District Court Opens the Door to Potential Restitution Claims in FCPA Cases

September 10, 2019

On September 3, the United States District Court for the Eastern District of New York unsealed an order (the "Court's Order") in *United States v. OZ Africa Management GP, LLC* ruling that, under certain circumstances, the Mandatory Victims Restitution Act (18 U.S.C. § 3663A) ("MVRA")—which affords restitution to victims in a variety of cases—applies to conspiracies to violate the Foreign Corrupt Practices Act ("FCPA").[1] The Court's Order relates to the 2016 FCPA resolution with New York-based Och-Ziff Capital Management Group LLC ("Och-Ziff"), where Och-Ziff agreed to pay over $400 million to settle FCPA charges with the U.S. Department of Justice ("DOJ") and U.S. Securities and Exchange Commission ("SEC").[2] In connection with these resolutions, Och-Ziff's wholly owned subsidiary, OZ Africa Management GP, LLC ("OZ Africa"), also pleaded guilty to one count of conspiracy to violate the FCPA for bribes paid in Africa.[3]

Prior to OZ Africa's sentencing, investors in the Canadian mining company Africo Resources Ltd. ("Africo") sought restitution under the MVRA, arguing that they are entitled to up to $1.8 billion because of OZ Africa's bribery scheme.[4] The Court's Order found that the scheme at issue involved the use of state instrumentalities to "expropriate Africo's mining rights without Africo's knowledge," which was an "offense against property" that was "committed by fraud or deceit, within the scope of the MVRA."[5] The Court also ruled that the Africo investors qualify as victims under the MVRA, and requested supplemental briefing to determine the appropriate amount of restitution, if any, owed in this case.

FCPA cases rarely, if ever, involve claims for restitution under the MVRA—and, in fact, the DOJ objected to the restitution claim here. While it remains to be seen how this ruling might be applied in future FCPA cases, the Court's Order raises an issue that companies and their counsel should consider when evaluating the risks and costs associated with an FCPA resolution.

---

[1] Mem. & Order, *United States v. OZ Afr. Mgmt. GP, LLC*, 16-515 (E.D.N.Y. Aug. 29, 2019), ECF No. 51.

[2] Press Release, DOJ, Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay $213 Million Criminal Fine (Sept. 29, 2016); Press Release, SEC, Och-Ziff Hedge Fund Settles FCPA Charges (Sept. 29, 2016).

[3] Mem. & Order, *OZ Afr. Mgmt.,* 16-515, at 5.

[4] *Id.*

[5] *Id.* at 8 n.6.

Case Background

According to its Deferred Prosecution Agreement with DOJ, starting in late 2007, Och-Ziff employees began discussions with a businessperson based in the Democratic Republic of the Congo ("DRC") about creating a joint venture to acquire mining assets and pursuing opportunities in the diamond sector.[6] The businessperson said he expected Och-Ziff to help fund corrupt payments to government officials and local partners to gain assets and rights in these sectors.[7] Between 2007 and 2013, Och-Ziff entered into multiple DRC-related transactions with the businessperson,[8] profiting over $90 million.[9] Och-Ziff also engaged a third party to assist in securing investments from the Libyan Investment Authority ("LIA") in its hedge funds, aware that the party they engaged would pay bribes to government officials in order to secure those investments.[10] LIA eventually invested $300 million in the fund.[11] Och-Ziff accrued approximately $100 million from the fees and incentive income associated with LIA's investment.[12]

As relevant to the Court's Order, a wholly owned subsidiary of Och-Ziff, OZ Africa, also engaged in a bribery scheme to secure mining rights in the DRC. As part of this scheme, OZ Africa and an Israeli businessperson, Dan Gertler, attempted to gain ownership of rights to a copper mine in the DRC. Africo, a Canadian company, held a 75% interest in those mining rights.[13] In 2007, Africo learned that its interest had been sold to Akam, a DRC-based company, as a result of an *ex parte* default judgment that had been entered against Africo in a wrongful termination suit. Africo sued Akam over this ownership interest.[14] While the litigation was pending, Gertler and OZ Africa offered to invest in Africo in exchange for a 60% share of the company.[15] To ensure shareholder approval, Gertler and OZ Africa paid bribes to DRC government officials, including judges, "to ensure that Africo did not obtain a favorable court ruling in its case against Akam that could have affected the outcome of the Africo shareholder vote."[16] Unaware of the bribery,

---

[6] Deferred Prosecution Agreement, *United States v. Och-Ziff Capital Mgmt. Grp. LLC*, 16-516, A-8 (E.D.N.Y. Sept. 29, 2016).

[7] *Id.* at A-8-9.; *see also* Press Release, DOJ, Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay $213 Million Criminal Fine (Sept. 29, 2016)

[8] Deferred Prosecution Agreement, *Och-Ziff*, 16-516 at A-10.

[9] *Id.* at A-20.

[10] *Id.*

[11] *Id.* at A-24.

[12] *Id.* at A-28.

[13] Plea Agreement, *United States v. OZ Afr. Mgmt. GP LLC*, No. 16-515, Ex. 3 at 6 (E.D.N.Y. Sept. 29, 2016), ECF No. 11; Mem. & Order, *OZ Afr. Mgmt.*, 16-515 at 3.

[14] Mem. & Order, *OZ Afr. Mgmt.*, 16-515 at 2-3.

[15] *Id.* at 3.

[16] *Id.*

Africo's shareholders approved the takeover.[17] The copper mine was never developed; Africo has since maintained that it would have developed the mine had it retained control.[18]

In its September 2016 deferred prosecution agreement with Och-Ziff, DOJ charged the company with two counts of conspiracy to violate the FCPA's anti-bribery provisions, one count of falsifying books and records, and one count of failing to implement adequate controls for its conduct in DRC and Libya.[19] As part of the DOJ resolution, Och-Ziff agreed to implement internal controls, retain a compliance monitor for three years, cooperate with the ongoing investigation, and pay a fine of $213 million.[20] OZ Africa pleaded guilty to conspiracy to violate the anti-bribery provisions of the FCPA for its conduct related to the bribery scheme.[21]

The SEC also entered a cease-and-desist order against Och-Ziff, finding that it violated the books and records and internal controls provisions of the FCPA.[22] Och-Ziff was required to pay $199 million in disgorgement, including prejudgment interest, and retain a monitor.[23]

The Court's Order

In the aftermath of these resolutions, former shareholders of Africo filed a motion against OZ Africa seeking restitution under the MVRA.[24] The former shareholders alleged that they suffered an estimated $1.8 billion in losses based on the estimated projected value of their share in the mining project as a result of OZ Africa's bribery.[25] In opposing the motion, OZ Africa assumed "for argument's sake that the MVRA applies to the FCPA or bribery in general."[26] OZ Africa argued that the former shareholders were not "victims" under the MVRA because (i) their interest in mining rights did not constitute "property" under the MVRA and (ii) the alleged theft of those mining rights was not a direct and proximate cause of the takeover.[27] DOJ also submitted letters to the Court, arguing that while the shareholders may be potential victims of OZ Africa's crimes, they are not entitled to restitution under the MVRA because they had not demonstrated "direct or proximate causation for quantifiable harm from

---

[17] *Id.* at 4.

[18] *Id.*

[19] Press Release, DOJ, Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay $213 Million Criminal Fine (Sept. 29, 2016).

[20] Deferred Prosecution Agreement, *United States v. Och-Ziff Capital Mgmt. Grp. LLC*, No. 16-516, at 8-12.

[21] Press Release, DOJ, Och-Ziff Capital Management Admits to Role in Africa Bribery Conspiracies and Agrees to Pay $213 Million Criminal Fine (Sept. 29, 2016).

[22] *In the Matter of Och-Ziff*, No. 3-17595, 29 (Sept. 29, 2016).

[23] *Id.* at 35-37.

[24] Mem. & Order, *OZ Afr. Mgmt.*, 16-515, at 5.

[25] *Id.*

[26] Def's Mem., *United States v. OZ Afr. Mgmt. GP, LLC*, 16-515, at 18 (E.D.N.Y.) ECF No. 37.

[27] *Id.*

the defendant's conduct."[28] Moreover, DOJ argued that any damages "are too speculative to merit a restitution award."[29]

In addressing the motion, the Court considered several issues bearing on the applicability of the MVRA to the former shareholders and the underlying offense. Without ruling on the amount of restitution owed, the Court determined that a conspiracy to violate the FCPA can constitute an offense triggering restitution under the MVRA and that the investors were considered "victims" within the scope of the statute.[30]

The Court began by briefly addressing whether the offense to which the defendant pleaded guilty—a conspiracy to violate the FCPA—constituted an offense under the MVRA. The MVRA provides that an "offense against property," which includes "offense[s] committed by fraud or deceit," requires the court to grant restitution to the victims of that offense.[31] Here, the Court noted that the parties did not "meaningfully dispute" that a conspiracy to violate the FCPA "is an offense against property that can trigger restitution under the MVRA."[32] In a footnote, the Court reasoned that the language "committed by fraud or deceit" referred to the *manner* in which the defendant commits the crime and, as such, the MVRA can apply to conspiracies to violate the FCPA depending on the nature of the conduct.[33] The Court determined that the conspirators' actions in concealing stolen assets and bribes and using them as leverage constituted an offense against property.[34]

The Court also addressed whether the Africo investors were considered "victims" within the meaning of the MVRA. Most notably, the defendant challenged the Africo shareholders' "attenuated" mining rights, arguing they did not lose any "property" as required under the statute.[35] In rejecting the defendant's argument, the Court relied on a broad interpretation of the MVRA—indicating the statute did not contain a carve-out for "holders of intangible property rights." The Court noted that while the attenuated connection might make the restitution calculation more difficult, it did not foreclose the investors from being considered victims.[36] In further support of this point, the Court emphasized that individuals can be victims under the MVRA even where they do not have a private right of action.[37]

---

[28] Letter from Richard P. Donogue et al. to Hon. Nicholas G. Garaufis, *United States v. OZ Afr. Mgmt. GP, LLC*, 16-515 (March 2, 2018), ECF No. 39, at 11, 13.

[29] *Id*. at 15.

[30] Mem. & Order, *OZ Afr. Mgmt.*, 16-515 at 8 n.6, 20.

[31] *Id*. at 7 (quoting 18 U.S.C. § 3663A(c)(1)).

[32] *Id*. at 8.

[33] *Id.* at 8 n.6.

[34] *Id*.

[35] *Id.* at 11-12.

[36] Mem. & Order, *OZ Afr. Mgmt.*, 16-515 at 11-12.

[37] *Id.* at 12-13.

Ultimately, the Court determined there was sufficient support for a claim of restitution under the MVRA.[38] However, the Court indicated it was "unprepared" to determine how much restitution is owed and ordered the parties to submit supplemental briefing on several specific issues related to the restitution calculations.[39]

Considerations in Future FCPA Cases

The Court's Order raises key issues that companies and their counsel should consider when evaluating the risks and costs associated with FCPA resolutions going forward.

- **Restitution as an Additional Avenue of Recovery.** First, the Court's Order opens the door to a potential avenue of recovery that has rarely been seen in FCPA cases—restitution for victims under the MVRA. The MVRA, which makes it mandatory for courts to order restitution, has not traditionally been invoked in FCPA cases in part because it addresses restitution in sentencing proceedings under Title 18 of the U.S. Code, and the FCPA is codified under Title 15 of the U.S. Code. However, restitution remains a viable option in FCPA cases where the FCPA charges are accompanied by charges under Title 18, such as conspiracy, money laundering, or wire fraud. The Court's order makes clear that, depending on the circumstances, a conspiracy to violate the FCPA resulting in the deprivation of property—including intangible property rights—falls within the ambit of the MVRA.
- **Potential for Additional Claimants.** Second, given the MVRA's broad definition of who may qualify as a victim, the Court's Order may embolden parties affected by FCPA cases—such as competitors and other third parties—to attempt to seek restitution. Indeed, the Second Circuit has held that even a foreign government can qualify as a victim under the MVRA.[40] In light of the Court's Order, it is thus possible that parties that have not typically been granted monetary awards in FCPA matters may now seek to bring claims for restitution on the heels of such resolutions.
- **Amount of Restitution.** The Court's Order also left open the question of how much, if any, restitution should be afforded to FCPA victims. The MVRA requires restitution if an offense specified under Title 18 has been committed, <u>except</u> if the court finds that "(a) a number of identifiable victims is so large as to make restitution impracticable; or (b) determining complex issues of fact related to the cause or amount of the victim's losses would complicate or prolong the sentencing process to a degree that the need to provide restitution to any victim is outweighed by the burden on the sentencing process." Given the potential complexities involved in calculating the amount of an FCPA victim's losses, particularly with respect to intangible property rights, it remains to be seen how the Court's Order (and any subsequent ruling from the Court on the proper amount of restitution) might impact future FCPA cases.

---

[38] *Id.* at 18.

[39] *Id.* at 20.

[40] *See United States v. Bengis*, 631 F.3d 33, 40-41 (2d Cir. 2011) (holding that the South African government was a "victim" under the MVRA).

- **Types of Charges in FCPA Resolutions**. Finally, the Court's Order could have an impact on the considerations that defendants give to resolving FCPA matters with conspiracy charges under Title 18 of the United States Code, or substantive FCPA offenses under Title 15 instead. As discussed above, because the MVRA applies to Title 18 offenses—and not, at least by its plain language, to Title 15 offenses—the Court's Order could cause defendants to consider limiting their exposure to restitution under the MVRA by resolving matters based purely on substantive FCPA offenses under Title 15.

On September 6, OZ Africa filed a motion for reconsideration of the Court's Order, arguing that it was "premised on a mistake of fact" in that Africo is not a defunct company and thus "could not itself be a victim under the MVRA."[41] The Court also set deadlines for the parties to submit supplemental briefing on the amount of restitution owed.

The outcome of this dispute may weigh on the issues set forth above and in future FCPA cases.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

Greg D. Andres	+1 212 450 4724	greg.andres@davispolk.com
Martine M. Beamon	+1 212 450 4262	martine.beamon@davispolk.com
Angela T. Burgess	+1 212 450 4885	angela.burgess@davispolk.com
Neil H. MacBride	+1 202 962 7030	neil.macbride@davispolk.com
Tatiana R. Martins	+1 212 450 4085	tatiana.martins@davispolk.com
Fiona R. Moran	+1 202 962 7137	fiona.moran@davispolk.com
Paul J. Nathanson	+1 202 962 7055	paul.nathanson@davispolk.com
Neal A. Potischman	+1 650 752 2021	neal.potischman@davispolk.com
Patrick S. Sinclair	+852 2533 3305	patrick.sinclair@davispolk.com
Kenneth L. Wainstein	+1 202 962 7141	ken.wainstein@davispolk.com

[41] Mem. in Support of Def.'s Mot. for Reconsideration, *United States v. OZ Afr. Mgmt. GP, LLC*, 16-515, at 3 (E.D.N.Y.), ECF No. 55.

DOJ Clarifies Position on Agency Liability under the FCPA post-*Hoskins*; New FCPA Chief Named

December 9, 2019

On December 4, 2019, Assistant Attorney General Brian Benczkowski, the head of DOJ's Criminal Division, provided remarks at the ACI Foreign Corrupt Practices Act ("FCPA") Conference near Washington, DC. In particular, Mr. Benczkowski clarified that DOJ will not automatically seek to impose agency liability on parent companies for FCPA violations by subsidiaries, joint ventures, and affiliates. Mr. Benczkowski also announced a new permanent chief of the Fraud Section's FCPA Unit, and in response to questions from the audience, he stressed the Criminal Division's desire to reduce protracted negotiations over corporate resolutions.

2019 Enforcement Trends & Leadership Changes

Mr. Benczkowski began by noting the record number of FCPA cases against individual defendants in 2019: 34 publicly announced charges and 31 publicly announced guilty pleas, both the highest figures ever. He further announced that prosecutor Christopher Cestaro, the current Acting Chief of the Fraud Section's FCPA Unit, has been promoted to become the Unit's permanent Chief. Mr. Cestaro replaces Daniel Kahn, who has become Senior Deputy Chief of the Fraud Section.

Developments in FCPA Agency Liability

Mr. Benczkowski then turned to the impact of the Second Circuit's decision and the subsequent guilty verdicts in *United States v. Hoskins*.[1] In *Hoskins*, a British national was charged under the FCPA for facilitating a bribery scheme for the American subsidiary of a French company. Specifically, the government alleged that Hoskins retained consultants who bribed Indonesian officials to secure a $118 million contract for the American subsidiary. Hoskins moved to dismiss the indictment, arguing that as a former employee who had never worked for an American company and had never been to the United States, he could not be prosecuted under the FCPA, even as a co-conspirator. The district court agreed, dismissing the FCPA conspiracy charges. On the government's interlocutory appeal, the Second Circuit affirmed in part and reversed in part. As we noted in a **prior client alert**, the Second Circuit agreed with the district court that DOJ could not expand the FCPA's jurisdictional reach by alleging that Hoskins was a co-conspirator, but disagreed that Hoskins could not be prosecuted for FCPA charges at all, and held that the government *could* prosecute Hoskins if it could show that he was acting as an agent of a U.S. domestic concern. On remand, the government sustained that burden, and the jury found Hoskins guilty on each of the FCPA charges.

In his remarks, Mr. Benczkowski clarified that despite the result in *Hoskins*, DOJ would not "suddenly be taking the position that every subsidiary, joint venture, or affiliate is an 'agent' of the parent company simply by virtue of ownership status," nor would DOJ argue "that every parent company should automatically be held liable for the acts of its subsidiaries, joint ventures, or affiliates based on an agency theory." Mr. Benczkowski instead pointed to the District Court's jury instructions, which required the jury

[1] 902 F.3d 69, 72 (2d Cir. 2018); Jury Verdict, *United States v. Hoskins*, No. 3:12-cr-00238 (D. Conn. Nov. 8, 2019), ECF No. 583.

"to evaluate Hoskins' conduct to look for proof of an agency relationship and control by the principal," and made clear that "a person or entity may be an agent for some business purposes and not for others." Accordingly, "[b]efore pursuing an FCPA case based on an agency theory . . . the Department will need to measure the facts against the legal standard articulated by the court." Finally, Mr. Benczkowski noted that DOJ would likely favor prosecution in cases where agency structures were used to try to shield a parent or individual from liability, and added that decisions to bring an FCPA case under an agency theory would—like all prosecutions—be guided by the exercise of prosecutorial discretion and the factors embodied in DOJ's Corporate Enforcement Policy and principles for prosecuting business organizations.

Increased Transparency

Mr. Benczkowski then turned to the importance of corporate compliance programs and cast **DOJ's recent compliance guidance** as part of an ongoing effort by the Department to increase the transparency of and build trust in its enforcement decisions, alongside other efforts such as the DOJ's revised voluntary self-disclosure guidance, policy against piling-on, and FCPA Corporate Enforcement Policy. Mr. Benczkowski concluded his prepared remarks by noting that the Criminal Division would continue "to demonstrate [its] adherence to and application of [its] policies by [its] actions, including in press statements, public resolution documents, and program-related declinations."

In response to a question from the audience, Mr. Benczkowski was also critical of past practice for the resolution of corporate criminal matters, where, at times, parties might start from unreasonable positions and lengthy negotiations would result. He stressed a desire to end such long, protracted negotiations over the form and amount of a resolution and to have negotiations start at a place tethered objectively to the law and the facts—an obligation he stressed was shared by both prosecutors and defense counsel.

Potential Impact

Mr. Benczkowski's statements highlight a continuation of the Criminal Division's policy of adopting more transparent measures and a more nuanced approach to corporate resolutions. The speech comes after a string of developments—including the implementation of the **Corporate Enforcement Policy**, **clarifications** to that Policy, updated **guidance on corporate compliance programs**, among **others**—that collectively may help corporations better address concerns raised by DOJ in corporate investigations and facilitate their resolution.

In this vein, Mr. Benczkowski's remarks on agency-based culpability make clear that each case will require a fact-intensive analysis of a putative agent's role relative to its principal, rather than a formalistic assessment of corporate structure. A determination will need to be made not only as to whether an agency relationship exists, but also whether that relationship extends to the particular conduct at issue.

In total, recent developments signal that a diverse set of factors may be relevant to assessing corporate culpability, and that DOJ may take a more contextual approach to corporate criminal resolutions.

Mr. Benczkowski's remarks are available **here**.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

New York

Greg D. Andres	+1 212 450 4724	**greg.andres@davispolk.com**
Martine M. Beamon	+1 212 450 4262	**martine.beamon@davispolk.com**
Angela T. Burgess	+1 212 450 4885	**angela.burgess@davispolk.com**
Tatiana R. Martins	+1 212 450 4085	**tatiana.martins@davispolk.com**

Washington, DC

Robert A. Cohen*	+1 202 962 7047	**robert.cohen@davispolk.com**
Neil H. MacBride	+1 202 962 7030	**neil.macbride@davispolk.com**
Paul J. Nathanson	+1 202 962 7055	**paul.nathanson@davispolk.com**
Linda Chatman Thomsen	+1 202 962 7125	**linda.thomsen@davispolk.com**
Kenneth L. Wainstein	+1 202 962 7141	**ken.wainstein@davispolk.com**

Hong Kong

Patrick S. Sinclair	+852 2533 3305	**patrick.sinclair@davispolk.com**

*Mr. Cohen is admitted to practice in New York and Maryland, and is practicing in DC under the supervision of partners of the firm.

DOJ Clarifies Corporate Enforcement Policy

December 3, 2019

On November 20, 2019, the Department of Justice ("DOJ") modified its Corporate Enforcement Policy to clarify what level of disclosure is expected from companies in the early stages of an investigation. In short, the Policy reaffirms that companies should disclose known information—and the individuals involved—at the outset of investigations, while recognizing companies may not yet know all the relevant facts or individuals at that time.

The Corporate Enforcement Policy, first introduced as a pilot program concerning FCPA-related investigations in April 2016 and formalized in November 2017 by then–Deputy Attorney General Rod Rosenstein, offers incentives to companies that voluntarily disclose misconduct, timely remediate, and cooperate fully with the DOJ. Absent certain aggravating circumstances, a company following these steps can receive a declination assuming it fully disgorges any associated profits.[1] In March 2018, DOJ extended the Corporate Enforcement Policy beyond FCPA violations as nonbinding guidance concerning any corporate investigation. Since the Policy was introduced, DOJ has issued thirteen public FCPA declinations under its terms.[2]

The new language clarifies the extent of information expected in self-disclosures and acknowledges that companies often have limited knowledge at the preliminary stages of investigations.

- A new footnote to the self-disclosure provision states that "the Department recognizes that a company may not be in a position to know all relevant facts at the time of a voluntary self-disclosure, especially where only preliminary investigative efforts have been possible."[3] A company in this position should "make clear that it is making its disclosure based upon a preliminary investigation or assessment of information," but still fully disclose "the relevant facts known to it at that time."[4] The same applies to the disclosure of individuals involved, with companies likewise directed to provide relevant facts about any individuals known "at the time of the disclosure."[5] The language thus distinguishes between information provided during the disclosure phase versus what might be required as part of "cooperation" as dictated by the Yates Memo.
- The definition of "full cooperation" now advises cooperating companies to notify DOJ of evidence not in its possession of which the company "is aware," no longer extending this to evidence of which the company "should be" aware.[6]

These changes come on the heels of other recent developments in DOJ's approach to corporate enforcement, including a decision in March not to prohibit companies from using "disappearing" messaging services like WhatsApp in order to receive full credit for remediation.[7]

---

[1] *See* U.S. Dep't of Justice, Justice Manual § 9-47.120 (Nov. 2019).

[2] *See* U.S. Dep't of Justice, Corporate Enforcement Policy Declinations (Sept. 26, 2019), **https://www.justice.gov/criminal-fraud/corporate-enforcement-policy/declinations**.

[3] Justice Manual § 9-47.120 at n. 1.

[4] *Id.*

[5] Justice Manual § 9-47.120 at 3(a).

[6] Justice Manual § 9-47.120 at 3(b).

[7] *See* Justice Manual § 9-47.120 at 3(c) (modified this year to discourage, rather than prohibit, "ephemeral messaging platforms").

The revised policy is available **here**.

A redline comparison between the old and new policies can be found **here**.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

New York

Greg D. Andres	+1 212 450 4724	**greg.andres@davispolk.com**
Martine M. Beamon	+1 212 450 4262	**martine.beamon@davispolk.com**
Angela T. Burgess	+1 212 450 4885	**angela.burgess@davispolk.com**
Tatiana R. Martins	+1 212 450 4085	**tatiana.martins@davispolk.com**

Washington, DC

Robert A. Cohen	+1 202 962 7047	**robert.cohen@davispolk.com**
Neil H. MacBride	+1 202 962 7030	**neil.macbride@davispolk.com**
Paul J. Nathanson	+1 202 962 7055	**paul.nathanson@davispolk.com**
Linda Chatman Thomsen	+1 202 962 7125	**linda.thomsen@davispolk.com**
Kenneth L. Wainstein	+1 202 962 7141	**ken.wainstein@davispolk.com**

Hong Kong

Patrick S. Sinclair	+852 2533 3305	**patrick.sinclair@davispolk.com**

*Mr. Cohen is admitted to practice in New York and Maryland, and is practicing in DC under the supervision of partners of the firm.

Supreme Court to Review SEC's Authority to Seek Disgorgement

November 4, 2019

On Friday, November 1, 2019, the Supreme Court granted certiorari in *Liu v. Securities and Exchange Commission*,[1] a case that challenges the SEC's long-held position that it has authority to seek disgorgement for securities laws violations as a form of equitable relief. This view has come under fire since *Kokesh v. Securities and Exchange Commission*, in which the Supreme Court held that disgorgement constituted a "forfeiture" or "penalty," rather than a remedial tool, and was therefore subject to a five-year statute of limitations. As we noted previously, several justices observed during oral argument in *Kokesh* that the SEC did not have express statutory authority to seek disgorgement in district court actions, and the *Kokesh* opinion affirmatively stated that the Court was reserving judgment on the question of whether the SEC had the authority to seek disgorgement at all. These statements signaled an invitation for a challenge to the SEC's disgorgement authority. With the grant of certiorari in *Liu*, the Court appears ready to address the issue directly. Any decision that further restricts the SEC's ability to obtain disgorgement could have major ramifications for the SEC's enforcement efforts.

Kokesh v. SEC

The federal securities laws give the SEC authority to seek several types of relief in enforcement actions, including injunctive relief and civil monetary penalties. The SEC has long taken the position that disgorgement constitutes equitable relief that is within the inherent authority of district courts to grant, arguing that it serves a remedial purpose by requiring violators to give up their ill-gotten gains.

In *Kokesh*, the Supreme Court addressed the narrow question of whether the statute of limitations in 28 U.S.C. § 2462—which governs any "action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture"—applies to SEC enforcement actions for disgorgement. The Court held that disgorgement constituted a "forfeiture" or "penalty" under § 2462, based in part on the fact that the disgorged funds are not always returned to victims, and also signaled that there is an open question regarding whether the SEC is authorized to seek disgorgement at all:

- Chief Justice Roberts noted that "the SEC devised this remedy or relied on this remedy without any support from Congress."
- Justice Sotomayor asked "[c]an we go back to the authority? . . . [H]ow could [the statutory provision authorizing the SEC to seek equitable relief] be the basis of disgorgement [when there is no restitution to investors]?"
- Justice Alito stated that "it would certainly be helpful and maybe essential to know what the authority for [disgorgement] is."

[1] *Liu v. Sec. & Exch. Comm'n*, No. 18-1501, 2019 WL 5659111 (U.S. Nov. 1, 2019).

- Justice Gorsuch questioned whether and when the SEC has to return disgorged funds to victims "because there's no statute governing" disgorgement and "[w]e're just making it up."

The Court did not decide the issue and made clear in a footnote that it was not expressing any "opinion on whether courts possess authority to order disgorgement in SEC enforcement proceedings or on whether courts have properly applied disgorgement principles in this context."[2]

Liu v. SEC

In *Liu*, the SEC sued Charles Liu and Xin Wang for violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and SEC Rule 10b-5. The SEC alleged that Liu and Wang defrauded investors by leading them to believe that they were funding an enterprise that met the EB-5 immigrant investor program requirements, which offers lawful permanent residence status to aliens who make a substantial investment in a U.S. enterprise, when the enterprise did not actually meet the requirements.

The district court granted summary judgment to the SEC and found that Liu and Wang violated Section 17(a)(2) of the Securities Act. The court issued an injunction, imposed civil monetary penalties of $6.7 million on Liu and $1.5 million on Wang, and ordered disgorgement of "all funds received from [the] illegal conduct, together with prejudgment interest thereon," which amounted to $26.4 million.

The Supreme Court decided *Kokesh* after the district court's decision in *Liu*, but prior to Liu and Wang's appeal to the Ninth Circuit. In their appeal, Liu and Wang argued that the district court lacked authority to award disgorgement under the principles of *Kokesh*. The Ninth Circuit noted that the Supreme Court had not reached the issue and that therefore *Kokesh* was not "clearly irreconcilable" with pre-*Kokesh* law of the circuit upholding similar disgorgement awards.[3] As a result, the Ninth Circuit declined to overturn the district court's order.

Liu and Wang sought certiorari on the basis that this question is important and recurring for the circuit courts because, pre-*Kokesh*, the circuit courts had held that disgorgement was remedial, not punitive, and therefore equitable in nature.[4] They argued that *Kokesh*'s ruling that disgorgement constitutes a "forfeiture" or "penalty" turned that reasoning on its head, undermining the historical justification the SEC has used to seek disgorgement. The Supreme Court granted certiorari on November 1, 2019.

Potential Impact on SEC Enforcement

A Supreme Court decision in *Liu* eliminating the SEC's ability to seek disgorgement in district court could have profound consequences for the agency's enforcement program. Disgorgement is by far the SEC's largest financial remedy. In its 2018 annual report, the Enforcement Division reported that it obtained more than $2.5 billion in disgorgement in fiscal year 2018 and more than $11 billion combined in the last

---

[2] *Kokesh v. Sec. & Exch. Comm'n*, 137 S. Ct. 1635, 1642 n.3 (2017).

[3] *Sec. & Exch. Comm'n v. Liu*, 754 F. App'x 505, 509 (9th Cir. 2018), *cert. granted sub nom. Liu v. SEC*, No. 18-1501, 2019 WL 5659111 (U.S. Nov. 1, 2019).

[4] Several district and circuit courts have upheld the SEC's authority to seek disgorgement post-*Kokesh*. *See, e.g.*, *Sec. & Exch. Comm'n v. de Maison*, No. 18-2564, 2019 WL 4127328, at *1 (2d Cir. Aug. 30, 2019) (upholding district court decision ordering disgorgement and noting that the panel was bound by Second Circuit precedent because the Supreme Court explicitly said in *Kokesh* that it was not deciding the question of whether the SEC had the authority to seek disgorgement); *Sec. & Exch. Comm'n v. Ahmed*, 343 F. Supp. 3d 16, 27 (D. Conn. 2018) ("[N]othing in Kokesh disturbed Second Circuit precedent that disgorgement is a proper equitable remedy."); *Sec. & Exch. Comm'n v. Berkey*, 374 F. Supp. 3d 355, 359 (S.D.N.Y. 2019) ("[S]ince *Kokesh*, the Second Circuit has upheld disgorgement awards . . . and numerous district courts in this circuit have imposed disgorgement as a penalty.") (internal citations omitted); *Sec. & Exch. Comm'n v. Weaver*, 773 F. App'x 354, 357 (9th Cir. 2019) ("*Kokesh* specifically declined to consider [whether the SEC is authorized to seek disgorgement], so that case is not 'clearly irreconcilable' with our longstanding precedent on this subject.") (internal citations omitted).

four fiscal years.[5] This far exceeded the total amount of penalties during the same time periods, with $1.4 billion ordered in penalties in fiscal year 2018 and $4.7 billion total over four years.[6]

If the Court were to rule that the Commission does not have authority to seek disgorgement, the SEC might respond in several ways:

- First, it could articulate a need for legislation to authorize the SEC to seek disgorgement.[7]
- Second, the SEC might argue that it may seek disgorgement-style relief, perhaps restyled as "remediation," if it returns the money to investors. As discussed above, in *Kokesh*, the Court concluded that disgorgement is not "compensatory" because disgorgement in SEC actions often is paid to the government, not investors, and that courts have ordered disgorgement regardless of whether the money would be returned to investors.[8] In response to an unfavorable decision in *Liu*, the SEC might argue that an award is compensatory, and within a district court's equitable authority, if the money will be returned to investors. Even if it were successful in making this distinction, the results could be relatively modest—the Enforcement Division reported that it returned $794 million to investors in fiscal year 2018.[9]
- Third, the Enforcement Division might seek larger penalties to make up for any loss of authority to seek disgorgement. In district court cases, the SEC is authorized to seek penalties based on a "tier" analysis of the severity of the conduct,[10] or an amount up to "the gross amount of pecuniary gain to such defendant as a result of the violation."[11] The SEC might try to use the "gross pecuniary gain" provision to seek penalties that include what it would have sought in disgorgement. If this strategy were ineffective, the SEC would have to argue for penalties closer to the maximum tier amount authorized by statute. With either approach, it is uncertain whether district court judges or a majority of SEC commissioners would agree to larger penalties to compensate for reduced disgorgement authority.
- Fourth, the SEC might consider pursuing more cases in administrative proceedings, where it has express statutory authority to "enter an order requiring accounting and disgorgement, including

---

[5] *See* **SEC 2018 Annual Report** at 11. The SEC's 2019 Annual Report is expected soon.

[6] *Id.*

[7] For example, in March 2019, a bipartisan bill, known as the **Securities Fraud Enforcement and Investor Compensation Act**, was introduced in the Senate to offset losses from *Kokesh* by giving the SEC ten years to seek restitution for fraud victims and to codify the SEC's ability to seek disgorgement in district court. The Enforcement Division has stated that it may have to forgo approximately $900 million in disgorgement due to *Kokesh* for matters that had already been filed as of FY2018. ***See*** **SEC 2018 Annual Report** at 12.

[8] *Kokesh*, 37 S. Ct. at 1644.

[9] *See* **SEC 2018 Annual Report** at 11.

[10] Tier 1 is the base-level penalty for each "violation" in district court cases. Tier 2 allows for larger penalties if the violation involved "fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement." Tier 3 further allows for increases to the penalty if, in addition to meeting the requirements of Tier 2, the violation involved substantial losses or created a significant risk of substantial losses to other persons. At each tier, the penalty is lower for natural persons than for all other persons. The tier analysis is essentially the same across the Securities Act, Exchange Act, Investment Company Act, and Investment Advisers Act.

[11] Securities Act of 1933, 15 U.S.C. § 77t(d)(2); Securities Exchange Act of 1934, 15 U.S.C. § 78u(d)(3); Investment Company Act of 1940, 15 U.S.C. § 80a-41(e)(2); Investment Advisers Act of 1940, 15 U.S.C. § 80b-9(e)(2).

reasonable interest."[12] This strategy would involve additional risk because of the challenges to the constitutionality of the SEC's administrative proceedings that we explained in a **prior alert**.[13]

Oral argument on the case is likely to be scheduled for early next year, with a decision expected by the summer. It is difficult to predict the future impact on the SEC—how the Court will rule in this case, whether it will limit the SEC's ability to seek disgorgement, and how the SEC might respond to such a decision. What is clear is that this case could have a dramatic impact on the SEC's enforcement program and will be a priority for the SEC in the year ahead.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

New York

Greg D. Andres	+1 212 450 4724	greg.andres@davispolk.com
Martine M. Beamon	+1 212 450 4262	martine.beamon@davispolk.com
Angela T. Burgess	+1 212 450 4885	angela.burgess@davispolk.com
Tatiana R. Martins	+1 212 450 4085	tatiana.martins@davispolk.com

Washington DC

Robert A. Cohen*	+1 202 962 7047	robert.cohen@davispolk.com
Neil H. MacBride	+1 202 962 7030	neil.macbride@davispolk.com
Paul J. Nathanson	+1 202 962 7055	paul.nathanson@davispolk.com
Annette L. Nazareth	+1 202 962 7075	annette.nazareth@davispolk.com
Linda Chatman Thomsen	+1 202 962 7125	linda.thomsen@davispolk.com
Stefani Johnson Myrick	+1 202 962 7165	stefani.myrick@davispolk.com

*Mr. Cohen is admitted to practice in New York and Maryland, and is practicing in DC under the supervision of partners of the firm.

[12] Securities Act of 1933, 15 U.S.C. § 77h-1(e); Securities Exchange Act of 1934, 15 U.S.C. § 78u-3(e); Investment Company Act of 1940, 15 U.S.C. § 80a-9(e); Investment Advisers Act of 1940, 15 U.S.C. § 80b-3(j).

[13] As we previously noted, the Court's decision in ***Lucia v. SEC***, which found that SEC administrative law judges ("ALJs") are subject to the Appointments Clause of the Constitution, raised the question of whether the statutory removal protections afforded to SEC ALJs are also unconstitutional. That issue is currently being considered by the Fifth Circuit in *Cochran v. SEC*, No. 19-10396 (5th Cir.).

SFO Announces New Corporate Cooperation Guidance

August 13, 2019

On August 6, the United Kingdom's Serious Fraud Office ("SFO") published new guidance on the steps companies should take in order to receive cooperation credit in the SFO's charging decisions. The document, titled "Corporate Co-operation Guidance" (the "SFO Guidance"),[1] outlines similar steps to those set forth in the United States Department of Justice's Corporate Enforcement Policy ("CEP"), indicating that SFO Director Lisa Osofsky, formerly of the FBI, is ushering in familiar U.S.-based standards in her new role leading the SFO.

Despite many similarities, the SFO Guidance differs from the CEP in a few significant respects. The most noteworthy of these differences is that the SFO Guidance indicates that a company may not obtain cooperation credit unless it waives privilege over witness accounts, notes, and transcripts obtained during the course of the company's investigation. Second, by requiring companies to provide such material, the SFO Guidance could come into tension with the recent *United States v. Connolly* decision from the Southern District of New York, in which Chief Judge Colleen McMahon admonished the Department of Justice for "outsourcing" its investigation to company counsel, rather than relying on its own investigation and resources.[2]

As set forth below, it remains to be seen how these differences will play out in matters being jointly investigated by the DOJ and SFO, such that the subject company can cooperate effectively in both countries without foregoing cooperation credit from either agency.[3]

The SFO Guidance

The SFO Guidance defines cooperation as "providing assistance to the SFO that goes above and beyond what the law requires."[4] Under preexisting SFO guidance, if a company takes a "genuinely proactive approach" including "self-reporting and remedial actions," this conduct would weigh in favor of not prosecuting the company.[5] Similarly, cooperation can carry "considerable weight" in a decision to grant a

---

[1] Serious Fraud Office, Operational Handbook, *Corporate Co-operation Guidance* (2019), *available at* https://www.sfo.gov.uk/download/corporate-co-operation-guidance/# ("*SFO Guidance*").

[2] *United States v. Connolly*, Case No. 16-cr-370, 2019 WL 2120523 (S.D.N.Y. May 2, 2019).

[3] Recent examples of companies jointly investigated by the DOJ and SFO include Guralp Systems Limited (2018) and Rolls-Royce plc (2017).

[4] *SFO Guidance* at 1.

[5] Serious Fraud Office, Guidance on Corporate Prosecutions 8 (2010).

company a Deferred Prosecution Agreement ("DPA") under the SFO's 2013 DPA Code of Practice, if that cooperation is "genuinely proactive."[6]

The new SFO Guidance does not so much alter the landscape as elaborate upon the type of conduct expected in order to obtain cooperation credit. Much of the SFO Guidance is devoted to detailing the best practices that organizations should take to preserve and provide physical evidence. Some of these best practices include:

- Preserving digital and hard-copy versions of relevant material using methods that prevent damage or destruction
- Ensuring digital integrity of electronic materials
- Providing materials in an organized, useful way that makes it easy for the SFO to digest
- Assisting in identifying material that might help any accused individual or entity or that might undermine the case for prosecution
- Providing relevant background information on the company
- Notifying the SFO of other government agencies the company has been contacted by or reported to
- Making relevant personnel available to explain the company's financial records[7]

Other notable examples include reporting the misconduct of relevant actors—regardless of seniority or position—directly to the SFO within a reasonable time as well as preserving evidence and providing it to the SFO.

The SFO Guidance also provides some examples of behavior considered inconsistent with cooperation, including tactical delay, information overload, and unjustifiably blaming others.[8] Though the SFO Guidance endeavors to give examples of how corporations ought to behave, it also emphasizes that cooperative conduct is not a matter of specific checklists so much as "the nature and tone of the interaction" between the organization and the SFO.[9]

Privilege Waiver

The most significant difference between the SFO Guidance and the CEP is the SFO Guidance's approach to privileged information. Under the SFO Guidance, companies seeking cooperation credit "by providing witness accounts should additionally provide any recording, notes and/or transcripts of the interview and identify a witness competent to speak to the contents of each interview."[10] Indeed, under the SFO Guidance, while a company will not be penalized if it chooses not to waive privilege, an "organization that does not waive privilege and provide witness accounts does not attain the corresponding factor against prosecution that is found in the DPA Code."[11]

---

[6] Serious Fraud Office, Deferred Prosecution Agreements Code of Practice 2.8.2.i. (2013).

[7] *SFO Guidance* at 2-4.

[8] *Id.* at 1.

[9] *Id.* at 2.

[10] *Id*. at 5.

[11] *Id*.

This is a stark departure from the approach taken in the CEP, which explicitly states that "eligibility for cooperation or voluntary self-disclosure credit is not in any way predicated upon waiver of the attorney-client privilege."[12] Indeed, the "in any way" language found in the CEP was recently added in March 2019, erasing any doubt that cooperation credit under the CEP was in any way related to a company's willingness to waive privilege.

In this regard, one important point to note is that, while the attorney-client privilege is similar in many respects in the U.S. and U.K, the U.K. takes a more narrow approach when it comes to employee interviews. As a general matter, in the U.K., employee interviews are not protected by the legal advice privilege, but a recent U.K. Court of Appeal decision ruled against the SFO in finding that, in certain circumstances, interview notes are protected if the interview was conducted in anticipation, and for the dominant purpose, of litigation.[13] Thus, companies seeking to comply with the SFO Guidance should be prepared to waive privilege over employee interview notes that may otherwise be protected under U.K. law.

Moreover, the SFO Guidance notes that a company asserting privilege "will be expected to provide certification by independent counsel that the material in question is privileged."[14] This presents an added burden for companies conducting internal investigations, and it remains to be seen how much pushback independent counsel will receive from the SFO regarding privilege determinations.

Other Key Differences from the DOJ's Corporate Enforcement Policy

The SFO Guidance differs from the CEP in a few other notable respects.

- **No Presumption in Favor of Non-Prosecution.** The SFO Guidance states that a company's cooperation will be a relevant consideration in the SFO's charging decision, but that "even full, robust co-operation" will "not guarantee any particular outcome."[15] Thus, unlike the CEP, the SFO Guidance does not establish any presumption in favor of a particular enforcement outcome based on a company's level of cooperation. Instead, the SFO retains full discretion to determine the correct outcome based "upon the particular facts and circumstances" of each case.[16]
- **Reporting Requirements.** Another difference between the two policies is in regard to the depth of their reporting requirements. In order to achieve cooperation credit under the SFO Guidance, a company must "identify[] suspected wrong-doing and criminal conduct together with the people responsible, regardless of their seniority or position in the organization."[17] The CEP, on the other hand, only requires that companies disclose "relevant facts about all individuals *substantially*

[12] Justice Manual Title 9-47.120, *FCPA Corporate Enforcement Policy*, *available at* **www.justice.gov/jm/jm-9-47-120** ("*Corporate Enforcement Policy*").

[13] *See Dir. Serious Fraud Office v. Eurasian Nat. Res. Corp. Ltd.* [2018] EWCA (Civ) 2006, (Eng.).

[14] *SFO Guidance* at 5.

[15] *Id*. at 1.

[16] *Id.*

[17] *Id*.

involved in or responsible for the violation of law."[18] Thus, companies may face a heavier burden in identifying relevant individuals to the SFO as compared with their reporting obligations to the DOJ.

- **Personal Communications Records.** The SFO Guidance also differs slightly from the CEP in its approach to personal communications records. Both the SFO Guidance and CEP make clear that strong recordkeeping practices will be rewarded, but in the context of communication records, the CEP places a slightly more stringent burden on companies. The CEP requires companies seeking cooperation credit to "implement[] appropriate guidance and controls on the use of personal communications and ephemeral messaging platforms."[19] Thus, companies must formally outline the permissible uses of these platforms to optimize compliance and record retention. While the SFO Guidance emphasizes strong recordkeeping practices such as maintaining an audit trail of the acquisition and handling of digital material, it asks only that companies "alert the SFO to relevant digital material that the organisation cannot access – for example . . . messaging apps."[20]

Implications on Joint Investigations

The differences between the SFO Guidance and the CEP pose a number of questions for how companies being jointly investigated by the SFO and DOJ can cooperate fully and effectively under each agency's guidance. On the one hand, for example, waiving privilege over witness interviews and related accounts to comply with the SFO Guidance risks waiving that same privilege with respect to the DOJ—an action flatly not required under the CEP to obtain cooperation credit. Indeed, such waiver could also have broader implications in other proceedings (such as civil litigation) beyond any joint investigation conducted by the DOJ.

As set forth above, other differences such as reporting requirements and approach to personal communication records could force companies to elect courses of action that go beyond what is required under the agencies' individual guidance. Indeed, when faced with the option of which guidance to follow, one factor that companies might consider is the presumption in favor of non-prosecution found in the CEP—a presumption that the SFO Guidance has clearly carved out.

Some of the cooperation requirements set forth in the SFO Guidance could also come into tension with language in Chief Judge Colleen McMahon's recent opinion in *U.S. v. Connolly*. For example, the SFO Guidance requires that companies "consult in a timely way with the SFO before interviewing potential witnesses or suspects" and "mak[ing] employees and (where possible) agents available for SFO interviews."[21] This approach diverges from that counseled by the *Connolly* decision, which criticized the government's directing of employee interviews as well as the company's having sought government permission to interview its own personnel.[22] The requirement that companies waive privilege over the

---

[18] Indeed, when then-Deputy Attorney General Rod Rosenstein announced this revision in November 2018, he cited "the inefficiency of requiring companies to identify every employee involved [in wrongdoing] regardless of their culpability." He further emphasized that "investigations should not be delayed merely to collect information about individuals whose involvement was not substantial." *See* Remarks at the American Conference Institute's 35th International Conference on the Foreign Corrupt Practices Act (Nov. 29, 2018), *available at* **https://www.justice.gov/opa/speech/deputy-attorney-general-rod-j-rosenstein-delivers-remarks-american-conference-institute-0**.

[19] *Corporate Enforcement Policy*.

[20] *SFO Guidance* at 3.

[21] *Id*. at 4.

[22] *United States v. Connolly*, Case No. 16-cr-370, 2019 WL 2120523 at *6, *12 (S.D.N.Y. May 2, 2019).

notes, accounts, and transcripts of witness interviews also risks allowing the government to do precisely what Chief Judge McMahon warned against in *Connolly*: "outsourc[ing] the important development stage of [the government's] investigation" to the company and then relying on that information to "buil[d] its own investigation."[23]

It remains to be seen how these potential tensions may play out in practice or whether the SFO will issue additional guidance or statements addressing these concerns.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

Greg D. Andres	+1 212 450 4724	greg.andres@davispolk.com
Martine M. Beamon	+1 212 450 4262	martine.beamon@davispolk.com
Angela T. Burgess	+1 212 450 4885	angela.burgess@davispolk.com
Neil H. MacBride	+1 202 962 7030	neil.macbride@davispolk.com
Tatiana R. Martins	+1 212 450 4085	tatiana.martins@davispolk.com
Fiona R. Moran	+1 202 962 7137	fiona.moran@davispolk.com
Paul J. Nathanson	+1 202 962 7055	paul.nathanson@davispolk.com
Neal A. Potischman	+1 650 752 2021	neal.potischman@davispolk.com
Martin Rogers	+852 2533 3307	martin.rogers@davispolk.com
Kenneth L. Wainstein	+1 202 962 7141	ken.wainstein@davispolk.com

[23] *Id*. at *12.

Second Circuit Holds the FCPA Does Not Extend to Non-U.S. Persons Under Conspiracy and Accomplice Liability Theories Absent U.S. Nexus

August 31, 2018

On August 24, 2018, the Second Circuit held in ***United States v. Hoskins*** that a nonresident foreign national cannot be found liable for violating the anti-bribery provisions of the Foreign Corrupt Practices Act ("FCPA") under conspiracy or accomplice theories if that individual could not otherwise be held directly liable under the statute.[1] This question arose in the context of the Department of Justice's ("DOJ") criminal prosecution of Lawrence Hoskins, a U.K. national charged for his involvement in a corporate bribery scheme to secure a lucrative Indonesian construction contract. Even though the defendant is a foreign national who worked for a non-U.S. company and had not set foot in the United States as part of the bribery scheme, DOJ charged him with conspiring with a U.S. affiliate of his employer, and others, to violate the FCPA. The Second Circuit rejected this theory, finding that Congress had placed careful limits on extraterritorial liability under the FCPA, and that these limits cannot be breached through conspiracy or accomplice liability.

The *Hoskins* decision challenges DOJ's expansive interpretation of the FCPA's reach, but its impact remains to be seen. In response to *Hoskins*, DOJ may shift its focus away from conspiracy and aiding-and-abetting theories and focus more on charging foreign nationals and companies as agents of domestic U.S. companies or U.S. issuers. Agents are clearly covered by the FCPA, but an aggressive interpretation of agency to reach foreign defendants with a minimal U.S. nexus could also run into judicial headwinds in the future.

Background

The anti-bribery provisions of the FCPA apply to three categories of persons or entities: (1) foreign and domestic issuers of U.S.-registered securities and their officers, directors, employees, or agents who make use of U.S. interstate commerce in furtherance of a corrupt payment; (2) "domestic concerns" (including U.S. nationals, U.S. residents, and companies organized or with their principal place of business in the United States) and their employees, agents, and other related persons if they make use of U.S. interstate commerce and, for certain U.S. persons, for conduct outside the United States regardless of whether they use U.S. interstate commerce; and (3) any other person or entity who, while in the United States, acts in furtherance of a corrupt payment.[2]

In July 2013, DOJ indicted Lawrence Hoskins, a British executive of Alstom U.K., a British subsidiary of French power and transportation company, Alstom S.A., for participating in a bribery scheme to win a $118 million contract to build power stations for the state electricity company in Indonesia. DOJ did not allege that Hoskins was an employee of Alstom's U.S. subsidiary, Alstom Power, Inc. ("Alstom U.S."), nor that Hoskins violated the FCPA while on U.S. soil. Instead, DOJ argued that Hoskins was "one of the people responsible for approving the selection of, and authorizing payments to," certain consultants,

[1] __ F.3d __ (2d Cir. 2018).

[2] 15 U.S.C. §§ 78dd-1–77dd-3.

knowing that a portion of the payments was actually intended for Indonesian officials in exchange for influence and assistance in obtaining contracts. DOJ further argued that although Hoskins did not travel to the United States, he communicated with U.S.-based co-conspirators regarding the alleged scheme.

In a 12-count indictment, DOJ charged Hoskins with conspiring with Alstom U.S., its employees, and foreign persons to violate the FCPA. DOJ alleged that he conspired both in his capacity as an "agent" of a domestic concern (Alstom U.S.) and independent of this alleged agency relationship. The indictment also charged Hoskins with substantive violations of the FCPA as an agent of a domestic concern and by aiding and abetting such violations. In December 2014, Alstom S.A. entered into a deferred prosecution agreement with DOJ for charges related to its own alleged misconduct.

In the lower court, Hoskins moved to dismiss certain counts against him on the theory that he could not be held liable for conspiring to violate the FCPA if he was not a member of any of the enumerated classes of defendants to whom the statute applied.[3] In analyzing DOJ's conspiracy theory, the district court, basing its analysis on the Supreme Court's ruling in *Gebardi v. United States*[4], found that because FCPA liability only attaches to three precisely articulated groups of persons, Congress intended to limit liability to only certain entities and individuals. The district court accordingly dismissed the charges based on conspiracy to violate the FCPA, reasoning that "where Congress chooses to exclude a class of individuals from liability under a statute, the Executive may not . . . override the Congressional intent not to prosecute that party by charging it with conspiring to violate a statute that it could not directly violate."

The district court also denied Hoskins's motion to dismiss the charge that he acted as an agent of Alstom U.S. in violating the FCPA, finding that Hoskins failed to show that the facts in the indictment were insufficient to establish an "agency" relationship between himself and Alstom U.S.[5] Although the district court acknowledged that an agency analysis is a highly factual one, it observed that Hoskins had certain responsibilities related to Alstom U.S.'s efforts.

After the district court denied DOJ's motion for reconsideration, DOJ filed an interlocutory appeal to the Second Circuit. The appeal addressed a single question: whether the district court correctly dismissed the conspiracy charges in the indictment to the extent that DOJ had charged Hoskins with conspiracy without demonstrating that Hoskins fell into one of the categories of persons to which the FCPA applies directly.

Second Circuit Decision

With respect to conspiracy generally, the Second Circuit observed that under common law and federal conspiracy statutes, individuals who cannot be held liable for their own acts under a particular law may still be found guilty of conspiring to commit that crime or acting as an accomplice—for example, a getaway driver in a bank robbery may be prosecuted even though his own actions do not meet the statutory elements of the crime of bank robbery. An exception exists, however, where there is clear legislative intent to exclude certain individuals from the law's purview. For example, the Supreme Court held in *Gebardi v. United States* that a woman who had acquiesced to being transported across state lines in violation of the Mann Act could not be prosecuted for conspiracy, because Congress intended to exclude that class of people from prosecution under the Act.[6]

---

[3] *See United States v. Hoskins*, 123 F. Supp. 3d 316 (D. Conn. 2015).

[4] 287 U.S. 112 (1932).

[5] *See United States v. Hoskins*, No. 3:12-cr-238 (D. Conn. Dec. 29, 2015).

[6] 287 U.S. 112, 119 (1932).

To determine whether Congress possessed an intent to exclude certain foreign nationals from conspiracy liability in enacting the FCPA, the Second Circuit analyzed the text and structure of the statute. The court also considered the principle that U.S. law does not apply extraterritorially without clear congressional authorization. The Second Circuit found that the text and structure of the FCPA—which describes in detail the categories of people that are covered but fails to include any provision for liability of nonresident foreign nationals who act outside U.S. territory and are not employees or agents of domestic concerns or issuers—suggests that Congress did not intend to create such liability.

As part of its analysis, the Second Circuit engaged in a lengthy review of the legislative history of the FCPA. It found that during the original drafting process in the 1970s and the amendment process in 1998, Congress sought to craft the FCPA in a manner that would quell concerns about the scope of liability it created and the breadth of extraterritorial application of the anti-bribery provisions. The court noted that while the Senate initially planned to craft a bill that did not mention individual liability and relied on accomplice theories to connect individual action to corporate wrongdoing, it later rejected this approach in favor of a bill that listed "with great precision" explicit categories of individuals and entities covered by the law. In amending the law in 1998, Congress carefully delineated additional areas of liability, expanding the FCPA's reach to cover foreign nationals that committed acts within the United States and to U.S. companies and persons that committed acts wholly outside the United States. Based on this history, the Second Circuit found that the drafters of the FCPA made an "affirmative decision to exclude from liability" certain classes of people, and that the government could not "override that policy using the conspiracy and complicity rules." Accordingly, the Second Circuit held that the "FCPA clearly dictates that foreign nationals may only violate [the FCPA] outside the United States if they are agents, employees, officers, directors, or shareholders of an American issuer or domestic concern."

The Second Circuit also addressed conspiracy charges against Hoskins that stemmed from his alleged role as an agent for Alstom U.S. The Second Circuit determined that the district court erred in dismissing these charges, observing that the government could still seek to show that Hoskins "acted as an agent of a domestic concern"—Alstom U.S.—that was "liable as a principal for the substantive FCPA counts charged in the indictment." The court held that the government should be allowed to make a showing that Hoskins conspired with Alstom's U.S. employees and other foreign nationals *as an agent* of Alstom U.S. in violation of the FCPA.

Limitations and Implications of the Decision

The Second Circuit's decision may have implications for foreign nationals and companies, in particular because the decision challenges DOJ's views concerning conspiracy and accomplice liability, as articulated in the widely relied-upon 2012 *Resource Guide to the U.S. Foreign Corrupt Practices Act*.[7] In reference to accomplice liability, the *Resource Guide* states: "A foreign company or individual may be held liable for aiding and abetting an FCPA violation or for conspiring to violate the FCPA, even if the foreign company or individual did not take any act in furtherance of the corrupt payment while in the territory of the United States." The *Resource Guide* further notes: "Individuals and companies, including foreign nationals and companies, may also be liable for conspiring to violate the FCPA—i.e., for *agreeing* to commit an FCPA violation—even if they are not, or could not be, independently charged with a substantive FCPA violation." *Hoskins* narrows both expansive interpretations such that foreign companies and individuals who have neither committed any act within the territory of the United States nor acted as an agent of a U.S. entity or person could potentially use *Hoskins* as a defense to liability under the anti-bribery provisions of the FCPA.

[7] U.S. DEP'T OF JUSTICE, CRIMINAL DIV. & U.S. SEC. & EXCH. COMM'N, A RESOURCE GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT (2012).

The Second Circuit's decision may also influence DOJ's anti-bribery enforcement strategy. Under the Second Circuit's decision, foreign companies and nationals may not be charged with conspiring to violate, or aiding and abetting violations of, the FCPA's anti-bribery provisions without a sufficient nexus to the U.S., but these entities and individuals may still face liability for causing violations of these same provisions as agents of a U.S. issuer or domestic concern. Accordingly, this narrowing of accomplice and conspiracy liability may prompt DOJ to rely more heavily on agency theories in future FCPA enforcement actions or, in certain limited circumstances, to rely on other statutes and theories that lack the FCPA's restrictions, such as the Money Laundering Control Act. We could also see further developments in the *Hoskins* case itself: the increased focus on agency theories may result in a more direct challenge to DOJ's assertions of agency and a more detailed analysis by the district court of agency theories under the FCPA.

Despite contradicting some of DOJ's broad pronouncements regarding the reach of the FCPA, the effect the Second Circuit's decision will have on FCPA enforcement is not yet clear and several factors may limit the impact of the Second Circuit's opinion. First, the decision may be overturned or limited by *en banc* review or a petition for certiorari to the U.S. Supreme Court. Second, other Circuit Courts, such as the D.C. Circuit, which often has concurrent jurisdiction over FCPA matters, may opt not to follow the Second Circuit's decision. Finally, while the government may emphasize agency theories of liability in the wake of the Second Circuit's decision, this might not have a significant effect on liability outcomes as many foreign nationals are already charged on agency theories in conjunction with aiding and abetting or conspiracy theories.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

Martine M. Beamon	**212 450 4262**	**martine.beamon@davispolk.com**
Angela T. Burgess	**212 450 4885**	**angela.burgess@davispolk.com**
Denis McInerney	**212 450 4477**	**denis.mcinerney@davispolk.com**
James W. Haldin	**212 450 4059**	**james.haldin@davispolk.com**
Neil H. MacBride	**202 962 7030**	**neil.macbride@davispolk.com**
Paul J. Nathanson	**202 962 7055**	**paul.nathanson@davispolk.com**
Neal A. Potischman	**650 752 2021**	**neal.potischman@davispolk.com**
Patrick S. Sinclair	**+852 2533 3305**	**patrick.sinclair@davispolk.com**
Linda Chatman Thomsen	**202 962 7125**	**linda.thomsen@davispolk.com**
Kenneth L. Wainstein	**202 962 7141**	**ken.wainstein@davispoil.com**