entity retain the agent. Before creating the joint venture, seek to have the foreign partner terminate its relationship with all such agents and wind-up any outstanding financial obligations to them.

- Require the foreign partner to secure FCPA representations from any foreign agents to which it will make payments under pre-existing contracts after the venture is established.

- Implement a comprehensive FCPA compliance program for the new venture.

- Structure the joint venture or merger agreement so that the U.S. company is able to disassociate itself from the venture if it uncovers corrupt activity that it is unable to prevent.

For a fuller discussion of these and other FCPA issues, see Stephen F. Black and Roger M. Witten, *Complying with the Foreign Corrupt Practices Act*, 11 Business Law Monographs (Matthew Bender 2000) (2001 edition forthcoming). If you have any questions or need additional information, please contact:

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