CLIENT MEMORANDUM

U.S. Regulators Settle FCPA Enforcement Actions Based on Hiring Relatives of Government Officials

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AUTHORS

Martin J. Weinstein | Robert J. Meyer | Jeffrey D. Clark | William J. Stellmach

On November 17, 2016, the U.S. Department of Justice (the "DOJ"), the Securities and Exchange Commission (the "SEC"), and the Board of Governors of the Federal Reserve System (the "Federal Reserve") announced settlements with JPMorgan Chase & Co. and its subsidiary JPMorgan Securities (Asia Pacific) Limited ("JPMorgan-APAC") (together, "JPMorgan") covering alleged violations of the U.S. Foreign Corrupt Practices Act (the "FCPA") related to hiring relatives of foreign government officials in China and other Asian countries. The alleged violations surrounded hiring the children of government officials and private clients in order to obtain or retain investment banking business. The settlements involved criminal, civil, and regulatory sanctions totaling more than $264 million. The settlement, the second with a U.S. bank based on hiring the children of government officials, is reportedly among a larger group of similar cases under investigation by U.S. authorities, demonstrates a continued focus on FCPA enforcement in the financial services industry, as well as an aggressive interpretation of the FCPA's "anything of value" and corrupt intent elements. Companies doing business internationally should take note of the FCPA compliance risks related to hiring relatives of or candidates referred by clients, potential clients, and government officials and should implement compliance controls pertaining to such practices.

According to settlement documents, as early as 2006 JPMorgan had a compliance review process designed to ensure that candidates for employment who had been referred to the company by potential clients or government officials were not hired as part of a *quid pro quo* arrangement to win business from the referral source. According to regulators, however, JPMorgan bankers turned this program on its head, using it instead to hire referred candidates specifically for the purpose of influencing senior government officials and private clients to award business to the bank. Through this effort, known informally within JPMorgan as the "Sons and Daughters Program," between 2006 and 2013, JPMorgan hired approximately 200 interns and full-time employees and won more than $100 million in business in China and Taiwan from entities connected to these hires. This business includes investment banking mandates from state-owned entities in China from which the company earned $35 million in profits.

As part of its "revamped" Sons and Daughters Program," JPMorgan sought out referral candidates with a "directly attributable linkage to business opportunity" and hired referred candidates who were less qualified than the regular pool of candidates hired through JPMorgan's standard hiring process. Despite receiving the same title and pay as merit-based hires, in some instances the referral hires only "performed ancillary work such as proofreading" or received other special treatment. JPMorgan executives tracked hires referred by specific clients and the revenue attributable to those hires, allocating the cost of the hires as a marketing expense. JPMorgan employees also allegedly falsified documentation related to the hiring process, including by using pre-completed compliance questionnaires stating that the firm had "no expected benefit" from the hire.

In order to establish a violation of the FCPA's antibribery provisions, the government must prove, among other elements, that the defendant provided "anything of value" to a foreign government official "corruptly," that is, with "an intent to wrongfully influence the recipient."[1] In the JPMorgan case and other, similar cases based on hiring "princelings," the government's theory is that providing a job—even an unpaid internship[2]—to a relative of a government official amounts to giving a "thing of value" to the official. In certain circumstances, the thing of value inuring to the benefit of an official from hiring his or her relative is clear: if the person hired is a financial dependent of the official, the payment of a salary and other benefits may offset financial obligations for which the official otherwise would be responsible. As is evident from the documents quoted in the JPMorgan settlement documents, evidence of an active interest or pressure brought to bear by a government official in the hiring of his or her relative can be viewed as circumstantial evidence that the hiring is a thing of value to the official. In other circumstances, such as the hiring of a financially independent, emancipated adult relative of a government official, it is less clear that the government could demonstrate that a thing of value is being provided to the official.

In order to demonstrate corrupt intent, the government must prove that the thing of value was given as part of a *quid pro quo*, *i.e.*, with "the specific intent to give something of value *in exchange* for an official act."[3] A payment to promote

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1 H.R. Rep. 640, 95th Cong., 1st Sess. 7-8 (Sept. 28, 1977); S. Rep. No. 114, 95th Cong., 1st Sess. 10 (May 2, 1977).

2 The Bank of New York Mellon Corporation, Exchange Act Release No. 75720 (Aug. 18, 2015).

3 *United States v. Sun-Diamond Growers*, 526 U.S. 398, 404-06, 119 S. Ct. 1402, 143 L. Ed. 2d 57 (1999) (emphasis in original). Legislative history indicates that Congress intended the FCPA's corrupt intent element to mirror that same element in the federal domestic bribery statute. S. Rep. No. 114, 95th Cong., 1st Sess. 10 (May 2, 1977) .

generalized goodwill is not sufficient to satisfy this element. In the JPMorgan settlement documents, prosecutors quote language from certain emails that they claim evidences corrupt intent on the part of JPMorgan employees. In some instances, however, the quoted language is more suggestive of an intent to engender goodwill than of an attempt to secure a specific benefit through a *quid pro quo* arrangement. In one instance, in which a senior official at a Chinese state-owned financial services firm referred another senior official's son to JPMorgan-APAC, documents indicate that employees believed that the hire would "place JPMorgan in a more favorable position for securing future business from the client." Although this language appears to suggest an intent to build general goodwill, six months later JPMorgan-APAC became the exclusive financial advisor to the Chinese company. Such circumstantial evidence of corrupt intent demonstrates the nuanced FCPA compliance risks presented by hiring relatives of foreign government officials.

The conduct outlined in the JPMorgan settlement includes efforts to secure business from both state-owned and private customers. Although the FCPA's antibribery provisions reach only corrupt payments to or for the benefit of "foreign officials," which includes officers and employees of state-owned or -controlled companies, JPMorgan's Sons and Daughters Program applied to private and government customers alike. U.S. regulators likely included references to JPMorgan's attempts to secure business from private businesses in the factual recitation in the settlement documents in an attempt to demonstrate corrupt intent with regard to the Sons and Daughters Program generally. Although private-to-private "commercial" bribery is not actionable under the FCPA's antibribery provisions, it could implicate the FCPA's books and records and internal controls provisions, state commercial bribery laws (sometimes chargeable by federal authorities as violations of the federal Travel Act where conduct involves interstate commerce), and, if the company or conduct has a connection to the United Kingdom, the U.K. Bribery Act.

JPMorgan, which did not voluntarily disclose the conduct to enforcement authorities, entered into a non-prosecution agreement with the DOJ under which it will pay a criminal penalty of $72 million, which reflects a 25% discount off the bottom of the applicable U.S. Sentencing Guidelines range justified, according to the DOJ, based on the company's full cooperation and "extensive remedial measures." The company agreed to pay $130.6 million in disgorgement and prejudgment interest to settle parallel charges by the SEC that it violated the antibribery, books and records, and internal controls provisions of the FCPA. JPMorgan also agreed to a consent order to cease and desist from future violations of the FCPA and a $62 million civil penalty to forestall formal administrative proceedings by the Federal Reserve pursuant to the Federal Deposit Insurance Act. As a registered bank holding company, JPMorgan is supervised by the Federal Reserve.

According to the settlement documents, JPMorgan undertook significant remedial measures. In addition to ending the Sons and Daughters Program, JPMorgan disciplined 29 employees, imposed more than $18.3 million in financial sanctions on former or current employees, and instituted a worldwide enhancement of its anticorruption compliance program and hiring practices. As part of that program, JPMorgan now requires that all hires be routed through a centralized human resources application process and that all candidates referred by a client, potential client, or government official be reviewed and approved by JPMorgan's anticorruption office. The company also instituted procedures and practices for monitoring and auditing referral hiring.

Conclusion

The FCPA enforcement action against JPMorgan further underscores the aggressive posture that U.S. regulators have taken regarding the hiring of relatives of foreign government officials. Companies doing business overseas should adopt written policies and procedures governing the hiring, whether for a full-time position or an internship, of relatives of government officials and clients. Referrals from clients, potential clients, and government officials should be vetted to ensure that the candidate possesses appropriate qualifications for a genuine job opportunity. Companies also should design internal controls to ensure that if a foreign government official refers a candidate, the appropriate human resources and compliance personnel are made aware of and can provide input regarding the referral. Companies should conduct due diligence on such referral candidates to determine the nature of the candidate's connection to the foreign official or customer and whether that connection might have the potential to affect the business interests of the company.

Moreover, the JPMorgan settlement, along with the recent FCPA settlement by hedge fund Och-Ziff Capital and other reported ongoing investigations, is a reminder that U.S. government regulators are squarely focused on financial services firms. Financial services firms—especially those with client referral programs and state-owned entities as clients—would be well served to carefully review their compliance programs to make sure such programs include robust procedures for FCPA compliance.

If you have any questions regarding this memorandum, please contact Martin J. Weinstein (202-303-1122, mweinstein@willkie.com), Robert J. Meyer (202-303-1123, rmeyer@willkie.com), Jeffrey D. Clark (202-303-1139, jdclark@willkie.com), William J. Stellmach (202-303-1130, wstellmach@willkie.com) or the Willkie attorney with whom you regularly work.

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