Forecasting the Future of FCPA Enforcement

By Alberto Gonzales, Richard Westling, and William Athanas

Prosecutions under the Foreign Corrupt Practices Act have skyrocketed in the last several years as the U.S. Department of Justice has trained its sights on incarcerating individuals who make corrupt payments to foreign officials in exchange for securing a competitive business advantage. The government initially focused on corporations, obtaining huge fines via negotiated resolution against those entities that paid bribes overseas. Seeking to maximize the deterrent effect of the FCPA, the government increased prosecutions of the individuals who actually authorized and paid the bribes. This, however, generated an unintended consequence: more FCPA trials.

The past several months have produced a number of setbacks. Convictions have been vacated, indictments have been dismissed with prejudice, and orders belittling the government’s case and finding that prosecutors engaged in misconduct have been entered. A massive sting operation that produced charges against 22 individuals in early 2010 resulted in lengthy trials of two different groups of defendants, and produced not a single conviction.

Very recently, it was reported that Wal-Mart may have violated the FCPA during the mid-2000s. Given the recent losses the government has suffered in other cases, its decision on how to proceed in the Wal-Mart case will be closely scrutinized.

In any event, for those engaged in international commerce, these outcomes give rise to an important question: what do these setbacks mean for the future of FCPA enforcement?

Evolution of FCPA Enforcement

From its passage in 1977 until roughly 2000, the FCPA lived a quiet existence. The Department of Justice and the Securities & Exchange Commission together initiated, on average, three prosecutions per year. During this period, the government secured convictions in virtually every FCPA case.

In 2005, buoyed by an increased allocation of resources, the government embarked on an aggressive initiative resulting in a ten-fold increase in the number of FCPA prosecutions. The Justice Department dramatically increased the number of prosecutors assigned to handle such cases. Investigative resources also increased, evidenced most notably by the Federal Bureau of Investigation’s decision to dedicate an entire squad of agents based in its Washington, D.C. field office to the investigation of FCPA matters.
In 2008, the Justice Department began to string together a series of FCPA triumphs in cases against companies. Among those ensnared were Siemens ($450 million), KBR / Halliburton ($579 million), and BAE Systems ($400 million).

In the government’s view, these successes represented only half the battle. At an American Bar Association event in September 2008, Mark Mendelsohn, then the Justice Department’s chief FCPA prosecutor, stated, "The number of individual prosecutions has risen--and that’s not an accident. . . . It is our view that to have a credible deterrent effect, people have to go to jail." (Mendelsohn Says Criminal Bribery Prosecutions Doubled in 2007, 22 Corporate Crime Reporter 36 [September 16, 2008]).

The government backed up Mendelsohn's tough talk. Individual indictments climbed from six in 2006 to 48 in 2010. Twenty-two of those charged in 2010 were ensnared in a government sting operation known as the "Shot Show" case, because all but one of the defendants were arrested at the Shooting, Hunting, Outdoor Trade Show in Las Vegas.

In the Shot Show case, two FBI agents posed as foreign officials from the African country of Gabon, seeking bribes in exchange for contracts to provide tactical military products. A cooperator facing a prison term for FCPA violations recruited others from the tactical weapons industry to participate in the bribery scheme. The resulting indictments represented the largest number of individual defendants ever indicted in a single FCPA case.

Negative FCPA Enforcement Outcomes

The government’s FCPA winning streak came to an abrupt end in July 2011. The Shot Show trials were a disaster for the Justice Department: the first resulted in a hung jury; the second resulted in the dismissal of a conspiracy charge and outright acquittal of one defendant; and the third led to two acquittals by jury and another hung jury for the remaining defendants.

In February 2012, the government moved to dismiss its Shot Show case as to all defendants, including those awaiting trial. The court granted the motion and suggested that the Justice Department’s failure served as "a true learning experience for both the Department and the FBI as they regroup to investigate and prosecute FCPA cases."

During that time, the Justice Department experienced another major blow. A case in Los Angeles charged Lindsey Manufacturing and two of its senior officers with violating the FCPA in connection with efforts to secure contracts from the Mexican state-owned utility, Comision Federal de Electricidad (CFE). The government obtained convictions for all three defendants in May 2011. However, the defendants filed post-trial motions seeking to vacate their convictions, claiming that the government had engaged in a pattern of misconduct, both prior to and after indictment.

After characterizing the government’s investigation as "sloppy, incomplete, and notably overzealous," the court vacated the convictions and dismissed the indictment with prejudice. The court observed that "there were no oral admissions (secretly recorded or otherwise); no writings acknowledging the payments were corrupt, no evidence of furtive conduct" and concluded that "the evidence was, at best, murky."

In January 2012, the government embarked on the trial of John O'Shea in Houston. The alleged bribes were paid via the same intermediary used by the Lindsey defendants to secure contracts from CFE. When the government rested its case, the defendant filed a motion for judgment of acquittal. In granting the motion, the judge disparaged the government’s case by remarking that the primary witness knew "almost nothing," his testimony was more "gossip" than fact, and his "answers were abstract and vague." He characterized the documents offered by the government as "modest in their extent and inconclusive in their reach" and found the government failed to shoulder its burden of proof.

Likely Impact on Future of FCPA Enforcement

Assessing the likely future of FCPA enforcement first requires a brief discussion of how the Justice Department sets its goals and priorities. In deciding which crimes require the most attention, the government focuses on two key factors: the nature and scope of the threatened harm and the extent to which an allocation of resources will serve to reduce that threat.
Law enforcement priorities for the Justice Department begin with those of the President. If the President campaigns on a platform of attacking corporate fraud and white-collar crimes, then these become priorities of the Justice Department, and the President's budget will reflect these priorities.

From there, the Attorney General develops priorities through a formal internal budget process. Input is solicited from senior-level Justice Department officers, U.S. Attorneys, the department's investigative agencies, other outside law enforcement agencies, and other outside parties. Priorities will also be influenced by unexpected crises or challenges, such as the September 11 terrorist attacks. A public scandal involving a major U.S. corporation and a foreign official would be an event that could push FCPA prosecutions higher on the Justice Department's priority list.

Individual U.S. Attorneys have their own priorities for their districts and have considerable discretion on how their offices allocate resources, but it is expected that they will first meet the priorities established by the Attorney General in Washington, D.C.

Next, it is necessary to define "setback" in the context of enforcement prioritization. Because white-collar prosecutions usually turn on questions of intent, the government must prove its case circumstantially. Given the vagaries that can accompany such evidence, it is not uncommon for juries or judges to disagree with the inferences the government draws, nor is it unusual for judges to express displeasure regarding the manner in which the government has set about to prove its case.

Such differences of opinion do not constitute "setbacks" for the purposes of this analysis. Rather, the focus here is on outcomes that qualify as negative under any objective standard: jury acquittals on all counts; judicial acquittals at the close of the government's case; and post-trial dismissals with prejudice based on findings of prosecutorial misconduct.

The question is whether these outcomes indicate a systemic failure in prosecution theory, evidence gathering, or trial presentation. In addition, one must factor in the ratio of negative outcomes to positive, and whether a negative result stems from an isolated element (e.g., cooperating witness) that skews the analysis and falsely suggests that a prosecutorial approach is fundamentally flawed.

Viewed under this framework, the Justice Department's recent results do not necessarily reflect structural flaws in its FCPA enforcement efforts. While the sample size of FCPA prosecutions is relatively small, even when factoring in these recent negative outcomes, the government still enjoys a remarkable record of success. Moreover, the losses appear to involve identifiable deficiencies that can be easily rectified.

FCPA enforcement efforts will not be abandoned altogether or even to a significant degree. In the relatively short history of FCPA enforcement, the Justice Department has achieved staggering successes. The government has built a framework—training prosecutors and agents, cultivating relationships with foreign law enforcement agencies, and sensitizing companies to the benefits of uncovering and self-disclosing violations—designed to prosecute FCPA cases in an efficient and effective manner.

Adverse results in three cases are unlikely to cause the government to scrap that framework or abandon its enforcement priorities. Moreover, given the current administration's policies relating to corporations in areas such as tax and antitrust policy, we believe this administration will continue to pursue FCPA violators, particularly at the corporate level, irrespective of these recent setbacks.

However, some adjustment in the government's focus is likely, at least in the short term. The Shot Show case rested too much on a cooperating witness who had little credibility. Going forward, FCPA prosecutions that rely on cooperator testimony are likely to receive a thorough vetting to ensure that a sufficient quantum of independent evidence exists to support a conviction in the event the jury finds the cooperator wholly untrustworthy.

Discarding sting operations as an investigative methodology in FCPA cases is another possible move. Reports from the second Shot Show trial revealed that the jurors were skeptical of this law enforcement tactic. Whether or not the
circumstances constituted entrapment as a legal matter, jurors were troubled by the prospect of convicting defendants ensnared in a concocted scenario.

In an effort to move past these high-profile defeats, the Justice Department can be expected to return to its time-tested formula for success: targeting corporations whose employees violate the FCPA, and reaching negotiated settlements to answer for such conduct. Those companies doing business overseas should recognize that the resources that had been designated for investigating and prosecuting individual defendants will be focused in their direction.

The Wal-Mart scandal may provide the first high-profile test of the post-defeat strategy the government will employ. In late April 2012, The New York Times published an article detailing Wal-Mart’s apparent systematic plan to aid its expansion efforts in Mexico in the mid-2000s by making approximately $24 million in payments to local officials in order to obtain necessary construction licenses and permits. Because the FCPA contains an exception for payments that merely speed government action, as opposed to influencing the exercise of discretionary authority, there remains some question about whether the payments themselves actually violated the statute. Nevertheless, the surrounding circumstances—including alleged efforts to conceal the payments and to stymie a subsequent internal investigation—suggest that knowing violations occurred and are expected to result in massive government-imposed sanctions.

At this point, Wal-Mart has a significant credibility problem in the eyes of government FCPA enforcers. The government’s perception right now is that the company not only failed to take adequate measures to prevent violations of the FCPA by its employees, but also allowed for an investigative whitewash once those apparent violations came to the attention of senior management. Together, those factors suggest a deliberate and concerted effort to violate the law.

While it is likely too late for Wal-Mart to avoid government sanctions, the company maintains the ability to limit those penalties to a substantial degree by demonstrating just the opposite: a genuine commitment to FCPA compliance. This means determining what happened in Mexico, finding out who authorized the conduct in question, taking appropriate disciplinary actions against those individuals, and installing measures to minimize the risk of future violations. This process starts with conducting an independent and thorough investigation into the activity and includes disclosure of its unvarnished results to the government, as well as developing a comprehensive plan for future compliance.

Ultimately, with regard to its handling of FCPA matters, the government can be expected to chart a course between two extremes. The circumstances suggest that, at least in the near term, the focus will shift from seeking to convict individuals to resolving matters by way of negotiated resolutions with corporations. Individuals will still be charged, but cases on the margin are likely to be passed over, at least until the Justice Department regains its prosecutorial bearings. Corporations engaged in international commerce would be wise to take heed of these developments, and understand that they will be the ones in the line of fire when the government refocuses its sights.

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