The Next FCPA Frontier: Banking and Private Equity?

On Friday, January 14, 2011, *The Wall Street Journal* ("the *Journal*") reported that the Securities and Exchange Commission ("SEC") is investigating "whether bank and private equity firms violated the bribery laws in their dealings with sovereign wealth funds." The *Journal* indicated that the SEC sent letters of inquiry to several banks and private equity firms requesting that the entities retain documents related to these financial relationships. Sovereign Wealth Funds ("SWF") were described in the article as "investment funds owned and generally operated by overseas governments." While the *Journal* reports that the letters were not specific in stating the reasons for the inquiry, the inquiries "appear to be tied to a broad Foreign Corrupt Practices Act ("FCPA") investigation of the banking industry." As early as two years ago, the Department of Justice ("DOJ") announced that it was reviewing investments by companies in these funds, and the investment of the funds in U.S. firms. U.S. companies were warned to perform the appropriate due diligence on fund representatives and to assess the representatives' ties to the foreign government.

According to the *Journal*, the probe is in the early stages. The SEC's correspondence referenced in the article is typical when the agency is commencing a probe. For example, in 2010, it was widely reported that at least five pharmaceutical companies received letters from the SEC and the DOJ requesting information and documents, and advising each company that it was under investigation for foreign bribery in identified countries.

One of the key issues raised by the instant inquiry will be whether these SWFs and the employees who run these funds would be considered foreign officials under the definition set forth in the FCPA. The FCPA defines "foreign official" as follows:

"Foreign official" means any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization."

Given enforcement actions in recent years, government regulators clearly believe that employees of entities run or controlled by a foreign government fall within the statute's definition.

For now, financial institutions need to review and assess their risk profiles as they relate to the companies' relationships with individuals acting on behalf of SWFs. The government expects, at a minimum, that all U.S. "issuers"[1] and "domestic concerns"[2] will have in place compliance policies and practices that act as preventative measures against fraud and corruption in the formation of business relationships. These policies include processes for vetting potential business relationships and the use of contractual terms that directly set forth compliance obligations. This expectation applies with equal force to banks and private equity funds that fall within these definitions. The policies should include requirements of due diligence prior to the formation of business relationships, particularly in foreign

countries where there is history of corruption, and gift, travel and entertainment policies that place defined and reasonable limits on these expenditures.

The risk of liability under the FCPA does not fall solely on the company; senior executives with management responsibilities are also at risk. The lessons learned from prior enforcement actions make it clear that government regulators expect senior executives to properly supervise activities that relate to interactions with foreign officials and governments. For example, in 2009, the SEC filed suit against the CEO and CFO of nutritional supplement manufacturer Nature's Sunshine based on the executives' supervisory responsibilities over others engaged in foreign bribery — conduct of which the CEO and CFO had no knowledge. These executives were charged because they were the "control persons" over the violators, and should have supervised their actions.

Government regulators continue to cast a wide net in the area of FCPA enforcement. Banks and private equity firms must closely watch the events in this probe as they unfold.

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[1] An "issuer" is any entity that has a class of securities registered pursuant to the Securities Exchange Act of 1934 or that is required to file reports under that Act. This definition includes U.S. publicly traded companies and foreign public companies that may be listed on U.S. stock exchanges through the use of American Depositary Receipts.

[2] A "domestic concern" is any individual who is a citizen, national, or resident of the United States, as well as any corporation, partnership, association, joint-stock company, business trust, unincorporated organization or sole proprietorship that has its principal place of business in the United States, or that is organized under the laws of a State of the United States.