CLIENT MEMORANDUM

Two Recent FCPA Enforcement "Firsts": Settlement with Large Hedge Fund and Two of Its Senior Executives and Two DOJ Pilot Program Declinations Requiring Disgorgement

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A Large U.S. Hedge Fund Resolves FCPA Charges with a Deferred Prosecution Agreement, Compliance Monitor, and Significant Monetary Fines for Two of Its Senior Executives.

In what the U.S. Department of Justice (the "DOJ") touted as the first-ever settlement involving charges against a hedge fund for violations of the Foreign Corrupt Practices Act (the "FCPA"),[1] the DOJ and the Securities and Exchange Commission (the "SEC") on September 29, 2016, announced their respective agreements with a large U.S. asset management firm (the "firm"), and some of its affiliates, to settle charges arising from illicit payments to government officials in several African countries that were made to obtain investments in firm-managed funds and certain other business opportunities. As a result, the firm will pay combined U.S. criminal and regulatory penalties of approximately $412 million. The settlement underscores both the government's interest in FCPA compliance in the financial services industry and the inherent legal dangers for senior executives whose companies do business in high-risk countries.

1 In 2007, the DOJ announced a Non-Prosecution Agreement with Omega Advisors, Inc. in connection with its prosecution of Viktor Kozeny and Frederic Bourke which may be viewed here.

The firm's settlement with the DOJ resolves criminal charges involving bribery schemes related to obtaining investment opportunities for the firm in the diamond and mining sectors of the Democratic Republic of the Congo (the "DRC") and to securing an investment in firm-managed funds from the Libyan Investment Authority (a sovereign wealth fund), in both cases using illicit payments made through local agents. The criminal charges also included the firm's failure to implement adequate internal accounting controls, resulting in bribe payments in the DRC, Libya, Chad, and Niger in connection with mining-related investments. To settle criminal charges of conspiracy to violate the FCPA's anti-bribery provisions, and of falsifying its books and records and failing to implement adequate internal controls, the firm entered into a deferred prosecution agreement (a "DPA") with the DOJ under which it will pay a criminal penalty of $213,055,689. The firm also agreed to a compliance monitor for three years, improved internal controls, and cooperation with the DOJ's ongoing investigation. A firm affiliate simultaneously pleaded guilty to a charge of conspiracy to violate the FCPA's antibribery provisions and will be sentenced next year.[2]

In a parallel administrative proceeding, the SEC settled charges that the firm violated the antibribery, books and records, and internal controls provisions of the FCPA through a series of payments to obtain investments from the Libyan Investment Authority and to obtain or retain favorable investment opportunities in Libya, Chad, Niger, and the DRC. The SEC Order also found that a firm affiliate violated the antifraud provisions of the Investment Advisers Act. To settle these civil charges, the firm agreed to pay $173,186,178 in disgorgement and $25,858,989 in interest.[3]

The SEC also alleged that the firm's Chief Executive Officer (the "CEO") and its Chief Financial Officer (the "CFO") ignored corruption risks and red flags and permitted illicit actions to proceed. In particular, the SEC Order alleges that despite being aware of the high risk of corruption posed by dealings with the firm's business partner in the DRC because of the partner's reputation and connections to senior DRC officials, the CEO personally approved, and the CFO authorized, transactions in which bribes were paid in the DRC but recorded as investments or loans in the firm's books and records. According to the SEC Order, although neither executive knew that bribes would be paid, their actions caused books and records and internal controls violations. Without admitting or denying the SEC's allegations, these senior executives consented to settle the charges. The CEO agreed to pay $1.9 million in disgorgement and $273,718 in interest, while the CFO consented to a monetary penalty to be assessed later.

In Two Cases, the DOJ Declines to Prosecute for FCPA Violations but Requires Disgorgement of Profits to the U.S. Treasury.

In a separate development, the DOJ issued letters on September 29, 2016 to two unrelated Texas companies, advising each of the DOJ's decision to close its investigation of that company's alleged FCPA violations and to decline to prosecute, and confirming that the company has agreed to disgorge to the U.S. Treasury the profits associated with the

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2 The DOJ Release, the DPA, and the related Plea Agreement may be viewed, respectively, here, here, and here.

3 The SEC Release and Order may be viewed, respectively, here and here.

transactions involved in the allegations. These declinations are the latest in a series concluded under an FCPA Pilot Program (the "Pilot Program") announced earlier this year to encourage voluntary self-disclosure and remediation.[4]

According to the letter released by the DOJ, the first company is an industrial supply and maintenance concern whose Chinese subsidiary illegally provided cash and other items of value totaling $44,545—including meals, gifts, and entertainment—to influence purchasing decisions by employees of state-owned and -controlled customers while recording them as customer-related "maintenance" or "cooperation" fees. The company also paid travel and related expenses for employees of a Chinese governmental entity on a ten-day visit to the United States and Canada that involved only a half-day of business activity. The illicit payments resulted in sales that generated profits to the company of approximately $335,342, which the company agreed to disgorge.[5]

According to the DOJ, the second company is a manufacturer, supplier, and service provider in the energy industry whose employees, agents and/or distributors paid approximately $500,000 in bribes, through several schemes, to government officials in China and Venezuela to influence purchases of company products. Under one scheme, Venezuela's state-owned oil company, PDVSA, was charged inflated prices for the company's products. The company paid the excess amount it received to its Venezuela agent as "commissions" and other "fees." The agent then used a portion of those fees to pay bribes to employees of the state-owned company and other government officials. The illicit payments resulted in sales that generated profits of $2,719,412, which the company agreed to disgorge.[6]

As it has in connection with recent past declinations under the Pilot Program, the DOJ noted that each Texas company had voluntarily self-disclosed these matters to the government; conducted an internal investigation; cooperated with the DOJ's investigation; enhanced its compliance program and internal accounting controls; and taken remedial actions, including terminating employees involved in the matters and severing problematic relationships with agents and distributors. In addition, unlike in prior declinations, each company agreed to disgorge the profits generated by the actions involved in the allegations. Although two previous declinations under the Pilot Program involved disgorgement to the SEC, because the two Texas companies are not "issuers" of securities subject to the reporting requirements of the Securities Exchange Act of 1934, disgorgement pursuant to an SEC action was not possible. These cases represent the first instance in which the DOJ has required disgorgement in conjunction with a declination.

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[4] For further information on the Pilot Program, please see Willkie Farr & Gallagher LLP, "DOJ's Fraud Section Issues Guidance on Pilot Program for Self-Reporting, Cooperation, Remediation and Fine Reduction" (Apr. 5, 2016), available here. See also, Press Release, Leslie R. Caldwell, Assistant Att'y Gen., Crim. Div., U.S. Dep't of Justice, Criminal Division Launches New FCPA Pilot Program (Apr. 5, 2016), available here.

[5] The DOJ letter pertaining to this company is available here.

[6] The DOJ letter pertaining to this company is available here.

Conclusions

Historically, FCPA enforcement actions have concentrated on the energy, pharmaceutical, and other manufacturing industries. The recent hedge fund settlement, as well as other investigations that are reportedly pending, suggest an emerging interest by the U.S. government in FCPA enforcement in the financial services industry. Financial services firms—especially those managing or seeking investments from sovereign wealth funds or having other dealings with foreign government entities—should carefully review their compliance programs to make sure such programs include robust procedures for FCPA compliance. Senior financial services executives should understand they may be held liable for foreign bribery committed by others in the firm and, accordingly, show their employees and agents that they take compliance seriously. For firms registered with the SEC, such settlements can lead to serious consequences under the federal securities laws as well.

The two new declinations show that the DOJ remains committed to its Pilot Program and to attempting to operate its FCPA enforcement program with greater transparency. Unlike certain past declinations publicized by the DOJ, in which it was unclear from the public record whether the DOJ had a sufficient evidentiary and jurisdictional basis to bring criminal FCPA charges, the more detailed factual recitation in the letters issued to the two Texas companies strongly suggests that the DOJ had an adequate basis to bring charges but chose not to as a matter of discretion. In doing so, the DOJ is signaling its willingness to reward companies that voluntarily disclose potential FCPA violations and cooperate, take meaningful steps to remedy the conditions that led to them, and disgorge the benefits of illicit conduct.

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