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THE FOREIGN CORRUPT PRACTICES ACT AND ITS APPLICATION TO U.S. BUSINESS OPERATIONS IN CHINA

Eric M. Pedersen*

INTRODUCTION

As a result of globalization, "every public company, private domestic concern and private equity/hedge fund [is] in direct contact with a U.S. federal statute and, in many cases, with foreign laws as well that prohibit the offer, promise to pay, payment, or gift of money or anything of value—in other words, as the statute sees it: bribes—to a foreign government official."1 This is particularly true in the Asian-Pacific region, which is home to some of the most robust trade and security partners of the United States. With China quickly assuming a prominent place in the global community,2 it has become extremely attractive to U.S. businesses and investors.3 Likewise, U.S. capital markets are the most attractive destination for Chinese initial public offerings.4

* The positions and opinions expressed in this article are those of the author and do not represent the views of the United States Government, the Department of Defense, or the United States Navy. The author (L.L.M., Georgetown University Law Center, 2007; J.D., Gonzaga University School of Law, 2000; B.S., Sam Houston State University, 1996) is an active duty Navy Judge Advocate, presently serving as a Trial Counsel in the Pacific Northwest. The author would like to thank Professor Jonathan C. Drimmer, of the Georgetown University Law Center, for his invaluable guidance, comments, and patience on earlier drafts of this article, without which this article would never have come into being; Kimberly N. Dobson and the staff of the Hofstra University Journal of International Business and Law for all of their hard work and diligence in preparing the final draft of this article; his parents Tom and Sally Pedersen for their unwavering love and support and for making everything possible; his friends Chris Shaver, Jeff Wilser and Tania Krebs for being the positive role models that got him on the right path and inspired him to go to law school; his supervisor Kim Hinson for her support and mentorship during the writing of this paper; his children Gregory and Abigail who remind him every day what is truly important in life; and his wife and best friend Heather for her love, patience and understanding throughout both his legal education and career endeavors.

3 Peter S. Goodman, China Market is Fertile Field for Bribes American Firms Run Afoul of Law, SEATTLE TIMES, Aug. 28, 2005, at E1.
4 Kevin Hamilton, Battling for China’s IPOs: The London Stock Exchange Wants a Piece of the
Unfortunately, corruption in China is a significant issue and while China has recently adopted extensive anti-corruption measures, significant concern still remains over the extent to which these measures will be enforced. Given the fact that corruption in China is widespread, and the government still owns and manages the country’s largest companies, compliance with the Foreign Corrupt Practices Act (hereinafter “FCPA”) can be exceptionally challenging for U.S. corporations that conduct business operations in China.

The Securities and Exchange Commission (hereinafter “SEC”) and the Department of Justice (hereinafter “DOJ”) have recently begun an aggressive enforcement approach to the FCPA—which has its grounding in securities law and gives dual jurisdiction to both the SEC and DOJ—due largely to “companies moving more aggressively into emerging markets like... China.” In the wake of numerous domestic corporate scandals (e.g. Enron and WorldCom), the new U.S. interest in the bolstering economy of China has led to increased international actions to combat corruption, as well as increased class action lawsuits against Chinese-based companies listed in the United States. With the recent increase in FCPA cases pursued by the DOJ and the SEC, it is imperative that U.S. companies conducting business operations in China comply with the FCPA.
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This article will examine the Chinese economy and the FCPA’s recent impact on U.S. corporations and investors who conduct, or are contemplating conducting, business operations in China. Part I of this paper will summarize the provisions of the FCPA. Part II will look at the economy of China and how its vast potential for economic growth has drawn U.S. businesses to the Far East. Part III will explore the problem China presently faces internally with corruption. Part IV will analyze several recent, high-profile FCPA cases brought against U.S. corporations that conducted business operations in China. Part V will highlight the unique application of the FCPA in China, including the heightened scrutiny the U.S.-half of a U.S.-China joint venture has to investigate activities of the Chinese-half. This section will also explore how the definition of a “foreign official” may differ in business dealings with communist China in contrast to other countries. Part VI will discuss the extent to which the FCPA puts U.S. businesses at a competitive disadvantage to their foreign counterparts who do not vigorously enforce anti-bribery laws. This paper concludes that the FCPA does, in fact, put U.S. businesses at a competitive disadvantage in China; a rapidly developing country with enormous investment potential, yet a considerable problem with corruption. However, this paper also recognizes that adherence to the FCPA remains critical in the current, ongoing, international battle against corrupt business activities. Part VII will explore two potential remedial measures that could modify and strengthen the FCPA to accomplish its worthy purposes without negatively impacting U.S. business activities abroad.

PART I: THE FOREIGN CORRUPT PRACTICES ACT

The FCPA was passed in the wake of the Watergate scandal in the 1970s.\(^\text{17}\) After its passage, SEC investigations uncovered over 400 cases of U.S. businesses involved in illegal or questionable payments to foreign government officials amounting to over $300 million.\(^\text{18}\) This “included some of the largest and most widely held public companies in the United States.”\(^\text{19}\) The discovered abuses ranged “from bribery of high foreign officials in order to secure some type of favorable action by the foreign government” to payments “made to ensure that government functionaries discharge certain ministerial [sic] or clerical duties.”\(^\text{20}\) Congress found the payment of bribes to influence the acts and decisions of foreign officials to be unethical, unnecessary and “bad business,” as it “eroded public confidence in the integrity of the [American] free


\(^{19}\) *Id.* at 4.

\(^{20}\) *Id.*
Therefore, in 1977 Congress enacted the FCPA as a means of discouraging the bribery of foreign officials and restoring integrity to the American business system.\textsuperscript{22}

\section*{A. FCPA Provisions}

The provisions of the FCPA can be broken down into two distinct parts: (1) the prohibition against the bribery of foreign officials by American corporations,\textsuperscript{23} and (2) the requirements for record-keeping and accounting practices that prohibit the establishment of undercover accounts used to finance illegal payments.\textsuperscript{24}

The FCPA’s anti-bribery provisions prohibit people and corporations from engaging in a variety of activities and transactions. The statute explains that issuers of certain U.S. securities – or any officers, directors, employees, or agents of the issuers – cannot use the mails, phone systems, internet or any other instrumentality of interstate commerce “in furtherance of an offer, payment, promise to pay, or an authorization to make an offer, payment, or gift” to any foreign official, foreign political party, or candidate for a foreign political office.\textsuperscript{25} This provision applies to any situation in which there is a “corrupt” purpose of either (i) influencing an act or decision of that foreign official, (ii) obtaining or retaining business, (iii) directing a business to a particular person, or (iv) to securing an improper advantage.\textsuperscript{26} Simply put, the FPCA makes it unlawful for U.S. persons, U.S. companies and certain foreign issuers listed on U.S. securities exchanges, to make payments to foreign officials for the purpose of obtaining or retaining business for or with, or directing business to, any person.\textsuperscript{27} A simple offer, promise, or authorization of a bribe will trigger a violation of the FCPA.\textsuperscript{28}

Although the FCPA does not apply directly to a foreign subsidiary of a U.S. business that engages in conduct that is prohibited by the FCPA, the U.S. parent business will be deemed to have violated the FCPA if they “authorized, directed, or controlled the activity in question.”\textsuperscript{29} This form of “knowledge” is

\begin{thebibliography}{9}
\bibitem{21} \textit{Id.}
\bibitem{24} 15 U.S.C. §§ 78m(a), 78m(b) (2000).
\bibitem{25} Id. (emphasis added).
\bibitem{26} Id.
\bibitem{27} See generally \textit{id.}
\bibitem{28} 15 U.S.C. §§ 78dd-1(a), 2(a), 3(a) (2000).
\bibitem{29} LAY-PERSON’S GUIDE TO FCPA, FOREIGN CORRUPT PRACTICES ANTIBRIBERY PROVISIONS, http://www.usdoj.gov/criminal/fraud/docs/dojdoch.html.
\end{thebibliography}
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inferred under the FCPA if a corporation "is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or such person has a firm belief that such circumstance exists or that such result is substantially certain to occur."\textsuperscript{30} "Knowledge" also includes "conscious disregard and deliberate ignorance."\textsuperscript{31}

The FCPA's record-keeping and accounting provisions are the lesser known, but equally important, aspects of the FCPA which were added to the Securities and Exchange Act of 1934.\textsuperscript{32} These record-keeping provisions require U.S. corporations to keep books, records and accounts in reasonable detail, in a way that fairly reflects their transactions and the dispositions of their assets.\textsuperscript{33} The FCPA's accounting provisions require that every issuer of securities (i.e. businesses with securities registered with the SEC under section 12 or required to file reports under section 15(d) of the Securities and Exchange Act of 1934) to:

(A) make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer;
(B) devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that—
   (i) transactions are executed in accordance with management's general or specific authorization;
   (ii) transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain accountability for assets;
   (iii) access to assets is permitted only in accordance with

\textsuperscript{31} LAY-PERSON'S GUIDE TO FCPA, supra note 29.
\textsuperscript{32} Securities and Exchange Act of 1934 §13(b)(2), amended by Act of July 30, 2002, 15 U.S.C.A. §78m(b)(2) (2002) ("Every issuer which has a class of securities registered pursuant to section 12 and every issuer which is required to file reports pursuant to section 15(d) shall--A. make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; B. devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that—i. transactions are executed in accordance with management's general or specific authorization; ii. transactions are recorded as necessary (I) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and (II) to maintain accountability for assets; iii. access to assets is permitted only in accordance with management's general or specific authorization; and iv. the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.")
management's general or specific authorization; and (iv) the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.\textsuperscript{34}

These provisions give "the SEC authority over the entire financial management and reporting requirements of publicly held United States corporations,"\textsuperscript{35} Their purpose is to prevent issuers from concealing bribes and, more specifically, to discourage fraudulent accounting and reporting practices. These provisions also provide a basis for ascribing liability to U.S. parent companies of foreign subsidiaries. Since these accounting provision violations do not require proof of criminal intent, a corporation can more easily be held strictly liable for the actions of a foreign subsidiary under the FCPA.\textsuperscript{36}

B. Exceptions to the FCPA's Anti-Bribery Prohibitions

The prohibitions of the FCPA are subject to three exceptions. The first, which came by way of an amendment to the FCPA in 1988, permits the use of "grease" or "facilitating" payments to foreign officials for the purpose of expediting or securing the performance of a routine governmental action.\textsuperscript{37} "Grease" payments are usually small payments to minor government officials that provide extra incentive to perform routine governmental action.\textsuperscript{38} The phrase "routine governmental action" refers to actions that a government official would regularly perform.\textsuperscript{39} Examples of routine governmental action would include "obtaining permits, licenses, or other official documents to qualify a person to do business in a foreign country;" "providing police protection;" "loading and unloading cargo;" "processing governmental papers, such as visas and work orders;" and priority in scheduling inspections.\textsuperscript{40} The second exception is for legitimate business purposes and allows a U.S. corporation to utilize its funds for the purpose of educating a foreign official about its business,
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product, or activities. The last exception to the prohibition of the FCPA allows for the payments of bribes in countries where bribery is legal. This exception requires that the law permitting bribery be in writing, and is therefore rarely, if ever, invoked.

C. Inside Information

In 1998, the FCPA was amended again to implement the Organization of Economic Cooperation and Development (hereinafter “OECD”) on Combating Bribery of Foreign Public Officials in International Business Transactions. This amendment made several significant changes in the FCPA, including broadening the jurisdictional reach of the FCPA to non-U.S. persons acting within the United States, as well as to U.S. persons outside of the United States. The amendments also prohibited making corrupt payments to a foreign official for the purpose of “securing any improper advantage” to obtain or retain business As amended, the FCPA not only prohibits:

[P]ayments to foreign officials not just to buy any act or decision, and not just to induce the doing or omitting of an official function “to assist . . . in obtaining or retaining business for or with, or directing business to, any person,” but also the making of a payment to such a foreign official to secure an “improper advantage” that will assist in obtaining or retaining business.

U.S. corporations can still fall under the umbrella of the FCPA for making corrupt payments even if the purpose of such payments is not necessarily to obtain business. If a foreign, state-owned business was to solicit bids for a new business and kept certain information confidential, then anything provided or anything offered of value for the purpose of obtaining disclosure of that confidential information may result in an FCPA violation.

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43 Id.
47 United States v. Kay, 359 F.3d 738, 754 (5th Cir. 2004).
Use of inside information from a foreign official can subject a corporation to liability under Rule 10b-5 of the Securities and Exchange Act of 1934, which prohibits the use of material, non-public information for the purchase or sale of a security. In addition, an employee of a U.S. corporation who makes a payment, or promises to make a payment to a Chinese foreign official for the purpose of obtaining confidential, non-public information may subject the business to liability under the FCPA.

D. Penalties for FCPA Violations

Violations of either the accounting or bribery provisions of the FCPA can subject individuals and/or corporations to both criminal and civil penalties. Individual officers, directors and employees of a company may be prosecuted for violations of the FCPA even if their company is not liable. Criminal violations can lead to substantial fines and prison terms. Civil liability can also result in considerable fines. Additionally, the SEC has been increasingly ordering U.S. businesses to disgorge any profits made through violations of the FCPA, which often results in businesses settling FCPA suits at practically double the cost of settlement. In addition to civil and criminal penalties, an individual or corporation found to be in violation of the FCPA may be subject to additional governmental actions such as barring a corporation from conducting business with the federal government, refusing export licenses, and possible suspension or debarment from programs provided by the Commodity Futures Trading Commission and the Overseas Private Investment Corporation.

E. FCPA Enforcement

The FCPA has had a significant impact on the manner in which U.S. corporations conduct foreign business operations. Since its enactment:

[s]everal firms that paid bribes to foreign officials have been the subject of criminal and civil enforcement actions, resulting in large fines and suspension and debarment from federal

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55 Leary et al., supra note 9.
56 See LAY-PERSON’S GUIDE TO THE FCPA, supra note 29.
57 Leary et al., supra note 9.
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procurement contracting, and their employees and officers have gone to jail. To avoid such consequences, many firms have implemented detailed compliance programs intended to prevent and to detect any improper payments by employees and agents. 58

Recently, the DOJ has affirmed its commitment to stamping out global corruption through aggressive enforcement of the FCPA. 59 This has been observed through a significant increase in investigations by the DOJ and SEC. 60 By 2006, 49 individual and corporate defendants had been prosecuted by the DOJ, resulting in over 27 plea agreements. 61 In addition, over 38 cases were disposed of by the SEC, resulting in agreements to avoid further violations of the FCPA and disgorgements of profits received as a result of the corrupt activities. 62 U.S. corporations that conduct business in China have been one of the focuses of recent FCPA investigations. 63

PART II: THE ECONOMY OF CHINA

During the era of Mao Tse-tung, the phrase “revolution is not a dinner party” illuminated the Maoist vision for the future of an internationally respected China. 64 Mao saw the concept of collective political consciousness as more important for the greater good of the nation than material incentive, which was the goal of the corrupt and economically disparate Nationalist regime of the time. 65

After the death of Mao Tse-tung, Deng Xiaoping became the leader of the Communist Party of China and greatly reformed the Chinese economy based on economic development and market-oriented policies. 66 These economic reforms, which began in the late 1970's, led to an increase in economic growth in China which has astonished the world. “Between 1979 and 1997, the growth

58 See LAY-PERSON'S GUIDE TO THE FCPA, supra note 29.
60 Olson, supra note 12.
62 Id.
63 Olson, supra note 12.
65 Id.
66 Id.
rate of China’s Gross Domestic Product (GDP) was 9.8 percent annually.”  
Economic reforms have also led to a “gradual liberalization of prices,” fiscal transference, increased independence for state enterprises, “development of stock markets,” the “growth of the non-state sector,” the groundwork for a “diversified banking system,” and the overall “opening to foreign trade and investment.”

The worldwide growth rate has received the largest contribution from China since it joined the World Trade Organization (WTO) in 2001. Since 2003, China’s economy has grown an astonishing 10 percent each year and will likely increase 7 percent annually until 2020, when it is predicted to become the second largest economy in the world, behind the United States.

In the year 2004:

Americans spent $162 billion more on Chinese goods than the Chinese spent on U.S. products. And that gap has been growing by more than 25 percent per year, as China moves from building toys and tchotchkes into more-sophisticated appliances, auto parts, and semiconductors. China’s consumer class, meanwhile, is spending like lottery winners on everything from bagels to Bentleys—and will soon outnumber the entire U.S. population. China’s explosive growth “could be the dominant event of this century,” says Stapleton Roy, former U.S. ambassador to China. “Never before has a country risen as fast as China is doing.”

Recent developments indicate that the economy of China sees no signs of slowing, nor does the government desire the tapering off of its incredible development. In 2003, Chinese leadership claimed it would “continue to focus on the country’s economic development, with a goal to quadruple the country’s gross domestic product (GDP) within 20 years.” In 2006, the Chinese government announced its Five-Year Plan which states China’s intention to

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67 Id.
71 See Newman, supra note 70.
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pursue policies designed to improve the following five different areas of the Chinese society:
(a) growth in domestic consumption and exports to international markets
(b) development of inland and rural coastal areas
(c) development of rural and urban areas
(d) promotion of a harmonious society and economic growth, and
(e) the needs of both the environment and man. 73

Today China is the “fastest growing economy in the world,”74 and with its economy flourishing in ways never imagined, China has become an attractive place for U.S. corporations to conduct operations and investments. This is due not only to China’s “low-cost manufacturing facilities” and its “market for high-technology goods,”75 but also to its “good infrastructure, an educated workforce,” a soaring “rate of saving available to finance investment,” and its open economy.76

A study conducted by the U.S.-China Business Council (USCBC), revealed that 81% of U.S. businesses reported that their China operations were profitable.77 Additionally, more than half of those businesses claimed that profitability rates for their operations in China either met “or exceed[ed] their company’s global profit margin.”78 Former White House Council of Economics Advisor Kristen Forbes noted that “[c]ompanies are seeing some of their fastest growth in China, and it’s profitable growth.”79 Another commentator has noted that “China has become a magnet for investment and a huge potential market beckoning with growth.”80

Deng’s shift away from Maoist principles significantly paved the way for the present state of the economy in China. Consequentially, the shift away from the Maoist principles of an economically equal and internationally respected China have been pushed aside in favor of a new aphorism; one that encapsulates China today: “To get rich is glorious.”81
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PART III: CORRUPTION IN CHINA

United States businesses and investors seeking to take advantage of the lavish economic opportunities in China face challenging FCPA issues primarily because corruption is so widespread in China and its largest companies are owned and managed by the Chinese government. The battle against corruption in China, while not optimistically viewed, nevertheless seems to be an emerging theme of the Chinese government.

A. Climate of Corruption

Despite being an economy of unlimited economic potential, "[c]orruption in China is a significant issue." While China has enacted many extensive anti-corruption laws, enforcement of these laws is ostensibly driven by political concerns rather than an effort to fix the problem.

Transparency International is a global organization, influential among investors and traders, that performs assessments and opinion surveys on the perceived levels of corruption in over 150 countries. In its 2006 report, China was given a score of 3.3 on its 1 – 10 scale, with one being the most corrupt and ten being the least corrupt. A study done by the Carnegie Endowment for International Peace revealed that corruption in China accounted for approximately 13-16% of its gross domestic product. Angang Hu, of the Center for Chinese Study noted that "[c]orruption looms as one of the biggest political and economic challenges that faces China in the twenty-first century.

Between December 2002 and November 2003, there had been 174,580 leading officials at various levels across China disciplined for violations of anti-corruption laws. This figure includes 6,043 at the county level and 21 at the ministerial level. In the year 2004, over 500 Chinese suspects – most of whom were public officials - had violated various anti-corruption laws. In the first

82 Boltz, supra note 7.
83 See id. at 30-31.
85 Id.
87 Id.
ten months of 2006, China was faced with 8,010 cases involving commercial bribery, amounting to the equivalent of $110 million U.S. dollars.90

China has become “increasingly plagued by government officials and executives of state-owned companies who abscond with a large sum of public money and flee overseas to escape from prosecution and punishment.”91 Chen Liangyu, China’s Chief of Shanghai, was recently implicated in a corruption scandal involving the misuse of the Shanghai’s public social security fund.92 Tian Fengshan, former governor of Heilongjiang Province and former minister of land and resources in China, was recently sentenced to life in prison for accepting over 4.36 million yuan (approximately $538,000) in bribes.93 Both the former vice-mayor of Beijing and the former head of the National Statistics Bureau were also recently removed from their positions after corruption charges came to light.94 Other high ranking Chinese officials caught in acts of corruption included the top procurator of Tianjin, former vice governor of Anhui and former deputy head of the Jiangsu provincial legislature.95 The former vice director of China’s Assets Supervision and Administration Commission of Hainan Province, was recently tried and sentenced to life imprisonment for taking bribes totaling over 4 million yuan (approximately $513,000).96 Crimes committed by government officials in charge of state-owned enterprises have become a commonality in China, accounting for 41.5% of all corruption and bribery cases that were investigated in 2004.97

The increasing issue of corruption in China has been blamed on a litany of factors. Some argue that the low pay of China’s government officials has driven them to illegally seek additional income.98 Others argue that “China-based companies simply conclude that a certain amount of corruption is necessary to remain competitive, and they are willing to live with the risk of

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91 China to Ratify UN Convention Against Corruption, supra note 89.
94 President Hu Charts Path in Anti-Corruption Drive, supra note 92.
95 China’s Anti-Corruption Drive Fruitful, supra note 90.
98 Zengke He, Corruption and Anti-Corruption in Reform China, 33 COMMUNIST AND POST-COMMUNIST STUDIES 243, 251 (2000).
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possible government action against them.” Moreover,

[T]he most lucrative corruption occurs in the overlap of government or party authority with private enterprise, where business operators need official approval to acquire land, win contracts or make sales. Inducements in such transactions remain off the books, thus difficult for auditors to catch.}

This places U.S. businesses in the complex dilemma of balancing the desire to take advantage of the lucrative Chinese economy with complying with the FCPA and thereby avoiding problems with the DOJ and SEC. Compliance is even more problematic in a nation where business deals typically involve gift-giving and entertaining. Several U.S. multinational corporations have admitted that “their firms routinely win [Chinese] sales by paying what could be considered bribes or kickbacks...to purchasing agents at government offices and state owned businesses.”

B. Anti-Corruption Efforts in China

In a recent address to the Chinese Communist Party (CCP), disciplinary body President Hu Jintao emphasized China’s anti-corruption efforts. With the milieu of high-profile corruption cases which plagued China in early 2007, investigations into the behavior of foreign officials and commercial businesses have significantly increased. Chinese leadership has recognized that corruption is a problem, one that “could destroy the Communist Party.”

Corruption has a variety of significant effects on a country. It “distorts markets and competition, breeds cynicism among citizens, undermines the rule of law, damages government legitimacy, and corrodes the integrity of the private sector. It is also a major barrier to international development—systemic misappropriation by kleptocratic governments harms the poor.”

On October

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99 Boltz, supra note 7, at 31.
102 Goodman, supra note 3.
104 Id.
106 Corruption in China, supra note 6.
107 Ben W. Heineman, Jr. & Fritz Heimann, The Long War Against Corruption, FOREIGN AFF.
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31, 2003, the United Nations (UN) General Assembly adopted the Convention against Corruption,\(^\text{108}\) which essentially acknowledged the aforementioned statement as a problem on a global scale. The Convention imposed numerous requirements on its signatories to take affirmative steps to criminalize corruption and implement mechanisms to combat international crimes of corruption.\(^\text{109}\) The convention was “widely supported by developing countries”\(^\text{110}\) and was ratified by China in 2005 in an aggressive step to deal with its overwhelming problem with corruption.\(^\text{111}\)

China recently announced plans for the establishment of the Corruption Prevention Bureau as a means of fulfilling its obligations under the UN Convention against Corruption.\(^\text{112}\) Unfortunately, these plans have been criticized for lack of investigative power and for providing too much objective governmental discretion as to which officials will be investigated and prosecuted.\(^\text{113}\) The Chinese government, overall, has faced wide-spread international criticism for taking little action to deal with foreign multinationals for making corrupt payments.\(^\text{114}\) Overall efforts to address the problem of corruption have been criticized as being “half-hearted.”\(^\text{115}\) One commentator noted that “many China-based companies operate on a day-to-day basis with a lot fewer restrictions than companies in the United States despite the existence of numerous laws and regulations in China.”\(^\text{116}\) China has complex anti-bribery laws that are very similar to the FCPA in that they prohibit corrupt payments to foreign officials and kickbacks in commercial transactions, but these laws are never consistently or rigorously enforced.\(^\text{117}\) In fact, a recent OECD report criticized China for its weak enforcement of its multinational anti-corruption covenants.\(^\text{118}\)

Since corruption continues to be a more significant threat in China than in other nations, U.S. corporations conducting business operations in China are under constant exposure to FCPA actions initiated by either the DOJ or the SEC. The recent trend in enforcement activities illustrates the severity of

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\(^{109}\) Id.


\(^{111}\) China to Ratify UN Convention Against Corruption, supra note 89.

\(^{112}\) Corruption in China, supra note 6.

\(^{113}\) Id. at 44.


\(^{115}\) Corruption in China, supra note 6.

\(^{116}\) Boltz, supra note 7 at 28.

\(^{117}\) Dufree, supra note 5.

\(^{118}\) DeWoskin & Stones, supra note 105.
criminal and civil penalties arising from FCPA violations.

PART IV: RECENT FCPA ENFORCEMENT ACTIONS INVOLVING U.S.-CHINA BUSINESS OPERATIONS

Several recent, high-profile cases illustrate how U.S. corporate undertakings with China have led to FCPA actions brought by the DOJ and SEC.\(^{19}\) As one commentator noted "China has not loomed large in the U.S. caseload, but that is changing fast."\(^{10}\) The FCPA violations involving Diagnostic Products Corp., Schnitzer Steel Industries, Lucent Technologies, Inc. and InVision Technologies, Inc. serve to highlight this growing trend.

A. Diagnostic Products Corporation

Diagnostic Products Corporation (hereinafter "DPC") was a "producer and seller of diagnostic medical equipment" based in Los Angeles, California.\(^{121}\) DPC Tianjin Co. Ltd., was a wholly-owned subsidiary of DPC in China.\(^{122}\) From 1991 to 2002, DPC Tianjin made cash payments in the amount of $1.6 million to physicians and laboratory personnel who controlled purchasing decisions at various state-owned hospitals in China.\(^{123}\) The purpose of these payments was to obtain and retain business with these hospitals.\(^{124}\) Payments were usually made in cash and delivered either by DPC Tianjin's employees by way of mail or wire transfer.\(^{125}\) This practice, which was authorized by the general manager of DPC Tianjin, involved transactions with personnel who met the definition of "foreign officials" under the FCPA because they were employed by hospitals owned by the Chinese government.\(^{126}\) These corrupt payments were all recorded in DPC Tianjin's books and records as legitimate sales expenses.\(^{127}\)

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\(^{19}\) Leander, supra note 61.

\(^{10}\) Id.

\(^{121}\) Press Release, Dep't of Justice, DPC (Tianjin) Ltd. Charged with Violating the Foreign Corrupt Practices Act (May 20, 2005), available at http://www.usdoj.gov/opap/pr/2005/May/05_crm_282.htm

\(^{122}\) Id.

\(^{123}\) Id.

\(^{124}\) Id.


\(^{126}\) See Press Release, Dept of Justice, (DPC), supra note 121.

\(^{127}\) In the Matter of Diagnostic Products Corp., supra note 125.
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DPC pled guilty to violating the FCPA’s anti-bribery provisions and agreed to pay a criminal penalty of $2 million.\(^{128}\) As part of their plea agreement, DPC agreed to cooperate with ongoing DOJ and SEC investigations and to the appointment of an independent compliance consultant to monitor the implementation of “new internal policies and procedures.”\(^{129}\) In addition to action taken by the DOJ, the SEC ordered the DPC to cease and desist from further violations of the FCPA and to disgorge approximately $2.8 million in ill-gotten gains, which represented DPC’s net profit in China during DPC Tianjin’s misconduct.\(^{130}\)

B. Schnitzer Steel Industries

In October 2006, SSI International Far East Ltd. (hereinafter “SSI Korea”), which was a subsidiary of Schnitzer Steel Industries Inc. (hereinafter “Schnitzer Steel”), pled guilty in federal district court to violations of the FCPA, including violations of the FCPA’s anti-bribery and record keeping provisions.\(^{131}\) SSI Korea facilitated Schnitzer Steel’s buying and reselling of metal, including the sale of scrap metal by Japanese suppliers, to steel mills in China and South Korea.\(^{132}\) Over a five-year period between September 1999 and August 2004, SSI Korea made approximately $1.8 million dollars in corrupt payments “to officers and employees of nearly all of Schnitzer Steel’s government-owned customers in China and private customers in China and South Korea.”\(^{133}\)

SSI Korea wired money for the corrupt payments to secret bank accounts in South Korea, which were opened by the head of SSI Korea for the purpose of receiving such payments.\(^{134}\) The funds were then used to make corrupt cash payments to the managers of Schnitzer’s customers.\(^{135}\) SSI also gave gifts to managers of their government-owned customers.\(^{136}\) A senior official at Schnitzer Steel was aware of the corrupt payments and did, in fact, authorize the wire transfers of the money to the secret bank accounts.\(^{137}\)

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\(^{128}\) See Press Release, Dept' of Justice, (DPC), supra note 121.

\(^{129}\) Id.

\(^{130}\) In the Matter of Diagnostic Products Corp., supra note 125.


\(^{132}\) Id.

\(^{133}\) Id.


\(^{135}\) Id.

\(^{136}\) Id.

\(^{137}\) Id.
Japanese companies also provided SSI Korea with money to make corrupt payments to managers of the Chinese steel mills. SSI Korea would then deliver the money to the managers of the Japanese steel mill customers. Corrupt payments were made by SSI Korea, on behalf of their Japanese customers, to managers of Chinese government-owned steel mills in approximately eight different transactions. These payments were recorded in Schnitzer Steel’s books and records as refunds, rebates, sales commissions, and commission to the customer.

The payments to managers of government-owned customers in China amounted to over $204,000, while payments to private companies amounted to over $1.6 million. These payments were made to “managers of private customers in South Korea and private and government owned customers in China to induce them to purchase, and to secure an improper advantage with respect to the purchase of scrap metal from Schnitzer Steel.”

Profits derived from these corrupt payments included “realized gross revenue of approximately $602,139,470 and profits of approximately $54,927,319 on scrap metal sold to private sector Chinese and South Korean customers, and gross revenue of approximately $96,396,740 and profits of approximately $6,259,104, on scrap metal sold to government instrumentalities in China.”

As part of a deferred prosecution agreement entered into with the DOJ, Schnitzer Steel agreed to pay a criminal fine of $7.5 million and to “accept responsibility for the conduct of its employees, and the employees of its subsidiary, in making corrupt payments and aiding and abetting the making of false books and records entries; to adopt internal compliance measures; and to cooperate with ongoing criminal and SEC civil investigations.” Finally, given the fact that Schnitzer Steel had never provided training to its employees on the requirements of the FCPA and failed to monitor its employees, the parent company also agreed to the appointment of an independent compliance consultant to review and monitor the implementation of a FCPA compliance program.

In addition to criminal penalties, Schnitzer Steel incurred civil penalties from the SEC. Schnitzer Steel was ordered by the SEC to “cease and

138 Id.
139 Id.
140 Id.
141 Id.
142 Press Release, Dep’t of Justice, (Schnitzer), supra note 131.
143 Id.
144 Id.
145 Id.
146 In the Matter of Schnitzer Steel Industries, Inc., supra note 134.
147 Press Release, Dep’t of Justice, (Schnitzer), supra note 131.
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desist from committing or causing any violations and any future violations of Sections 13(b)(2)(A), 13(b)(2)(B), and 30A of the Exchange Act." Finally, Schnitzer Steel agreed to pay a civil fine in the amount of approximately $7.7 million to the United States Treasury.

C. Lucent Technologies, Inc.

Lucent Technologies, Inc. (hereinafter “Lucent”) was a telecommunications equipment operator with operations in China that “accounted for 11 per cent of its revenue” for the 2003 fiscal year. During an internal audit and subsequent investigation, Lucent discovered incidents and deficiencies in its internal control program for its operations in China that amounted to violations of the FCPA. Internal auditors also found that Lucent’s executive officials had bribed Chinese officials at state-owned telecommunications companies.

In September 2006, the SEC “warned Lucent Technologies to expect an ‘enforcement action’ over violations of the Foreign Corrupt Practices Act (FCPA) by executives at its Chinese operations.” This came even after Lucent fired four executives of its Chinese operations including the president, the chief operating officer, marketing executive and a finance manager. Like Schnitzer Steel, Lucent disclosed these violations to both the SEC and the DOJ. As of this writing, final disposition in this matter is still pending.

D. InVision Technologies, Inc.

InVision Technologies, Inc. (hereinafter “InVision”) was a company based in California that sold airport security screening products that were designed to detect explosives in passenger luggage. An investigation by the

148 In the Matter of Schnitzer Steel Industries, Inc., supra note 134.
149 Id.
152 Goodman, supra note 3.
155 Gold, supra note 151.
156 Dep’t of Justice, InVision Technologies Enters into Agreement with the United States, (Dec. 6,
DOJ and SEC revealed that from June 2002 through June 2004, InVision was aware of the high probability that some of its foreign sales agents and independent distributors in China were paying bribes in the amount of $95,000 to foreign government officials to obtain business for the company. Despite this knowledge, InVision still authorized payments to these agents or distributors, and allowed them to conduct these transactions on InVision’s behalf. These corrupt payments were recorded in InVision’s books and records as the cost of goods sold.

InVision paid a $500,000 criminal penalty for their violations of the FCPA. Additionally, the SEC issued a cease and desist order, directing InVision to pay disgorgement and mandating both independent consultation for management of InVision’s books and records as well as the implementation of an FCPA compliance program.

PART V: THE FCPA’S APPLICATION TO U.S. BUSINESS OPERATIONS IN CHINA

Recent enforcement actions by the DOJ and SEC illustrate how business operations in China present unique FCPA concerns for U.S. corporations hoping to take advantage of the booming Chinese economy. The corruption level in China substantially increases the duty of a U.S. corporation to investigate, and assume responsibility for, the Chinese-half of any U.S.-China joint venture. Additionally, with a great number of Chinese businesses still under the control or outright ownership of the Chinese government, U.S. corporations are constantly faced with the unique problem of determining who is a “foreign official” for purposes of the FCPA. These issues present very serious and significant challenges to U.S. corporations.

A. Joint Ventures in China

A joint venture is defined as “a business undertaking by two or more persons engaged in a single defined project. The necessary elements are: (1) an express or implied agreement; (2) a common purpose that the group intends to carry out; (3) shared profits and losses; and (4) each member’s equal voice in
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controlling the project."162 Usually joint ventures are formed when two parties have a unique contribution of resources to make towards the development of a commercial opportunity in a specific market, but neither party has all of the necessary resources to develop the opportunity.163 The U.S.-half of the joint venture will usually contribute the resources it has available in its own domestic market such as capital, trademarks, technology, management and any expertise with regard to the particular opportunity.164 The foreign-half of the joint venture may contribute the same resources as its joint U.S. counterparts. However, the foreign-half may contribute resources to the joint venture that would be expensive, if not impossible, for the U.S.-half to acquire. These resources may include insight into local customs and cultures, language skills, foreign business expertise, and most importantly, the right to pursue the foreign opportunity that would otherwise be limited by the laws of the foreign nation.165

In 1979, China passed the Sino-Foreign Equity Joint Venture Law, which was followed by a flood of similar legislations designed to promote investment in China.166 Joint ventures between U.S. and Chinese businesses are usually attractive ways for a U.S. business to take advantage of the Chinese market. Many U.S. businesses have come to the realization that in order to be competitive in domestic markets it is imperative to compete in global markets as well. The 1990’s saw a substantial increase in “foreign direct investment (FDI) and research and development (R&D)-related activity” by U.S.-owned businesses in China.167 This was significantly noticeable in China’s information technology sector, which saw a number of businesses increasing their technology development activities, to exploit China’s technological capabilities.168 The investments of U.S. corporations in China almost quadrupled between 1994 and 2001.169 Companies such as Ford, DuPont, Ford, IBM, Lucent Technologies, General Electric, Microsoft, General Motors, Motorola, Intel, and Rohm and Haas have taken part in international joint ventures in China.170 These joint ventures have provided opportunities for U.S. businesses to market directly to China. Unfortunately, these profitable opportunities have also led to heightened risk of violations of the FCPA.

162 BLACK’S LAW DICTIONARY (8th ed. 2004).
164 Id.
165 Id.
166 Id.
167 Id.
170 Id.
171 Id. at 2.
A U.S.-China joint venture runs an unreasonably substantial risk of FCPA violations for three reasons. First, the U.S.-half of the joint venture will usually lack control of general business operations. Second, the joint venture will most likely be largely owned by a Chinese entity that is accustomed to making or receiving corrupt payments. Finally, there is always a substantial risk that the Chinese entity will have some level of government ownership or control, thus rendering it a "foreign official" for purposes of the FCPA.

B. "Foreign Officials" in China

The FCPA only deals with corrupt payments made to foreign government officials, thus excluding the making of such payments to foreign persons who are not governmental officials. One of the more complex problems a U.S. corporation faces when doing business in China is determining exactly who falls into the category of a "foreign official." The FCPA defines a "foreign official" as:

[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 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.

In an FCPA opinion released in 1993 regarding a joint venture between a U.S. commercial organization and a commercial entity that was owned and supervised by a foreign government, the DOJ interpreted the phrase "officer or employee of a foreign government" to include government-owned businesses. This interpretation is also supported by the Organization for Economic Cooperation and Development Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which defined a "foreign public official" as:

[A]ny person holding a legislative, administrative or judicial office of a foreign country, whether appointed or elected; any person exercising a public function for a foreign country, including for a public agency or public enterprise; and any official or agent of a public international organization.


173 Org. for Econ. Co-operation & Dev., OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which defined a "foreign public official" as:

[A]ny person holding a legislative, administrative or judicial office of a foreign country, whether appointed or elected; any person exercising a public function for a foreign country, including for a public agency or public enterprise; and any official or agent of a public international organization.
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This presents a significant problem for U.S. businesses seeking to conduct business in China where “state-owned firms. . .are among the largest in China and include more than half the country’s industrial assets.” Most businesses that are listed on the Chinese stock exchanges are state owned enterprises with strong links to the government. Moreover, there is a tendency in China for business personnel to simultaneously hold multiple positions in the government or political arena. Thus, it is highly likely that the DOJ and SEC would view a senior executive of a large Chinese company as a “foreign official” for purposes of the FCPA.

The case involving Diagnostic Products (discussed in part IV, A) was a perfect example of the DOJ concluding that government-owned hospitals in China were government instrumentalities, thus rendering the physicians and laboratory personnel “foreign officials” under the FCPA. Despite an apparent move by China to begin the privatization of state owned enterprises, several questions still remain regarding a Chinese business that is not completely controlled by the state. Given the lack of clear guidance, U.S. corporations are forced into a precarious position where they must assume that everyone they deal with in China will fall into the category of a “foreign official.”

PART VI: IS THE FCPA PUTTING THE UNITED STATES AT A COMPETITIVE DISADVANTAGE IN CHINA?

One of the prevalent, on-going criticisms of the FCPA is that it puts U.S. businesses at a competitive disadvantage compared to their foreign counterparts who are under no such rigorous anti-bribery restrictions as the FCPA. In 1998 Congress realized that since the enactment of the FCPA, U.S. businesses “operated at a disadvantage relative to foreign competitors

Public Officials in International Business Transactions (Nov. 21, 1997), available at http://www.oecd.org/documentprint/0,3455,en_2649_37447_2017813_1_1_1_37447,00.html.

The Long and Winding Road to Privatization in China, supra note 8.


Dep't of Justice, supra note 121.


who...continued to pay bribes without fear of penalty.” With corporate protests over the FCPA growing, Congress directed the Executive Branch to begin negotiations with the Organization of Economic Cooperation and Development (OECD) to encourage the major trading partners of the United States to enact laws similar to the FCPA. Members of the Convention were required to implement laws criminalizing the bribery of foreign officials. The end results of the OECD Convention have been criticized due to conflicting laws that were subsequently enacted by the member nations, and an overall lack of uniform enforcement of anti-bribery provisions. Howard Weissman, Associate General Counsel-International of Lockheed Martin Corporation, noted:

I believe that some progress has been made in raising the awareness of non-U.S. companies of the need for anti-bribery compliance. I do not believe, however, that the “playing field” has been leveled yet for U.S. companies. I do not think this will happen until some of the other OECD countries have actually brought enforcement actions and imposed penalties on companies and individuals within their jurisdictions for directly or indirectly paying or offering bribes to foreign officials.

Critics of OECD, as well as other anti-corruption efforts, have been quick to point out the limited impact and enforcement of its measures and have also expressed pessimism on the prospects of any quick and efficient changes in the global business environment. A study conducted by World Bank concluded that “US anti-corruption legislation and the OECD anti-bribery Convention, were not leading ‘to higher standards of corporate conduct among foreign investors’.” The United States, therefore, remains at a competitive business disadvantage with other nations that conduct business operations in China and do not enforce the provisions of OECD or their own anti-bribery provisions as vigorously as the U.S. government enforces the FCPA. Moreover,

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China is not an OECD member nation and with the exception of a minor, distended corruption project of the Asia-Pacific Economic Cooperation (hereinafter "APEC"), Asia has no regional convention to deal with corruption.

The FCPA has not reduced corruption in other countries mainly because foreign countries that have no firm anti-corruption laws, or simply do not aggressively enforce the laws they do have, are eager to seize a business opportunity that a U.S. corporation could not take due to the FCPA. As a result, U.S. business operations have been significantly curtailed in emerging countries such as China. In fact, a survey of 250 of the top 1000 businesses in the United States by the General Accounting Office resulted in 30% of the respondents claiming that the FCPA had a negative impact on its overseas business operations. A study of the FCPA, conducted by the John F. Kennedy School of Government at Harvard University, revealed not only a significant decline in U.S business operations in corrupt countries since the enactment of the FCPA, but also a shift from the U.S. to foreign countries that were more willing to make corrupt payments. The study concluded that:

The apparent relative decline of American business activity in the more-corrupt countries after 1977 does not necessarily imply US legislation reduced total levels of foreign business activity, or even bribe payments by foreign multinationals, in these countries. The reason is that foreign firms may simply have replaced American firms in the more bribery-intensive activities in these countries, either by acquiring US operations or through the withdrawal of US firms from the market.

187 Organisation for Economic Co-operation and Development, Ratification of the Convention on the OECD, http://www.oecd.org/document/58/0,2340,en_2649_201185_1889402_1_1_1_1,00.html (listing the OECD member nations as Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom and United States).


legislation in 1976 and 1977 changes the relative attractiveness of more-corrupt and less corrupt locations for US investors, thereby encouraging ownership substitution between American and foreign investors.\textsuperscript{192}

The evidence is conclusive that the FCPA does, in fact, cause U.S. corporations to lose significant business opportunities in transitional economies such as China.

Corruption remains an unsettling issue in China; one that is, according to Prime Minister Wen Jiabo, becoming “more and more serious” and one that Chinese leadership has been criticized for failing to aggressively pursue.\textsuperscript{193} Nevertheless, if the United States is to remain competitive in a fast-paced, global environment, it cannot ignore or significantly reduce its business dealings in China. With a population of over 1.3 billion people\textsuperscript{194} – amounting to roughly one-sixth of the world’s population\textsuperscript{195} – and the expectation that China will be the world’s top trading nation in the next ten years,\textsuperscript{196} U.S. businesses simply cannot afford to cut themselves out of that customer base. China’s transition from a non-capitalist regime to a modern economy raises questions as to whether the United States should continue in its lonely quest to discourage corrupt payments through enforcement of the FCPA.

\textbf{PART VII: AMENDING, RELAXING OR REPEALING THE FCPA}

The vagueness of the FCPA, the current trend in government enforcement actions, and the lack of clear guidance by which U.S. businesses can legally operate, renders the Act unworkable in China’s current climate of corruption. Therefore, the intricate conflict between the need to take advantage of the thriving Chinese economy and the competitive disadvantage the United States presently faces, requires that the FCPA be revisited to determine what steps, if any, should be taken to modify, strengthen or abolish the Act together.

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{192} \textit{Id.} at 19-20.
\item \textsuperscript{193} \textit{Corruption in China}, supra note 6 at 44.
\item \textsuperscript{194} Central Intelligence Agency, The World Factbook, supra note 68.
\item \textsuperscript{195} \textit{Id.} (stating that the world population as of July 6, 2007 was 6.6 billion which was used to derive this fraction) available at https://www.cia.gov/library/publications/the-world-factbook/print/xx.html.
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A. Repealing the FCPA: A Duplicitous Act

While a U.S. corporation may be at a competitive disadvantage with other nations that do not rigorously enforce their anti-corruption laws, FCPA compliance remains critical for three reasons, aside from avoiding DOJ and SEC criminal and civil liability. The first reason is the recent international recognition of the negative impacts of corruption on a global level and the subsequent efforts to curtail corrupt international business practices. Second, China is slowly beginning to witness the overall impacts of corruption on its own economy and now has incentive to either comply with, or implement new, anti-corruption regulations. Third is the necessity for the United States to continue its efforts to level the proverbial “playing field” in its anti-corruption efforts and set an example for other nations with regard to international business transactions.

Over the last decade, there has been a rather remarkable international interest in combating corruption which can be seen by numerous regional conventions such as the Inter-American Convention against Corruption,\(^{197}\) the Criminal Law Convention on Corruption,\(^{198}\) the Civil Law Convention on Corruption,\(^{199}\) and the African Union Convention on Preventing and Combating Corruption.\(^{200}\) In addition to these various regional agreements, the United Nations (hereinafter “UN”) recently took action to combat corruption on a global level. In October of 2003, the UN General Assembly adopted the Convention against Corruption.\(^{201}\) The Convention imposed numerous requirements on its signatories to take affirmative steps to criminalize corruption and implement mechanisms to combat international crimes of corruption.\(^{202}\) The Convention, which was “widely supported by developing countries,”\(^{203}\) was ratified by China in 2005 in an aggressive step to manage its overwhelming problem with corruption.\(^{204}\)

Recent studies indicate that despite its economic growth, China is being negatively affected by corruption.\(^ {205}\) In the short run, corruption has

\(^{197}\) Hunt, supra note 185, at 261.
\(^{198}\) Id.
\(^{199}\) Id. at 261-62.
\(^{200}\) Id. at 262.
\(^{201}\) See G.A. Res. 58/4, supra note 108.
\(^{202}\) See id.
\(^{205}\) Andrew White, The Paradox of Corruption as Antitheses to Economic Development in Indonesia and China and Why Are the Experiences Different in Each Country?, 8 ASIAN-PAC. L. & POL’Y J. 1, 39.
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contributed to China's economic growth, however the long term effects of corruption may end up actually distorting the Chinese economy.\textsuperscript{206} Corruption has recently led to reduced economic output which has caused a drain on the Chinese economy.\textsuperscript{207} Professor Angang, an economist at Tsinghua University, noted that "China may very well be the country with the most enormous economic losses in the world caused by corruption."\textsuperscript{208} Thus, now more than ever, China has some incentive to deal with its corruption crisis.

The large number of countries that have signed on to the UN Convention against Corruption (including China) should be an unmistakable indication of the global willingness of nations to be subject to anti-corruption laws.\textsuperscript{209} As such, the United States must continue to set the global standard when regulating business operations in China by forcing U.S. corporations to comply with the provisions of the FCPA. The long term impacts of the failure to do so will greatly outweigh the short-term benefits of conducting business in China while utilizing corrupt practices.

In addition to undermining global efforts to curb corrupt practices, allowing corrupt payments would encourage U.S. businesses to develop effective bribery programs, rather than overall efficiency and a good work product. Prior to the enactment of the FCPA, the Senate Banking Committee noted:

[Bribery] short-circuits the marketplace by directing business to those companies too inefficient to compete in terms of price, quality or service, or too lazy to engage in honest salesmanship, or too intent upon unloading marginal products. In short, it rewards corruption instead of efficiency and puts pressure on ethical enterprises to lower their standards or risk losing business.\textsuperscript{210}

Abolishing the FCPA and allowing for corruption would undermine the economic interests of the United States by pressuring businesses to remain competitive through lowering their ethical standards rather than by encouraging competition based on quality products and services. As such, U.S. corporations must continue to set the global standard when conducting business operations in

\textsuperscript{206} Id.


\textsuperscript{208} Hu Angang, Public Exposure of Economic Losses Resulting from Corruption, 4 CHINA & WORLD ECON., 44, 48 (2002).

\textsuperscript{209} Delaney, supra note 110, at 429.

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China by complying with the provisions of the FCPA, even if that means operating at a competitive disadvantage with countries that do not aggressively enforce anti-corruption laws.

B. Strengthening the FCPA: Providing Real Time Guidance in a Fast-Paced Global Economy

The DOJ’s FCPA opinion procedure allows a business or individual seeking to take part in a foreign business operation to make a specific inquiry to the DOJ as to whether the proposed business conduct would violate the FCPA. This process is designed to “enable issuers and domestic concerns to obtain an opinion of the Attorney General as to whether certain specified, prospective—not hypothetical —conduct conforms with the Department’s present enforcement policy regarding the anti-bribery provisions of the Foreign Corrupt Practices Act of 1977.” The DOJ has 30 days to respond to the inquiry and must either issue an opinion as to whether the proposed conduct would violate the FCPA, or request additional information regarding the business operation. While the opinion procedure has the potential of being tremendously beneficial to U.S. corporations who have hesitations regarding a business transaction in China, the procedure, overall, is rarely utilized. In fact, the DOJ’s recent aggressive stance on FCPA enforcement has been criticized as “all stick and no carrot,” with criminal investigations on the rise, yet no increase in U.S. businesses’ use of the procedure. Since the procedure was enacted in 1980, there have been roughly 43 requests for guidance. From 1993 to 2006 there were only 22 requests made by U.S. businesses for guidance, with four or less requests made each year. The slow process of the opinion procedure was the most common criticism cited by U.S. businesses that are often in the position of having to put together complex business propositions for submission and do not have a month to wait for a DOJ opinion before engaging in an overseas transaction.

With China rapidly undergoing both social and economic change, the country is starting to witness consistent changes to its laws, region by region.
The Chinese government “looks at rules as works in progress. So, business decisions based on rules may not be correct a couple months later.” If the facts provided by a U.S. corporation regarding a foreign business transaction in the initial DOJ opinion procedure query are altered, then the DOJ opinion will not be binding on the U.S. business. This severely limits the flexibility by which a U.S. business can operate abroad.

China, while not traditionally a cultural environment accustomed to quick business dealings, is rapidly becoming an economic environment where U.S. corporations are forced into a position of seizing a business opportunity promptly. China’s rapid transformation from a state controlled-planned economy to a market-based economy requires that U.S. corporations move quickly to implement business operations or potentially lose the opportunity to a foreign competitor. As one commentator observed, “[y]ou may think you have a deal [in China] and a day or two later something changes — that’s just the way it is.” In this fast-paced Chinese economy, the 30-day opinion procedure of the DOJ (sometimes longer if additional information is requested) is simply too long for a U.S. corporation to wait before it can agree upon the terms of a Chinese business operation. Moreover, “companies are not likely to have complete information about a transaction until it is ready to go – which is usually the point when a company is least likely to be able to put it on hold while DOJ deliberates.” This presents a problem for corporations that may greatly benefit from the DOJ opinion procedure. Once the opinion procedure is triggered, a U.S. business has no way to predict when the procedure will be concluded.

The DOJ currently has sufficient resources available to investigate and prosecute cases involving bribery. However, more resources need to be devoted to the opinion procedure to assist the DOJ in fulfilling its responsibilities of providing real-time guidance to businesses at the outset of an overseas operation. The procedure would operate more effectively if, absent a response by the DOJ within one week, the U.S. business is able to proceed with the business transaction with the understanding that the DOJ agrees that the transaction will not violate the FCPA.

In addition to its slow pace, the opinion procedure has “no application to any party which does not join in the request for the opinion.” Moreover,

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218 Id.
220 Orfield, supra note 217.
221 Id.
222 Miller, supra note 213.
there is very little case law on the FCPA which sets precedent for a U.S. business to operate legally. Problems with FCPA compliance are the result not only of its vague language, but also the lack of guidance provided to U.S. businesses. Therefore, rather than confining its opinions to a specific set of individual facts, the opinion procedure must create precedent and provide overall guidance to U.S. corporations.

Strengthening the opinion procedure through efficiency and overall FCPA education would be beneficial to both U.S. corporations and the U.S. government. First, it will encourage a U.S. corporation to take advantage of the already under-utilized DOJ opinion procedure if the corporation believes it can receive real-time FCPA guidance. Second, given the recent increase in FCPA investigations conducted by the DOJ and SEC and the costs incurred, the benefits of devoting more resources to strengthening the opinion procedure would be worth the costs. Finally, allowing the opinion procedure to serve as precedent for later decisions would be a substantial step in furtherance of eliminating the vagueness of the FCPA.

C. Amending the FCPA: Eliminate the Vagueness or Fortify the Red Flags

The legislative history of the FCPA supports the argument that the Act was not meant to punish a U.S. corporation for mere negligence. However, as of late, the DOJ has been increasingly willing to prosecute U.S. businesses for conduct that is not clearly actionable under a strict reading of the FCPA by utilizing many varying theories of liability. This was most notably observed in the DPC prosecution, where FCPA violations were charged based on the theory that Tianjin Co. was acting as a subsidiary of its California-based company.

Employees of a U.S. corporation may “turn a blind eye and allow improper payments through third-party intermediaries under the misguided assumption that such payments will not violate U.S. law.” While a foreign agent is not subject to the FCPA, the agent’s conduct may create FCPA exposure for a U.S. corporation. This poses a substantial problem in China,
where conducting business operations generally requires the use of local agents and partners, and the “responsibility for dealing with local government officials and obtaining necessary approvals is typically not in the foreign investor’s hands but lies with the Chinese partner.” The FCPA prohibits not only direct bribery, but also corrupt payments through the use of such an intermediary. A U.S. business can therefore be liable under the FCPA for corrupt payments made through an intermediary if they knew or should have known the payments would go to a foreign official. Specifically, a business can be held liable even if it “is aware...that such circumstance [for bribery] exists.” The requisite “knowledge is established if a person is aware of a high probability of the existence of such circumstance [for bribery].” This extraordinarily broad language affords the DOJ the advantage of having to prove only that a U.S. business knew of the “likelihood” of a corrupt payment, rather than an actual corrupt payment.

In a situation where a corporation should have known that an intermediary has made or will make a corrupt payment, the DOJ will look at whether the corporation was aware of any “red-flags” that would trigger knowledge of an FCPA violation, including:

[U]nusual payment patterns or financial arrangements, a history of corruption in the country, a refusal by the foreign joint venture partner or representative to provide a certification that it will not take any action in furtherance of an unlawful offer, promise, or payment to a foreign public official and not take any act that would cause the U.S. firm to be in violation of the FCPA, unusually high commissions, lack of transparency in expenses and accounting records, apparent lack of qualifications or resources on the part of the joint venture partner or representative to perform the services offered, and whether the joint venture partner or representative has been recommended by an official of the potential

234 15 U.S.C. § 78dd-l(f)(2)(A) (2000) states that “[a] person’s state of mind is “knowing” with respect to conduct, a circumstance, or a result if—(i) such person is aware that such person is engaging in such conduct, that such circumstance exists, or that such result is substantially certain to occur; or (ii) such person has a firm belief that such circumstance exists or that such result is substantially certain to occur.”
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governmental customer.237

While attention to the red flags will help shield a U.S. business from FCPA liability, the red flag provisions are extraordinarily subjective and impose a significantly greater restriction on U.S. businesses than other countries, especially since a U.S. business is subject to the provisions of the FCPA even if the corrupt payments made have no connection to the U.S. business.238

The general red flag provisions, coupled with the statutory language of the FCPA, places a U.S. corporation conducting business operations in China at a constant, unreasonably dangerous risk. Given the current level of corruption in China, U.S. business operations are likely to trigger general red flag provisions such as “a history of corruption in the country,”239 thereby giving the DOJ the advantage of easily proving beyond a reasonable doubt that the U.S. business knew that “such circumstance [for bribery] exists.”240 In China’s present climate of corruption such circumstances always exist. A U.S. corporation can be held liable for acts of an intermediary even if the business lacked knowledge, intent, or participation in the act just by nature of the fact that China is regarded as an environment where corruption is high, and the circumstances in which corrupt payments can be made always exist in such an environment. The general red flag provisions are, therefore, either meaningless or overly broad when applied to U.S. business operations in China.

The FCPA should be amended to remove the broad language that would give rise to expansive theories of civil and criminal liability. Specifically, the requirement that a person or a corporation has a “knowing” state of mind if “such circumstances exist,” should be removed from the statute.241 An FCPA cause of action could still be initiated utilizing the knowledge inference of “aware that such person is engaging in such conduct,”242 if a U.S. corporation was aware that an intermediary was taking part in corrupt payments. Furthermore, this amendment would not impede the government from pursuing an FCPA action against a U.S. corporation that turned a blind eye to corrupt activities, since the knowledge inference of “substantially certain to occur”243 would remain intact. Thus, the “bury the head in the sand” approach

237  LAY-PERSON'S GUIDE TO FCPA, supra note 29 (emphasis added).
239  LAY-PERSON'S GUIDE TO THE FCPA, supra note 29.
243  Id.
to corrupt payments made by intermediaries would remain a non-defense to the
FCPA.

In the absence of an amendment to the FCPA removing the overly
broad scienter requirement for FCPA liability if “such circumstance (for
bribery) exists,” a common middle ground must be established with regard to
the red flag provisions of the FCPA. This middle ground would contain two
distinct factors essentially augmenting the red flag provision which is triggered
when “history of corruption in the country”244 exists. First, since the DOJ’s
opinion procedure provides little guidance or precedent, the provision should be
modified in a manner which would specifically construe the phrase “such
circumstances” to include specific enumerated acts of a foreign country that
would put a U.S. business on notice of a strong possibility of corrupt payments
being made, as opposed to simply looking at the annual Transparency
International report245 to determine the general corruption level in the country.
Second, if specific acts do exist, a U.S. business would then be required to have
adequate and enforceable corporate controls in place, the absence of which
would lead to a greater level of FCPA exposure. Removing the overly broad
language of the FCPA would eliminate much of its ambiguity and thereby allow
U.S. corporations with business operations in China to operate with less concern
of DOJ or SEC action, while still requiring those corporations to exercise due
diligence in corporate operations.

Alternatively, augmenting the red flag “history of corruption”
provision to provide more detailed criteria of its triggering mechanisms would
allow U.S. corporate compliance policies to be modified in a manner that would
reflect a new legal framework for avoiding FCPA liability. Neither course of
action would hinder the FCPA’s ability to effectuate its overall purpose of
combating corrupt payments abroad and instilling public confidence in the
global business environment.

CONCLUSION

The FCPA continues to be one of the most controversial U.S. laws246
due largely in part to the perception that U.S. businesses are not on an even
playing field in a competitive, global environment. Nonetheless, despite its
many shortcomings and less than practicable application to U.S. business
operations in China, the FCPA is essential in maintaining the stance of the
United States on eliminating corruption and preserving the integrity of the

244 LAY-PERSON'S GUIDE TO FCPA, supra note 29.
245 Transparency Int'l, the Global Coal. Against Corruption, TI Corruption Perceptions Index supra
note 84.

http://scholarlycommons.law.hofstra.edu/jibl/vol7/iss1/2
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global market. The FCPA is capable of achieving these advantages, without putting U.S. businesses at a competitive disadvantage in transitional nations such as China, with more guidance by the DOJ and less ambiguity in the statute.

While both U.S. corporations and the U.S. government would like to witness the elimination of China's corruption problem during this time when the Chinese economy continues to thrive, the problem is not one that is subject to a quick fix. As one commentator noted:

Viewed from the ground, one often finds sympathy for the cause of reducing corruption, but pessimism about the prospects. Some officials in private simply say that corruption is so deeply rooted in the fast-growing economy and its fabric so tightly interwoven, that it is difficult to discern whether things are improving or degrading. Most agree that this is not a battle to be won in some definable time frame; rather, it is a very long march.247

Corruption in China is not a problem that is going to disappear anytime in the near future. Developing methods to curb the problem with corruption will be a long arduous process. If China maintains some level of control of its corruption problem and witnesses a decrease in corruption overall, the level of governmental scrutiny faced by U.S. businesses will most likely decrease as well. However, at the present time, while the perception of China continues to be that of a corruption-plagued nation, the DOJ and SEC will continue to be increasingly focused on U.S. corporations with business operations in China.248

Recent FCPA enforcement actions should be an unmistakable indication to U.S. corporations that when conducting business operations in China, they must have a rigorous FCPA compliance program in place that will shield them from the appearance of impropriety. As one commentator noted, "[t]here is a common misperception that when 'no one is watching,' U.S. law does not apply. As the FCPA demonstrates, nothing could be further from the truth. Companies that believe otherwise, do so at their own peril."249 Recent cases and the continued focus on potential FCPA violations in China should be an indication to all U.S. businesses that someone is, in fact, always watching closely.

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247 DeWoskin, supra note 105.
248 Utterback, supra note 101.
249 Olson, supra note 12.