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Designing an FCPA Compliance Program: Minimizing the Risks of Improper Foreign Payments

Daniel L. Goelzer^{*}

I. INTRODUCTION

Every U.S. company, public or private, that conducts operations outside of the United States should devote serious consideration to creating and implementing an Foreign Corrupt Practices Act ("FCPA" or "Act") compliance program. In this context, an "FCPA compliance program" means a single, documented, corporate plan designed to reduce the likelihood that the company will engage in violations of the anti-bribery provisions of the FCPA, and to detect such violations and bring them to the attention of senior management, if they occur.¹ A well-designed compliance program has obvious importance in educating employees concerning their responsibilities in this complex and perilous area and in thereby protecting the company from the potential costs, liabilities, and reputational damage associated with violations of a high-profile, criminally-enforceable federal statute. In addition, a developing body of law suggests that corporate directors have a duty to assure that compliance programs reasonably designed to the risks of the business are in place, rather than merely attempting to deal with misconduct after it arises.²

This article outlines the process by which an FCPA compliance program may be structured for a multinational company. The article first

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¹ In enacting the FCPA, Congress also sought to curb bribery by preventing companies from creating off-the-books funds or other devices to conceal the use of corporate assets for improper purposes. Section 102 of the Act (Section 13(b)(2) of the Securities Exchange Act of 1934) requires public companies to keep accurate books and records and to devise and maintain adequate systems of accounting controls. See generally Daniel L. Goelzer, *The Accounting Provisions of the Foreign Corrupt Practices Act*, 5 J. CORP. LAW 1 (1979).

² See *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996).

briefly examines some key legal standards against which the effectiveness of such a program is measured. Second, it considers the process by which a compliance program is designed. Third, the three basic components of such a program — a corporate policy, control procedures, and monitoring — are addressed.

II. LEGAL ENVIRONMENT

Several bodies of law should be considered in determining whether to adopt an FCPA compliance program and, if so, what it should contain. The most obvious legal predicate for a compliance program is the FCPA itself. The program should be designed based on the extent to which the company's activities present risks of violations of the statutory prohibitions. In addition, developments related to the obligations of officers and directors generally may bear on the decision to create an FCPA compliance program.

A. The Foreign Corrupt Practices Act

A comprehensive description of the anti-bribery provisions of the FCPA is beyond the scope of this article. Set forth below, however, is an overview of basic issues of importance to the architect of a compliance program.

1. To Whom Does the FCPA Apply?

There are two parts to the anti-bribery provisions of the FCPA.³ Section 103 of the FCPA, which is codified as Section 30A of the Securities Exchange Act of 1934 ("Exchange Act"),⁴ applies to public companies. For these purposes, a "public company" is an issuer of a class of securities registered under Section 12 of the Exchange Act or required to file reports with the Securities and Exchange Commission ("SEC") under Section 15(d) of that Act by virtue of having made a public offering of securities. Section 30A prohibits any such company, or any officer, director, employee, or agent of such a company, from making payments to certain foreign persons or entities for the purpose of assisting the company in obtaining or retaining business with, or directing business to, any person.⁵

Similarly, Section 104 of the FCPA prohibits "domestic concerns" from making such payments.⁶ The term "domestic concern" includes any citizen, resident, or national of the United States and any corporation, part-

³Foreign Corrupt Practices Act of 1977, Pub. L. No. 95-213, 91 Stat. 1494, *as amended* by Title V of the Omnibus Trade & Competitiveness Act of 1988, Pub. L. No. 100-418, §§ 5001-03, 102 Stat. 1415, 1415-25 (codified as amended at 15 U.S.C. §§ 78m(b)(2), 78m(b)(3), 78dd-1, 78dd-2, 78ff (1994)).

⁴Section 30A(a) of the Securities Exchange Act, 15 U.S.C. § 78dd-1(a) (1994) [hereinafter Exchange Act].

⁵*Id.*

⁶15 U.S.C. § 78dd-2. Section 104 is not codified as part of the Exchange Act.

nership, association, stock company, business trust, unincorporated organization, or sole proprietorship which is organized under the laws of the United States (or a state) or which has its principal place of business in the United States.⁷ Therefore, the anti-bribery provisions of the FCPA apply to both publicly-held and private U.S. companies and to all U.S. citizens or residents.

2. What Types of Transactions Does the FCPA Prohibit?

The Act prohibits public companies and domestic concerns from "corruptly" making certain payments to assist in obtaining or retaining business. Such payments are prohibited if made to any one of three categories of persons.⁸ First, payments to foreign governmental officials are unlawful if they are made for the purpose of influencing any act or decision of the recipient in his or her official capacity, inducing him or her to omit to perform any act in violation of his or her duty, or using his or her influence to affect government decisions.⁹ Second, payments to foreign political parties or officials are unlawful if made for the purpose of influencing any act or decision made by the recipient in an official capacity, inducing an omission to act, or inducing the recipient to use influence with his or her government.¹⁰ Finally, it is unlawful to make such a payment to any person, while "knowing" that all or a portion of the payment will be offered, given, or promised, directly or indirectly, to a foreign governmental or political official for the purposes outlined above.¹¹ The Act defines the term "foreign official" to include officers and employees of a foreign government, or any department, agency, or instrumentality thereof (or any person acting in an official capacity on behalf of such a foreign department, agency, or instrumentality).¹²

3. When Does a Company "Know" That a Payment Will be Made to a Foreign Official or Other Prohibited Recipient?

The FCPA defines a person's state of mind to be "knowing" with respect to conduct, a circumstance, or a result, if such person is aware of the

⁷ 15 U.S.C. § 78dd-2(h)(1).

⁸ Exchange Act § 30A(a)(1)-(3), 15 U.S.C. § 78dd-1(a)(1)-(3); 15 U.S.C. § 78dd-2(a)(1)-(3).

⁹ Exchange Act § 30A(a)(1), 15 U.S.C. § 78dd-1(a)(1).

¹⁰ Exchange Act § 30A(a)(2), 15 U.S.C. § 78dd-1(a)(2).

¹¹ Exchange Act § 30A(a)(3), 15 U.S.C. § 78dd-1(a)(3); 15 U.S.C. § 78dd-2(a)(3).

¹² Exchange Act § 30A(f)(1), 15 U.S.C. § 78dd-1(f)(1); 15 U.S.C. § 78dd-2(h)(2). There is no guidance in the statute or the legislative history as to what constitutes an agency or instrumentality of a foreign government. The Foreign Sovereign Immunities Act, 28 U.S.C. § 1602 et seq. (1994), defines the term "agency or instrumentality of a foreign government" to include commercial enterprises, more than 50% of the equity of which is owned by a foreign government. If this definition of "agency or instrumentality of a foreign government" is applicable in the context of the FCPA, payments to employees of state-owned commercial enterprises are within the prohibitions of the Act.

conduct, circumstance, or result or has a "firm belief" that the circumstance exists or that the result is substantially likely to occur.¹³ In addition, knowledge is established when a person is aware of a "high probability" that a circumstance, such as a prohibited payment, has or will occur, unless the person "actually believes" that such circumstance does not exist.¹⁴ While this definition is complex, the result is that "knowledge" includes not only actual knowledge of prohibited payments, but also awareness of circumstances that should reasonably alert one to a "high probability" of a violation.¹⁵

4. When is a Payment Considered to be Made "Corruptly" and for the Purpose of "Obtaining or Retaining Business"?

The FCPA is aimed against attempts to obtain business through influence-buying abroad. The legislative history indicates that the word "corruptly" adds an element of intent to the violation and "connotes an evil motive or purpose."¹⁶ Further, since the statute requires that the payment be made in order to assist "in obtaining or retaining business for or with, or directing business to, any person,"¹⁷ only payments which are related to commercial activity are prohibited. The purpose for which a payment is made is, therefore, critical in determining whether the Act has been violated. A payment to an official in the government procurement department, which is intended to influence that official to award a contract to the payor, would certainly violate the Act. Payments related to foreign taxes or to influence the general political climate in a foreign country may be more arguable. The safest assumption, however, is that any "corrupt" payment to a prohibited recipient will raise serious FCPA issues.

¹³Exchange Act § 30A(f)(2)(A), 15 U.S.C. § 78dd-1(f)(2)(A); 15 U.S.C. § 78dd-2(h)(3)(A).

¹⁴Exchange Act § 30A(f)(2)(B), 15 U.S.C. § 78dd-1(f)(2)(B); 15 U.S.C. § 78dd-2(h)(3)(B).

¹⁵"When knowledge of the existence of a particular circumstance is required for an offense, such knowledge is established if a person is aware of a high probability of the existence of such circumstance, unless the person actually believes that such circumstance does not exist." Exchange Act § 30A(f)(2)(B), 15 U.S.C. § 78dd-1(f)(2)(B); 15 U.S.C. § 78dd-2(h)(3)(B).

The Conference Report on the 1988 amendments indicates that this knowledge standard encompasses a "conscious purpose to avoid learning the truth." H.R. Rep. No. 100-576, at 919 (1988) *reprinted in* 1988 U.S.C.C.A.N. 1949, 1952. Therefore, the disregard of circumstances that should alert one to bribery constitutes "knowledge" of such bribery:

[T]he Conferees also agreed that the so-called 'head-in-the-sand' problem -- variously described in the pertinent authorities as 'conscious disregard,' 'willful blindness,' or 'deliberate ignorance' -- should be covered so that management officials could not take refuge from the Act's prohibitions by their unwarranted obliviousness to any action (or inaction), language or other 'signaling device' that should reasonably alert them of the 'high probability' of an FCPA violation.

H.R. Rep. No. 100-576, at 920 (1988) *reprinted in* 1988 U.S.C.C.A.N. 1949, 1953.

¹⁶S. Rep. No. 95-114, at 10 (1977) *reprinted in* 1977 U.S.C.C.A.N. 4098, 4108.

¹⁷Exchange Act § 30A(a), 15 U.S.C. § 78dd-1(a); 15 U.S.C. § 78dd-2(a).

5. Are "Facilitating Payments" of the Type that are Necessary in Some Countries to Induce Government Functionaries to Perform Their Duties Prohibited?

Payments to foreign officials that are intended to encourage those officials to perform a routine governmental action (referred to euphemistically in the FCPA as "facilitating payments") are specifically excluded from the prohibitions of the Act.¹⁸ A routine governmental action is defined as an action ordinarily and commonly performed by a foreign official in connection with such things as issuing permits, licenses, or other official documents to qualify a person to do business; processing governmental papers such as visas and work orders; providing police protection; mail pick-up and delivery, or scheduling inspections; providing phone service, power and water supply, loading and unloading cargo; and similar actions.¹⁹ However, any decision by a foreign official to award new business to, or to continue business with, a particular person, or to take any action involved in the decision-making process "to encourage a decision to award new business or to continue business" is excluded from the definition of routine governmental action.²⁰ Reliance on this exclusion from the Act should, therefore, be limited. Under some circumstances, it may be difficult to determine whether a particular action is "ordinarily and commonly performed" or whether it could be deemed part of the "decision-making processes."

6. How Is the Line Drawn Between Legitimate Payments to Foreign Officials and Bribes?

Payments which are lawful under the "written laws and regulations" to which the foreign official is subject are not prohibited.²¹ Further, "reasonable and bona fide" expenditures, such as payments for travel or lodging, and payments directly related to the promotion or demonstration of products or services or to the performance of a contract with a foreign government or agency are permitted.²²

¹⁸ Exchange Act § 30A(b), 15 U.S.C. § 78dd-1(b); 15 U.S.C. § 78dd-2(b).

¹⁹ Exchange Act § 30A(f)(3)(A), 15 U.S.C. § 78dd-1(f)(3)(A); 15 U.S.C. § 78dd-2(h)(4)(A).

²⁰ Exchange Act § 30A(f)(3)(B), 15 U.S.C. § 78dd-1(f)(3)(B); 15 U.S.C. § 78dd-2(h)(4)(B).

²¹ Exchange Act § 30A(c)(1), 15 U.S.C. § 78dd-1(c)(1); 15 U.S.C. § 78dd-2(c)(1). The legislative history of the 1988 Amendments to the Act states that, in order for this exception to be available, the action in question must be specifically permitted under such written laws and regulations; the absence of a prohibition is not sufficient. H.R. Rep. No. 100-576, at 922, *reprinted in* 1988 U.S.C.C.A.N. 1949, 1955.

²² Exchange Act § 30A(c)(2), 15 U.S.C. § 78dd-1(c)(2); 15 U.S.C. § 78dd-2(c)(2).

7. Is a Company That Is Subject to the FCPA Also Liable for Violations Committed by its Foreign Subsidiaries?

The House version of the legislation that enacted the FCPA would have extended the anti-bribery prohibition to subsidiaries controlled (by virtue of a fifty percent or greater ownership interest) by a domestic concern. While this provision was deleted from the bill, the legislative history makes clear that domestic concerns may be vicariously liable for bribes paid on their behalf by other entities under certain circumstances. The Conference Committee Report states:

In receding to the Senate [*i.e.*, omitting the House provision regarding subsidiaries], the conferees recognized the inherent jurisdictional, enforcement, and diplomatic difficulties raised by the inclusion of foreign subsidiaries of U.S. companies in the direct prohibitions of the bill. *However, the conferees intend to make clear that any issuer or domestic concern which engages in bribery of foreign officials indirectly through any other person or entity would itself be liable under the bill.*²³

8. What are the Consequences of a Violation of the Act?

Penalties for violating the anti-bribery provisions of the Act are severe. Public companies are subject to criminal fines of not more than \$2,000,000 per violation.²⁴ Such companies are also subject to civil fines of up to \$10,000 in actions brought by the SEC.²⁵ Any officer or director of the company, or a stockholder acting on behalf of the company, and any employee or agent who is a U.S. citizen, resident, or national or is otherwise subject to U.S. jurisdiction, may be criminally fined not more than \$100,000 or imprisoned not more than five years, or both, for a willful violation.²⁶ These persons are also subject to a civil penalty in an SEC action of not more than \$10,000.²⁷ The FCPA expressly prohibits the company from paying any such fine levied on an individual associated with the company.²⁸ The SEC also can bring a civil action to obtain an injunction against future violations, or commence administrative cease and desist proceedings against a public company or persons who caused such a company to violate Section 30A.²⁹

Domestic concerns (including all U.S. citizens and residents) that are not within the SEC's jurisdiction are subject to a similar body of sanc-

²³ H.R. Rep. No. 95-831, at 14 (1997) *reprinted in* 1977 U.S.C.C.A.N. 4121, 4126 (emphasis added).

²⁴ Exchange Act § 32(c)(1)(A), 15 U.S.C. § 78ff(c)(1)(A).

²⁵ Exchange Act § 32(c)(1)(B), 15 U.S.C. § 78ff(c)(1)(B).

²⁶ Exchange Act § 32(c)(2)(A) and (B), 15 U.S.C. § 78ff(c)(2)(A) & (B).

²⁷ Exchange Act § 32(c)(1)(C), 15 U.S.C. § 78ff(c)(1)(C).

²⁸ Exchange Act § 32(c)(3), 15 U.S.C. § 78ff(c)(3).

²⁹ See Exchange Act §§ 21, 21B, 21C, 15 U.S.C. §§ 78u, 78u-2, 78u-3.

tions.³⁰ The U.S. Attorney General, rather than the SEC, has the responsibility for civil actions against such companies and persons.³¹

B. Organizational Sentencing Guidelines

One of the greatest incentives to formulating a corporate compliance program is the Federal Sentencing Guidelines.³² Chapter Eight of the Guidelines, "Sentencing of Organizations" (hereinafter "Organizational Sentencing Guidelines"), embodies various principles, including that "the fine range for any other organization should be based on the seriousness of the offense and the culpability of the organization."³³ Culpability, in turn, depends in part on "the steps taken by the organization prior to the offense to prevent and detect criminal conduct [and] the level and extent of involvement in or tolerance of the offense by certain personnel * * *."³⁴ Under this philosophy, an organization's culpability score is reduced if "the offense occurred despite an effective program to prevent and detect violations of law."³⁵ The benefit of this reduction may, however, be lost if a "high level" official of the organization or an official responsible for the administration of the program participated in, condoned, or willfully ignored the violation.³⁶ The Organizational Sentencing Guidelines define the phrase "effective program to prevent and detect violations of law" as —

a program that has been reasonably designed, implemented, and enforced so that it generally will be effective in preventing and detecting criminal conduct. Failure to prevent or detect the instant offense, by itself, does not mean that the program was not effective. The hallmark of an effective program to prevent and detect violations of law is that the organization exercised *due diligence* in seeking to prevent and detect criminal conduct by its employees and other agents.³⁷

The guidelines also set forth seven steps that "at a minimum" the organization must take in order to satisfy the due diligence requirement. These seven steps are listed below.³⁸

³⁰ 15 U.S.C. § 78dd-2(g).

³¹ See 15 U.S.C. §§ 78dd-2(d)(1), 78dd-2(g)(1)(B), 78dd-2(g)(2)(C).

³² U.S. SENTENCING GUIDELINES MANUAL, § 8 (1997) [hereinafter USSG].

³³ USSG Ch. 8, intro. cmt.

³⁴ *Id.*

³⁵ USSG § 8C2.5(f).

³⁶ *Id.*

³⁷ USSG § 8A1.2, application note 3(k) (emphasis added) (Application note 3(k) is hereinafter referred to as "Organizational Sentencing Guidelines Note (3)(k)").

³⁸ *Id.* Organizational Sentencing Guidelines Note (3)(k) also includes the caveat that the "precise actions necessary for an effective program to prevent and detect violations of law will depend upon a number of factors" including the size of the organization; the likelihood that certain offenses may occur because of the nature of its business; and the prior history of the organization. Moreover, "failure to incorporate and follow applicable industry practice or the standards called for by any applicable governmental regulation weighs against a finding of an effective program to prevent and detect violations of law." *Id.*

(1) The organization must have established compliance standards and procedures to be followed by its employees and other agents that are reasonably capable of reducing the prospect of criminal conduct.³⁹

This element would seem to require a statement of corporate policy (*i.e.*, a “compliance standard”) explaining the prohibitions of the FCPA and setting forth the company’s expectation that employees will refrain from violations. Whether such a code of conduct alone is “reasonably capable of reducing the prospect” of violations will depend on the nature of the company’s activities, past history of questionable payments, and other factors.

(2) Specific individual(s) within high-level personnel of the organization must have been assigned overall responsibility to oversee compliance with such standards and procedures.⁴⁰

“High-level personnel of the organization” means “individuals who have substantial control over the organization or who have a substantial role in the making of policy within the organization.”⁴¹ Directors, executive officers, and individuals in charge of a major business or functional unit of the organization are included within the concept of “high-level personnel.”⁴² In many cases, the General Counsel is designated as the company’s compliance officer. It may, however, be prudent to appoint a committee of senior personnel, including the General Counsel, in the event that judgments concerning the application of the FCPA are expected to arise frequently. Moreover, in the event that the company has decentralized management and numerous locations, it may be desirable to delegate responsibility for administration of the FCPA compliance program to senior personnel at various locations.

(3) The organization must have used due care not to delegate substantial discretionary authority to individuals whom the organization knew, or should have known through the exercise of due diligence, had a propensity to engage in illegal activities.⁴³

Persons found to have intentionally engaged in questionable foreign payments should not be left in positions that would permit them to repeat their conduct. Presumably, cases of serious and intentional violation would normally result in termination. In other cases, such as small payments made in violation of company policy but arguably within the “facilitating payment” exception to the FCPA, the institution of controls designed to prevent a repetition (*i.e.*, controls that deprive the individual of “substantial discretionary authority” with respect to such matters) may be appropriate.

³⁹ USSG §8A1.2, application note 3(k)(1).

⁴⁰ USSG §8A1.2, application note 3(k)(2).

⁴¹ USSG §8A1.2, application note 3(b).

⁴² *Id.*

⁴³ USSG §8A1.2, application note 3(k)(3).

(4) The organization must have taken steps to communicate effectively its standards and procedures to all employees and other agents, *e.g.*, by requiring participation in training programs or by disseminating publications that explain in a practical manner what is required.⁴⁴

The company's code of conduct or policy statement should be disseminated throughout the organization. It may also be appropriate to require employees (or at least employees in certain categories) to certify periodically in writing that they have read the policy, had the opportunity to ask questions, and understand it. It is also desirable to conduct periodic training programs concerning the requirements of the FCPA and the company's policy, especially for employees based in foreign countries or who otherwise are likely to encounter FCPA issues. Periodic dissemination of updating information concerning the FCPA, such as news reports of law enforcement proceedings, also evidence an effort to satisfy this due diligence factor.

(5) The organization must have taken reasonable steps to achieve compliance with its standards, *e.g.*, by utilizing monitoring and auditing systems reasonably designed to detect criminal conduct by its employees and other agents and by having in place and publicizing a reporting system whereby employees and other agents could report criminal conduct by others within the organization without fear of retribution.⁴⁵

This factor makes clear that mere promulgation of a compliance program, without follow-up, is not sufficient. Monitoring and auditing are discussed in detail below.

(6) The standards must have been consistently enforced through appropriate disciplinary mechanisms, including, as appropriate, discipline of individuals responsible for the failure to detect an offense. Adequate discipline of individuals responsible for an offense is a necessary component of enforcement; however, the form of discipline that will be appropriate will be case specific.⁴⁶

It is important that the company demonstrate a commitment to enforcing its policy. When violations are discovered, appropriate action should be taken against those involved. Not every violation may necessarily justify termination of the offender. Depending upon the circumstances, sanctions such as suspension, demotion, forfeiture of a portion of pay, reprimand, or reassignment may be sufficient to demonstrate that the company takes its policy seriously. If instances of possible violations of the policy are investigated and no action is taken against those involved, the reasons for that result should be documented.

⁴⁴USSG §8A1.2, application note 3(k)(4).

⁴⁵USSG §8A1.2, application note 3(k)(5).

⁴⁶USSG §8A1.2, application note 3(k)(6).

(7) After an offense has been detected, the organization must have taken all reasonable steps to respond appropriately to the offense and to prevent further similar offenses — including any necessary modifications to its program to prevent and detect violations of law.⁴⁷

Whenever a violation of the policy comes to light, the compliance program should be reviewed with a view to determining why the violation occurred and whether changes should be made in the program to prevent a reoccurrence. At the same time, it is important to recognize that no compliance program, in any field, can prevent a determined group of employees from engaging in misconduct. A program that tries to impose controls on every conceivable activity that might result in misconduct is likely to prove unwieldy and, in the long run, unenforceable.

C. Directors' Fiduciary Responsibilities

While the potentially severe consequences of FCPA violations and the potential Organizational Sentencing Guidelines benefits of an effective compliance program are the dominant reasons to implement an FCPA compliance program, other factors may also come into play. In particular, the Delaware Court of Chancery has recently suggested that directors of Delaware corporations have a fiduciary duty to monitor corporate activities with a view to detecting unlawful conduct.⁴⁸ In order to discharge this duty, adoption of a compliance program in areas where there is a risk of violations would seem to be necessary. Similarly, the SEC has suggested in certain enforcement proceedings that corporate officers and directors who are on notice of possible violations of the securities laws have an obligation, enforceable in SEC proceedings, to take steps to investigate and prevent any further violations from occurring.⁴⁹

1. Directors' Fiduciary Duty to Adopt a Program of Corporate Compliance

The recent *Caremark* decision of the Delaware Court of Chancery suggests that corporate directors have an affirmative duty to implement a compliance program to detect violations of law.⁵⁰ In *Caremark*, a derivative action was brought against the members of the company's board of directors to recover criminal and civil fines paid by the company as a result of violations by company employees of certain federal and state laws applicable to healthcare providers. The directors were not alleged to have condoned or authorized the violations; rather, they were alleged to have breached their fiduciary duty of care by failing to learn of the unlawful activity and by failing to adequately control Caremark's employees. In the

⁴⁷ USSG §8A1.2, application note 3(k)(7).

⁴⁸ See *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996).

⁴⁹ See *infra* Part II.C.2.

⁵⁰ *Caremark*, 698 A.2d at 967-70.

course of considering whether a proposed settlement of this action was fair and reasonable, the court considered whether directors have a legally enforceable obligation to monitor and detect violations of law by corporate employees. Chancellor Allen concluded:

Thus, I am of the view that a director's obligation includes a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists, and that failure to do so under some circumstances may, in theory at least, render a director liable for losses caused by non-compliance with applicable legal standards.⁵¹

In reaching this conclusion, the court noted that the Organizational Sentencing Guidelines "offer powerful incentives for corporations today to have in place compliance programs to detect violations of law, promptly to report violations to appropriate public officials, when discovered, and to take prompt, voluntary remedial efforts."⁵²

2. Securities Law Duty to Address Known Risks of Misconduct

The SEC has not yet directly taken the position that officers and directors who fail to implement a compliance program are themselves liable to SEC enforcement action if the company engages in violations of the law. There are, however, two recent enforcement proceedings that strongly suggest that SEC action may result where directors or officers are on notice of the possibility of securities law violations and fail to take prompt corrective actions. These proceedings are discussed below.

In *In re Cooper Companies*, the SEC issued a "Report of Investigation" concerning the conduct of the board of directors of Cooper.⁵³ In essence, the Commission found that the directors had failed to take action despite information that the senior officials of the company had engaged in fraudulent and manipulative trading in certain securities issued by the company. The SEC Report describes the board's failure to promptly inquire into these matters and to remove the offenders from positions in which they could issue public statements on behalf of the company as a failure to fulfill the board's "obligations under the federal securities laws when confronted with evidence of serious wrongdoing by persons it continued to entrust with day-to-day management of the company."⁵⁴ The SEC concluded:

The Commission considers it essential for board members to move aggressively to fulfill their responsibilities to oversee the conduct and performance of management and to ensure that the company's public statements are candid and complete. The Commission has long viewed the issue of corporate governance and the fiduciary obligations of members of management and the boards of directors of public companies to their investors as an issue of para-

⁵¹ *Id.* at 970.

⁵² *Id.* at 969.

⁵³ Cooper Cos. Report, Exchange Act Release No. 35082, [1994-1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85472, at 86,061 (Dec. 12, 1994).

⁵⁴ *Id.* at 86,062.

mount importance to the integrity and soundness of our capital markets. These obligations are particularly acute where potential violations of the federal securities laws involving self-dealing and fraud by management are called to the attention of the board of directors.⁵⁵

Recently, the SEC reiterated this point in *In the Matter of W.R. Grace & Co.*⁵⁶ That case involved a company's alleged failure to disclose benefits paid to a retired chief executive officer and a related party transaction between a senior official and the company. The SEC stated:

Serving as an officer or director of a public company is a privilege which carries with it substantial obligations. If an officer or director knows or should know that his or her company's statements concerning particular issues are inadequate or incomplete, he or she has an obligation to correct that failure. An officer or director may rely upon the company's procedures for determining what disclosure is required only if he or she has a reasonable basis for believing that those procedures have resulted in full consideration of those issues.⁵⁷

While these cases involve disclosure violations,⁵⁸ it may not be a long step to the conclusion that the same reasoning could be applied to violations of Section 30A of the Exchange Act. And, as the W.R. Grace report suggests, the Commission may also be moving in the same direction as the Delaware Chancery Court — both the court and the SEC have indicated that directors are obligated not only to take steps to terminate violations when they come to the directors' attention, but also to have procedures in place to detect and prevent violations before occurrence.⁵⁹ The balance of this article considers the process by which such a program may be designed with respect to the FCPA.

III. DESIGNING AN FCPA COMPLIANCE PROGRAM

In order to design an effective FCPA compliance program, several basic categories of information concerning the company and its operations must first be compiled. Even when the program designer is a company insider with intimate knowledge of the company, it may be useful for him or her to review and consider, in an organized manner, the environment in which the company operates and what the risks of questionable payments in that environment are. If the program is designed by counsel or other outside consultants, the need to gather information so that the program is properly tailored to the company is obvious.

⁵⁵ *Id.* at 86,065.

⁵⁶ W.R. Grace & Co., Exchange Act Release No. 39157, [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶85963, at 89,889 (Sept. 30, 1997).

⁵⁷ *Id.* at 89,897.

⁵⁸ *But see* John H. Gutfreund, Exchange Act Release No. 31554, [1992 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶85,067, at 83,597 (Dec. 3, 1992) (failure of senior officials of a brokerage firm to act promptly after learning of violations related to Treasury auction procedures and limitations by a trader constituted a breach of senior officials' supervisory duties).

⁵⁹ See notes 41-43, 44-49 and accompanying text.

Three basic kinds of information need to be collected — the risks of FCPA violations, the existing controls, and the resources and commitment available to administer and monitor the program. Armed with this information, the program architect should identify explicitly the objectives that he or she seeks to accomplish through the compliance program.

A. Identifying Risks

The most basic step in designing an FCPA compliance program is to determine the risks against which such a program is intended to protect. It is therefore necessary to gain an understanding of how and where the company does business abroad. A company with few foreign operations or that does business only in jurisdictions in which bribery is unlikely to occur, faces a far different task in designing a compliance program than does one whose business is dependent on the award of government contracts in a jurisdiction where bribery is endemic.

The first step in this process is to review the basic sources of information that describe the company's foreign operations and the circumstances under which the company has contact with, or requires action or approval by, foreign officials. The Organizational Sentencing Guidelines suggest that the failure to perform this type of risk analysis can be fatal to the effectiveness of the plan. "If because of the nature of an organization's business there is a substantial risk that certain types of offenses may occur, management must have taken steps to prevent and detect those types of offenses."⁶⁰ Such sources include SEC filings and other descriptions of the company's business operations; interviews with corporate officials; and securities analysts' reports, news articles, and other published sources of information. The compliance planner should learn the location, nature, and scope of foreign operations; the legal form in which the company conducts off-shore operations (e.g., through branches, subsidiaries, independent sales agents, or joint ventures); how and by whom foreign operations are managed; and the extent to which the company conducts operations in jurisdictions that could be viewed as "high risk" for FCPA violations.

While caution needs to be used so that the process of designing a compliance program does not evolve into an investigation of possible past misconduct,⁶¹ one aspect of understanding the risks that the program should address is uncovering any examples of questionable foreign payments sus-

⁶⁰USSG § 8A1.2, application note 3(k)(ii).

⁶¹Different considerations concerning attorney-client privilege, the rights of employees, the results and documentation of the inquiry, and other matters apply to investigations of specific past events of misconduct. Although beyond the scope of this article, much has been written about the conduct of an internal investigation. See, e.g., Ralph C. Ferrara et al., *Internal Corporate Investigations and the SEC's Message to Directors in Cooper Co.*, 65 U. CIN. L. REV. 75 (1996); Robert J. Bush, Comment, *Stimulating Corporate Self-Regulation -- The Corporate Self-Evaluative Privilege: Paradigmatic Preferentialism or Pragmatic Panacea*, 87 NW. U. L. REV. 597 (1993).

pected by management or previously identified by governmental authorities. Further, if the company has previously been involved in any formal U.S. or foreign proceeding in which it was alleged that bribery occurred, the circumstances obviously must be thoroughly reviewed and procedures designed to prevent a repetition of this event.⁶²

More frequently, however, corporate officials may merely have suspicions concerning particular activities, jurisdictions, or transactions that could lend themselves to questionable payments. Interviews with working-level employees may, for example, produce information that is not obvious from a review of documents and procedures. Depending on the situation, it may therefore be appropriate to visit foreign operations and interview local personnel.

B. Assessing Existing Controls

After the basic risks to which the company is subject have been determined, existing controls relevant to preventing and detecting improper payments should be inventoried. In some cases, the creation of a compliance program may consist largely of drafting a policy and collecting all of the existing controls and procedures designed to prevent illicit payments in a single document. These could include accounting controls designed to prevent the creation of unaccountable assets pools; approval procedures for the retention of agents; standard terms concerning FCPA compliance in agency, joint venture, and similar contracts; and comparable measures.

Conversely, the process of identifying existing controls may expose the need for additional controls. One possible source of information as to weaknesses or control failures is the outside auditor's internal control letter. Typically, the outside auditors of a public company will furnish the company with a letter summarizing the auditor's review of accounting controls, identifying weaknesses or deficiencies, and recommending specific corrections. As noted above, in enacting the FCPA, Congress both prohibited foreign bribery and broadly required that public companies maintain accurate books and records and establish adequate internal accounting controls.⁶³ While the design of a system of internal accounting controls is beyond the scope of this article, the existence of such a system is both a legal requirement and a cornerstone of an anti-bribery compliance program. The accuracy and adequacy of record-keeping and internal controls are key components of any effort to prevent or detect questionable foreign payments.

If additional procedural controls are needed, it is important that new procedures not overlap with or contradict existing controls. FCPA compli-

⁶²"An organization's prior history may indicate types of offenses that it should have taken actions to prevent. Recurrence of misconduct similar to that which an organization has previously committed casts doubt on whether it took all reasonable steps to prevent such misconduct." USSG § 8A1.2, application note 3(k)(iii).

⁶³USSG § 8A1.2, application note 3(k)(2); *see supra* Part II.A.2.

ance procedures should mesh smoothly with existing processes for obtaining approval for the retention of consultants, approval of cash expenditures, and similar activities.

C. Considering Available Resources

In designing a compliance program, it also is necessary to consider who will be responsible for implementing the program and what resources — in both money and management time — will be necessary to administer it. There needs to be a realistic assessment of whether the personnel responsible for implementing the program will be able to do so, consistent with the discharge of their other duties. The most thoughtfully designed and engineered program, if not enforced or applied, is as bad as no program at all. Therefore, the program needs to match not only the risks of the business, but also the capabilities and resources of those who will be implementing it.

The commentary concerning effective compliance programs in the Organizational Sentencing Guidelines calls for “high-level personnel” to be assigned “overall responsibility to oversee compliance.”⁶⁴ In practice, this often means that the company’s General Counsel is designated as the executive responsible for compliance matters, including FCPA compliance. If the compliance program calls for pre-approval of contracts with foreign agents or consultants, approval of particular types of expenditures, or similar recurring actions, it may also be necessary to assign lower-level personnel to process these actions under the supervision of the executive with overall responsibility. Care needs to be taken at both ends of the spectrum: Senior officials assigned responsibility for the program must have a willingness and commitment to treat this duty as a priority. More junior employees must be properly trained and have a thorough understanding of what is expected of them.

D. Defining Objectives

Once these basic categories of information have been collected, the next step in developing a compliance program is to define the program’s scope and objectives. While programs vary widely and must of course be tailored to the company’s circumstances, FCPA compliance programs typically attempt to address one or a combination of three broad objectives — documentation of company policy and education of employees, imposition of procedural controls, and monitoring of compliance.

Documentation and Education. The core of most FCPA compliance programs is a statement of corporate policy. This statement typically describes the requirements of the FCPA and expresses the company’s commitment to avoiding practices that could constitute violations. Such a policy statement documents that the company has considered

⁶⁴USSG § 8A1.2, application note 3(k)(2); *see supra* Part II.B.2.

the FCPA and alerted its employees to the importance of adherence thereto. Depending on the level of detail, the policy may also serve to inform or educate employees concerning prohibited practices.

Procedural Controls To Promote Compliance. Procedural controls, as discussed above, are designed to address the specific types of foreign activities in which the company engages and to impose checks or limitations on those which pose risks of violation.

Monitoring. Monitoring procedures should be devised to periodically verify compliance with the anti-bribery provisions of the FCPA and with the company's policy in high-risk areas of the business.

IV. ELEMENTS OF AN FCPA POLICY

An effective FCPA compliance program need not necessarily include any specific set of features. The program must, however, be carefully tailored to the company's unique circumstances and to the specific risks that employees, agents, affiliates, or others empowered to act on the company's behalf will engage in the kind of conduct prohibited by the FCPA. Moreover, this is a field in which too much may be more harmful than too little. A program that includes procedures and controls which are not followed in practice may prove to be an aggravating, rather than a mitigating, factor in the event of an FCPA violation. With these caveats in mind, set forth below are some features which may be considered for inclusion in an FCPA compliance program.

A. Statement of Corporate Policy

The first and most common component of a compliance program is a statement of corporate policy or a "code of conduct" that sets forth the company's expectation that employees will strictly adhere to the law.⁶⁵ Especially in the case of a large organization, such a policy statement is imperative.⁶⁶ The policy would generally include a description of the prohibitions in the FCPA, possibly with supporting detail or examples relevant to the company's activities. The policy should also describe the accounting provisions of the FCPA and set forth the company's expectation that all employees will adhere to the requirement that corporate books and records be accurate.

⁶⁵In many cases, a company may adopt separate codes of conduct or separate chapters or sections in an overall compliance manual to deal with different compliance issues, such as FCPA, antitrust, insider trading, anti-discrimination, environmental compliance, etc. In other cases, all of these topics may be combined in a single, comprehensive code.

⁶⁶USSG § 8A1.2, application note 3(k)(i):

The requisite degree of formality of a program to prevent and detect violations of law will vary with the size of the organization: the larger the organization, the more formal the program typically should be. A larger organization generally should have established written policies defining the standards and procedures to be followed by its employees and other agents.

In addition to educating employees concerning the applicable legal requirements, the policy statement may also include other types of information. For example —

Assignment of Compliance Responsibilities. The policy statement may include a statement of the assignment of responsibilities within the company for addressing questions that arise under the FCPA. If a compliance committee has been formed, its membership should be identified. If the General Counsel, or another senior official, is the focal point for FCPA compliance, that fact should be made clear.

Documenting the Corporate Culture. The policy statement should also serve as a reflection of senior management's commitment to FCPA compliance and evidence of the corporate compliance culture.

Gathering Information. The policy statement should inform employees concerning who should be contacted in the event that interpretive issues or other questions arise and concerning whom should be informed in the event that an employee believes that a violation has occurred. Mechanisms, such as employee hot-lines and anonymous reporting procedures, may also increase the likelihood that information concerning nascent FCPA issues will come to management's attention at an early stage.

Obviously, the creation and issuance of a policy statement is, in itself, not effective to prevent or detect violations of the FCPA.⁶⁷ At a minimum, the policy must be disseminated widely throughout the organization, such as by inclusion in employee handbooks or similar materials.⁶⁸ Periodic training concerning the FCPA and the company's compliance program may be appropriate for certain categories of employees.

B. Control Procedures

The second component of a compliance program is the creation and implementation of procedures designed to prevent violations of the law or of the corporate policy. In many cases, a policy statement may be sufficient as the company's FCPA compliance program. In cases where particular recurring situations arise in which there is a greater risk of FCPA violations occurring, it may be desirable also to create specific internal controls as part of the program. Such procedures might include due diligence with respect to agents, consultants, joint venturers, and other foreign partners; certifications or similar mechanisms to provide evidence that employees are aware of and have adhered to corporate policy; and devices to bring violations to management's attention.

Some examples of procedural controls include —

⁶⁷ See *id.* application note 3(k)(4).

⁶⁸ *Id.*

1. Contractual Terms

Consultants or agents involved in foreign operations or based outside the United States may be required to execute a contract containing FCPA compliance requirements. Such contractual terms should clearly and unequivocally indicate that the consultant or agent is prohibited from making any payments in violation of the FCPA on behalf of the company or in the course of acting on behalf of the company.

2. Expenditure Controls

Cash expenditures over a certain level may require special approvals and standardized documentation. Stricter approval requirements, or lower approval thresholds, may be applied in particular foreign jurisdictions. Documentation may be required for all such cash expenditures and specific procedures may apply to the retention of such documentation.

3. Due Diligence

A procedure for performing due diligence with respect to foreign agents, consultants, distributors, joint venture partners, investees, acquirees, and similar persons or entities that have relationships with the company and are involved in its foreign operations should be considered.⁶⁹ Whether such a person's improper payments would legally be attributable to the company depends on the circumstances of each situation. It is, however, usually prudent to develop information concerning the other party to such relationships in order to assess whether it is prudent to do business with that party.

Prospective agents might, for example, be required to provide responses to a standard list of questions, including such matters as educational and business background; identity of other clients; existence of any family or business relationship with government officials; credit and personal references; or prior involvement in criminal or regulatory proceedings. In addition to obtaining information directly from the individual, due diligence with respect to the retention of an agent could include a review of publicly available data sources, such as business directories, online information services, or the Internet.

Another facet of due diligence with respect to agents is to determine whether the fees to be charged are reasonable, relative to comparable services offered by others in the local market. If agents are entitled to reimbursement for expenses, a mechanism should be in place to require supporting documentation. In general, precautions should be taken to reduce the likelihood that the agent will receive or have access to company

⁶⁹In the author's view, the extent to which a U.S. company would have FCPA liability for payments made by a distributor of its products or a joint venture partner would depend on the facts and circumstances of the relationship. Prudence may, however, dictate that distributors and joint venture partners be subjected to the same due diligence procedures as agents.

funds that might be shared with government officials. In this regard, commissions based on a percentage of business generated or by a similar arrangement require close scrutiny.

4. Certifications

As noted above, certain categories of employees may be required to certify periodically that they have reviewed the corporate FCPA policy and have not engaged in and are not aware of any violations thereof.⁷⁰ In some cases, similar certifications by agents or joint venturers may be appropriate. Where certifications are required, a penalty — such as dismissal or termination of contract — should be provided in the event that a certification is later discovered to be false.

5. Facilitating Payment Procedures

A methodology for obtaining approval and documenting payments that raise FCPA “red flags,” but are deemed to be legal, may be desirable in situations in which such payments are common. Recurrent payments to secure the performance of ministerial actions,⁷¹ payments to governmental officials that are lawful under the written law of the foreign jurisdiction,⁷² and legitimate travel and entertainment expenses of foreign officials,⁷³ may justify a standardized approval and documentation process if they occur frequently.

C. Monitoring Mechanisms

The third component of a compliance program is a mechanism to monitor the implementation of the program. As discussed earlier, the Organizational Sentencing Guidelines contemplate “steps to achieve compliance . . . e.g., by utilizing monitoring and auditing systems reasonably designed to detect criminal conduct.”⁷⁴ The nature and extent of monitoring mechanisms adopted will depend on the company’s specific circumstances and its assessment of the level of violation risk.

“Monitoring” is often considered a responsibility of the internal audit staff. Internal auditors may indeed include among their procedures steps to determine whether procedural controls have been observed. Some other steps that may be taken to monitor compliance with an FCPA compliance program could include such things as —

⁷⁰ See *supra* Part II.B.4.

⁷¹ See *supra* notes 18-20 and accompanying text.

⁷² See *supra* note 21 and accompanying text.

⁷³ See *supra* note 22 and accompanying text.

⁷⁴ USSG § 8A1.2, application note 3(k)(5).

1. Review of Documentation Associated with Particular Transactions, Contracts, or Other Events

Foreign contracts, bids, tax disputes, distributorship agreements, and similar transactions that could be conducive to FCPA violations may be periodically reviewed to determine whether all relevant documentation is on file and whether anything in the file suggests the need for further inquiry.

2. Interviews with Employees Involved in High-Risk Areas of Corporate Activity

Periodic visits to foreign operations by internal auditors or staff members with compliance responsibilities may include interviews with local personnel during which such personnel are questioned concerning the existence of any circumstances suggesting FCPA violations.

3. Review of Supporting Documentation for Cash Expenditures

Similarly, audits of foreign locations normally include the review of documentation supporting cash expenditures and checks written and authorized locally. Auditors should insure that there is proper documentation on hand for all such payments. Any expenditures which appear to involve direct or indirect payments to foreign officials should be the subject of further inquiry.

4. Review of Consultants and Agents Contracts

As discussed earlier, due diligence should be performed with respect to foreign agents, and such persons may be required to execute contracts obligating them to comply with FCPA and company policies concerning payments to foreign officials. Files should be maintained documenting compliance with these requirements with respect to each foreign agent or other person covered by the policy that is retained, and these files should be reviewed periodically for completeness and conformity to the policy.

5. Review of Public Information Concerning Business Practices in Particular Jurisdictions

The official charged with administering the FCPA compliance program should stay abreast of public information concerning business practices in the jurisdictions where the company operates. News articles concerning questionable payments involving competitors, or reflecting adversely on agents retained by the company, could, for example, serve as an indication of problems which could also affect the company.

6. Review of Compliance with Periodic Certification Requirements

As has been discussed, some companies require all or some categories of employees to certify that they have read the FCPA policy statement and that they are not aware of any violations by any company personnel.⁷⁵ If such a periodic certification procedure exists, the files should be reviewed to ensure that it is actually being observed. Employees who have failed to execute the certification should be contacted and their certification obtained.

In some companies, the annual certification may take the form of a more detailed questionnaire in which particular employees are asked to respond to a series of questions concerning their involvement in or knowledge of any improper payments, record-keeping inaccuracies, or other types of misconduct. If such questionnaires exist, it is important that responses be carefully reviewed and any unusual responses subjected to follow-up inquiry.

7. Report to the Board

In light of the increasing focus on board responsibility for corporate compliance, the monitoring effort should include a periodic report to the company's board of directors. The directors should receive information concerning the results of monitoring, any recommended changes in the compliance program, any suspected violations meriting further follow-up, and any other matters arising out of the ongoing administration of the program. Any suggestions or inquiries from the directors should, of course, be pursued and resulting actions or changes documented.

V. CONCLUSION

The formulation of compliance programs has received increasing scrutiny in light of the Organizational Sentencing Guidelines. The *Caremark* decision may serve to increase further interest in the development of such programs. Similarly, the active SEC interest in FCPA enforcement, coupled with the substantial penalties and reputational risks which can arise from charges of foreign bribery, make FCPA compliance efforts an especially important focus for U.S. multinational companies. While a compliance program in this field cannot be designed from a textbook, the approach outlined in this article is intended to give the designer of such an FCPA compliance program a framework within which to consider how best to tailor that program to the needs and risks of his or her company.

⁷⁵ See *supra* Part II.B.4.