

CLIENT MEMORANDUM

Recent FCPA Enforcement Action Highlights Risks Related to Charitable Contributions

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AUTHORS

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A new Securities and Exchange Commission (“SEC”) resolution reflects an aggressive interpretation of what may constitute a thing of value to a foreign official under the Foreign Corrupt Practices Act (“FCPA”)—namely, *legitimate* charitable contributions, pre-cleared by outside counsel, but made with an alleged improper motive. On September 20, 2016, Nu Skin Enterprises, Inc. (“Nu Skin U.S.”), a Utah-based manufacturer of cosmetic and nutritional products, agreed to pay \$765,688 to settle SEC claims under the FCPA’s internal controls and books and records provisions in connection with a charitable donation made by its Chinese subsidiary (“Nu Skin China”). Nu Skin U.S. neither admitted nor denied any of the allegations in the settlement. Nu Skin’s common stock is listed on the New York Stock Exchange, thus it is an “issuer” subject to the FCPA.

Background

According to the SEC’s order instituting a settled administrative proceeding (the “SEC Order”), in 2013 Nu Skin China was under investigation by a provincial branch of the Administration of Industry and Commerce (“AIC”) for alleged violations of laws and regulations governing direct selling in China (“Direct Selling Laws”). Concerned about the impact an AIC action would have on Nu Skin China’s long-term business development, Nu Skin China personnel allegedly attempted to influence the outcome of the investigation by initiating a charity project in the province. A Nu Skin China employee contacted a high-ranking Chinese Communist party official (the “Party Official”) to obtain a recommendation of a charity

Recent FCPA Enforcement Action Highlights Risks Related to Charitable Contributions

Continued

located within the province. The Party Official recommended a charity that had not yet been established in the province and had no operations there. According to the SEC Order, the Party Official was “associated” with an entity that was “responsible for establishing the charity in the Province.”

The SEC alleged that shortly after the AIC informed Nu Skin China that it intended to charge Nu Skin China and some of its sales staff with violations of the Direct Selling Laws, “[s]enior personnel of Nu Skin China then made a decision to request that the Party Official personally intervene in the AIC matter in return for Nu Skin China making a One Million RMB donation to the charity identified by the Party Official.” The provincial head of the AIC had previously reported to the Party Official. Two days after a donation ceremony was held in the province—attended by the top official of the AIC, the Party Official, and representatives of Nu Skin China—Nu Skin received notice of the AIC’s final decision not to charge or seek a fine against the company. The SEC alleged that the improper purpose of the payment was further evidenced by the fact that Nu Skin China expedited assistance to the Party Official in obtaining letters from an influential U.S. person recommending his child for admission to U.S. universities.

Prior to finalizing the donation, Nu Skin China alerted Nu Skin U.S. to the proposed donation but did not disclose that the purpose of the donation was to influence the AIC investigation. Nevertheless, aware that a large charitable donation in China could pose FCPA risks, Nu Skin U.S. advised its subsidiary to consult with outside U.S. counsel to ensure that the donation complied with the FCPA. Outside counsel advised Nu Skin China to include anticorruption language in the written donation agreement. The anticorruption language was inserted into a draft of the donation agreement, but, unbeknownst to Nu Skin U.S., it was removed from the final, executed agreement. Despite the fact that Nu Skin U.S. identified the compliance risk and referred the matter to outside counsel, the SEC found that Nu Skin U.S. had insufficient internal controls in that it “did not ensure that adequate due diligence was conducted by Nu Skin China with respect to charitable donations to identify links to government or political party officials and to prevent payments intended to improperly influence such persons.”

The SEC also alleged FCPA books and records violations based on the fact that the payment “was inaccurately and/or unfairly described” on Nu Skin China’s expenditure authorization form “as a donation rather than a payment to influence the Party Official to favorably impact the outcome of the AIC investigation.” The SEC order does not contain any allegation that the donation was not in fact used for charitable purposes or any further explanation as to how the description of the payment was otherwise “inaccurate[] and/or unfair[].”

Analysis

The SEC’s position that a charitable contribution can constitute an improper payment under the FCPA is not new.¹ However, the enforcement action against Nu Skin is noteworthy because of the aggressive position by U.S. regulators

¹ Indeed, this view is consistent with positions taken by U.S. regulators in several prior enforcement actions beginning with a settled enforcement action against Schering-Plough in 2004. The SEC alleged that the pharmaceutical company had violated the FCPA when its subsidiary in Poland made a donation to a charity that was founded and directed by a government official for the purpose of influencing drug purchasing decisions. See

Recent FCPA Enforcement Action Highlights Risks Related to Charitable Contributions

Continued

regarding when a legitimate charitable donation may form the basis of an FCPA violation. This is particularly true here, where: (1) there is no allegation that the charity was not a bona fide charitable organization; (2) there is no allegation that the Party Official or any member of his family received a direct financial benefit as a result of the donation; (3) the Party Official is alleged to have only a tenuous connection to the charity; (4) and Nu Skin U.S.'s internal controls flagged the transaction as high-risk and referred the matter to outside counsel.

The books and records charges against Nu Skin U.S. also reflect an aggressive interpretation of the FCPA. Nu Skin China's expenditure authorization form accurately described the payment as a donation. The SEC faulted Nu Skin U.S., however, because the form did not expressly state that Nu Skin China made the donation with the intent of influencing the Party Official to impact favorably the AIC investigation. It is not clear that the absence of such a detailed description of the *motivation* of a payment renders the authorization false or misleading or would cause Nu Skin U.S. to run afoul of its obligation to "make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer."²

Conclusion

Notwithstanding the aggressive legal theories underlying the Nu Skin FCPA settlement, the case is a reminder to companies of the importance of monitoring charitable giving, particularly in high-risk locations. The first step toward managing FCPA risks associated with foreign charitable contributions is adopting a written charitable giving policy. Companies should also conduct due diligence to determine whether potential charitable recipients have direct or indirect connections to government officials. Companies should also thoroughly vet the purposes of any charitable contribution to ensure it is not being made at the behest of or in an attempt to influence a government official. Finally, Companies should consider implementing controls to ensure its donations are used for their intended purposes, such as compliance certifications, anticorruption provisions in donation agreements, and/or ongoing monitoring of charitable projects.

In the Matter of Schering-Plough Corp., No. 1:04-CV-00945, Order Instituting Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings and Imposing a Cease-and-Desist Order (D.D.C. June 9, 2004); *SEC v. Schering-Plough Corp.*, No. 1:04-CV-00945, Complaint (D.D.C. June 9, 2004). *Id.* The U.S. Department of Justice and the SEC took similar positions regarding donations to bona fide charities in enforcement actions against Eli Lilly Company and Alstom S.A. in 2012 and 2014, respectively. See *United States v. Alstom S.A.*, 3:14-cr-00246, Information, ¶ 28 (D. Ct. Dec. 22, 2014) (finding that Alstom paid bribes by "paying over two million dollars to a charity associated with a foreign official"); *SEC v. Eli Lilly Company*, 1:12-cv-02045, Complaint ¶¶ 2, 7 (describing payments made by Eli Lilly's subsidiary in Poland to a small charitable foundation founded by the head of a regional health authority).

² 15 U.S.C. § 78c(a)(37).

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Recent FCPA Enforcement Action Highlights Risks Related to Charitable Contributions

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