

CORPORATE COMPLIANCE WITH THE FCPA

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I. INTRODUCTION

American corporations have learned to live reasonably with, if not actually love, the Foreign Corrupt Practices Act.¹ Congress is currently being told that there are things that need correcting in the Act. Congress will eventually face these problems rather seriously so that a bill in some form will amend some of the things wrong with the Act. It is doubtful that any business person of good faith thinks there is anything wrong with the theses behind the Act. Business has learned, to its benefit, to live with the requirements of the Act.

II. HOW CORPORATIONS COMPLY WITH THE FOREIGN CORRUPT PRACTICES ACT

The only reliable way to make sure of compliance is to create what the Securities and Exchange Commission (SEC) enforcement staff and others have called a control atmosphere within the corporation.² There are many different ways that American corporations can do that. From my personal experience over the last seven years, here are a few ideas of how I think it is best to do this.

The corporation is a legal figment. It does not really exist aside from physical assets, some money, hopefully, and its employees; from the executives down to the janitors. The top employees, i.e., the chief executive officers working with the board of directors, have to come, at some point, to terms with setting up a system of corporate controls to carry out a policy of compliance with the Act, which was made effective December 19, 1977. If it was not done long before the effective date of the Act, a firm policy decision, at the very senior level, should be reached that the business must be governed by a few major principles. One principle is that in every area, in every country, where the cor-

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1. Foreign Corrupt Practices of 1977, Pub. L. No. 95-213, §§ 102-104, 91 Stat. 1494 (codified at 15 U.S.C. §§ 78a, 78m, 78dd-1, 78dd-2, 78ff (Supp. V 1981)), *reprinted in* Appendix I, *infra*.

2. See, e.g., Note, *The Foreign Corrupt Practices Act of 1977: A Transactional Analysis*, 13 J. INT'L L. & ECON. 367, 369 (1979).

poration operates, has sales or does business of any sort, a well-defined and well-understood set of business ethics and principles should be followed, no matter what the U.S. or other law says. The second point is that, aside from good ethics as defined by the corporation, it is important to know the relevant laws governing business conduct, including, but certainly not limited to, the Act. Then a corporation must do its level best to fit its interpretation of those laws and ethical principles into every tough situation that comes up, and do what is within the law. This is not a moralistic viewpoint. This is business common sense, and if people do not think it is, they are deluding themselves and are going to come to very great grief in the near future.

Most American corporations of size, and probably most that are not big, have not really deviated much from a good system of compliance with ethical principles. The horrid bribery disclosures of the 1975-76 era were aberrations, even in the context of that time. They were not a pattern of the American way of life, or of doing business abroad or in this country. To whatever extent a given corporation thought such practices were a good idea then, the United States government, press and public have made it perfectly obvious that at least American corporations are not going to be tolerated if they do business in a way that is nonethical or nonlegal. It is a matter of good, hard business common sense to create a control atmosphere. It will not be perfect because there will always be the proverbial bad apple who will not believe that a corporation is sincere, and who will think that it really wanted him to go out and make a sale using devious methods because "no one is really ethical." Since American industry hires some quirky people, as well as perfectly lovable and normal people, occasionally there will be someone who will go off the deep end and do something reprehensible. The only way to explain that deviation to the Justice Department, the SEC or anyone else is to show you have a long history of an excellent control atmosphere, and a set of controls, such as those hinted at in section 102 of the Foreign Corrupt Practices Act.

The only decent policy decision at the top level is that a corporation must adhere to high ethical standards. A corporation must adhere to the law, or else it will lose its reputation. We are now living in the tenth year of the post-Watergate era. If a business does anything that is truly exciting to the press and the government, it will be of a serious, reprehensible nature. The

shareholders may not be interested in it. Competitors may not even be interested. But this is the very sort of thing that is eventually going to come out before the public. There is no type of improper action that one can take which will not eventually come to light. Suppose a person who set up a corrupt deal is a known bad actor, who was being considered for termination. As things develop, it becomes more and more obvious that he has been doing something wrong. When it comes to the point of terminating him, what is this person going to do? He is going to attempt extortion. If you encouraged him in this, so much the worse. If he did it on his own, maybe you can explain it to someone. If you condoned it, you are setting yourself up for a great deal of grief. He has annuity and cannot be fired. He may become a very expensive employee, depending upon what it was that was done, and how desirous the corporation is of not having anyone know about it. It simply makes no sense whatsoever to permit anyone to do business for a corporation in a way that would not stand the light of day on the front page of the better known newspapers.

It is certainly material, as the SEC has said, to investors, customers, the government, and the public in general, that they be informed whether or not a given U.S. business' order input is obtained through legitimate and straightforward methods, or whether it is extremely fragile and subject to termination or expropriation because of the unethical way it was obtained. Some devious business dealings, should they occur, are things which have to be disclosed in the normal course of compliance with U.S. securities laws. Not every little peccadillo has to be disclosed. Many considerations determine whether a given deviation from a policy of law and ethics is material or not.

III. DAMAGE CAUSED BY NONCOMPLIANCE

What kind of damage is done by publicized unethical behavior? You lose business and you lose your most valuable asset, which is your corporate reputation. A great deal of the value of a corporation's shares has to do with what the investing public believes is your prospect for the future. And, if you lose your reputation for not having a reasonable amount of the expected ethical virtues, it is very difficult to recapture that reputation. And a good reputation is more valuable to a corporation than any large business deal. You can always make another deal, and, if necessary, close down a part of your business.

It is not an unusual situation for senior business executives to lose a piece of business. You can lose it because your product is not as competitive as someone else's, or your financing is not as good, or your service is not as convenient. Or in a foreign country, your agent is not as influential as a competitor's agent. Parenthetically, there is nothing wrong with having an influential agent. In fact, a corporation would be rather insane to hire noninfluential agents. There is nothing necessarily evil, reprehensible, or questionable about having agents. Indeed, in certain countries, you must have agents in order to do any business locally because of national statutory law. Also, of course, you want to comply with that law.

On top of that, if a corporation violates the Act, the most exciting thing is the penalty. The penalty can be a million dollar fine per violation. I believe that is equal to the largest penalty in the U.S. for any given type of criminal violation. A corrupt payment may be a thousand dollars; still there is a million dollar fine if the government thinks the case is worth prosecuting and it is proved. Also, five years in prison is provided for American executives who knowingly participate in bribery, whether based in Bahrein or somewhere in the United States. I am sure that sooner or later people will suffer these penalties. There are numerous cases pending for investigation now, and some of them will be worthy of prosecution. So the penalties here are not inconsiderable.

On top of loss of reputation, these stiff penalties are one thing that U.S. industrialists would just as soon do without. If there were a possibility of revising the Act, so the penalties were either reduced or removed completely, everyone in business would like it better. However, I do not think that is politically feasible at the present time, nor will it probably ever be. Business people must agree with the basic principle, which is: "Thou shalt not get business through bribery."

As well, you have civil litigation. You have the very hyperactive plaintiff bar waiting in the wings to have the government prove its case, and then file suit against you the next day with a shareholder's derivative action for many millions of dollars. Hiring your own lawyer to defend the suit is a cost that is not inconsiderable.

Even worse than that, of course, is the terrible annoyance and disruption of your own senior management being harrassed by depositions and the trial, if it reaches that point. There will be

competitor action; competitors will say: "Don't buy from them, they're in trouble." You'll get customer reaction. Finally, a judgment may even have to be paid, on top of the fine. But, again, I think loss of corporate reputation is the most serious thing. This is not my view alone; I think reputation is commonly perceived as being very vital in the United States. Anything that imperils reputation is an unreasonable risk, no matter what the immediate gain is to be.

What is necessary is a top-level decision of the chief executive on the question of what the corporate ethical standards will be and what the law-compliance posture will be. The corporation cannot stop there because the chief executive is not omnipresent; he is not in on everything. The board of directors meets once a month, presumably, and cannot know what is going on day to day, except that which is reported to it. For this reason, there must be communication with people who are actually doing the business. And you have to communicate to reasonably low middle-management levels what your policy is. You cannot just give it to ten senior people. Then some training work is necessary to make sure that all managers understand how serious you are, that there aren't any "corrupt countries" where there are exceptions. It must be made clear to everyone from regular executives to marketing people, especially to the lawyers, that you are really willing to forego business and not punish them if they forego an order, because they did not pay the price, a bribe. If you do all these necessary things, I think you will have a control atmosphere to enforce an adequate code of corporate conduct which ought to insure compliance with the Foreign Corrupt Practices Act.

It is sensible for American business to try to persuade the American government to press foreign governments and international groups to require similar types of business ethics principles. Americans should not be taken advantage of by competitors abroad who are not playing by the same rules. It is very difficult to accuse a competitor of having got business by bribery. One might, possibly, in a given situation, have evidence. It is hard for the Department of Justice to find evidence of bribery, and very hard for competitors to find that evidence. And bribery by a competitor is an easy way out for an incompetent or ineffectual marketing person to excuse a loss of a sale; just as it is very easy too for extortionate foreign parties to claim that you have to pay a bribe, which very often is not the case. You do not have to pay the

bribe, you just waste some corporate assets if you do so. Another point is that most every country in the world has a law against bribery, making it a crime.

Some non-American industrialists may think that all I have said up to now about ethics is nonsense. But "men of the world," while they do not like to bribe, find bribery an unpleasant obligation under certain circumstances. They certainly never pay excessive bribes, but only what is absolutely necessary to get business. These people perceive Americans as "Boy Scouts," and that is unfortunate, but we can live with that kind of opinion. It makes little difference whether your competitor is paying bribes or not. You will not know whether they are doing it, there is no way to prove it, and the fact that foreigners do not like our policy is simply unfortunate. Maybe we can nudge them in that direction over the text ten, twenty, or thirty years; it is probably going to be a slow process. Meanwhile, I do not think America will go under. I think we still have enough economic vitality in this country, and in other countries where we may have interests, so we can survive even bribery by competitors, where it might exist.

IV. CODE OF CORPORATE CONDUCT

The first duty of the chief executive officer is to see that the corporation adopts a code of corporate conduct specifying fairly precisely how various ethics and legal problems of doing business are going to be addressed. The code should consist of legal-type principles that managers, aided by lawyers and auditors, will be asked to enforce. The code of conduct should be presented to the board of directors, either all at once or in pieces, in order to obtain their concurrence in it, because some of them may otherwise feel it is costing business, whether or not they have information that could bring them to that conclusion. They read the news and they may get the idea that the loss of an order resulted from a failure to make an appropriate payment.

The chief executive officer has to use whatever facilities are appropriate to establish mechanisms within the corporate entity to assure that the code is adhered to. Once a year, at the first general meeting, maybe more often, the chief executive can hand out the code as updated, to every one of the senior officers in attendance at that meeting. It may be ten and it may be one hundred people; whoever is in charge of each profit center should receive a copy of the corporate code. The chief executive should

personally say, "This code is mine, this is the board of directors', this is your 'law.' And I don't care what the statutes say, you adhere to this. And if you're not an American, don't get mad, the United States government did not force the export of its law. These are our principles, they at least come up to the level of U.S. law. They're seriously taken by us, they'd better be by you, or else you're out of a job." There should be filed, every year, a set of certifications from recipients which say, "I've got the code, I've read it, I've understood it, I've discussed it with my senior people reporting to me, they have told me they understand it and will adhere to it, and enforce it."

For establishment of everyday corporate compliance mechanisms, a corporation should take one or more lawyers within the organization, and place them in charge of interpreting the code, especially in light of the FCPA and the SEC requirements. They can help assure that proper auditing is done and that proper actions are taken with regard to controls, and with regard to checking out, in a methodical basis, compliance with the code. The internal auditing staff could be approached, and one or more of the auditors could be assigned as compliance auditors, and be given the assignment of doing nothing but compliance auditing. These auditors should go into every unit, on a regular basis, and do an audit based upon the components of your code of conduct in order to detect deviations from it. The compliance auditors can be guided by management and lawyers, to help them discern what is material and what is not material. They learn pretty quickly how to do one of these audits. They can come up with an eighty-phase compliance audit grid rather quickly, which is a guide for auditing each subsidiary.

There should be an active education program for all of your units, as well as for headquarters people, to explain the meaning, the purpose and, above all, the seriousness of your code of corporate conduct. Staff departments and unit marketing should know the code, as should quasi-autonomous subsidiaries doing business in another country. There is, then, an educational problem of explaining what these policies mean in practice. The lawyers who are compliance officers should lecture on actual cases and explain how they were handled to correct deviations from the code. It should be possible, then, to illustrate in a concrete manner what your corporate code of conduct means.

Though they are based in the audit department, the com-

pliance auditors function for the compliance officers as the main source of compliance information. It is a good idea not to make the lawyers into detectives or auditors. They ought to spend their time on interpretation and advice to those at the management level. And if there are deviations from the code, the lawyers will have to decide what the legal consequences are, what existing corporate controls, if any, were circumvented as well as the method of circumvention, what additional efforts, including additional controls, are necessary to prevent a recurrence of the same type of violation, whether the deviations should or must be publicly reported, and what disciplinary action might be appropriately taken against a particular violator. The chief executive officer and the board of directors, or the legal affairs committee of the board of directors, should receive regular reports as to the status of the compliance program and any serious deviations.

Furthermore, there is now a good rule of evidence as enunciated by Mr. Justice Rehnquist in *Upjohn Co. v. United States*.³ This opinion decided several important matters. It now appears that the regular and detailed inquiries by internal corporate lawyers into deviations from corporate policy that have criminal or civil overtones are not going to be discoverable by anyone, insofar as they are embodied in a writing prepared by corporate counsel, for counsel, or to enable counsel to perform its function with regard to advising management. The *Upjohn* opinion resolved the legal issue whether information that is conveyed to legal counsel, at the counsel's request, by corporate employees other than the so-called "control group" (a very small group that has the authority to make or enforce corporate policy) is subject to the attorney-client privilege. The Court decided that if lower-level corporate employees give information to counsel in writing, it is protected from discovery under the attorney-client privilege. And the control group test is now stone-cold dead.

The only way you find out the detail of what is going on in a corporation is to ask numerous middle level and slightly higher level people. Counsel has to ask a middle level manager to recon-

3. In *Upjohn Co. v. United States*, 449 U.S. 383 (1981), a pharmaceutical company made questionable payments to foreign officials which were investigated internally by corporate lawyers. The company submitted the information garnered from this investigation voluntarily to the SEC. The Internal Revenue Service (IRS) filed this suit to collect alleged past-due revenues based on those payments. The IRS attempted to use discovery to gain access to the information of the Upjohn internal investigation.

struct what happened, or to assemble figures from here, there and the other place. Obviously, this rule does not in any way protect from discovery information that already exists and was not prepared by or for counsel to advise a client. There is no rule that if information is put into a memo to a lawyer, somehow magically it becomes sacrosanct and no one can look at it. Something that independently exists and was not prepared for the use of a lawyer to perform his professional functions does not obtain protection by conveying it to a lawyer.

In any event, I think that corporate efforts to comply with the Foreign Corrupt Practices Act, if handled by, and for the information of counsel, are likely to be protected from disclosure to other litigating parties. So, there is no reason not to have a full and frank disclosure within the corporation, with the lawyers obtaining information on possible code of conduct or FCPA violations for their professional purposes.

V. CORPORATE CONDUCT AND THE ACCOUNTING AND BRIBERY PROVISIONS

The accounting provisions are important, and they fit with the bribery provisions. If you account correctly for expenditures, it is likely to stop bribery, if it exists. If you do bribe, you had better put in a "bribe" account, or some kind of account that adequately reflects precisely what was done. And if you do not want to identify adequately an auditable account reflecting what you did, you had better not do it.

I think American industry does properly object to the FCPA provision authorizing a prosecutor and a jury to decide you had "reason to know" what a third party was doing with your money. This allows a jury or prosecutor to indulge in second-guessing as to what you must have known about your agents, whether or not this has any relation with what you actually did know, or could reasonably have found out, about your agent's conduct. But I do not think this is anything to be disturbed about, if there is a proper control atmosphere within the corporation.

At one time the SEC and the Justice Department went to the extent of saying, "Well, we think you're probably liable for the bad conduct of your foreign joint venturer. We think you had better monitor your joint venturer's actions for your own protection." It was also once asserted that Americans were responsible for the conduct of their distributors, even if they were true distributors:

independent businessmen, buying from you, taking all risks of ownership, taking all credit risks, reselling, and clearly not an agent. The government once asserted that a company could be responsible if its distributor used corrupt methods to sell to ultimate users. But I do not think the government is now going to press these extreme FCPA theories.

In a company in which a minority's interest is held, are you responsible for the good conduct of the majority? Assume you have a minority on the board. I think you are responsible for knowing what is going on within the company. If you own twenty percent or more, you should not take that investment position unless you have got someone on the board that can learn what is going on. And I think that you should make appropriate objections at the board level, if there are things you suspect are improprieties or if the accounting is not up to American standards. I think you have got to do what you can to make sure that a joint venture in which you have an equal interest, or an entity in which you have a minority interest, is properly run. If it really disturbs you, you ought to sell out, because sooner or later you are probably going to have to anyway.

VI. FEATURES OF A CODE OF CORPORATE CONDUCT

Now what should be included in a code of corporate conduct? The existence of such a code, and its enforcement to the best of human ability, presents a reasonable argument that deviations from required conduct not done corruptly, and, in many cases, are not a proper subject for a prosecution. I believe each American corporation should have something like the International Telephone and Telegraph Code of Corporate Conduct.⁴

The first policy is on business practices, and it simply states that our policy is to adhere to high ethical and legal standards and to obey the laws everywhere. There are also references to sales and marketing representatives; five principles on accounting; and practice 1.01 that develops the theme of proper accounting for assets. These are the documents that should be handed out at least once a year. Everyone at a responsible management level should know them, adhere to them, and be in position to try to enforce them with the help of accountants and lawyers. And the

4. I.T.T. CODE OF CORP. CONDUCT, Appendix III, *infra*.

standard practice simply says that you have to be sure of where your assets are going; you have to be sure that the stated purpose is the actual purpose for which you are spending your funds, and that the purpose as stated is the actual purpose, and that it conforms to your policy.

This particular document, 1.01, provides that you have to have paper showing the authorized parties making the request for corporate money; approval by a person having authority to approve, and that the documents showing the purpose for which the expenditure was made are held permanently in the corporate records for the purpose of audit. Furthermore, it states that everything in excess of \$50,000 to be expended for particular types of purposes, like public relations, advertising, security, proxy solicitation, printing, taxes, legal or consulting services must be personally approved by the chief executive. These are the chief categories in which questionable payments might be disguised. This provision in effect says: you have to take this proposed payment to the boss, and make your case to him, but if something is wrong with this payment, you not only stated that it was proper, but on top of that, you went to the chief executive and told him that it was proper. This is a fairly effective way of preventing people from requesting payments that are not proper. It puts two people on the line, the chief executive officer and the person requesting the payment. I think that deviations from accountability should, as the last paragraph of 1.01 states, be required to be made known to the chief executive officer. He is going to be responsible for this type of enforcement.

Policies 2 and 3, I think, are a good idea because, if you have a control atmosphere, you do not want any kind of conflict of interest by your own employees. If you do not try to control conflict of interest, you probably do not have a control atmosphere; you probably cannot be sure that your ethical conduct requirements are being observed in any other area, such as obtaining and retaining business. It is important to have your senior people certify annually as to their status regarding conflict of interest, to require them to present, if necessary, a negative report, "I have no conflict of interest," and to require employees to report possible conflicts as they arise. I think it is important for you to make sure that your own corporate personnel do not accept gifts, gratuities or accommodations other than as expressly allowed by your policy. If you

are going to say, "Don't give other people gifts," and your people are in the habit of taking substantial gifts, it is very easy for them then to justify the giving of corporate funds.

In policy 4, we forcefully bring to the attention of managers, in writing, that adherence to the key policies is a condition of working for the company, and that they lose their jobs if they are found later to have deviated from, or assisted in a deviation from, or not reported a deviation from, the ethical standards. You may not want to adopt a strict nonpartisan posture for the corporation. In many countries, a political contribution is perfectly legal on the part of corporations. It is easier and safer to say no. We have a firm policy against contributions, and it saves money to say no. The only exception to that would be a political action committee. If you want to have one, they are perfectly legitimate and allowed under American law.

Policy 6 in the package is a detailed list of standards of corporate conduct for your corporation's employees in their relations with government employees. I think it perfectly legitimate to offer the head of a ministry, whom you are going to try to sell something to, an all-expense trip to the United States or to wherever your factory is located. However, this practice must be well-known to his superior, a common practice in his country, and for a business purpose. You must not let him stop over in some garden spot or supply him with a charge account in order to buy personal things at corporate expense. Just the hotel, food and transportation I think are quite legitimate, as long as it is perfectly well known to the superiors in his ministry. I do not think it is corrupt and I do not think it is for his personal use. In many countries, governments expect this, they want the Americans to bear the cost of their doing business as a matter of public policy.

Finally, policy 7 has in it the standards that ought to be observed whenever you use agents. The second item refers to a very detailed form of agreement, which the general counsel will have prepared, having all kinds of proper clauses in it whereby the agent agrees to do certain things and not to do certain things. The important principle is that there is nothing wrong with hiring a legitimate agent who is actually in business performing real services that you can point to. There is nothing wrong with a well-connected person who can speak for you, as long as you have no reason to know, or to believe, that he is passing along money or other gifts.

I do not think that the government has ever taken a contrary position. Agents per se are not suspect, and are specifically required in some countries. They should not be overcompensated for a great many good reasons. You should know who they are. You should have people in that country who can tell you what their reputation is before you hire them. You have to do your best to identify a good, reliable businessman who performs real services and who is adequately but not grossly compensated. You must have no reason to believe he is passing along money. Moreover, I think that compliance with policy number 7 will probably keep you out of trouble with the U.S. government and with any other government.