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Financial Reform Law Establishes Financial Incentives for FCPA Whistleblowers

The President has just signed a law that will bolster the U.S. government's increasingly aggressive efforts to identify and pursue violations of the Foreign Corrupt Practices Act (FCPA). As part of the new financial reform legislation, the U.S. enforcement authorities will now pay potentially hefty awards to corporate whistleblowers who voluntarily provide original information that leads to an SEC enforcement action recovering monetary sanctions in excess of \$1 million.¹ Although this provision incentivizes whistleblowing with respect to a wide range of securities law violations, we focus here specifically on the ominous ramifications for FCPA compliance and enforcement. Among other things, we expect that this new law will place even greater pressure on companies to ensure that their overseas business practices are fully compliant with the FCPA.

Enacted in 1977, the FCPA has two basic parts. First, the FCPA anti-bribery provisions prohibit companies and individuals from providing, offering, or promising bribes to non-U.S. government officials.² Separately, the FCPA accounting provisions require that U.S. publicly-traded companies keep books, records and accounts that accurately and fairly reflect the companies' transactions, as well as establish a system of internal controls adequate to detect and prevent improper payments.³

In recent years, federal law enforcement authorities have prioritized both sets of provisions, and the Obama administration seems intent on continuing that trend.⁴ Prosecutions of companies and individuals for violations of the FCPA have increased dramatically - since 2006, the government has brought more FCPA cases than it did from 1977 to 2005 combined. Just last year, DOJ obtained more FCPA-related indictments, primarily of individual defendants, than over the previous seven years combined.

Not only is the number of FCPA enforcement actions on the rise, but the severity of the sanctions is also increasing. Since 2008, the U.S. authorities have negotiated the three largest FCPA settlements

For more information, contact:

Christopher A. Wray
+1 (202) 626 5570
cwray@kslaw.com

Zachary J. Harmon
+1 (202) 626 5594
zharmon@kslaw.com

Russell G. Ryan
+1 (202) 661 7984
rryan@kslaw.com

Courtney D. Trombly
+1 (202) 626 2935
ctrombly@kslaw.com

Brandon S. Long
+1 (202) 626 5441
blong@kslaw.com

King & Spalding
Washington, D.C.
1700 Pennsylvania Avenue, NW
Washington, D.C. 20006-4707
Tel: +1 (202) 737 0500
Fax: +1 (202) 626 3737

www.kslaw.com



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in history – an \$800 million settlement with Siemens,⁵ a \$579 million settlement with KBR/Halliburton,⁶ and, just this year, a \$400 million settlement with UK-based BAE.⁷

The new whistleblower legislation is the latest signal from the U.S. government that FCPA enforcement activity—including severe punishment for individual and corporate violators alike—will continue to be a priority at all levels of the government for the foreseeable future. The law states that whistleblowers who voluntarily provide information leading to the successful enforcement of U.S. securities laws, including the FCPA, “shall” receive a payment of between 10% to 30% of any enforcement action over \$1,000,000. The law is intended to elicit “original information” from whistleblowers who have independent information not already known to the SEC and not merely derived from existing investigations, audits, or reports. The SEC will have discretion to set the amount of the whistleblower award between 10-30%, based on the significance of the information to the success of the action, the whistleblower’s degree of assistance, and the interest of the SEC in using whistleblower payments to deter problematic conduct in the future.⁸

Sweetening the deal, the law also allows whistleblowers to be paid for information leading to “related actions” brought by DOJ and other federal and state enforcement bodies. To put this in perspective, if the law had been in force when the Siemens investigation originated, whistleblowers providing “original information” to the SEC would have netted between \$80 million and \$240 million in connection with the final DOJ and SEC resolutions.

For whistleblowers, this law provides extraordinarily lucrative incentives to report perceived misconduct; but for companies, it may signal a dramatic shift in how FCPA issues are identified, internally investigated, and potentially disclosed. Instead of reporting potential FCPA issues through appropriate internal company channels, where they can be investigated and remediated in accordance with the company’s internal compliance protocols, employees will have incentive to report issues directly to government enforcement authorities in hopes of securing an award. Even assuming that all employees act in good faith in such situations, the risk of unnecessary or unduly expensive investigations is very high. Once the conduct is reported, the government authorities may have only this whistleblower information in deciding whether to initiate investigations and, if so, how to scope the investigations. It remains to be seen whether government authorities will err on the side of caution, lacking much basis for evaluating the credibility of the whistleblower, the likelihood that the reported conduct could have occurred based on the company’s business models, the effectiveness of the company’s compliance programs, and other relevant factors. Whereas a company’s internal compliance and legal personnel may be intimately familiar with such important factors and details, government authorities are unlikely to have the benefit of such information when assessing a whistleblower’s allegation. Large or small, FCPA investigations can be extremely disruptive and expensive to a company, and the likelihood of unnecessary investigations may increase significantly in the face of such lucrative whistleblower incentives. For their part, whistleblowers will be well-insulated from internal reprimand by laws that criminalize whistleblower retaliation, as well as provisions in the bill establishing civil remedies for retaliation.

Moreover, since the U.S. FCPA authorities are adamant that companies receive meaningful benefits from the authorities when they self-report FCPA violations, this new law could encourage a race to disclosure.



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Specifically, both parties—the whistleblower and the company—will have significant incentives to be the first to report issues to the government. While this may seem like a positive development from a policy perspective, the FCPA authorities lack the time and resources to deal with untold numbers of preliminary, unsubstantiated, uninvestigated issues. This could lead to the unintended impact of incentivizing both whistleblowers and companies to race to the government with “placeholder” disclosures. In the case of whistleblower disclosures, the authorities may have no choice but to address these disclosures in some manner.

It is worth noting that, following on the heels of the newly-enacted whistleblower legislation, another bill, recently introduced by Vermont Representative Peter Welch and referred to the House Committee on Oversight and Government Reform, would in certain circumstances restrict companies found to be in violation of the FCPA from receiving contracts or grants from the U.S. government.⁹ We will continue to monitor this debarment bill as it undergoes the legislative process, and will offer important updates when appropriate.

Both pieces of legislation, the new whistleblower law and the debarment bill, reinforce the U.S. government’s continued resolve to stamp out corrupt behavior by U.S. individuals and companies that are operating outside of the United States, and the need for companies to be vigilant with respect to compliance in their overseas operations.

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This alert provides a general summary of recent legal developments. It is not intended to be and should not be relied upon as legal advice.

¹ Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. § 922 (2010), available at http://financialservices.house.gov/Key_Issues/Financial_Regulatory_Reform/Conference_report_final_2.pdf.

² 15 U.S.C. §§ 78dd-1, 78dd-2, 78dd-3.

³ 15 U.S.C. § 78m(b).

⁴ Officials at the highest levels of the U.S. government continue to make public statements promising aggressive prosecution of corruption. For instance, on May 31, 2010, in a speech before the Organisation for Economic Cooperation and Development (OECD), U.S. Attorney General Eric Holder proclaimed fighting corruption to be “one of the highest priorities of the Department of Justice.”

⁵ This amount includes \$450 million in fines paid to DOJ, along with \$350 million in disgorgement of profits to the SEC. In addition, Siemens paid \$856 million in fines and disgorgement to German authorities.

⁶ This amount includes \$402 million in fines paid to DOJ, and \$177 million in disgorgement to the SEC.

⁷ This amount represents payment of \$400 million in fines to DOJ. In addition, BAE settled claims with the UK Serious Fraud Office, agreeing to pay penalties of approximately \$50 million.

⁸ The SEC has been tasked with drafting rules and regulations that further define how this new program will be carried out.

⁹ Overseas Contractor Reform Act, H.R. 5366, 111th Cong. (2010), available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h5366ih.txt.pdf.