

RECENT TRENDS: Foreign Corrupt Practices and the CFTC

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Overview

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I. FOREIGN CORRUPT PRACTICES AND THE CFTC



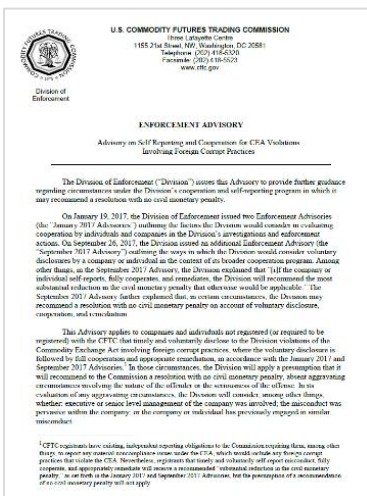
Foreign Corrupt Practices and the CFTC

“ Companies and individuals engaging in foreign corrupt practices should recognize that this sort of misconduct might constitute fraud, manipulation, false reporting, or a number of other types of violations under the CEA, and thus be subject to enforcement actions brought by the CFTC. ”

- James McDonald, CFTC Director of Enforcement
(ABA Conference in New York, March 6, 2019)



March 2019 Enforcement Advisory



ENFORCEMENT ADVISORY

Advisory on Self Reporting and Cooperation for CEA Violations Involving Foreign Corrupt Practices

This Advisory applies to companies and individuals not registered (or required to be registered with the CFTC that timely and voluntarily disclose to the Division violations of the Commodity Exchange Act involving foreign corrupt practices, where the voluntary disclosure is followed by full cooperation and appropriate remediation, in accordance with the January and September 2017 Advisories. In those circumstances, the Division will apply a presumption that it will recommend to the Commission a resolution with no civil monetary penalty, absent aggravating circumstances involving the nature of the offender or the seriousness of the offense. In its evaluation of any aggravating circumstances, the Division will consider, among other things, whether: executive or senior level management of the company was involved; the misconduct was pervasive within the company; or the company or individual has previously engaged in similar misconduct.



March 2019 Enforcement Advisory: Key Takeaways

Market participants should expect enhanced scrutiny of spot market activities in high-risk jurisdictions

- Scope of CFTC enforcement authority remains unchanged
- Further expansion of parallel enforcement program with Department of Justice
- Focus on “foreign” corrupt practices may present novel questions of jurisdiction
- Presumption of no Civil Monetary Penalty:
 - Extends only to non-registrants
 - Is contingent on full cooperation and appropriate remediation
 - Does not foreclose disgorgement, forfeiture and/or restitution



May 2019 Whistleblower Alert

CFTC Whistleblower Alert: Blow the Whistle on Foreign Corrupt Practices in the Commodities and Derivatives Markets

Under the Whistleblower Program of the Commodity Futures Trading Commission (CFTC), individuals can become eligible for both financial awards and certain protections by identifying Commodity Exchange Act (CEA) violations connected to bribes of foreign government officials or similar conduct.

What can you do if you suspect misconduct?

You do **not** need to be a company “insider” (like an employee or trader) to be a whistleblower. **Victims of**

fraud and **other market participants** who observe misconduct committed by others may also qualify as whistleblowers. The Whistleblower Rules define a whistleblower as **one or more individuals**; a company or another entity cannot meet the definition.



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What are foreign corrupt practices?

Foreign corrupt practices include actions that seek to improperly influence foreign officials with personal payments or rewards – commonly thought of as bribes. Companies and individuals engaging in such practices may be liable for fraud, manipulation, false reporting, or a number of other types of violations under the CEA and Commission Regulations. For more information, please see below and refer to the [March 2019 Division of Enforcement Advisory](#).

What types of misconduct should you be on the lookout for?

The CFTC will enforce the CEA provisions that encompass foreign corrupt practices. Such misconduct may include:

- Corrupt practices that **alter the prices in commodity markets** that drive U.S. derivatives prices
- Bribes employed to **secure business** in connection with regulated activities like trading, advising, or dealing in swaps or derivatives, and out of funds investors believed were being used to invest
- Corrupt practices used to **manipulate benchmarks** that serve as the basis for related derivatives contracts, as prices that are the product of corruption might be falsely reported to benchmarks

What can you do if you suspect misconduct?

You do not need to be a company “insider” (like an employee or trader) to be a whistleblower. Victims of fraud and other market participants who observe misconduct committed by others may also qualify as whistleblowers. The Whistleblower Rules define a whistleblower as **one or more individuals**; a company or another entity cannot meet the definition.

If you see something suspicious, you can:

- Complete a [Form TCR \(Tip, Complaint, Referral\)](#) correctly and as completely as possible
- Provide details that are specific, credible, and timely
- Include as much information about the misconduct as possible – e.g., price effect or intent
- Attach supporting documents or files to your Form TCR, as long as they are not protected by the attorney-client privilege
- Supplement your Form TCR filing with any additional information via mail, fax, or email

About the CFTC

We are the U.S. regulator charged with ensuring the integrity of the futures & swaps markets.

About the Whistleblower Program

We will pay **monetary awards** to persons who voluntarily provide us with original information on a Form TCR about violations of the CEA or its rules, if that information leads to a successful CFTC enforcement action resulting in more than \$1 million in monetary penalties. The program also affords **confidentiality and anti-retaliation protections**.

For more information go to: www.cftc.gov/whistleblower

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May 2019



May 2019 Whistleblower Alert: Key Takeaways

The CFTC has identified several key fact patterns of interest

- May 2019 Whistleblower Alert defines “foreign corrupt practices” as including “actions that seek to improperly influence foreign officials with personal payments or rewards – commonly thought of as bribes.”
- Identifies several key fact patterns of interest:
 - Corrupt practices that alter the prices in commodity markets that drive U.S. derivatives prices
 - Bribes employed to secure business in connection with regulated activities, like trading, advising or dealing in swaps or derivatives, paid out of funds investors believed were being used to invest
 - Corrupt practices used to manipulate benchmarks that serve as the basis for related derivatives contracts, as prices that are the product of corruption might be falsely reported to benchmarks



II. THE RELEVANT STATUTES



A. THE COMMODITY EXCHANGE ACT (“CEA”)



The Commodity Exchange Act (“CEA”)

CEA (7 U.S. C. §1, *et seq.*):

- Regulates commodity futures and swaps (except security-based swaps) and certain derivatives-industry professionals
- Prohibits customer abuse by registrants, fraud, market manipulation, or other disruptive trade practices
- Establishes various recordkeeping and reporting requirements for registrants and market participants and financial requirements for registrants
- Includes enforcement authority for fraud or manipulation of commodity contracts in interstate commerce

Enforced by:

- DOJ (criminal)
- CFTC (civil)
- Private causes of action
- Self-regulatory organizations (*e.g.*, NFA, designated contract markets (futures exchanges), and swap execution facilities)



Potential Sanctions for Violations

Civil and administrative sanctions are available under CEA Section 6(c)(10) for violations of CFTC regulations, and include, but are not limited to:

- Trading bans.
- Suspension or revocation of CFTC registration.
- Undertakings, such as requiring:
 - Implementation of specific policies and procedures.
 - Creation of new executive-level positions in risk and/or compliance.
 - Periodic reporting to the CFTC.
 - Additional document and/or data retention.
 - Periodic audits.
 - Mandatory training for employees.
 - Appointment of a monitor.
- Restitution.
- Disgorgement.
- 6(c)(10)(C) provides for civil monetary penalties for any person of not more than \$161,115 (adjusted annually for inflation) or triple the monetary gain **for each violation**.
- 6(c)(10)(C) provides for civil monetary penalties for any person of not more than \$1,162,183 (adjusted annually for inflation) or triple the monetary gain **for each violation** in cases of manipulation or attempted manipulation under 6(c) or 9(a)(2).



Potential Sanctions for Violations

- Criminal penalties are also available for willful, knowing violations of certain provisions of the CEA and CFTC Regulations.
- These include fines of up to \$1,162,183 per violation and imprisonment for not more than 10 years per violation.
- The Department of Justice may also bring criminal charges against institutions or individuals for:
 - Wire fraud (18 U.S.C. § 1343).
 - Commodity fraud (18 U.S.C. § 1348).
- Conspiracy charges also are possible and can carry even greater penalties.



B. THE FOREIGN CORRUPT PRACTICES ACT (“FCPA”)



The Foreign Corrupt Practices Act (“FCPA”)

Anti-Bribery Provisions (15 U.S.C. § 78dd-1, *et seq.*)

- Prohibit “use of the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of” a payment (of money or any other “thing of value”) to a foreign official, political party, party official, or intermediary, in order to secure a business advantage

Accounting Provisions (15 U.S.C. § 78m(b))

- Books and records provisions provide that books and records of covered securities issuers must accurately reflect transactions and assets
- Internal controls provisions require U.S. issuers to implement and maintain internal accounting controls adequate to reasonably ensure compliance with accounting, reporting, and oversight standards

Enforced by:

- DOJ (criminal)
- SEC (civil)



FCPA: Covered Persons

Anti-bribery provisions apply to:

- Issuers of securities on U.S. stock exchanges (15 U.S.C. § 78dd-1)
- U.S. persons and companies (“domestic concerns”) (15 U.S.C. § 78dd-2)
- Non-U.S. persons and companies engaged in prohibited conduct within the territory of the U.S. (15 U.S.C. § 78dd-3)

Accounting provisions apply to:

- Issuers of securities on U.S. stock exchanges (15 U.S.C. § 78m)



FCPA: Covered Persons

Agents and Other Representatives

- FCPA aiding and abetting and conspiracy liability may extend to additional persons and entities, including foreign agents, consultants, representatives, distributors, or JV partners of U.S. issuers and domestic concerns.
 - However, a non-U.S. national cannot be liable as an accomplice or co-conspirator if he did not commit any relevant acts while present in U.S. territory and did not act as the agent of a U.S. company in connection with the alleged scheme. *United States v. Hoskins*, 902 F.3d 69 (2d Cir. 2018).
- Foreign officials are not subject to the FCPA, and cannot be charged with conspiracy to violate the FCPA. *United States v. Castle*, 925 F.2d 831 (5th Cir. 1991).
 - However, DOJ has charged foreign officials with related crimes—such as money laundering—based on their receipt of bribes.



Potential Sanctions for Violations – Corporations

- \$2 million fine or up to twice the benefit gained from the bribe under anti-bribery provisions
- \$25 million fine under accounting provisions
- Disgorgement / Forfeiture / Restitution
- Criminal fines calculated under U.S. Sentencing Guidelines

Potential Sanctions for Violations – Individuals

- \$250,000 fine or up to twice the benefit gained from the bribe; up to five years imprisonment under anti-bribery provisions
- \$5 million fine; up to 20 years imprisonment under accounting provisions
- Disgorgement / Forfeiture / Restitution
- Criminal fines calculated under U.S. Sentencing Guidelines

Criminal Resolutions

Potential Collateral Consequences

- Debarment from entering into government contracts or other business transactions with government entities
- Suspension or bar from selling securities in the U.S., or restrictions on issuance of securities
- Imposition of independent compliance monitor
- Satellite or collateral litigation, such as derivative suits, class actions, and customer litigation, including under the securities laws or RICO
- Other related consequences: Goodwill, stock price, and burden



III. APPLICATION OF KEY PROVISIONS OF THE FCPA



FCPA Anti-Bribery Provisions

“Foreign Official”

- The statute defines “**Foreign Official**” as “any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.”

The FCPA also proscribes corrupt payments to:

- (1) foreign political parties;
- (2) officers of foreign political parties;
- (3) candidates for foreign political office; and
- (4) officials of public international organizations.



FCPA Anti-Bribery Provisions

“Instrumentality of a Foreign Government”

- **“Instrumentality of a foreign government”** has been construed broadly.
- A federal appeals court has defined the term to include any “entity controlled by the government of a foreign country that performs a function the controlling government treats as its own.” *United States v. Esquenazi*, 752 F.3d 912, 925 (11th Cir. 2014)

Examples may include:

- Fully or partially state-owned companies (including where government owns minority stake but exercises significant operational control or decision-making authority)
- Government-created, -owned, and -controlled commissions
- Other government-controlled entities that receive government funding, provide public services, and/or are led by government appointees



FCPA Anti-Bribery Provisions

“Anything of Value”

- **“Anything of value”** – Not defined by statute, and has been construed broadly in enforcement context
- Examples include:
 - Cash
 - Gifts
 - Meals
 - Entertainment
 - Travel
 - Reimbursements
 - Favorable terms in financial transactions such as loans and asset sales
 - Employment opportunities for relatives of foreign officials
- DOJ and SEC guidance emphasizes that there is no minimum threshold value.
 - The SEC has taken action based on the provision of gifts worth less than \$25,000.



FCPA Anti-Bribery Provisions

“Obtaining or Retaining Business”

Examples may include:

- Winning government contracts or licenses
- Obtaining reduced customs or tax liability
- Circumventing import rules
- Avoiding contract termination
- Gaining access to government-controlled markets



FCPA Anti-Bribery Provisions

Facilitating Payments

FCPA exempts “facilitating payments” made to expedite routine governmental action. (15 U.S.C. § 78dd-1(b).)

- Facilitating payments are permissible only when made in exchange for a benefit to which the payor is already entitled.
 - A payment made to encourage a discretionary act does not qualify as a permissible facilitating payment.
- Covered entities must accurately record all facilitating payments and should consider implementing stringent approval and documentation policies to govern such payments.
- Facilitating payments are not lawful in all jurisdictions.



FCPA Anti-Bribery Provisions

Reasonable and *Bona Fide* Expenditures

Examples of “reasonable and *bona fide*” expenses acknowledged by DOJ include:

- Travel and other expenses for site visits to company facilities
- Travel and other expenses for training programs or board meetings
- Travel and other expenses for product demonstrations or other promotional activities

Practical guidelines for assessing expenditures:

- Amounts of stipends and reimbursements should be reasonable in light of items identified.
- Companies should not provide additional stipends or spending money beyond what is necessary to pay for actual expenses incurred.
- All expenditures should be transparent, subject to internal approval, and accurately recorded in the company’s books and records.



FCPA Anti-Bribery Provisions

The Local Law Defense

- Affirmative defense for a payment that is “lawful under the written laws and regulations of the [recipient]’s country” at the time of payment.
- Defense is difficult to satisfy and has never been successfully invoked to defeat FCPA charges in litigation.
 - It is not sufficient to show the absence of any law prohibiting a payment in the recipient’s country.
 - Defendant must show that a written local law expressly permits the payment.
 - One federal court held that the defense was not satisfied where a local law absolved the payor of a bribe from liability in the event of extortion. *United States v. Kozeny*, 582 F. Supp. 2d 535 (S.D.N.Y. 2008).



FCPA Anti-Bribery Provisions

Intent

- Violation of the anti-bribery provisions requires a “corrupt” mental state.
 - FCPA legislative history states that “corrupt” signifies an “evil motive or purpose” or “an intent to wrongfully influence the recipient” of a payment. S. Rep. No. 95-114, at 10 (1977).
 - The Supreme Court has held that “[c]orrupt’ and ‘corruptly’ are normally associated with wrongful, immoral, depraved, or evil.” *Arthur Andersen LLP v. United States*, 544 U.S. 696, 705-06 (2005) (non-FCPA context).
 - The Fifth Circuit has held “that Congress intended for the FCPA to apply broadly to payments intended to assist the payor, either directly or indirectly, in obtaining or retaining business for some person[.]” *United States v. Kay*, 359 F.3d 738, 755 (5th Cir. 2004).
- Although a violation arguably requires an intent to exert wrongful influence, a violator need not know that its conduct violates the FCPA.



FCPA Anti-Bribery Provisions

Intermediary Payments

The anti-bribery provisions cover indirect payments to foreign officials.

- The FCPA prohibits making a payment to a third party (such as an agent or consultant) while “knowing” that the third party will transfer some or all of the payment to a foreign official for an improper purpose.

“Knowledge” can consist of:

- Awareness of a high probability
- Authorization after the fact
- Willful blindness or conscious avoidance



FCPA Anti-Bribery Provisions

Red Flags

“Red Flags” that could indicate potential corruption include the following:

- Contracts awarded to entities with no experience in the relevant field
- Payments for government contracts made to offshore accounts or indirectly to third parties
- Requests that payments or commissions be made in cash or in an unusual currency



FCPA Accounting Provisions

Books and Records

Common mischaracterizations of bribes include:

- Commissions
 - Consulting fees
 - Rebates or discounts
 - Intercompany accounts
 - Supplier or vendor payments
 - Charitable donations
 - Miscellaneous or other generic expenses
- Books and records include “[v]irtually any tangible embodiment of information made or kept by an issuer.” S.E.C. v. *World-Wide Coin Investments, Ltd.*, 567 F. Supp. 724 (N.D. Ga. 1983).
 - While covered entities must record transactions “in reasonable detail,” the books and records provisions do not require “a degree of exactitude and precision” that is “unrealistic.”



FCPA Accounting Provisions

Internal Controls

- The statute does not require implementation of any particular controls. Instead, the components required for an effective program depend on the specific risk profile of a business.

Elements of an effective program may include:

- Integrity and ethics policies
- Anti-corruption and anti-money laundering policies
- Risk assessment procedures
- Policies and procedures designed to ensure that management directives are carried out faithfully
- Information and communication systems
- Transaction and risk monitoring policies
- Employee training programs



FCPA Enforcement

DOJ FCPA Corporate Enforcement Policy

- DOJ announced FCPA enforcement policy in November 2017
- Presumed resolution by declination where company (i) voluntarily self-discloses, (ii) fully cooperates, and (iii) remediates, absent “aggravating circumstances.”
 - Sets forth factors considered by DOJ in assessing whether a company has satisfied these requirements.
- DOJ revised the policy in March 2019. The changes relate to:
 - (i) guidance on individual accountability in investigations of corporate wrongdoing,
 - (ii) corporate policies and controls regarding the use by employees of “ephemeral” messaging systems,
 - (iii) DOJ’s cooperation policy with respect to deconfliction requests, and
 - (iv) the application of the enforcement policy to acquiring companies in the M&A context.



IV. COMPARING THE FCPA AND THE CEA



Comparing the FCPA and the CEA

Substantive Application

	FCPA	CEA
Extraterritoriality	Extraterritorial application to U.S. persons and U.S. issuers. Jurisdiction over foreign non-issuers may be limited to actions taken in U.S.	Applies to conduct with a “direct and substantial” effect on U.S. markets
Substantive coverage/ Prohibition	Covers any offer, payment, promise to pay, or authorization of anything of value to a foreign government official	Covers “any manipulative or deceptive device or scheme to defraud,” similar to and modeled after §10(b) of Securities Exchange Act of 1934
Definition of “Foreign Official” within scope	“[A]ny officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization,” or any person acting in “official capacity for or on behalf” of any such entity	No definition of “foreign official” specified by statute
Exceptions/ Defenses	Limited exception for “routine government actions.” Limited affirmative defenses for lawful payments in other countries and reasonable and <i>bona fide</i> business expenses	No statutory exceptions or defenses similar to those in FCPA



Comparing the FCPA and the CEA

Self-Reporting Incentives

	FCPA Corporate Enforcement Policy	Advisory on CEA Violations Involving Foreign Corrupt Practices
Eligibility	Available where company (i) voluntarily self-discloses; (ii) fully cooperates; and (iii) remediates, absent “aggravating circumstances” such as executive or senior level involvement; pervasiveness of the misconduct, history of similar misconduct	
Incentive	Presumed resolution by declination If criminal resolution is warranted, 50% reduction off of the low end of U.S.S.G fine range, and generally no monitor requirement (if effective compliance program implemented)	Presumption of no civil monetary penalty for non-registrants that self-report; registered entities receive a “substantial reduction” for self-reports
Other penalties	Requirement that a company pay all disgorgement, forfeiture, and/or restitution resulting from the misconduct at issue “may be satisfied by a parallel resolution with a relevant regulator” (e.g., SEC)	CFTC will “appropriately account” for penalties imposed by other agencies, including “dollar-for-dollar credit” for other disgorgement or restitution payments



IV. KEY IMPLICATIONS FOR COMMODITY AND FUTURES MARKET PARTICIPANTS



Implications of CFTC's Expanded Focus

Additional complexity for foreign bribery matters:

- Self-reporting decisions
- Scoping and conducting internal investigations
- Negotiating settlements
- Potential for expanded extraterritorial focus of CFTC investigations



Looking Ahead

- CFTC officials have said there are multiple open investigations into matters involving foreign bribery.
- Companies with overseas business activities should monitor any publicized developments in these matters and begin considering connections between any foreign corruption concerns and possible CEA violations.
- It remains to be seen how the CFTC's expansion into the anti-bribery enforcement arena will affect the investigative and resolution burdens on participants in U.S. and non-U.S. commodity markets.



FIA

