Debevoise & Plimpton

FCPA Update
October 2016
Volume 8
Number 3

FCPA Update

A Global Anti-Corruption Newsletter

Also in this issue:

Click here for an index of all *FCPA Update* articles

If there are additional individuals within your organization who would like to receive *FCPA Update*, please email prohlik@debevoise.com, eogrosz@debevoise.com, or pferenz@debevoise.com

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

On September 29, 2016, the U.S. Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") entered into a $412 million settlement with Och-Ziff Capital Management Group ("Och-Ziff") and its wholly-owned subsidiary, OZ Africa Management GP, LLC ("OZ Africa"). The DOJ and SEC allege that Och-Ziff paid tens of millions of dollars in bribes, through intermediaries, to government officials in Libya, the Democratic Republic of the Congo ("DRC"), Chad, and Niger in order to obtain investments and other business.[1] The settlement

Continued on page 2

1. Unless otherwise noted, these alleged facts are drawn from statements of fact accompanying the Deferred Prosecution Agreement and subsidiary plea agreement. See United States v. Och-Ziff Capital Management Group LLC, Cr. No. 16-516, Deferred Prosecution Agreement (E.D.N.Y. Sept. 29, 2016) ("DPA"), Attachment A ("Statement of Facts"), https://www.justice.gov/opa/pr/och-ziff-capital-management-admits-role-africa-bribery-conspiracies-and-agrees-pay-213. The SEC's administrative order largely tracks the facts set forth in the DOJ's papers. See In the Matter of Och-Ziff Capital Management Group LLC, et al., SEC Admin. Pro. 3-17595 (Sept. 29, 2016) ("SEC Order"), https://www.sec.gov/news/pressrelease/2016-203.html.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 1

marks the first time the U.S. authorities have brought a major FCPA enforcement proceeding against a hedge fund and may signal increased anti-corruption scrutiny for investment advisors.

Relevant Conduct

Conduct in Libya

The conduct described in the settlement documents primarily involves Och-Ziff's efforts, beginning in 2007, to secure investments by the Libyan Investment Authority ("LIA") in its hedge funds. An Och-Ziff employee, identified as Employee 3,[2] engaged the services of an unnamed third-party Libyan agent to facilitate such investments. The regulators describe Employee 3 as a U.S. citizen and senior executive at Och-Ziff – specifically, a member of the company's partner management committee and the head of its London office – and attribute a substantial portion of the allegedly improper conduct to him. The Libyan agent is described as "a London-based middleman with connections to foreign officials in Libya," and – rather than having experience as a financial consultant or advisor – was simply known as a middleman with connections to foreign government officials.[3]

The Libyan agent facilitated meetings between Employee 3 and Libyan officials, including officials of the LIA, although the Libyan agent's role on behalf of Och-Ziff was not disclosed to the LIA. According to the settlement documents, Employee 3 knew that the Libyan agent would need to pay bribes to government officials to facilitate the investments. Ultimately, in December 2007, the LIA invested $300 million in two Och-Ziff funds. Through its relationship with the Libyan agent and Och-Ziff's resulting transactions in Libya, Och-Ziff ultimately received approximately $100 million in fees and incentive income.

Throughout 2007, Employee 3 and the Libyan agent engaged in discussions regarding the agent's fee. As part of these discussions, the agent told Employee 3 that the agent would need to discuss the amount of the fee with an "undisclosed third-party" to confirm whether the fee amount would be acceptable.

Shortly after the LIA made its $300 million investment in Och-Ziff's funds, an Och-Ziff officer sent Employee 3 a consultancy agreement and anti-corruption side letter to be executed between OZ Management LP and the agent's SPV. Among other things, the side letter included anti-corruption representations from the SPV and stated that "[t]he Investor [the LIA] has been informed in writing of the

Continued on page 3

2. The DOJ refers to these employees by number; the SEC refers to them by letter. The SEC identifies Employee 3 as Employee A.
3. Statement of Facts ¶ 13.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 2

[Consultancy] Agreement and the consideration payable to [the agent] thereunder."[4] In fact, the LIA was never notified about the fees that Och-Ziff agreed to pay to the agent's SPV; nor did Och-Ziff seek acknowledgement from the LIA that it had received such notification. The consultancy agreement and side letter were executed on January 15, 2008, but backdated so that they appeared to be executed on December 5, 2007. Also, despite Och-Ziff policies requiring due diligence on its business partners, the company did not conduct any diligence on the agent's SPV before entering into the consulting agreement.

The consulting agreement provided for payment by Och-Ziff of a $3.75 million fee to the agent's offshore SPV, based in the British Virgin Islands. In its books and records, Och-Ziff recorded the fees paid to the Libyan agent as "Professional Services—Other."[5] According to the settlement documents, of the $3.75 million paid to the Libyan agent's SPV, $2.5 million was transferred to accounts held for the benefit of the Libyan officials.

"Although it is too soon to say whether the Och-Ziff resolution marks the beginning of a series of FCPA enforcement actions involving investment advisors, it reinforces the importance of robust anti-corruption policies, procedures, and controls even for industries not previously subject to significant anti-corruption enforcement activity."

In addition, in October 2007, about a month before the LIA's $300 million investment, Och-Ziff Employee 3 arranged for a $40 million investment by Och-Ziff in a Libyan real estate development project founded by the Libyan agent. Och-Ziff paid a $400,000 "deal fee" to an entity controlled by the Libyan agent, which it knew would compensate the Libyan agent for bribes it had to pay in connection with the project. The Gaddafi family also was involved with the development project, and Employee 3 and other Och-Ziff investment professionals in London knew of the Gaddafi family's involvement.

Continued on page 4

4. Statement of Facts ¶ 83. The SEC faulted Och-Ziff's decision to enter into a contract only with the SPV – rather than the agent himself – because such an engagement resulted in binding only the SPV to the anti-corruption representations contained in the side letter. SEC Order at 8.

5. SEC Order at 9.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 3

Conduct in Sub-Saharan Africa

In addition to the Libya-related conduct, in late 2007, two Och-Ziff employees, Employee 3 and Employee 5,[6] engaged in discussions with an Israeli businessman ("DRC partner") operating in the DRC in order to obtain "special access" to certain investment opportunities in that country's diamond and mining sectors. The DRC partner informed the two employees that it would have to pay money to DRC officials and local partners to secure such access, and that it expected Och-Ziff to help fund these payments. The employees did not inform anyone in Och-Ziff's legal or compliance departments about these discussions. The company did conduct certain due diligence on this DRC partner and learned that the partner had been willing to use political influence to facilitate, among other things, acquisitions.[7]

According to the SEC, despite the company's awareness of the corruption risk surrounding its involvement with the DRC partner and its business in the DRC, it moved forward on several transactions with the DRC partner between March 2008 and February 2011. The DRC partner provided the promised access to these transactions by – with the knowledge of Employees 3 and 5 – paying bribes to senior government officials in the DRC. Och-Ziff allegedly received more than $90 million in profits from the DRC-related investment opportunity in exchange for payments of "tens of millions of dollars" in bribes to DRC officials.

The SEC Order alleges additional Och-Ziff conduct in other African countries. For example, in 2007 and 2008, Och-Ziff investor funds provided loans of more than $86 million and funds of more than $10 million to assist, among other things, with the acquisition of mining rights in Chad and Niger. In 2011, a fund created by Och-Ziff invested in oil rights in the Republic of Congo through an oil exploration and development company controlled by Och-Ziff and a South African business partner. In connection with this deal, Och-Ziff failed to disclose certain material information regarding the transaction and the relevant partners in it. In 2011, the same fund purchased shares in a London-based oil exploration company in provide capital for a South African business partner. Those funds were ultimately used by the partner, through a consultant, to pay bribes to government officials in Guinea.

Employees 3 and 5 allegedly were aware of – or wilfully blind to – bribes paid to foreign government officials and middlemen to facilitate these transactions. In addition, Och-Ziff failed to conduct due diligence surrounding the use of these funds.

Continued on page 5

6. The SEC identifies Employee 5 as Employee B.

7. In 2008, an Och-Ziff employee was also informed through an audit that the DRC partner's records likely reflected certain payments made to DRC officials. Employee 5 effectuated the removal of that language from a revised report of the audit.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 4

The SEC Order finally includes details about transactions by OZ Management, a registered investment adviser that managed certain investor funds entrusted to Och-Ziff. According to the SEC, OZ Management authorized the use of funds in transactions that ultimately led to bribes paid to foreign government officials. OZ Management also improperly recorded the transactions as investments or convertible loans rather than bribe payments, despite knowledge by Employees 3 and 5 to the contrary.

Inadequate Accounting Controls

Both regulators alleged that Och-Ziff failed to maintain adequate internal accounting controls to prevent the bribe payments detailed above. Moreover, where improper transactions were flagged, Och-Ziff did not take corrective measures such as verifying certain payments or exercising audit or cancellation rights.

With respect to the Libyan conduct, the DOJ noted that "Och-Ziff further permitted Och-Ziff Employee 3 to enter into arrangements for deal fees and payments without requiring contracts, proof of services or legal pre-approval, including for an earlier $400,000 deal fee to [the Libyan agent] in connection with the [real estate development project] where no agreement was in place and . . . Employee 3 knew that the fee would be used for bribe payments."[8] The SEC Order notes that this conduct occurred despite the company's finalization, in April 2008, of its anti-corruption policy and procedures.[9]

Settlement With U.S. Regulators

As set forth in detail below, Och-Ziff agreed to pay a total of $412 million to settle with the DOJ and the SEC for its conduct in Africa. This fine is the fourth largest imposed in any FCPA resolution.

DOJ Resolution

Och-Ziff entered into a three-year deferred prosecution agreement ("DPA") with the DOJ for two counts of conspiracy to violate the anti-bribery provisions of the FCPA, one count of violating the FCPA's books and records provisions, and one count of violating the FCPA's internal controls.

The DOJ cited the following as relevant considerations when entering into the DPA: (1) Och-Ziff's failure to voluntarily self-disclose, which resulted in its ineligibility "for a more significant discount on the fine amount or the form of resolution"; (2) Och-Ziff's cooperation with the DOJ, which resulted in a

Continued on page 6

8. Statement of Facts ¶ 94.
9. SEC Order at 27.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 5

20% discount off the bottom of the U.S. Sentencing Guidelines ("the Guidelines") range of penalties; (3) Och-Ziff's provision to the DOJ of all of the relevant facts of which it was aware, including facts relevant to individual misconduct; (4) Och-Ziff's significant remediation, including improving its compliance program and internal controls and committing to continue that process to ensure compliance that satisfies the elements of a corporate compliance program set forth in an attachment to the DPA;[10] (5) Och-Ziff's agreement to the imposition of an independent compliance monitor for the pendency of the DPA; (6) the seriousness of the offense, including the high value of bribes paid and the involvement of a high-level Och-Ziff employee; (7) Och-Ziff's lack of criminal history; and (8) Och-Ziff's commitment to continue cooperating with the DOJ. The fact that the DOJ expressly referred to Och-Ziff's failure to self-report and its corresponding ineligibility for a further reduction in its penalty, while at the same time praising Och-Ziff's cooperation, is instructive – particularly in the absence of any legal obligation for the company to self-report.

In assessing Och-Ziff's cooperation, the DOJ praised the investigation conducted by the company's audit committee and counsel, which included regular reports to the DOJ, production of "voluminous evidence located in foreign countries," and the company's efforts to make available current and former employees for interviews. However, the DPA notes that Och-Ziff "did not receive additional credit because of issues that resulted in a delay to the early stages of the investigation, including failures to produce important, responsive documents on a timely basis, and in some instances producing documents only after the [DOJ and SEC] flagged for the Company that the documents existed and should be produced, and providing documents to other defense counsel prior to their production to the government."[11] The DOJ's reference to the sharing of documents with other defense counsel is particularly striking given that it appears to be undisputed that the DOJ received the very same documents and that Och-Ziff's sharing of documents with defense counsel before the DOJ in no way hampered or impaired the DOJ's investigation.

The DOJ's calculation of Och-Ziff's fine began with $222 million – the amount of pecuniary gain, i.e., Och-Ziff's gross revenue from the transactions at issue[12] – then applied several mitigating and aggravating factors, most importantly the participation of senior personnel in the offense and Och-Ziff's cooperation and acceptance of responsibility, ultimately yielding a penalty of $213 million.

Continued on page 7

10. The DPA requires Och-Ziff to conduct a review of its existing internal controls, policies, and procedures, and adopt new policies where necessary to ensure that it has a rigorous system of internal accounting controls and anti-corruption compliance program. *See* DPA, Attachment C ("Corporate Compliance Program") at C-1.
11. DPA ¶ 4(b).
12. United States Sentencing Guidelines § 8C2.4(a)(2).

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 6

While the DPA focuses on Och-Ziff's conduct in both Libya and the DRC, the subsidiary's guilty plea relates only to its conduct in the DRC. OZ Africa pled guilty to one count of conspiracy to violate the FCPA's anti-bribery provisions. In the plea agreement, the DOJ listed substantially the same factors considered as those set forth in the DPA.

Och-Ziff, in a press release, stated that it will pay the regulators using "cash on hand and an investment of up to $400 million made by certain of the company's partners through a perpetual preferred stock offering" in order to ensure Och-Ziff can continue investing on behalf of clients.[13]

"Appropriate oversight of agents and other third-party intermediaries *after* they are hired takes on particular significance in light of the Och-Ziff resolution, making the vigorous exercise of audit rights in high-risk jurisdictions, with findings reported to both the legal and compliance functions, especially important."

SEC Resolution

To resolve the SEC's claims, Och-Ziff and OZ Management agreed to pay approximately $199 million, comprised of approximately $173 million in disgorgement and approximately $26 million in interest. The Administrative Order specifically notes that "Och-Ziff acknowledges that the Commission is foregoing a one-time [$173 million] civil penalty for these charges based upon the imposition" of the $213 million penalty assessed in connection with Och-Ziff's settlement with the DOJ.

The SEC found that Och-Ziff violated the FCPA through its intentional payment of bribes to Libyan officials, its failure to accurately record these bribes on its books and records, and its failure to keep a system of internal accounting controls that would ensure that the company would not pay bribes. OZ Management's violation of the Investment Advisers Act was predicated on its failure to prevent the use of managed investor funds by a business partner in corrupt transactions and its omission of material information in certain transactions in its disclosures to investors.

Continued on page 8

13. Press Release, Och-Ziff Reaches Settlements with U.S. Department of Justice and U.S. Securities and Exchange Commission to Resolve FCPA Investigation (Sept. 29, 2016), http://shareholders.ozcap.com/phoenix.zhtml?c=213764&p=irol-newsArticle&ID=2206997.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 7

Enforcement Activity Involving Individuals

The SEC also entered into settlement agreements with Och-Ziff's CEO, Daniel Och, and CFO, Joel Frank. The SEC Order states that Och was aware of corruption risks in transactions in the DRC, but nonetheless approved investor funds in those transactions, resulting in violations of the FCPA's books and records provisions. Och agreed to pay $2.2 million to the SEC on a no-admit, no-deny basis. That sum represents disgorgement in the amount of approximately $1.9 million, which the SEC Order states represents his "share of gain to Och-Ziff resulting from the transactions with DRC Partner," as well as approximately $274,000 in prejudgment interest.[14] The SEC noted that a penalty would be assessed against Frank on a future date.

Enforcement proceedings also may be brought against other individuals in connection with this matter. Indeed, the DOJ already has charged a Gabonese national, Samuel Mebiame, with conspiracy to bribe foreign government officials in connection with obtaining mining rights in Chad, Niger, and Guinea.[15] The DOJ alleges that Mebiame worked as a "fixer," paying bribes to high-ranking government officials in Niger and Chad on behalf of a mining company owned by a joint venture between Och-Ziff and a separate entity.

Conclusion

Although it is too soon to say whether the Och-Ziff resolution marks the beginning of a series of FCPA enforcement actions involving investment advisors, it reinforces the importance of robust anti-corruption policies, procedures, and controls even for industries not previously subject to significant anti-corruption enforcement activity.[16] Anti-corruption training, including of senior personnel, is essential. Hedge funds, private equity firms, and other investment advisors also would be well-advised to ensure that they have in place appropriate procedures for anti-corruption diligence on transactions and investments. Appropriate oversight of agents and other third-party intermediaries *after* they are hired takes on particular significance

Continued on page 9

14. SEC Order at 35.
15. Press Release, Department of Justice, Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay $213 Million Criminal Fine (Sept. 29, 2016), https://www.justice.gov/usao-edny/pr/och-ziff-capital-management-admits-role-africa-bribery-conspiracies-and-agrees-pay-213#_ftn1.
16. Although the DOJ and SEC, in the settlement papers, discuss certain deficiencies in Och-Ziff's internal controls, they fail to acknowledge that Employee 3 and, to a lesser extent, Employee 5 appear to be primarily responsible for the misconduct. We note that no compliance program can prevent in all cases the actions of an employee determined to circumvent controls.

In First Major FCPA Enforcement Action Against a Hedge Fund, U.S. Settles With Och-Ziff Capital Management

Continued from page 8

in light of the Och-Ziff resolution, making the vigorous exercise of audit rights in high-risk jurisdictions, with findings reported to both the legal and compliance functions, especially important.

Paul R. Berger

Colby A. Smith

Rushmi Bhaskaran

Kayla Bensing

Paul R. Berger and Colby A. Smith are partners in the Washington, DC office. Rushmi Bhaskaran and Kayla Bensing are associates in the New York office. The authors may be reached at prberger@debevoise.com, casmith@debevoise.com, rbhaskaran@debevoise.com, and kbensing@debevoise.com. Full contact details for each author are available at www.debevoise.com.

Continued on page 10

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

On September 29, 2016, the U.S. Department of Justice ("DOJ") issued two letters "closing its investigations" into alleged violations of the U.S. Foreign Corrupt Practices Act by HMT LLC, a Texas based manufacturer, supplier and servicer of above ground liquid storage tanks, (the "HMT Declination")[1] and NCH Corporation, a Texas based industrial supply and maintenance corporation (the "NCH Declination).[2] Unlike in the three earlier "declinations" the DOJ issued since the start of its FCPA Enforcement "Pilot Program,"[3] the companies here (HMT and NCH) are not issuers, so there were no parallel Securities and Exchange Commission ("SEC") enforcement actions. Each declination also includes what are described as findings of the DOJ's investigation underlying violations of the FCPA and a requirement that each company pay "disgorgement" to the U.S. Treasury. The HMT and NCH declinations therefore raise the question of whether and to what extent the Pilot Program, in addition to offering guidance on how to receive a declination, has altered the meaning of what a declination ordinarily will be. Specifically, under what circumstances can a company receive a declination without the DOJ publicizing its "findings" and the company paying disgorgement (i.e., a "clean" declination)?

These questions should be considered in light of the recent but pre-Pilot Program declination granted to Harris Corporation[4] (which also included a SEC declination)[5] for which there was a parallel SEC enforcement action against former Harris employee Jun Ping Zhang (the "Zhang Order") on September 13, 2016.[6]

Continued on page 11

1. Letter from Lorinda Laryea to Steven A. Tyrrell, Re: HMT LLC, (Sept. 29, 2016) ("HMT Declination"), https://www.justice.gov/criminal-fraud/pilot-program/declinations.
2. Letter from Laura N. Perkins to Paul E. Coggins, Re: NCH Corporation, (Sept. 29, 2016) ("NCH Declination"), https://www.justice.gov/criminal-fraud/pilot-program/declinations.
3. *See* Andrew M. Levine, Bruce E. Yannett and Philip Rohlik, "Early Thoughts on the DOJ's Pilot Program, the Continued Breadth of the Accounting Provisions, and Possible Implications for Self-Reporting," FCPA Update, Vol. 7, No. 12 (July 2016).
4. Harris Corporation, Form 10-Q for the Quarter Ended April 1, 2016 at 19 (filed May 4, 2016), https://hsprod.investis.com/shared/v2/irwizard/sec_item_new.jsp?epic=hrs1&cik=&ipage=10915082&DSEQ=&SEQ=&SQDESC=.
5. Securities and Exchange Comm'n, "SEC Charges Former Information Technology Executive with FCPA Violations; Former Employer Not Charged Due to Cooperation with the SEC," Administrative Proceeding File No. 34-78825, https://www.sec.gov/spotlight/fcpa/fcpa-cases.shtml.
6. *In the matter of Jun Ping Zhang*, Order Instituting Cease-and-Desist Proceedings, Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and Desist Order, Securities Exchange Act of 1934 Rel. No. 78825 (Sept. 13, 2016), https://www.sec.gov/litigation/admin/2016/34-78825.pdf.

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

Continued from page 10

The HMT and NCH Declinations

Both the HMT and NCH Declinations are approximately two pages in length and begin with the typical wording of a declination, that the DOJ is "closing its investigation of your client . . . concerning violations of the Foreign Corrupt Practices Act."[7] Thereafter, each declination appears to follow a novel course in stating that "[o]ur investigation found" or "[t]he Department's investigation found" particular wrongdoing: that HMT employees and agents "paid . . . bribes"[8] in Venezuela and China, and NCH's Chinese subsidiary "illegally provided things of value" in China.[9] Each of the letters continues with specific factual findings.

Between 2002 and 2011, HMT allegedly retained a sales agent in Venezuela to promote sales to Petroleos de Venezuela, S.A. ("PDVSA"). The agent allegedly would provide PDVSA with inflated quotations for HMT materials, and the difference between the price quoted to PDVSA and the price quoted to the agent would be remitted to the agent as commissions and contracting fees from HMT's bank account in Texas. In turn, the agent allegedly would use part of the excess funds to pay bribes in Venezuela.[10] The HMT Declination goes on to allege that one HMT regional manager in Texas was "explicitly told" of the bribery scheme, while another was "provided with information . . . sufficient to notify him that the Venezuelan agent was paying [] bribes[.]"[11] Similarly, in China, between 1999 and 2011, HMT's Chinese subsidiary allegedly engaged a distributor that "illegally paid bribes" to Chinese government officials at state-owned enterprises.[12] As with the conduct in Venezuela, a U.S. citizen regional manager received emails "sufficient to provide notice that bribes were being paid . . . ."[13] According to the HMT Declination, the total amount of alleged bribes paid was "approximately $500,000."[14]

The NCH Declination alleges that NCH's Chinese subsidiary "illegally provided things of value worth approximately $44,545 to Chinese government officials" between 2011 and 2013.[15] These things of value were cash, gifts, meals, and entertainment recorded by the Chinese subsidiary as "customer maintenance fees,"

Continued on page 12

7. HMT Declination at 1; NCH Declination at 1.
8. The term "bribery" was also used in the JCI, Nortek, and Akamai "declinations."
9. HMT Declination at 1; NCH Declination at 1.
10. HMT Declination at 1.
11. *Id.* at 2.
12. *Id.*
13. *Id.*
14. *Id.* at 1.
15. NCH Declination at 1.

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

Continued from page 11

"customer cooperation fees," and "cash to customer," and were reviewed by a U.S.-based executive.[16] NCH also allegedly paid $12,000 for several employees of a government customer to take a ten-day trip to North American, only a half-day of which was business related, after being advised that the trip might violate the FCPA.[17]

Each declination letter then lists six factors supporting the declinations: (1) voluntary self-disclosure; (2) "thorough and comprehensive" internal investigation; (3) full cooperation (including the disclosure of all relevant facts about the individuals involved); (4) agreement to disgorge profits from the allegedly improper conduct; (5) compliance program and internal controls enhancement; and (6) "full remediation."[18] HMT agreed to disgorge $2,719,412, and NCH agreed to disgorge $335,342 to the U.S. Treasury within ten days of the date of the declination letter.[19]

"The benefits of a Pilot Program declination are therefore muted by the requirement to pay disgorgement, the reputational damage from published allegations, and the related potential for collateral consequences, as well as the reality of the Pilot Program's baseline encouragement of self-reporting and cooperation."

Declinations or Informal NPAs?

Prior to the Pilot Program, the DOJ did not commonly publicize declinations. However, the DOJ's "Declinations" page on its website[20] now includes five "declinations:" Nortek, Akamai, JCI, HMT and NCH. It is worth noting that all of these declinations involved self-disclosure prior to the announcement of the Pilot Program and are therefore declinations applying the policy set out in the Pilot Program rather than, strictly speaking, declinations rewarding self-reporting since the DOJ announced the Pilot Program. Nonetheless, differences between the resolutions with HMT and NCH, on the one hand, and the other three listed matters, on the other hand, raise the question of what the DOJ means by "declination."

Continued on page 13

16. *Id.*
17. *Id.*
18. HMT Declination at 2; NCH Declination at 2.
19. HMT Declination at 2; NCH Declination at 2.
20. U.S. Department of Justice, Declinations, https://www.justice.gov/criminal-fraud/pilot-program/declinations (last updated Sept. 29, 2016).

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

Continued from page 12

The HMT and NCH Declinations differ from the three prior declinations in two ways. First, the HMT and NCH Declinations explicitly include factual assertions (summaries of what the DOJ's "investigation found") that arguably would establish a violation of the FCPA, including its jurisdictional predicate (i.e., some U.S. nexus), statements missing from the publicly available information in the Nortek, Akamai, and JCI enforcement actions.[21] Second, both the HMT and NCH Declinations require disgorgement, a precondition for a declination as addressed in a footnote in the DOJ's memo announcing the Pilot Program.[22] While these two aspects were (arguably) unnecessary in the earlier "declinations," as both a statement of facts and disgorgement were present in the parallel SEC actions, their inclusion in the HMT and NCH Declinations raises questions about the benefits of a declination and the difference between a declination and a non-prosecution agreement.

When assessing FCPA risks and the potential consequences of a FCPA violation, there are at least five factors that a company should consider: (1) the risk of a criminal charge or civil complaint; (2) possible fines or disgorgement to be paid as a result of an enforcement action; (3) the investigative costs of lost productivity and legal and professional fees associated with cooperation with an investigation (which can be greater than any fine or disgorgement); (4) reputational damage ensuing from FCPA allegations; and (5) the potential for the collateral consequences of debarment or lawsuits by competitors arising from an enforcement action. As with an NPA, by including allegations and disgorgement, the HMT and NCH Declinations expose the companies to the costs associated with factors two to four and, in the case of HMT, the allegations in the declination include the name of the recipient, arguably providing a starting point for the costs associated with the fifth factor.

It is certainly significant that neither HMT nor NCH was required to accept the factual assertions in the Declinations. In addition, as an assistant chief of the Fraud Section recently pointed out,[23] the recent HMT and NCH declinations (unlike traditional NPAs) included neither requirements of ongoing reporting or cooperation nor the threat of future prosecution in the case of a breach. However, given the Pilot Program's design to encourage self-reporting and cooperation,

Continued on page 14

21. *See* Levine et al., "Early Thoughts on the DOJ's Pilot Program," *supra* note 3 (noting the lack of a jurisdictional predicate). In a recent Q&A, an assistant chief of the Fraud Section described a case with insufficient evidence to proceed or no jurisdictional predicate as a "traditional declination," while stating that a declination under the Pilot Program could involve "otherwise sufficient evidence to proceed and . . . evidence in the jurisdiction." See Marieke Brejer, "DOJ prosecutor: FCPA Pilot Programme generating more voluntary disclosures," Global Investigations Review (Oct. 26, 2016) (Q&A with Assistant Chief of the Fraud Section Leo Tsao), http://globalinvestigationsreview.com/article/1069920/doj-prosecutor-fcpa-pilot-programme-generating-more-voluntary-disclosures.

22. U.S. Department of Justice, Criminal Division, "The Fraud Section's Foreign Corrupt Practice Act Enforcement Plan and Guidance," at 9 n.6.

23. Marieke Brejer, "DOJ prosecutor: FCPA Pilot Programme generating more voluntary disclosures," *supra* n. 21.

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

Continued from page 13

the lack of formal obligations to do so may be somewhat superfluous. The benefits of a Pilot Program declination are therefore muted by the requirement to pay disgorgement, the reputational damage from published allegations, and the related potential for collateral consequences, as well as the reality of the Pilot Program's baseline encouragement of self-reporting and cooperation.

The Pilot Program therefore appears to have created a dilemma for the DOJ. By providing somewhat detailed allegations relating to a declination, the DOJ laudably has answered the calls of commentators and practitioners for more transparency with regard to what can merit a declination, information which, over time, could become useful to companies doing business in high-risk jurisdictions. At the same time, the greater transparency arguably makes declinations, and therefore self-reporting, less advantageous to companies that uncover wrongdoing by their employees, certainly relative to a clean declination in the traditional sense.

A Traditional Declination – Harris Corporation

Shortly before the HMT and NCH Declinations, an earlier declination came to light involving Harris Corporation ("Harris"). On September 13, 2016, the SEC released a Cease-and-Desist Order (the "Zhang Order" or the "Order")[24] against Jun Ping Zhang ("Zhang"), a U.S. citizen and the former CEO of Harris Corporation's Chinese subsidiary Hunan CareFx Information Technology, LLC ("CareFx China"). Without admitting or denying the findings, Zhang accepted a cease-and-desist order prohibiting him from any future violations of Sections 30A, 13(b)(2)(A), and 13(b)(5) of the Exchange Act, and Exchange Act Rule 13b2-1, as well as payment of a $46,000 civil penalty.[25]

Zhang is described as a United States citizen and resident, though the Zhang Order does not specify whether he was based in China or the United States during the relevant period. The allegations against Zhang are commonplace in relation to China-related enforcement actions, mainly alleging that Zhang approved, or was involved in approving, relatively small value gifts, meals, and entertainment to hospital directors and other Chinese healthcare professions (for example vacation travel, a replacement computer and camera, iPhones, gift cards, and cash).[26]

Harris's role is more interesting from the point of view of companies engaging in acquisitions. Although the Zhang Order explicitly states that Zhang and those working under him "caused Harris to violate" the books and records provisions,"[27]

Continued on page 15

24. Zhang Order, *supra* note 6.
25. *Id.* at 7.
26. *Id.* at ¶¶ 12-17.
27. *Id.* at ¶ 26.

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

Continued from page 14

it appears that most of the activity took place before Harris acquired CareFX China, which represented a tiny percentage (less than 0.1%) of Harris's global operations.[28] Indeed, the order specifically states that Zhang hid[29] the activity from Harris and failed to disclose it during Harris's pre-acquisition due diligence.[30] After acquiring CareFX China, Harris conducted FCPA trainings and conducted an FCPA audit, discovering the illicit conduct within a "few months"[31] and thereafter remediating, and selling part of and ultimately closing the business.

Several months prior to the Zhang Order, Harris disclosed on its 10-Q for the period ending April 1, 2016 (prior to the April 5, 2016 announcement of the Pilot Program) that the DOJ had:

> determined not to take any action against [Harris Corp.] related to this matter. The DOJ further advised us that its decision was based on its overall view of the evidence as to our level of acquisition due diligence, our voluntary disclosure to the DOJ and SEC, our remediation efforts and our cooperation throughout the investigation, which is continuing.[32]

Harris did not disclose that it was required to pay any disgorgement to the U.S. Treasury, and the declination is not listed on the DOJ's declinations page on its website. In its announcement of its cease and desist order against Zhang, the SEC also declined to bring any action against Harris, noting "the company's efforts at self-policing that led to the discovery of [Zhang's] misconduct shortly after the acquisition, prompt self-reporting, thorough remediation, and exemplary cooperation with the SEC.[33]

The allegations against Zhang are not materially different from the allegations against unnamed employees in the NCH Declination, and yet Harris, unlike NCH, was not subject to a disgorgement remedy (even by the SEC). There are at least four possible explanations for this distinction. First, the Harris declination occurred before the Pilot Program required disgorgement as a precondition for a declination, suggesting that a company finding itself in Harris's position might be required to disgorge profits in the future. Second, the Harris declination (without disgorgement) is specific to the acquisition context, suggesting that a similar

Continued on page 16

28. *Id.* at ¶ 4.
29. *Id.* at ¶ 9.
30. *Id.* at ¶ 10.
31. *Id.*
32. Harris Corporation, Form 10-Q, *supra* note 4.
33. Securities and Exchange Comm'n, Administrative Proceeding File No. 34-78825, *supra* note 5.

The Difficulty of Defining a Declination: An Update on the DOJ's Pilot Program

Continued from page 15

outcome still could be available to companies following the DOJ's advice set forth in Opinion Release 14-02 (and elsewhere).[34] Third, Harris involved an individual enforcement action (albeit a SEC action), thereby advancing the goals of the DOJ's Yates Memorandum and the Pilot Program, such that the DOJ may not have viewed a disgorgement remedy as necessary. Fourth, irrespective of the acquisition context and individual enforcement action, the circumstances surrounding Harris's conduct were different than NCH's meriting a different outcome.

As always, the decision whether or not to self-report possible misconduct to the DOJ is a fact-intensive one and requires careful consideration. Companies considering self-reporting under the Pilot Program would benefit from examining closely these recent DOJ declinations and their surrounding circumstances, whether such conduct involves gifts, meals, and entertainment expenses in China or similar conduct elsewhere.

Bruce E. Yannett

Andrew M. Levine

Philip Rohlik

Bruce E. Yannett and Andrew M. Levine are partners in the New York office. Philip Rohlik is a counsel in the Shanghai office. The authors may be reached at beyannett@debevoise.com, amlevine@debevoise.com, and prohlik@debevoise.com. Full contact details for each author are available at www.debevoise.com.

Continued on page 17

34. U.S. Department of Justice, Opinion Release 14-02 (Nov. 7, 2014).

Argentine Government Considers New Anti-Corruption Legislation

Argentina's government is taking concrete steps to act on campaign promises to combat corruption. Soon after assuming power in December 2015, President Mauricio Macri sent to Congress a set of bills known as the "anti-corruption package."[1] These bills exemplify the Macri administration's attempts to foster a more transparent government, amidst ongoing investigations of corruption charges and other allegations against prior government officials, including former President Cristina Fernández de Kirchner.

The anti-corruption package also reflects Argentina's desire to engage productively with the international economic community, including by establishing the necessary conditions and legal structures to attract foreign investment and develop cross-border commerce. Another clear objective of these bills is to improve Argentina's prospects for membership in the Organization for Economic Cooperation and Development ("OECD").

The Anti-Corruption Bills

The new anti-corruption bills include three main proposals: a plea-bargaining bill, an asset recovery bill, and an international bribery bill.[2]

The plea-bargaining bill proposes a reduction in, or potential exemption of, sentences for those who cooperate with the government's prosecution of criminals in corruption cases.[3] Specifically, the bill encompasses particular crimes against the public administration pertaining to corruption of or by public officials, and establishes that cooperation agreements would be offered only to those who provide information about perpetrators or participants in crimes who are at least as senior in the relevant hierarchy as the cooperators themselves.[4] Plea-bargaining is not new in the Argentine legal system, as it is currently applicable to drug-related crimes, terrorism, kidnapping, human trafficking, and money laundering.[5]

Continued on page 18

1. *See* Gustavo Ybarra, *Retoma el Senado su actividad con las leyes anticorrupción [Senate Returns to Work with Anticorruption Laws]*, LA NACION (Aug. 1, 2016), http://www.lanacion.com.ar/1923574-retoma-el-senado-su-actividad-con-las-leyes-anticorrupcion; Espelta et al., Argentina: Bills Propose Plea-Bargaining And Asset-Recovery For Corruption Cases, MONDAQ (July 11, 2016), http://www.mondaq.com/Argentina/x/508466/White+Collar+Crime+Fraud/Bills+Propose+PleaBargaining+And+AssetRecovery+For+Corruption+Cases.
2. Gustavo Ybarra, *Amplio apoyo en el Senado al paquete de leyes anticorrupción [Anticorruption Bills Face Large Support in the Senate]*, LA NACION (Sept. 8, 2016), http://www.lanacion.com.ar/1935638-amplio-apoyo-en-el-senado-al-paquete-de-leyes-anticorrupcion.
3. Proyecto de ley del arrepentido [Bill of the Repentant], arts. 1, 5 (2016), *see also* Ybarra, *supra* note 2.
4. Proyecto de ley del arrepentido, arts. 2, 3.
5. Laura Serra & Gabriel Sued, *Diputados apura leyes clave para la lucha anticorrupción [Representatives Rush Key Laws for Anticorruption Fight]*, LA NACION (June 23, 2016), http://www.lanacion.com.ar/1911577-diputados-apura-leyes-clave-para-la-lucha-anticorrupcion; Espelta et al., *supra* note 1.

Argentine Government Considers New Anti-Corruption Legislation

Continued from page 17

The asset-recovery bill aims to accelerate the seizure of assets acquired as a result of or related to corrupt activities.[6] Pursuant to this bill, such assets – located either in Argentina or abroad – would be forfeited to the state, without compensation, through an expedited process.[7] This bill attempts to remedy the government's current inability to seize assets obtained through illegal activities until anti-corruption enforcement proceedings are completed, which often leaves the government with a devalued asset.

Finally, the international bribery bill addresses one of the OECD's specific requirements: for Argentina to have a law punishing international bribery.[8] This bill would allow the government to pursue local businesspeople who pay bribes outside the borders of Argentina and public officials who accept bribes.[9] Additionally, this bill proposes two main changes to the current legislation in Argentina. First, it extends the reach of the law by allowing for prosecution of companies (not just individuals) for corruption-related crimes.[10] *Second*, it allows Argentine judges to try public officials for corruption-related crimes committed outside of the country without having to prove that those crimes had effects in the country (as required under the current law).[11]

Recent Developments in Congress

Two of the three anti-corruption bills proposed, the plea-bargaining bill and the asset-recovery bill, were approved by the Argentine House of Representatives in June 2016 and received preliminary approval by Argentina's Senate in early September 2016 after undergoing some modifications.[12] The revised bills were sent back to the House of Representatives for final approval.[13] On October 19, 2016, the House of Representatives passed the revised plea-bargaining bill into law.[14]

Unlike the other two bills, the international bribery bill is not yet moving through Argentina's legislature. Through efforts led by its Anti-Corruption Office,

Continued on page 19

6. Proyecto de ley de extinción de dominio [Asset-forfeiture Bill], Capítulo 1, art. 1 (2016).
7. *Id.*
8. Fórmula de sanción [Endorsement Petition], Proyecto de ley de responsabilidad penal de las personas jurídicas [Legal Persons Responsibility Bill] (2016).
9. *Id.*
10. Proyecto de ley de responsabilidad penal de las personas jurídicas, arts. 1, 3 (2016).
11. *Id.* art. 3.
12. Ybarra, *supra* note 1.
13. Ybarra, *supra* note 2.
14. *See* Laura Serra, *Es ley la figura del arrepentido para casos de corrupción [In Cases of Corruption, the Repentent Person is Law]*, La Nacion, (Oct. 20, 2016), http://www.lanacion.com.ar/1948638-es-ley-la-figura-del-arrepentido-para-casos-de-corrupcion; *Diputados aprobó la Ley del Arrepentido [Representatives Pass the Law of the Repentant]*, Infobae, (Oct. 19, 2016), http://www.infobae.com/politica/2016/10/19/se-vota-una-ley-clave-para-la-lucha-contra-la-corrupcion/.

Argentine Government Considers New Anti-Corruption Legislation

Continued from page 18

the Argentine government has been actively promoting this bill, potentially preparing the field for Congress to consider it.

In the Senate's sessions in September 2016, in which the plea-bargaining bill and the asset-recovery bill received preliminary approval, the Senate also discussed and passed a new law providing for expedited prosecution of criminals caught in the act.[15] Although not applied exclusively to corruption crimes, this new law is particularly relevant to the event that appears to have prompted expedited approval by the House of Representatives of the anti-corruption bills: the arrest of a former senior official who reportedly was caught burying millions in cash in a convent in Buenos Aires.[16]

"Under the bill, a company may be able to mitigate its legal culpability and potential penalties when it takes an active role in preventing and detecting crimes against the public administration. . . . Underscoring this point, the bill proposes making companies responsible for any crimes resulting from ineffective controls and supervision."

What Do the Bills Mean for Argentina?

In general, the anti-corruption bills highlight the active efforts of the new Argentine government to fight corruption, seeking to increase transparency and promote Argentina worldwide as a trustworthy recipient of foreign investments.[17]

More specifically, as noted, one of the main goals of the proposed legislation is to strengthen Argentina's chances to enter the OECD. Indeed, although Argentina has ratified the OECD Convention, the Inter-American Convention Against Corruption (IACAC), and the United Nations Convention against Corruption (UNCAC), it has been subject to harsh criticism by the OECD for its failure to prosecute foreign bribery.

The approval of the pending legislative package would be a strong step in the right direction and can be viewed as a direct response to the OECD's prior recommendations and criticisms. The proposed anti-corruption legislation would prohibit international bribery (specifically, bribes to foreign public officials abroad), would expand liability to legal entities (where currently limited to individuals), and would provide for punishment of legal entities, not just individuals.

Continued on page 20

15. *Id.*
16. *See, id.*; Ybarra, *supra* note 1.
17. Fórmula de sanción, Proyecto de ley de responsabilidad penal de las personas jurídicas (2016).

Argentine Government Considers New Anti-Corruption Legislation
Continued from page 19

What Do These Bills Mean for Companies?

If the new bills are passed and vigorously enforced, they could have a significant impact on companies in Argentina not already subject to a transnational corruption law, such as the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act, or Brazil's Clean Company Act.

The international bribery bill itself highlights the need for companies in Argentina to promote a culture of compliance and to implement strong anti-corruption compliance procedures. Under the bill, a company may be able to mitigate its legal culpability and potential penalties when it takes an active role in preventing and detecting crimes against the public administration. That possibility should encourage companies to work harder to prevent corruption and may strengthen enforcement against individual wrongdoers. Underscoring this point, the bill proposes making companies responsible for any crimes resulting from ineffective control and supervision.

Further, the bill seems to reflect the reality in Argentina and worldwide that corrupt activities often involve the use of intermediaries. The bill addresses this by penalizing a company for any corrupt acts undertaken by a person acting on behalf of the company or by those acts from which the company could derive a benefit carried out by suppliers, contractors, agents, distributors, or any other person that has a contractual relationship with the company. Accordingly, if enacted, screening and monitoring of third parties will become increasingly important for companies subject to the proposed legislation.

For those conducting business in Argentina, it remains imperative to monitor developments relating to the pending anti-corruption legislation and to consider how best to implement appropriate policies, produces, and controls that effectively mitigate anti-corruption risk.

Andrew M. Levine

Sarah Coyne

Lucila I. M. Hemmingsen

Carolina Kupferman

Andrew M. Levine and Sarah Coyne are partners in the New York office. Carolina Kupferman is an associate in the New York office. Lucila I.M. Hemmingsen is a former associate. Mr. Levine, Ms. Coyne, and Ms. Kupferman may be reached at amlevine@debevoise.com, scoyne@debevoise.com, and ckupferm@debevoise.com. Full contact details for the authors are available at www.debevoise.com.

FCPA Update

FCPA Update is a publication of
Debevoise & Plimpton LLP

919 Third Avenue
New York, New York 10022
+1 212 909 6000
www.debevoise.com

Washington, D.C.
+1 202 383 8000

London
+44 20 7786 9000

Paris
+33 1 40 73 12 12

Frankfurt
+49 69 2097 5000

Moscow
+7 495 956 3858

Hong Kong
+852 2160 9800

Shanghai
+86 21 5047 1800

Tokyo
+81 3 4570 6680

Paul R. Berger
Co-Editor-in-Chief
+1 202 383 8090
prberger@debevoise.com

Sean Hecker
Co-Editor-in-Chief
+1 212 909 6052
shecker@debevoise.com

Andrew M. Levine
Co-Editor-in-Chief
+1 212 909 6069
amlevine@debevoise.com

Sarah Coyne
Co-Editor-in-Chief
+1 212 909 6968
scoyne@debevoise.com

Philip Rohlik
Co-Executive Editor
+852 2160 9856
prohlik@debevoise.com

Farhana Choudhury
Assistant Editor
+1 212 909 6529
fchoudhury@debevoise.com

Bruce E. Yannett
Co-Editor-in-Chief
+1 212 909 6495
beyannett@debevoise.com

Karolos Seeger
Co-Editor-in-Chief
+44 20 7786 9042
kseeger@debevoise.com

David A. O'Neil
Co-Editor-in-Chief
+1 202 383 8040
daoneil@debevoise.com

Erich O. Grosz
Co-Executive Editor
+1 212 909 6808
eogrosz@debevoise.com

Jane Shvets
Deputy Executive Editor
+44 20 7786 9163
jshvets@debevoise.com

Please address inquiries regarding topics covered in this publication to the editors.

Please note:
The URLs in FCPA Update are provided with hyperlinks so as to enable readers to gain easy access to cited materials.