

FCPA Update

A Global Anti-Corruption Newsletter



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U.S. Authorities Reach Record-Breaking Settlement with Swedish Telecom Company

On December 6, 2019, U.S. enforcement authorities announced substantial FCPA settlements with Telefonaktiebolaget LM Ericsson (“Ericsson”), a multinational telecommunications company headquartered in Sweden. The SEC and DOJ found that, over a 16-year period, Ericsson used third-party agents and consultants to bribe high-level officials in Djibouti and committed books and records and internal control violations relating to its operations in Djibouti, China, Vietnam, Indonesia, Kuwait, and Saudi Arabia.¹ According to the SEC and DOJ papers, certain high-level executives at the company were involved in making a number of the improper payments and in knowingly and willfully failing to implement sufficient controls.²

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1. Deferred Prosecution Agreement ¶ 4(f), *United States v. Telefonaktiebolaget LM Ericsson* (Nov. 26, 2019) (hereinafter “DPA”); Complaint ¶ 34–54, *Securities and Exchange Commission v. Telefonaktiebolaget LM Ericsson* (Dec. 6, 2019) (hereinafter “SEC Complaint”).

2. See, e.g., DPA Attachment A ¶ 109.

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Ericsson agreed to pay more than \$1 billion to the U.S. SEC and DOJ to resolve the charges, making it one of the largest FCPA settlements ever reached.³ Ericsson also agreed to continue cooperating with both agencies in their related investigations and prosecutions, and to appoint an independent compliance monitor for a three-year period.⁴ As part of the DPA, an Ericsson subsidiary also agreed to plead guilty to conspiracy to violate the anti-bribery provisions of the FCPA.⁵ Subsequently, and prompted by the U.S. investigations, Sweden's prosecution authority reportedly opened a preliminary investigation into possible bribery by the company.⁶

Alleged Conduct

As part of the U.S. settlements, Ericsson admitted to using third parties in Saudi Arabia, China, and Djibouti to bribe government officials and pay for lavish trips and entertainment. The agents were often engaged through sham contracts and paid via false invoices.⁷ Ericsson subsidiaries also created funds for improper purposes and engaged in sham transactions in Vietnam, Indonesia, and Kuwait. Specifically:

- In **Djibouti**, the company's subsidiaries paid \$2.1 million in bribes to high-ranking foreign officials to win a contract valued at approximately \$22.5 million from a state-owned telecommunications company.⁸ To conceal these payments, employees entered into a sham consulting contract with a company owned by the wife of a foreign official. Employees at the subsidiary prepared a due diligence report that failed to disclose the spousal relationship between the owner of the consulting company and a foreign official, and authorized the payments to the consulting firm while knowing that the consultant would transfer a substantial portion of the fees to the two foreign officials who had decision-making power over the contract. The employees also improperly recorded the bribes in the company's books and records.⁹
- In **Saudi Arabia**, Ericsson's local branch entered into sham contracts with two consultants whom employees believed had influence over Saudi officials at a state-owned telecommunications company, despite red flags indicating a high probability that the consultants would pass on at least a portion of their fees

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3. U.S. Sec. & Exch. Comm'n, "SEC Charges Multinational Telecommunications Company with FCPA Violations" (Dec. 6, 2019), available at <https://www.sec.gov/news/press-release/2019-254>; U.S. Dep't of Justice, "Ericsson Agrees to Pay Over \$1 Billion to Resolve FCPA Case" (Dec. 6, 2019), available at <https://www.justice.gov/opa/pr/ericsson-agrees-pay-over-1-billion-resolve-fcpa-case>.

4. DPA ¶¶ 4(h)–(j).

5. *Id.* ¶ 4(j).

6. *Sweden Opens Ericsson Bribery Probe After U.S. Settlement: Paper*, Reuters (Dec. 12, 2019), available at <https://www.reuters.com/article/us-usa-ericsson-sweden/sweden-opens-ericsson-bribery-probe-after-u-s-settlement-paper-idUSKBN1YG248>.

7. See, e.g., DPA Attachment A ¶¶ 35, 66, 67, 84, 90, 110.

8. *Id.* ¶ 34.

9. *Id.* ¶¶ 35–36.

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to the officials.¹⁰ The contracts described identical services that were never intended to be performed, and at least part of the payments were made to a Channel Islands bank account. Over just eleven months, Ericsson's local branch paid approximately \$40 million to the two consultants and received nine contracts from the Saudi state-owned company valued at more than \$700 million. Ericsson also funded leisure travel and entertainment for Saudi foreign officials and their families, including plane fare, spa services, shopping, and five-star accommodations, while falsely booking the expenses as legitimate travel and entertainment.¹¹

- In **China**, Ericsson paid for leisure travel for Chinese officials, using false invoices and sham service providers to generate the funds.¹² The company also paid third-party service providers more than \$31 million via contracts for services that were never performed.¹³ These payments were also recorded improperly in Ericsson's books and records.

“In this era of vigorous anti-corruption enforcement, as the Ericsson resolutions reflect, any company operating internationally must take great care to ensure that third-party agents, particularly those interacting with government entities and officials, do not engage in corrupt conduct.”

- In **Vietnam**, Ericsson made approximately \$4.8 million in payments – sometimes in cash – to a consulting company.¹⁴ These payments were used in fact to create an off-the-books fund for paying third parties whom employees knew could not pass Ericsson's due diligence processes.¹⁵

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10. SEC Complaint ¶ 34.

11. *Id.* ¶¶ 45, 54.

12. DPA Attachment A ¶ 65.

13. *Id.* ¶ 66.

14. *Id.* ¶ 82.

15. *Id.* ¶ 83.

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- Ericsson engaged in a similar scheme in **Indonesia**, where it made approximately \$45 million in payments to a consulting company to create another set of funds for improper uses.¹⁶ The company likewise mischaracterized these payments and improperly recorded them in Ericsson's books and records.¹⁷ Ericsson employees referred to the funds by code names, including one, the "fridge," which held millions of dollars in cash to be used for customer entertainment and a pleasure trip to Bali.
- In **Kuwait**, Ericsson engaged a consulting company owned by relatives of a government official. The consulting company provided competitor bid information and other inside information. Ericsson paid the consultant \$450,000 through a fake invoice for services never performed.¹⁸ As with other payments at issue, this amount also was recorded inaccurately in Ericsson's books and records.¹⁹ Further, according to the government's papers, Ericsson facilitated the payment of the bribes by "knowingly and willfully fail[ing] to implement and maintain sufficient internal accounting controls."²⁰ Its employees knew about significant control weaknesses and the role that high-level executives and other employees played in making improper payments to third parties.²¹ Nonetheless, Ericsson failed to implement adequate controls, including relating to proper documentation and accounting for payments; due diligence of consultants and other third parties; a process for ensuring that payments correspond to actual services; and oversight procedures for third-party retention and payment.²²

Terms of Settlement

Ericsson agreed to pay approximately \$540 million in disgorgement and pre-judgment interest to the SEC and a criminal monetary penalty of over \$520 million to DOJ. In addition, Ericsson agreed to enhance its existing compliance program and agreed to retain an independent compliance monitor, who will assess Ericsson's compliance with its anti-corruption compliance program and with the DPA's terms for a three-year period.²³

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16. *Id.* ¶ 89.

17. *Id.* ¶¶ 88, 93.

18. *Id.* ¶¶ 95–96.

19. *Id.* ¶ 107.

20. *Id.* ¶ 108; SEC Complaint ¶ 83.

21. DPA Attachment A ¶ 109.

22. *Id.* ¶ 115.

23. DPA Attachment D ¶ 2.

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Notably, although DOJ thanked law enforcement authorities in Sweden for their assistance, there was no coordinated resolution between U.S. and Swedish authorities, and no public announcement of an investigation into the company by Swedish authorities until December 12, 2019.²⁴

Compliance Procedures Regarding Third Parties

In this era of vigorous anti-corruption enforcement, as the Ericsson resolutions reflect, any company operating internationally must take great care to ensure that third-party agents, particularly those interacting with government entities and officials, do not engage in corrupt conduct. The FCPA's anti-bribery provisions prohibit making a payment to "any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised . . . to any foreign official" for purposes of influencing the foreign official's decisions.²⁵ As both the SEC and DOJ have pointed out, "third parties, including agents, consultants, and distributors, are commonly used to conceal the payments of bribes to foreign officials."²⁶ Indeed, some of the largest FCPA enforcement actions – now including the Ericsson settlement, as described above – have involved improper payments by third-party agents, consultants, or services providers.

The Ericsson case, with its record-breaking settlement, serves as an important reminder that companies must implement and maintain compliance procedures to address and mitigate the risk of dealing with third parties in higher risk jurisdictions around the world. While there is no one-size-fits-all approach to mitigating third-party risk, there are certain best practices that apply:

1. **Identify which types of third parties present anti-corruption risk and plan accordingly.** This often involves working with your procurement or vendor management departments to implement policies and procedures tailored to relevant risk factors and that, among other things, ensure that appropriate resources are in place for onboarding and working with different types of third parties, especially those posing the greatest risks.
2. **Determine initial appropriateness of engaging a third party.** As an initial step, consider why a third party is necessary in the first place, rather than leveraging a company's internal resources. There are many good business reasons to work through third parties, such as accessing particular industry expertise or geographic presence. But there are many inappropriate reasons too.

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24. *Sweden Opens Ericsson Bribery Probe After U.S. Settlement: Paper, supra* n. 6.

25. 15 U.S.C. § 78dd-1(a)(3) (emphasis added)

26. U.S. Sec. & Exch. Comm'n & U.S. Dep't of Justice, A Resource Guide to the U.S. Foreign Corrupt Practices Act 60 (2012)..

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3. **Conduct risk-based due diligence.** Adequate screening is critical and must be tailored to relevant risks, such as where the third party will operate and whether the third party will interact with government entities and officials. Where red flags are identified, they should be addressed and resolved prior to retention. Additionally, such due diligence must be updated periodically.
4. **Ensure that compensation is reasonable.** Certain types of compensation pose greater corruption risks, particularly those involving generous success-based formulas. Make sure that the total compensation is appropriate under the circumstances and avoid atypical payment mechanisms, such as payments in cash or to unrelated entities in different jurisdictions.
5. **Formalize an appropriate written agreement.** A contract should specify important elements such as the precise services to be provided and the basis for compensation. Additionally, parties engaging third parties should seek to include relevant compliance provisions, such as representations and warranties, covenants, and audit and termination rights.
6. **Provide relevant training to employees.** Ensure that compliance officers and other relevant employees understand the company's process for managing third parties. Maintain a system to handle red flags, and ensure that employees are trained to recognize and escalate these risks.
7. **Monitor, monitor, monitor.** Exercise care to monitor and oversee the activities of third-party agents. In addition to actively understanding what steps such third parties are taking and with whom, this may include providing training to third parties, obtaining periodic compliance certifications, and exercising audit rights, among other steps.

Conclusion

Ericsson's settlement of over \$1 billion in penalties leaves its mark as the second largest global anti-corruption settlement in history, trailing only Petrobras's \$1.78 billion settlement in 2018.²⁷ It also ranks as the largest FCPA settlement ever, as measured by penalties paid to U.S. enforcement authorities.

Meanwhile, with the inclusion of the Ericsson settlement, this year has seen the highest aggregate amount ever paid in FCPA penalties. The record-breaking Ericsson settlement reinforces the importance of anti-corruption compliance procedures with respect to third-party agents, in particular, including careful oversight of such agents.

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27. U.S. Sec. and Exch. Comm'n, SEC Enforcement Actions: FCPA Cases (last modified Nov. 19, 2019), available at <https://www.sec.gov/spotlight/fcpa/fcpa-cases.shtml>.

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Germany Begins Reform of Corporate Criminal Liability

As envisaged by the current German government's Coalition Treaty, reform of the criminal liability of corporate businesses is now underway. The German Federal Ministry of Justice recently submitted, for intra-governmental discussion purposes only, a first draft of a Corporate Sanctions Act (the "Draft Act") regulating criminal liability for corporate crimes committed in the context of a business. It is meant to replace, two years after its promulgation, the current administrative liability for corporate misconduct under the Administrative Offences Act.

The Draft Act is a newly designed law on the criminal liability of corporations in Germany, technically residing between the standard German individual criminal liability and administrative misdemeanor liability. It provides a complete set of new regulations dealing with the interaction between the accused company and the prosecution – and while not going as far as it could, it clearly reflects more than ten years of experience with U.S.-style internal investigations and prosecutions spurred by the Siemens matter and several other cases in Germany.

Separate from the current system, the Draft Act provides a new set of sanctions on German and also (with some special ramifications) foreign legal entities if top management commits a corporate crime, which is defined as a criminal deed that violates duties of the company or is intended to enrich the company illegally. Corporate crimes committed by lower ranking employees trigger liability if management could have prevented or considerably impeded the crime from occurring, for example by implementation and enforcement of adequate compliance measures. A new feature of the proposed law is that corporations domiciled in Germany may also be held responsible for corporate crimes committed abroad if the wrongdoing would be a punishable crime both in Germany and in the foreign jurisdiction. Contrary to the extraterritorial U.S. and U.K. jurisdiction under the U.S. FCPA or the U.K. Bribery Act, however, criminal liability under the German Draft Act would not extend to crimes committed by foreign subsidiaries.

The following three categories of sanctions replace the current single sanction of a maximum fine of EUR 10 Million:

1. A fine of up to EUR 10 Million or, in case the global revenues of the responsible "economic unit" (defined, as in competition law, to include all controlled companies of a business, locally or abroad) exceeds EUR 100 Million per year, up to 10% of the revenues.

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2. A formal *warning* coupled with a *contingent fine* operating for a period of one to up to five years, if the court finds that a fine under category 1, Above, is not appropriate. The novelty is that the court in such case may issue an *imposition* on the company to compensate the injured persons or make a payment to the government. It can also direct the company to implement certain measures to prevent future corporate crime from occurring and to show evidence of implementation to avoid the contingent fine. The evidence needs to be rendered by an expert appointed by the company with the consent of the court, a completely new concept for Germany and one that shows some similarity to the U.S. concept of a monitor.
3. *Dissolution* of the company in egregious cases.

In addition to the sanctions and as already permitted by the existing law, the court may order the disgorgement of ill-gotten gross profits of the crime, which may be reduced by related expenses only to the extent they were not used to commit the crime.

The new sanctioning concept comes with publication options. In a case involving a large number of injured persons, the court may order the publication of the sanction, but on the internet only for a period of no longer than one year. The Federal Ministry of Justice will set up a register of sanctions to which only the company and prosecuting authorities in Germany and the EU have access, and only for a period of ten years. Here, one needs to keep in mind that there are also separate registers available, such as the central trade registers and the special procurement register, available to authorities involved in public procurement.

The Draft Act provides guidance on the factors to be taken into account for sanctioning. Those include the severity of the crime, the efforts necessary to detect and compensate the injured persons, the measures employed in order to prevent and detect future crimes (namely internal investigations; see below), the degree of fault and the motives of the criminal individual, the modus operandi as well as the number and the hierarchical positions of the individual perpetrators, prior misconduct, and the consequences of the wrongdoing for the company's business. The weight assigned to the factors remains in the discretion of the court, and the sanctions are not as predictable as under the U.S. Sentencing Guidelines, the U.S. Department of Justice's Corporate Enforcement Policy, or the U.K Sentencing Guidelines for use in courts in England and Wales with regard to fraud, bribery, and money laundering offences.

One key difference from the current law is that the Draft Act commands mandatory prosecution – there is no longer discretion. It is expected that the workload of prosecutors, the necessity for special continuing education, and

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the need for outside service providers will increase significantly. The Draft Act counterbalances the expected additional caseload for the prosecution with several additional grounds to decline or end the proceedings, including de minimis cases, companies severely suffering from the consequences of the crime, an expected foreign sanction for the same crime (this would be one of the first statutory regulations in corporate criminal law of the concept of *ne bis in idem* (double jeopardy)), or insolvency of the company. The prosecutor can in particular suspend the prosecution in case of internal investigations and require a final report within a certain timeframe, also a novelty in corporate criminal matters in Germany.

It is indeed remarkable how much weight and importance the Draft Act assigns to internal investigations of the affected company. If done as required by the Draft Act, for which there is a set of requirements (see below), it can have a mitigating effect of

“A new feature of the proposed law is that corporations domiciled in Germany may also be held responsible for corporate crimes committed abroad if the wrongdoing would be a punishable crime both in Germany and in the foreign jurisdiction.”

up to 50% of the fine (but not the disgorgement) and, as mentioned, serve as a basis for the prosecutor to defer (but not decline) the investigation. The clear aim is to cause companies to cooperate and to combine their investigation and remediation efforts with the state investigation in the interest of full and continuous cooperation.

To qualify for a possible reduction in fine, internal investigations need to fulfill the following requirements: the investigation needs to (i) contribute materially to the discovery of the corporate crime, (ii) if conducted by outside counsel, then by a lawyer who is *not* the company's defense counsel, and (iii) provide full and continuous cooperation, in particular by sharing the results including all relevant documentary evidence and final reports with the prosecution, while (iv) observing certain essential fair trial standards: interviews conducted with employees require that the interviewee has been informed of (x) the possibility that the testimony may be used in a criminal prosecution, of (y) a right to have a lawyer or a member of the works council present, and of (z) a right to refuse testimony if the person would expose herself to criminal prosecution. The investigation has to comply with relevant laws, in particular data protection and employment relations laws.

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A particular issue in internal investigations under German law is the attorney-client privilege. In internal investigations, the privilege serves as a tool to control the reporting of findings and to protect company employee witnesses, who under German labor law have to be fully forthcoming when asked about their work and any wrongdoing committed. The German law privilege is based on professional secrecy and already limited in scope in comparison to the broader U.S. attorney-client privilege and attorney work product doctrine or the U.K. legal advice or litigation privileges: compared to internal investigations in the United States or the United Kingdom, the Draft Act puts internal investigations in Germany into a different role in that the results of an internal investigation, including interview records, must be fully communicated to the prosecution. The company does not have an option to select the information it needs to produce and to protect certain witnesses to enable them to be fully forthcoming in the interest of the company. This puts the investigation at a considerable disadvantage compared to the United States and United Kingdom, and pushes outside counsel into the role of a quasi-public investigator (but without the powers that a prosecutor has, including arrests and attachment of evidence).

So the new Draft Act places companies between Scylla and Charybdis: accept the new rules of the internal investigation and risk incomplete fact-finding, or play the investigation by different rules and obtain more information (including information that may be needed to remedy any compliance deficiencies) but risk foregoing a reduction of the sanction. It puts a considerable burden on legal advisors to the company to optimize investigations such that they serve either – or preferably both – purposes.

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