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FCPA Update

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Second Circuit Defers to the SEC in Overturning a District Court's Rejection of Settlement with "Neither Admit or Deny" Language

On June 4, 2014, the United States Court of Appeals for the Second Circuit overturned a widely publicized Southern District of New York decision by Judge Jed S. Rakoff, holding that Judge Rakoff abused his discretion in requiring, as a condition of approving the settlement between the Securities and Exchange Commission ("SEC") and Citigroup Global Markets Inc. ("Citi"), that the SEC establish the "truth" of the allegations against Citi.[1] In rejecting the district court's analysis, after having earlier stayed the trial court's order,[2] the Second Circuit noted that settlements are "primarily about pragmatism" and provide parties with a "means to manage risk." The assessment of those risks, the Second Circuit held, is "uniquely for the litigants to make."

For companies subject to the SEC's authority to enforce the FCPA, the Second Circuit's decision in the *Citi* matter provides some comfort that a corporate resolution requiring judicial approval, once achieved, should be subject to appropriate deference when it comes before a district court for review. At the same time, however, the decision also reinforces the understanding that resolutions achieved by settlement, even if approved by a court, do not constitute legal precedent.

Background

Although it has shifted policy recently to require admissions from settling defendants in some cases, the SEC historically has permitted defendants to enter into settlement agreements in which a settling party neither admits nor denies the SEC's allegations. For defendants, this approach has allowed them to settle disputes with the SEC without incurring the stigma of an admission of wrongdoing or the collateral consequences that might arise in related shareholder or other litigation. For the SEC, the approach has

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1. *See S.E.C. v. Citigroup Global Mkts., Inc.*, No. 11-5227-cv (2d Cir. June 4, 2014).
2. *S.E.C. v. Citigroup Global Mkts., Inc.*, 673 F.3d 158 (2d Cir. 2012); *see also* Debevoise & Plimpton LLP, Client Update: Second Circuit Signals Support for the SEC's Use of "Neither Admit Nor Deny" Language in Consent Settlements," http://www.debevoise.com//clientupdate20120316b.

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allowed it to more easily resolve cases that might be difficult or resource intensive to bring to trial.

Judge Rakoff's decision in late 2011 threatened to disrupt this historic practice. In that case, the SEC sought the court's approval of its proposed settlement with Citi stemming from Citi's sales of mortgage-backed securities. In the proposed settlement, Citi would neither admit nor deny the SEC's claims, but would consent to a permanent injunction from future violations of certain provisions of the Securities Act and pay $285 million in disgorgement and penalties. Judge Rakoff rejected the settlement, finding that because Citi did not admit to any facts or wrongdoing in the settlement and the SEC had not proven them at trial, the court could not find that the proposed settlement was "fair, reasonable, adequate, and in the public interest" – the standard for approving settlements with injunctions that Judge Rakoff applied to the case and that became a central focus of the Second Circuit's ruling.[3] Judge Rakoff also criticized the SEC for bringing only negligence-based fraud charges against Citi and faulted the entire SEC settlement process, which he wrote is frequently viewed in the business community "as a cost of doing business imposed by having to maintain a working relationship with a regulatory agency."[4] Following Judge Rakoff's lead, several other district courts from around the country scrutinized SEC consent decrees and challenged the agency to establish the adequacy of those settlements.

The Second Circuit's Decision

Both the SEC and Citi appealed Judge Rakoff's ruling, and after initially staying Judge Rakoff's decision in March 2012 pending a decision on the merits, the Second Circuit issued its ruling on the merits on June 4, overturning Judge Rakoff's opinion and order, finding that "the district court had abused its discretion by applying an incorrect legal standard in assessing the consent decree."[5] The Second Circuit's opinion gives great deference to the SEC in the settlement process; however, the opinion acknowledges a role for the courts – and clarified the standard the district courts should use – when reviewing proposed settlements.

According to the Second Circuit, when a district court reviews a proposed SEC settlement, it must determine whether the proposed settlement is "fair and reasonable." The Second Circuit disagreed with Judge Rakoff's view that a court must assess the "adequacy" of the settlement before approving it, noting that unlike in a class action where a settlement usually precludes future claims, private litigants in the kind of case presented in the *Citi* matter typically can still bring a private action after an SEC settlement.[6] The Second Circuit then clarified the correct standard courts should apply

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3. *S.E.C. v. Citigroup Global Mkts., Inc.*, 827 F. Supp. 2d 328, 331 (S.D.N.Y. 2011).

4. *Id.* at 333.

5. *S.E.C. v. Citigroup Global Mkts., Inc.*, No. 11-5227-cv, slip op. at 2 (2d Cir. June 4, 2014).

6. *Id.* at 19. The FCPA, of course, does not create a private right of action, although a number of private litigants seeking relief in the wake of disclosure of bribery issues by an SEC-registered company have sought to plead around that uncontroversial notion by invoking the Racketeer Influenced or Corrupt Organizations Act or by bringing securities claims related to the alleged non-disclosure of the misconduct.

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when evaluating if a proposed consent decree is "fair and reasonable," and added that the "primary focus of the inquiry… should be ensuring the consent decree is procedurally proper."[7] The Second Circuit also cautioned courts "not to infringe on the SEC's discretionary authority to settle on a particular set of terms."[8]

> "'[T]he job of determining whether the proposed [settlement] best serves the public interest… rests squarely with the SEC.'"

If a settlement includes injunctive relief, the district court must also find that the "public interest would not be disserved" by approval of the settlement. Here again, in cases involving the SEC or other administrative agencies, the Second Circuit deferred to the judgment of the agency, noting that "the job of determining whether the proposed [settlement] best serves the public interest… rests squarely with the SEC."[9]

The Second Circuit rejected as "an abuse of discretion" Judge Rakoff's determination that the SEC be required to "establish the 'truth' of the allegations against a settling party as a condition for approving the [settlement]."[10] The Second Circuit noted that, while trials are "primarily about the truth," consent decrees are "primarily about pragmatism" and, as such, they provide parties with an important tool to "manage risk." The assessment of the risks of litigation, the Court observed, is "uniquely for the litigants to make." It is outside a court's "purview" to demand, as a condition for approving a consent decree, that the parties present "'cold, hard, solid facts, established either by admissions or by trials[.]'" Even where the SEC's case against defendants may be strong, the Court noted, there are risks with proceeding to trial for a resource-limited agency like the SEC, which is why consent decrees often serve as an important enforcement tool.

In a concurring opinion, Judge Lohier stated that, in his view, the perceived modesty of any monetary penalty in a proposed consent decree should not be a reason for rejecting a settlement provided the "fair and reasonable" standard articulated by the majority was satisfied. In addition, Judge Lohier noted that the factual record before the district court was sufficient to satisfy the "fair and reasonable" standard, and therefore he was inclined to reverse and direct the district court to enter the consent decree.

Settlements Going Forward

The Second Circuit decision gives deference to the SEC to shape its settlement agreements as the agency finds appropriate. The court acknowledged that in many instances, the *status quo ante* of allowing defendants to "neither admit nor deny" allegations will be sufficient.[11] The court also expressly stated there was "no basis in law for the district court to require an admission of liability as a condition for approving a settlement between the parties."[12] However, the court noted that, "[t]he decision to require an admission of liability before entering into a consent decree rests squarely with the S.E.C.," leaving open the possibility for the SEC to seek such an admission where it finds it appropriate.[13]

In June 2013, SEC Chair Mary Jo White announced a policy shift for the agency that, while perhaps not in direct response to Judge Rakoff's ruling, nevertheless mirrored the policy shift advocated by Judge Rakoff. Specifically, Chair White announced that the SEC would require in certain cases that defendants admit to wrongdoing or else face trial. Chair White explained that the agency would seek admissions, for example, in cases where a large number of investors have been harmed; where the conduct posed a significant risk to the markets; where

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7. *Id.* at 21.
8. *Id.*
9. *Id.* at 24.
10. *Id.* at 21.
11. *Id.* at 22 ("[F]actual averments by the S.E.C., neither admitted nor denied by the wrongdoer, will suffice to allow the district court to conduct its review.").
12. *Id.* at 17.
13. *Id.*

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admissions would aid investors in deciding whether to deal with a party in the future; and where it would send a message to the market.[14] Since the policy shift, the SEC has announced several settlements in which defendants admitted wrongdoing, and, according to recent comments by Director of Enforcement Andrew Ceresney, the agency has others in the pipeline. None of the cases in which an admission of wrongdoing has been required by the SEC is an FCPA matter, but it is likely only a matter of time before a corporate FCPA resolution appears in the statistics.

Although the SEC seems poised to continue its pursuit of admissions in certain cases and to take more cases to trial if such admissions are not forthcoming, the agency's recent trial losses might serve to embolden defendants to reject the SEC's attempts to seek admissions and to take the agency to trial. It remains to be seen whether defendants who face the prospect of an admission or other onerous settlement terms that might not differ materially from a negative trial outcome, will instead opt to litigate with the SEC rather than settle, especially if they believe they have a reasonable chance of success at trial. In the modern era of SEC enforcement of the FCPA, no company has taken its chances at trial, leaving companies and individuals alike subject to the FCPA with a paucity of precedent that governs the outcome of SEC enforcement actions.

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14. Mary Jo White, Chair, SEC, Deploying the Full Enforcement Arsenal (Sept. 26, 2013), http://www.sec.gov/News/Speech/Detail/Speech/1370539841202.

British Bankers' Association Releases New Anti-Bribery and Anti-Corruption Guidelines

On May 6, 2014, the British Bankers' Association ("BBA") – the U.K.'s leading association for the banking sector – published a 51-page guide entitled "Anti-Bribery and Corruption Guidance" ("the Guidance").[1] While BBA guidance issued in December 2011 had focused on adequate policies and procedures under the U.K. Bribery Act 2010 ("the Act"),[2] the new Guidance also provides meaningful direction with respect to regulatory requirements and other guidance issued by the Financial Conduct Authority ("FCA"), which regulates financial institutions.

The Guidance emphasizes that "the anti-bribery responsibilities of banks do not end with the U.K. Bribery Act."[3] The Guidance notes that banks need to be aware of obligations owed to the FCA in addition to those of the Act, stressing that these are not always identical. Banks and other regulated companies should be mindful that the FCA can take regulatory action against entities and individuals performing controlled functions for failing to address adequately the risk of corruption or bribery.[4] The FCA does not require proof of actual or attempted corruption or bribery, which would be necessary for a conviction under the Act.[5]

Whereas the FCA's Chairman has stressed that the agency will increasingly look towards the "tone in the middle" to improve ethical standards,[6] the Guidance follows the Act's focus on setting a "tone from the top."[7] The BBA presents three examples of how companies can foster such an attitude from management: (1) introducing "business line champions," *e.g.* nominating senior managers to be responsible for anti-bribery work in their business; (2) publishing online the company's anti-bribery policies; and (3) ensuring senior management is equipped to fulfill its role in assisting with anti-bribery actions.[8] In affirming the need for banks to keep abreast of anti-bribery and anti-corruption compliance developments, the Guidance refers to the Parliamentary Commission on Banking Standards' recommendations on banks' whistleblower obligations and notes the FCA's support for these principles, which include an enhanced role for board members in their firms' whistleblowing regime.

The Guidance also offers a number of practical recommendations on governance structures and implementation programs to assist the banking sector in addressing bribery and corruption. To identify bribery risks and effectively develop anti-bribery procedures, the Guidance urges banks to undertake periodic risk assessments of their business as a whole. The BBA notes that "there is no exact science" as to what a risk assessment should include or how it should be done; the BBA points to the range of resources available for companies to draw from, specifically mentioning the 2013 Transparency International publication "Diagnosing Bribery Risks – Guidance For The Conduct of Effective Risk Assessment."[9]

The BBA further calls on banks to conduct due diligence on third parties, given that both the Act and FCA permit a firm to be held liable "for corrupt payments made, offered, or promised by

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1. BBA, Anti-Bribery and Corruption Guidance 2014 (May 6, 2014), https://www.bba.org.uk/policy/financial-crime/anti-bribery-and-corruption/anti-bribery-and-corruption-guidance/.
2. BBA, Bribery Act 2010 – Guidance on compliance (Dec. 20, 2011), https://www.bba.org.uk/wp-content/uploads/2011/12/Bribery_Guidance_-_final.pdf.
3. The Guidance at 3.
4. *See* FCA, "Financial Conduct Authority Handbook," §§ 3.2.6R and 6.1.1R (Apr. 1, 2013), http://www.fshandbook.info/FS/.
5. *See, e.g.*, FCA Press Rel., "Besso Limited fined for anti-bribery and corruption systems failing" (Mar. 19, 2014), http://www.fca.org.uk/news/press-releases/besso-limited-fined-for-antibribery-and-corruption-systems-failings.
6. John Griffith-Jones, FCA Chairman, Speech during the annual meeting of the Chartered Institute for Securities and Investments (July 3, 2013), http://http://www.cisi.org/bookmark/genericform.aspx?form=29848780&url=annualconference13. The Department of Justice and Securities and Exchange Commission have similarly underscored the value of the "message in the middle" approach. *See* DOJ & SEC, "A Resource Guide to the U.S. Foreign Corrupt Practices Act," 57 (Nov. 4, 2012), http://www.justice.gov/criminal/fraud/fcpa/guide.pdf.
7. The Guidance at 21.
8. *Id.* at 24.
9. *Id.* at 28.

British Bankers' Association Releases New Anti-Bribery and Anti-Corruption Guidelines ■ Cont. from page 5

> "Although considerable revisions have been made to its earlier guidelines, the BBA's message remains straightforward: ensure that corporate procedures reflect current legislation, regulations, and recommendations."

an associated person it retains, even if it did not know the associated person intended to pay or offer a bribe."[10]

In this regard, the Guidance recommends monitoring a variety of red flags and accurately recording due diligence results.

More broadly, the Guidance highlights clear written policies regarding gifts and hospitality, a system of monitoring and reviewing a bank's policies, employee training on bribery prevention, and a bribery-specific policy for managing incidents as important means for implementing procedures that seek to ensure compliance.

Although considerable revisions have been made to its earlier guidelines, the BBA's message remains straightforward: ensure that corporate procedures reflect current legislation, regulations, and recommendations. Some of the BBA's commentary is directed at banks in particular, but the underlying principles are broadly relevant to all companies, whether or not in the regulated financial sector.

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10. *Id.* at 31.

Debevoise Lawyers Tackle Questions About Anti-Corruption Landscape in Recent *International Financial Law Review* Survey

Debevoise partner Andrew Levine served as Guest Editor of "Anti-Corruption Survey 2014," recently published by the *International Financial Law Review* ("IFLR"). As the lead contributor, Mr. Levine crafted an anti-corruption survey answered by subject matter experts from around the world, including several Debevoise lawyers. The survey addresses questions regarding the anti-corruption legal landscape, potential penalties, investigation, and adjudication, highlighting global challenges and trends.

In response to the survey, Mr. Levine and Debevoise counsel Steven Michaels of the firm's New York office co-authored the US chapter (click here). Debevoise international counsel Matthew Getz and associate Robin Lööf of the firm's London office co-authored the UK chapter (click here). And Debevoise international counsel Philip Rohlik and associate Sebastian Ko of the firm's Hong Kong office co-authored the Hong Kong chapter (click here).

In addition, as part of the publication, Mr. Levine and Mr. Michaels co-authored an essay for IFLR on "Best Practices in Compliance Programs" (click here). The essay discusses challenges in designing and implementing an effective anti-corruption compliance program, especially given the evolving web of anti-corruption laws and the increasingly aggressive regulatory environment. Specifically, the essay provides insight into risk-based practices designed reasonably to ensure compliance with the anti-corruption laws of various jurisdictions and to meet the expectations of government regulators globally. The essay also emphasizes that the value of an appropriately tailored compliance program is well worth the cost.