

White-Collar Crime

COMMENTARY

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5th Circuit Confirms an Expansive Reading of The FCPA in *United States v. Kay*

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Introduction

With ever-increasing regularity, the Securities and Exchange Commission and the Department of Justice are bringing, and settling, cases involving alleged violations of the Foreign Corrupt Practices Act. The sizes of such settlements continue to grow; most recently, energy services firm Willbros Group disclosed that it reached a tentative FCPA-related settlement with the DOJ and SEC for \$32.3 million in penalties and disgorgement.

Last April oil and gas company Baker Hughes Services International announced that it had settled FCPA-related charges for a record total of \$44 million in penalties, disgorgement and prejudgment interest. These recent settlements are just two of many reached last year that evidence an FCPA enforcement agenda that is more aggressive than at any other time in the statute's 30-year history.

Two reasons often cited for the geometric rise in foreign bribery prosecutions are an increase in regulatory commitment and resources and the opening up to U.S. companies of major Asian markets that have a history of corruption. While these are certainly contributing factors, the government's success also can be attributed to a confluence of circumstances that dissuade defendants from litigating FCPA claims.

For example, the rise and prevalence of deferred prosecution agreements provide entities with a safe, predictable avenue for resolving FCPA claims. Through such agreements, companies agree to, among other things, pay a fine and promise to commit no further violations of the FCPA, a result that feels a lot more like a civil consent decree than the resolution of criminal charges. Additionally, the statute's language is both vague and

broadly worded, and few courts have addressed its scope. Given this uncertainty, companies are particularly hard-pressed to justify embarking upon years of costly litigation.

As a result, the issuance of a court decision interpreting the scope and contours of the FCPA is a rare and noteworthy occasion. In contrast to decisions regarding long-standing and heavily litigated criminal statutes, FCPA decisions continue to analyze and struggle with basic questions regarding the statute's scope and interpretation. An example is the U.S. Court of Appeals for the 5th Circuit's decision in *United States v. Kay*, 359 F.3d 738 (5th Cir. 2004) ("*Kay II*"), where the court validated the government's expansive reading of the statute, holding that the FCPA can cover payments to foreign officials to reduce foreign taxes and customs duties, as opposed to only payments made to secure new or renew existing business. More recently, the 5th Circuit issued another decision in *Kay* in which it affirmed and expanded upon its previous analysis, shedding further light on the extent of the FCPA's scope and application. See *United States v. Kay*, No. 05-20604, 2007 WL 3088140 (5th Cir. 2007) ("*Kay III*").

Kay I and II

The Foreign Corrupt Practices Act is comprised of two sections: anti-bribery provisions and accounting and record-keeping provisions. The anti-bribery provisions prohibit bribes to foreign government officials for the purpose of obtaining or retaining business or directing business to another person. 15 U.S.C. § 78dd-1(a)(1).¹

In 2001 David Kay and Douglas Murphy, executives at an American company that exported rice to Haiti in the 1990s, were charged with 12 counts of violating the FCPA. *Kay II* at 741. The indictment alleged that the defendants

paid Haitian customs officials to accept false documents that understated by one-third the quantity of rice shipped to the country by their employer, American Rice Inc., thereby reducing customs duties ARI owed to the Haitian government. *Id.*

Upon the defendants' motion to dismiss the indictment, the U.S. District Court for the Southern District of Texas considered — as a matter of first impression — the question of whether payments to foreign government officials made for the purpose of reducing customs duties and taxes fell within the scope of the FCPA's anti-bribery provision. See *United States v. Kay*, 200 F. Supp. 2d 681 (S.D. Tex. 2002) ("*Kay I*").

The court began by reviewing the plain language of the FCPA, which it concluded is ambiguous as to the scope of the "business nexus" element, the requirement that a bribe be made in order to assist in obtaining or retaining business. *Id.* at 683. After looking to the FCPA's legislative history for guidance on the issue, the court rejected the government's argument that the statute should be construed broadly so as to encompass payments made to reduce customs duties or tax obligations and, accordingly, dismissed the indictment. *Id.* at 686.

On appeal, the 5th Circuit agreed that the FCPA's language is ambiguous but rejected the District Court's conclusion that, as a matter of law, bribes paid to foreign officials as consideration for the evasion of customs duties and sales taxes could not fall within scope of the statute's anti-bribery provisions. *Kay II* at 740. The court conducted a lengthy analysis of the FCPA's legislative history, noting that "Congress meant to prohibit a range of payments wider than only those that directly influence the acquisition or retention of government contracts or similar commercial or industrial arrangements." *Id.* at 749.

More specifically, "[t]he congressional target was bribery paid to engender assistance in improving the business opportunities of the payor or his beneficiary, irrespective of whether that assistance be direct or indirect, and irrespective of whether it be related to administering the law, awarding, extending or renewing a contract, or executing or preserving an agreement." *Id.* at 750.

The 5th Circuit was quick to note, however, that a bribe paid to lower customs duties or sales taxes does not automatically constitute a violation of the FCPA; "[i]t still must be shown that the bribery was intended to produce an effect — here, through tax savings — that would 'assist in obtaining or retaining business.'" *Id.* at 756. Accordingly, the appeals court remanded the case to the District Court for further proceedings consistent with its conclusions.

Kay III

On remand, a jury found defendants Kay and Murphy guilty of authorizing more than \$500,000 in bribes to Haitian customs officials in violation of the FCPA.² The defendants once again appealed to the 5th Circuit.

On appeal, the court addressed, among others, the following issues:

- Whether the FCPA, given its ambiguity, failed to give fair notice that the defendants' conduct was illegal and thus violated their due-process rights;
- The interpretation of the FCPA's willfulness element; and
- The scope of the FCPA's requirement that the defendant use interstate commerce in furtherance of the payments in question.

Adopting a uniformly pro-government view on all these issues, the 5th Circuit affirmed the convictions.

Fair Notice

The defendants argued, at length, that the FCPA failed to give fair notice that their conduct was illegal. In doing so, they addressed four "standards of fair notice":

- The enforcement of a vague statute;
- The retroactive application of a "novel" interpretation of a statute;
- Whether the statute, standing alone or as construed, made the law reasonably clear at the time that the criminal conduct occurred; and
- The rule of lenity.

The defendants first argued that the 5th Circuit's previous finding in *Kay II* that the FCPA was ambiguous as a matter of law should have led the court to dismiss the prosecution under the vagueness doctrine. *Kay III* at 7. The court dismissed this argument, however, reasoning that the question of "[w]hether 'obtaining or retaining' business covers the general activities that an entity undertakes to ensure continued success of a business or the defendants' more limited definition of contractual business is an ambiguity but not one that rises to the level of vagueness and unfair notice." *Id.* at 8.

Despite the statute's ambiguity, the court noted, "[a] man of common intelligence would have understood that ARI, in bribing foreign officials, was treading close to a reasonably defined line of illegality." *Id.* at 9.

The defendants further argued that the District Court erred in its retroactive application of the 5th Circuit's interpretation of the FCPA in *Kay II*. *Id.* at 10. The appeals court dismissed this argument, noting that its prior decision did not expand the scope of the statute or create a new and independent principle of law, but rather interpreted and applied the statute's meaning to the facts of the case. *Id.* at 12.

The court reasoned that the FCPA's terms did not explicitly circumscribe the business practices that might fall under the "business nexus" test. And, by the defendants' admission, bribery to obtain favorable tax and customs obligations was common practice to guarantee the maintenance of a successful business in Haiti in the 1990s; thus, it was not a novel application of the FCPA to find that the defendants made these payments for the purpose of "retaining business." *Id.*

The court also dismissed the defendants' contention that its reliance on legislative history to interpret a criminal statute was inappropriate, noting that many other sources, including the FCPA's text, its title and the dictionary definition of "business," provided support for the court's resolution of ambiguity of the business nexus test. *Id.* at 13.

The 5th Circuit similarly rejected the defendants' argument that the FCPA failed to give fair notice at the relevant time that the conduct in question was illegal, reiterating that the FCPA was not void for vagueness but rather contained an ambiguous provision that did not rise to unfair notice under vagueness and retroactivity principles. *Id.* at 14.

The court also noted that the mere fact that prior prosecutions under the FCPA only targeted conduct aimed at securing business did not limit the statute's application to a wider range of activities. "To find unfair notice whenever a court specified new types of acts to which a criminal statute applied would stifle courts' ability to interpret and fairly apply criminal statutes." *Id.* at 16.

Finally, the 5th Circuit held that the FCPA is not sufficiently ambiguous as to merit application of the rule of lenity, which provides that in construing an ambiguous criminal statute, the court should resolve the ambiguity in favor of the defendant. The appeals court explained that the rule is applicable as a last resort of interpretation in situations of extreme ambiguity where a court "can make no more than a guess as to what Congress intended." *Id.* at 17.

The FCPA's legislative history, however, showed that "Congress meant to prohibit a range of payments wider than only those that directly influence the acquisition or retention of government contracts or similar commercial or industrial arrangements." *Id.* at 19.

The Willfulness Requirement

To obtain a criminal conviction under the FCPA, the government must prove that the defendant both corruptly and willfully violated subsections (a) or (g) of Section 78dd-1. *Id.* at 19. The defendants in *Kay* argued that the District Court failed to adequately instruct the jury on the willfulness element. *Id.* at 20.

Because the FCPA does not define the term "willfully," the 5th Circuit looked to the common-law interpretation of the word to determine the sufficiency of the jury instructions. The court examined "three levels of interpretation" of the term "willful" in the criminal context, all of which require that a defendant have acted intentionally. *Id.* at 22.

The first, least stringent interpretation of the term is that the defendant's mere knowledge that he committed the act — regardless of his knowledge of the specific terms of the statute, or even of its existence — constitutes willfulness. *Id.* at 23. The second, "intermediate" level of criminal willfulness requires the defendant to have known that his actions were in some way unlawful "under the general rules of law." *Id.*

"The strictest level of interpretation of criminal willfulness requires that the defendant knew the terms of the statute and that he was violating the statute." *Id.* at 24. The appeals court determined that, as the 2nd Circuit had previously held,³ the FCPA does not fall within the narrow category of statutes that imports this strict standard. *Id.* at 24, 29-30. The court concluded that, regardless of which of the first two levels of criminal willfulness applied, the District Court's jury instructions sufficiently captured both. *Id.* at 24.

Although, as the defendants charged, the District Court did not use the exact term "specific intent," its instructions were sufficient in that they required that the defendants have acted corruptly, committed the act intentionally and knowingly, and acted with a bad motive to accomplish either an unlawful end or an unlawful result. *Id.* at 27, 30.

The Use of Interstate Commerce

Finally, the defendants argued that the indictment insufficiently alleged, and the government failed to prove at trial, that they "made use of the mails or any means or instrumentality of interstate commerce" in furtherance of an illegal bribe. *Id.* at 33. The defendants contended that the purpose of the bribes was to further the use of barges and similar interstate commerce in order to ship the documents and rice into Haiti. *Id.* at 33-34. The payments,

however, were made in person in Haiti, with cash drawn from local bank accounts. *Id.* at 34.

In response, the 5th Circuit looked to the plain language of the FCPA, which covers individuals or companies that “make use of ... any means or instrumentality of interstate commerce ... in furtherance of an offer, payment, promise to pay or authorization [to pay].” 15 U.S.C. § 78dd-2. The court concluded that the interstate-commerce element was satisfied by evidence that the defendants used interstate commerce to ship false documents that under-reported ARI’s imports and were used to calculate, and thus further, the bribes.

In short, the court held that the FCPA’s anti-bribery provision is satisfied not only by the use of interstate commerce to make the corrupt payment at issue, but also by the use of interstate commerce for activities that support a scheme that involves such a payment. *Id.* at 36.

Conclusion

The 5th Circuit’s recent affirmation of the conviction of the defendants in *Kay* demonstrates at least one circuit court’s broad reading of the FCPA’s anti-bribery provisions’ scope and elements. Given the court’s interpretation of the statute, the dearth of contradictory jurisprudence on the subject and a regulatory climate where the government is taking extremely aggressive positions in litigating cases involving allegations of corporate crime, we are unlikely to soon see an end to the recent surge of

FCPA enforcement actions filed, and sizeable settlements reached, by the SEC and Justice Departments.

Notes

¹ The FCPA does not, however, criminalize all bribes made to foreign officials. Payments made to facilitate or expedite performance of routine governmental action, known as “grease” payments, are explicitly excluded from the statute’s scope. 15 U.S.C. § 78dd-1(b). “Grease” payments include payments made for the purpose of “obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country, processing governmental papers ... [and] actions of a similar nature.” 15 U.S.C. § 78dd-1(f)(3).

² The jury also found Murphy guilty of obstruction of justice in connection with a parallel civil investigation by the SEC regarding the payments at issue.

³ *Stichting Ter Behartiging Van de Belangen Van Oudaandeelhouders in Het Kapitaal Van Saybolt Int’l B.V. v. Schreiber*, 327 F.3d 173, 181 (2d Cir. 2003).

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