



Eleventh Circuit Expands Reach of Foreign Corrupt Practices Act

Michael E. Burke

On May 16, 2014 in its *U.S. v. Esquenazi* decision, the 11th Circuit Court of Appeals upheld the Department of Justice's broad definition of a key part of the Foreign Corrupt Practices Act ("FCPA"). At issue was 'instrumentality' within the FCPA's definition of 'foreign official' (defined by the statute as 'any officer or employee of a foreign government or any department, agency, or *instrumentality* thereof' [emphasis added]). The 11th Circuit is the first appellate court to rule on this issue and its holding has immediate and broad impact on all U.S. businesses subject to the FCPA.

What is an Instrumentality?

'Instrumentality' is one of the vaguest parts of the FCPA's definition of 'foreign official.' Over the past several years, the Department of Justice has used this vagueness to expand the term's scope and, by extension, the FCPA's reach. As a result, employees, officers and directors of many more foreign businesses, including state-owned or state-controlled enterprises, have been brought within the FCPA's definition of 'foreign official.' This expansive definition increased the compliance burden on U.S. businesses and others subject to the FCPA, by forcing them to determine (i) whether their partner/customer/counterparty would be considered to be an instrumentality of a foreign government pursuant to the FCPA; and (ii) which employees within their partner/customer/counterparty may be deemed to be 'foreign officials.'

Previous Guidance on Instrumentality

The Resource Guide to the Foreign Corrupt Practices Act (the "Guide") jointly issued by the Department of Justice and the Securities and Exchange Commission in November 2012 discusses the agencies' view of 'instrumentality.' The Guide does not have the force of law but does present a useful snapshot of the regulators' positions on key issues at the time of publication.

The Guide notes that many foreign governments operate through state-owned or state-controlled entities, and 'instrumentality' is meant to account for such operations in an attempt to treat foreign governments in as consistent a manner as possible. Whether a specific entity is an 'instrumentality' is unique to each situation and requires an analysis of the entity's ownership, control, status, and function. The Guide states that courts have developed a non-exclusive list of factors to be considered in determining whether an entity is an 'instrumentality': (i) the foreign state's extent of ownership of the entity; (ii) the foreign state's degree of control over the entity (including whether key officers and directors of the entity are, or are appointed by, government officials); (iii) the foreign state's characterization of the entity and its employees; (iv) the circumstances surrounding the entity's creation; (v) the purpose of the entity's activities; (vi) the entity's obligations and privileges under the foreign state's law; (vii) the exclusive or controlling power vested in the entity to administer its designated functions; (viii) the level of financial support by the foreign state (including subsidies, special tax treatment, government-mandated fees, and loans); (ix) the entity's provision of services to the jurisdiction's residents; (x) whether the governmental end or purpose sought to be achieved is expressed in the policies of the foreign government; and (xi) the general perception that the entity is performing official or governmental functions. *Guide p. 20.* The Guide provides that:

While no one factor is dispositive or necessarily more important than another, as a practical matter, an entity is unlikely to qualify as an instrumentality if a government does not own or control a majority of its shares. However, there are circumstances in which an entity would qualify as an instrumentality absent 50% or greater foreign government ownership. *Id.*

The Guide does not create a bright line rule, and points out that courts have not established a bright-line rule, on the issue of whether the entity in question must perform a function traditionally performed by a government agency in order to be deemed an 'instrumentality.' Any multipart, non-exclusive list of factors defining a key term in a statute increases the uncertainty on the part of those regulated. The vagueness of the 'instrumentality' concept has enabled the Justice Department to be aggressive in its FCPA-related investigations.

The Esquenazi Appeal

In 2011, a jury found appellant Esquenazi guilty on several substantive FCPA counts in connection with bribes paid to Telecommunications D'Haiti, and imposed on him the longest FCPA-related jail term to-date. On appeal to the 11th Circuit, appellant argued that the Department of Justice's construction of 'instrumentality' was overly expansive and not consistent with Congress's intent in drafting the FCPA. More specifically, appellant argued that (i) the facts that the National Bank of Haiti owned 97% of the stock in Telecommunications D'Haiti and the Haitian government appointed board members and directors to Telecommunications D'Haiti do not make Telecommunications D'Haiti an 'instrumentality' of a foreign government; and (ii) lower court erred by not instructing the jury to determine whether Telecommunications D'Haiti performed governmental functions *similar to governmental departments and agencies* [emphasis added]. Therefore, according to appellant, any bribes paid to Telecommunications D'Haiti would be outside the scope of the FCPA.

Eleventh Circuit Ruling

The 11th Circuit panel upheld the Justice Department's definition of 'instrumentality' by defining it as "an entity controlled by the government of a foreign country that performs a function the controlling government treats as its own." The concepts of 'control' and 'a function the government treats as its own' are, according to the panel, fact-specific. The court provided a list of factors it considered relevant to deciding the issue. In order to determine whether a government 'controls' an entity, parties subject to the FCPA should examine (i) the foreign government's formal designation of that entity; (ii) whether the government has a majority interest in the entity; (iii) the government's ability to hire and fire the entity's principals; and (iv) how the government manages the profits and losses of the entity.

In analyzing whether an entity 'performs a function the government treats as its own,' persons subject to the FCPA should examine whether: (i) the entity has a monopoly over the function it exists to carry out; (ii) the government subsidizes the costs associated with the entity providing services; (iii) the entity provides services to the public at large in the foreign country; and (iv) the public and the government of that foreign country generally perceive the entity to be performing a governmental function. In elaborating on the concepts of 'control' and 'a function the government treats as its own,' the court took guidance from commentary in the OECD Anti-Bribery Convention.

What's Next?

The *Esquenazi* decision ratifies the Justice Department's construction of 'instrumentality,' and expands the number of foreign entities within the FCPA's coverage. In separating 'control' from 'performs a function the government treats as its own,' the court indicates that entities with significant government ownership and control may be deemed instrumentalities even if they perform a government function at the lowest level, or not at all. The court also indicates that an entity with very minor government ownership may be deemed an 'instrumentality' for FCPA purposes if it significantly performs a government function. This decision likely will trigger more FCPA-related inquiries and investigations by the Department of Justice.

Companies subject to the FCPA immediately should review their compliance program to confirm whether their 'instrumentality' analysis is consistent with the *Esquenazi* decision. Foreign companies that may have formerly been considered outside the FCPA's ambit, including the partners/customers/counterparties of U.S. companies, may now be deemed to be 'instrumentalities' pursuant to the statute. Companies should also re-train relevant officers, directors and employees on the expanded scope of 'instrumentality.'

Authors and Contributors

Michael E. Burke

Partner, DC Office

202.677.4046

michael.burke@agg.com

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Atlanta Office

171 17th Street NW
Suite 2100
Atlanta, GA 30363

Washington, DC Office

1775 Pennsylvania Ave., NW,
Suite 1000
Washington, DC 20006

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