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Industry-Wide Investigations Under the Foreign Corrupt Practices Act

CLAUDIUS O. SOKENU AND ARTHUR LUK

The authors analyze recent industry-wide investigation developments under the Foreign Corrupt Practices Act.

The Department of Justice and Securities and Exchange Commission (“Commission” or “SEC”) recently have been involved in a variety of industry-wide investigations of the medical devices and oil and gas industries.

MEDICAL DEVICES

In recent years, the Justice Department and SEC have turned their attention to corrupt payments made to government-employed healthcare providers around the world. A number of medical device makers, including Smith & Nephew, Biomet Inc., Stryker Corp., Zimmer Holdings Inc., Wright Medical, and Medtronic Inc., began internal investigations of potentially corrupt activities and disclosed these investigations to the government. Kara Novaco Brockmeyer, the Chief of the FCPA Unit of the SEC stated, “[t]he SEC will continue to hold companies liable as we investigate the medical device indus-

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try for this type of illegal behavior.”¹ The first half of this year has certainly shown this statement to be true.

Smith & Nephew

On February 6, 2012, United States-based Smith & Nephew Inc. (“Smith & Nephew”) and its British parent company, Smith & Nephew plc (“S&N plc”) agreed to pay a total of US\$22.2 million to settle violations of the FCPA alleged by the Justice Department and SEC. Smith & Nephew is a wholly-owned subsidiary of London-based S&N plc, a maker of orthopedic, endoscopy, and wound-care products. Because S&N plc trades on the New York Stock Exchange, it is an “issuer” within the meaning of the FCPA, and accordingly, is required to make and keep accurate books, records, and accounts of its assets.

According to the criminal information and deferred prosecution agreement (“DPA”) filed in connection with the Justice Department’s case, between 1998 and 2008, Smith & Nephew paid up to US\$9.4 million in bribes to publicly employed Greek healthcare providers to induce the purchase of its products.² Smith & Nephew allegedly sold its products to a distributor at full price and then transferred the amount of the distributor discount to off-shore shell companies controlled by the distributor. The distributor then allegedly paid “cash incentives” to publicly employed healthcare practitioners. The government further alleged that Smith & Nephew then recorded the payments as “marketing services,” and that S&N plc incorporated these records into its books, even though no services were actually performed.³

Smith & Nephew commenced a thorough investigation and voluntarily disclosed information about potentially illicit payments to the government. The DPA acknowledges Smith & Nephew’s thorough self-investigation of the underlying conduct, its cooperation with the government’s investigation, and the remedial efforts and compliance improvements undertaken by the company.

Pursuant to its DPA with the Justice Department, Smith & Nephew agreed to pay a US\$16.8 million criminal fine,⁴ and pursuant to its settlement with the SEC, S&N plc agreed to disgorge US\$5.4 million.⁵ The DPA with the Justice Department also requires that Smith & Nephew continue to implement and develop its compliance program and requires Smith & Nephew

to retain an independent compliance monitor for 18 months to review its anti-corruption compliance program.⁶ In addition, S&N plc agreed to the entry of a court order permanently enjoining further violations of certain sections of the FCPA.⁷

Biomet

In another enforcement action stemming from the industry-wide probe of the medical device industry, on March 26, 2012, US-based orthopedic manufacturer Biomet Inc. (“Biomet”) agreed to pay US\$22.8 million to settle charges by the Justice Department and the SEC that it had violated the FCPA.⁸ The fines include a US\$17.2 million criminal penalty and nearly US\$5.6 million in disgorgement of profits and prejudgment interest.

According to the government’s allegations, between 2000 and 2008, Biomet and its wholly-owned subsidiaries made more than US\$1.5 million in corrupt payments to doctors at public hospitals in Argentina, Brazil, and China to obtain business. In Brazil and Argentina, Biomet or its distributor allegedly made payments to doctors in public hospitals in exchange for the purchase of Biomet products. In China, Biomet’s distributor allegedly gave doctors money and/or travel for purchasing Biomet products.⁹

According to the government, Biomet’s internal auditors discovered these improper payments in Brazil in 2002 and in Argentina in 2006. The auditors allegedly notified personnel in the United States about these payments, but the payments still continued until 2008. The improper payments in China by Biomet’s distributor apparently came to the attention of Biomet personnel in 2001. To conceal the true nature of these payments to doctors in Argentina, Brazil and China, the company allegedly falsely recorded these improper payments on its books and records as “commissions,” “consulting fees,” “royalties,” or “scientific incentives.”¹⁰ In China, Biomet’s Director of Internal Audit apparently instructed others to mislabel improper payments to doctors related to clinical trials as “entertainment.”¹¹

Although Biomet cooperated with the government, the company’s failure to address bribery and the complicity of the audit department in foreign bribery likely contributed to the government’s insistence in the settlement that Biomet retain a compliance monitor for 18 months. As Kara Novaco

Brockmeyer of the SEC's FCPA Unit declared, "[a] company's compliance and internal audit should be the first line of defense against corruption, not part of the problem."¹²

OIL & GAS

In the first half of 2012, the Justice Department and the SEC have continued their long-running assault to root out corruption in the oil and gas industry. While several of the recent Justice Department and SEC enforcement actions relate to the large Nigeria-based corruption scheme involving the TSKJ joint venture — comprised of Technip S.A., Snamprogetti Netherlands B.V., Kellogg Brown & Root LLC, and JGC Corporation — the Justice Department and the SEC have also continued to investigate potential violations of the FCPA in Nigeria, Angola and Libya.

Former KBR CEO, Commerical VP, and Attorney Sentenced to Prison over Bribery Scheme

In February 2009, Kellogg Brown & Root LLC ("Kellogg"), a former Halliburton subsidiary, agreed to pay a US\$402 million criminal fine and *KBR, Inc.*, Kellogg's parent, agreed to disgorge US\$177 million to settle enforcement actions by the Justice Department and SEC, respectively, for violations of the FCPA.¹³ Three years later, the individuals who orchestrated the bribery scheme — Kellogg's former CEO, Albert "Jack" Stanley; its former Commercial Vice President, Wojciech Chodan; and an attorney serving as an intermediary for KBR, Jeffrey Tesler — were sentenced under plea agreements for their roles in the scheme between 1995 and 2004 to pay Nigerian officials at least US\$180 million in bribes in order to obtain contracts to build liquefied natural gas facilities on Bonny Island, Nigeria worth approximately US\$6 billion.¹⁴

On February 23, 2012, Stanley was sentenced to 30 months in prison and ordered to pay close to US\$11 million in restitution.¹⁵ That same day, Tesler was sentenced to 21 months in prison and was ordered to pay close to US\$150 million in forfeitures.¹⁶ On February 22, 2012, Chodan received one year of probation, and was ordered to pay a total of approximately US\$750,000 in fines and forfeitures, reflecting his assistance to the government in its prosecution of Tesler.¹⁷

SEC Charges Three Noble Executives in Bribery Scheme

In November 2010, Noble Corporation, a Swiss offshore drilling company with its principal offices in Sugar Land, Texas, resolved charges that it violated the FCPA by paying US\$74,000 to a Nigerian freight forwarder knowing that some of the payments would be used to bribe Nigerian customs officials and that it falsely recorded the bribes as legitimate expenses in its financial records.¹⁸ The company agreed to pay a US\$2.59 million criminal penalty pursuant to a non-prosecution agreement (“NPA”) entered into with the Justice Department, which recognized the company’s early voluntary disclosure of the bribes, internal investigation of the conduct at issue, cooperation with the government, and implementation of remedial measures. The company also resolved claims brought by the SEC, agreeing to disgorge US\$5.5 million.¹⁹

Following its resolution of charges against the company, on February 14, 2012, the SEC charged three executives with violating the FCPA.²⁰ According to the SEC’s complaint, Noble Corporation’s chief executive officer, Mark A. Jackson, and a Director and Division Manager of Noble’s Nigerian subsidiary, James J. Ruehlen, bribed customs officials to process false paperwork purporting to show the export and re-import of oil rigs in a scheme designed to save significant costs associated with obtaining new permits.²¹ The complaint alleges that hundreds of thousands of dollars in bribes were paid (including payments that were not the basis of Noble’s DPA) through a customs agent for Noble’s Nigerian subsidiary with Jackson’s and Ruehlen’s approval to obtain 11 permits and 29 permit extensions. Jackson is alleged to have approved the payments and concealed them from the company’s audit committee and auditors, and Ruehlen is alleged to have prepared false documents, sought approval for the bribes, and processed and paid the bribes.²² A third company official, Thomas F. O’Rourke, a former controller and head of internal audit at Noble, settled the enforcement action brought by the SEC by consenting to the entry of an order requiring him to pay a US\$35,000 penalty for assisting in the approval of the bribes and their false recording as legitimate operational expenses.²³

Both Jackson and Ruehlen have moved to dismiss the SEC’s complaint, arguing, among other things, that the complaint fails to distinguish between corrupt payments made to obtain or retain business (*i.e.*, bribes) and otherwise permissible facilitation payments; that the SEC’s interpretation of

the facilitation payment exception in the FCPA provides unconstitutionally vague notice to individuals; that the complaint fails to allege corrupt intent sufficiently; that the complaint fails to specify the particular books, records or accounts that were allegedly falsified; and that the five year statute of limitations on most of the alleged conduct has already elapsed.²⁴

Halliburton Faces Angola Bribery Probe

The SEC sent Halliburton a subpoena related to an investigation into its Angolan operations for possible violations of the FCPA.²⁵ This subpoena follows Halliburton's October 2011 announcement that it had opened an internal investigation in response to an anonymous e-mail tip about possible corruption. The e-mail at issue, sent in December 2010, indicated that certain current and former personnel violated internal company policies and the FCPA — claims mostly related to the use of an Angolan vendor. Halliburton has briefed the Justice Department and the SEC on the status of its investigation and has indicated that it intends to continue to cooperate with the government agencies.

Cobalt International Energy's Angola Probe

In its Form 10-K for the year ended December 31, 2011, filed with the SEC on February 21, 2012, Cobalt International Energy Inc. ("Cobalt") revealed that the Justice Department and the SEC have launched a formal probe into allegations that one of its oil drilling contractors bribed foreign officials in Angola.²⁶ According to the filing, the investigation relates to whether Nazaki Oil and Gas SA ("Nazaki"), a Cobalt contractor assigned to oil blocks by the Angolan government, bribed senior government officials. The Angolan government "assigned" Cobalt to work with Nazaki and an additional corporation — contractors with whom Cobalt acknowledged it had limited familiarity. Nazaki has denied the allegations.²⁷

According to Cobalt's Form 10-K, the allegations first surfaced in the fall of 2010, and by March 2011, the SEC started an investigation into the matter. Cobalt alerted the Justice Department shortly thereafter and disclosed that it is cooperating with both agencies.

SEC Widens Libya-Related Oil and Gas Probe

At least six other companies operating in the oil and gas industry disclosed that they were the subjects of ongoing investigations regarding their operations in Libya. Italy's Eni SpA — the parent of Snamprogetti Netherlands B.V., one of the members of the TSKJ joint venture — disclosed in its annual report that the SEC has issued subpoenas to it relating to potential FCPA violations in Libya. According to its annual report filed with the SEC on April 5, 2012, Eni received a subpoena focused on “certain illicit payments to Libyan officials” relating to the company's activities in Libya between 2008 and 2011.²⁸ Eni then received a second subpoena at the end of December 2011 asking for additional information relating to the prior subpoena. Eni stated that it was “fully collaborating with” the SEC.²⁹

Similarly, France's Total S.A., another major international oil and gas producer, disclosed in its annual report filed with the SEC on March 27, 2012, that it had received a subpoena from the SEC in June 2011 relating to its operations in Libya. Total stated that it was cooperating with the SEC's investigation.³⁰ It also stated that late in 2011 the company declined a settlement proposal from the Justice Department and the SEC to resolve the agencies' inquiry into whether payments made to Iranian officials under an agreement entered into by a consultant of the company regarding an Iranian gas field violated the FCPA. Total stated that it is continuing discussions with the agencies.³¹

Another international energy company, Marathon Oil Company, disclosed in its annual report filed with the SEC, on February 29, 2012, that it received a subpoena from the SEC on May 25, 2011, requiring production of documents related to payments made to the government of Libya, or to officials and persons affiliated with officials of the government of Libya.³² The company stated that it was cooperating with the SEC.

In addition to Eni, Total and Marathon Oil, three other companies have confirmed Libya-based SEC corruption probes. Exxon Mobil Corp., ConocoPhillips Co., and Occidental Petroleum Corp. have each announced that they have received similar SEC subpoenas relating to Libyan operations between 2008 and 2011.³³

Allegations of Bribes Against Consortiums of Major Oil and Gas Companies in Kazakhstan

In March 2012, the oil ventures Karachaganak Petroleum Operating BV (“KPO”) and Tengizchevroil LLP received an anonymous tip regarding allegations of bribery in their Kazakhstani operations. The KPO venture, of which Italy’s Eni and UK natural gas company BG Group are the principal operators, and US-based Chevron and Russia-based Lukoil are minority partners, confirmed in June that they have begun an internal investigation into the matter.³⁴ Tengizchevroil, a joint venture between Chevron (50 percent share), ExxonMobil (25 percent), KazMunayGas (20 percent) and LukArco (5 percent), has likewise confirmed launching an internal investigation.³⁵ The joint ventures’ logistics contractor, Deutsche Post AG’s DHL unit, has also launched an internal investigation.

According to the whistleblower, KPO authorized DHL to regularly make “extra verification” payments to customs officials in Aksai City, Kazakhstan in exchange for the officials overlooking problems with shipments’ paperwork that might otherwise have delayed them for weeks or even months. The alleged payments typically equaled US\$400 and were meant to address inconsistencies with shipment documents, such as an extra box of nails in one instance, and two extra gaskets in another, according to media reports.³⁶ Some accounts suggest that KPO ordered DHL to cease making any such payments, but, upon doing so, DHL found nearly every KPO shipment blocked from passage through customs. DHL allegedly resumed payments the very next day.³⁷

Kazak customs authorities reportedly investigated the allegations of corruption, without uncovering any evidence of wrongdoing. In a letter sent to the *Wall Street Journal*, a Kazak official on the customs committee stated that “evidence of abuse of official position and receiving of illegal gratification from representatives of KPO, was not found in the activities of the executives of the customs post ‘Aksai.’”³⁸

As for Tengizchevroil, the tipster alleged that the joint venture and DHL participated in a scheme to bribe Kazakhstani customs officials to avoid the officials’ delaying shipments due to discrepancies between the description of goods in shipping documentation as compared to the contents of the shipment itself. It also alleged that DHL paid “convoy bribes” on behalf of the

joint venture. As a requirement of Kazakh law, cargo vehicles are on occasion required to have an escort through customs. According to the allegations, the logistics agents regularly paid US\$150 to US\$300 in bribes to customs officials to ensure that escorts did not delay the shipments of Tengizchevroil's equipment. DHL allegedly reimbursed the bribes.³⁹

US authorities have yet to confirm whether they have launched a probe into the matter. Kazakhstan's Customs Control Committee, a branch of the country's Ministry of Finance, has launched an on-site audit of the customs post in Aksai City.⁴⁰

NOTES

¹ Press Release, SEC, SEC Charges Smith & Nephew PLC with Foreign Bribery (Feb. 6, 2012), *available at* <http://www.sec.gov/news/press/2012/2012-25.htm>.

² See Information, *United States v. Smith & Nephew Inc.*, No. 1:12-cr-00030 (D.D.C. Feb. 6, 2012), Dkt. Entry No. 1 [hereinafter "Smith & Nephew Info."]; Letter from Justice Department to Paul Gerlach & Angela Burgess, *United States v. Smith & Nephew Inc.*, No. 1:12-cr-00030 (D.D.C. Feb. 15, 2012), Dkt. Entry No. 3.1 [hereinafter "Smith & Nephew DPA"]; Press Release, Justice Dep't, Medical Device Company Smith & Nephew Resolves Foreign Corrupt Practices Act Investigation (Feb. 6, 2012), *available at*: <http://www.justice.gov/opa/pr/2012/February/12-crm-166.html>.

³ Smith & Nephew Info., *supra* note 2, at 5.

⁴ Smith & Nephew DPA, *supra* note 2, at 5.

⁵ See SEC Charges Smith & Nephew PLC with Foreign Bribery, Litigation Release No. 22252 (Feb. 6, 2012), *available at* <http://www.sec.gov/litigation/litreleases/2012/lr22252.htm> [hereinafter "S&N plc Litigation Release"].

⁶ Smith & Nephew DPA, *supra* note 2, at 6-7.

⁷ S&N plc Litigation Release, *supra* note 5.

⁸ See Press Release, Justice Dep't, Third Medical Device Company Resolves Foreign Corrupt Practices Act Investigation (Mar. 26, 2012), *available at* <http://www.justice.gov/opa/pr/2012/March/12-crm-373.html>.

⁹ See Information, *United States v. Biomet, Inc.*, No. 12-cr-00080 (D.D.C. Mar. 26, 2012), Dkt. Entry No. 1.

¹⁰ See *id.* at 6-12.

¹¹ See *id.* at 12.

¹² Press Release, SEC, SEC Charges Medical Device Company Biomet with Foreign Bribery (Mar. 26, 2012), *available at* <http://www.sec.gov/news/press/2012/2012-50.htm>

¹³ See Press Release, Justice Dep't, Kellogg Brown & Root LLC Pleads Guilty to Foreign Bribery Charges and Agrees to Pay \$402 Million Criminal Fine (Feb. 11, 2009), *available at* <http://www.justice.gov/opa/pr/2009/February/09-crm-112.html>. Other participants of the TSKJ joint venture have also settled FCPA charges against them. Technip agreed to pay a \$240 million criminal penalty and \$98 million in disgorgement on June 28, 2010, to resolve enforcement actions brought by the Justice Department and SEC. Ten days later, on July 7, 2010, Snamprogetti and its parent *Eni SpA* agreed to pay a \$240 million criminal penalty and \$125 million in disgorgement to resolve enforcement actions brought by the agencies. On April 11, 2011, JGC agreed to pay a \$218.8 million criminal penalty to resolve an enforcement action brought by the Justice Department.

¹⁴ See Press Release, Justice Dep't, Former Chairman and CEO of Kellogg, Brown & Root Inc. Sentenced to 30 Months in Prison for Foreign Bribery and Kickback Schemes (Feb. 23, 2012), *available at* <http://www.justice.gov/opa/pr/2012/February/12-crm-249.html>.

¹⁵ Minute Entry, *United States v. Tesler*, 4:09CR00098 (S.D. Tex. Feb. 23, 2012).

¹⁶ Minute Entry, *United States v. Tesler*, 4:09CR00098 (S.D. Tex. Feb. 23, 2012).

¹⁷ Minute Entry, *United States v. Tesler*, 4:09CR00098 (S.D. Tex. Feb. 22, 2012).

¹⁸ See Press Release, Justice Dep't, Oil Services Companies and a Freight Forwarding Company Agree to Resolve Foreign Bribery Investigations and to Pay More Than \$156 Million in Criminal Penalties (Nov. 4, 2010), *available at* <http://www.justice.gov/opa/pr/2010/November/10-crm-1251.html>.

¹⁹ *Id.*

²⁰ See Press Release, SEC, SEC Charges Three Oil Services Executives With Bribing Customs Officials in Nigeria (Feb. 24, 2012) *available at* <http://www.sec.gov/news/press/2012/2012-32.htm> [hereinafter "Noble Executives SEC Press Release"].

²¹ See Complaint, *SEC v. Jackson*, No. 4:12-cv-00563 (S.D. Tex. Feb. 24, 2012), Dkt. Entry No. 1.

²² See *id.* at 7-36.

²³ See Noble Executives SEC Press Release, *supra* note 20; Complaint, *SEC v. O'Rourke*, No. 4:12-cv-00564 (S.D. Tex. Feb. 24, 2012).

²⁴ See Motions to Dismiss For Failure To State A Claim, *SEC v. Jackson*, No. 4:12-cv-00563 (S.D. Tex. May 8, 2012), Dkt. Entry No. 35 (Jackson) and No. 36 (Ruehlen).

²⁵ See Halliburton Co., Quarterly Filings (Form 10-Q), at 19 (Oct. 21, 2011), available at http://www.sec.gov/Archives/edgar/data/45012/000004501211000354/edsept201110q_final.htm.

²⁶ See Cobalt Int'l Energy, Inc., Annual Report (Form 10-K), at 50-51 (Feb. 21, 2012), available at <http://www.sec.gov/Archives/edgar/data/1471261/000104746912001183/a2207234z10-k.htm>.

²⁷ *Id.*

²⁸ See Eni SpA, Annual Report (Form 20-F), at F-92 (Apr. 5, 2012), available at <http://www.sec.gov/Archives/edgar/data/1002242/000131143512000005/sj0412en20f2011.htm#192>.

²⁹ *Id.*

³⁰ See Total, S.A., Annual Report (Form 20-F/A), at F-94-95 (Mar. 27, 2012), available at http://www.sec.gov/Archives/edgar/data/879764/000119312512134298/d278816d20fa.htm#rom278816_38

³¹ See *id.* at F-93-94.

³² Marathon Oil Corp., Annual Report (Form 10-K), at 29 (Feb. 29, 2012), available at <http://www.sec.gov/Archives/edgar/data/101778/000119312512088742/d270787d10k.htm>.

³³ See Joe Palazzolo, *SEC Eyeing ExxonMobil's Ties to Libyan Sovereign Fund*, Wall St. J. (June 20, 2011), available at <http://blogs.wsj.com/corruption-currents/2011/06/20/sec-eyeing-exxonmobiles-ties-to-libyan-sovereign-fund/>.

³⁴ C.M. Matthews and Joe Palazzolo, *Oil Giants Launch Bribe Probes in Kazakhstan*, Wall St. J. (June 6, 2012), available at <http://online.wsj.com/article/SB10001424052702303296604577450442633804840.html> [hereinafter "KPO Probe"].

³⁵ C.M. Matthews, *Second Oil Venture Probes Corruption Allegations in Kazakhstan*, Wall St. J. (June 13, 2012), available at <http://blogs.wsj.com/corruption-currents/2012/06/13/second-oil-venture-probes-corruption-allegations-in-kazakhstan/> [hereinafter "Tengizchevroil Probe"].

³⁶ See KPO Probe, *supra* note 34.

³⁷ See *id.*

³⁸ C.M. Matthews, *Kazak Authorities Say No Evidence of Corruption at Customs Post*, Wall St. J. (July 2, 2012), *available at* <http://blogs.wsj.com/corruption-currents/2012/07/02/kazak-authorities-say-no-evidence-of-corruption-at-customs-post/>.

³⁹ See Tengizchevroil Probe, *supra* note 35.

⁴⁰ C.M. Matthews, *KPO Probe Highlights Customs Risks*, Wall St. J. (June 8, 2012), *available at* <http://blogs.wsj.com/corruption-currents/2012/06/08/kpo-probe-highlights-customs-risks/>.