LATHAM & WATKINS

March 2007

International Dispute Resolution

A Publication from Latham & Watkins' International Dispute Resolution Practice

The Foreign Corrupt Practices Act: US Liability for Non-US Companies

Non-US corporations are often surprised to learn of their potential for US criminal liability for conduct performed entirely abroad. In fact, a myriad of US criminal laws are applicable to companies that opt to do business, have bank accounts, or have securities listed in the US. This article briefly analyses one such law, the Foreign Corrupt Practices Act (FCPA), and reviews some of the ways in which domestic and non-US companies can be criminally liable in the US for activity undertaken outside the US.

To be subject to the FCPA, a company need not have any physical presence in the US. Jurisdiction attaches to any US "issuer" or "domestic concern" who participates in proscribed activity. An "issuer" is a foreign or domestic company with securities registered in the US or one subject to Securities Exchange Commission (SEC) reporting requirements. A "domestic concern" is any company with its principal place of business in the US or organized under the laws of any US state, as well as any individual who is a US citizen or resident.

The FCPA prohibits payments or offers of payment to foreign officials for the purpose of obtaining or retaining business. "Issuers" and "domestic concerns" are liable even where the conduct occurs entirely outside the US. As a result, a non-US company with securities registered on a US exchange can be prosecuted for a bribery attempted anywhere in the world. Similarly, a US citizen, working abroad for a non-US company, can be prosecuted for an FCPA violation even where all the conduct occurred abroad. Finally, foreign companies and individuals are subject to the FCPA if they cause an act in furtherance of a corrupt payment to take place within the US. In this way, foreigners can be sanctioned under the FCPA where a very limited US territorial nexus exists.

The FCPA also requires issuers to establish and maintain certain accounting and record-keeping practices intended to deter and detect corrupt payments. Specifically, issuers must make and keep books, records and accounts which detail the transactions and disposition of assets. "Records" for this purpose include correspondence, memoranda, tapes, disks, papers and other documents. The FCPA also codifies existing auditing standards and internal controls.

. . . a non-US company with securities registered on a US exchange can be prosecuted for a bribery attempted anywhere in the world.

Sanctions for companies and individuals under the FCPA are substantial and have increased in recent years. Under the federal sentencing guidelines and alternative fine provisions, fines can far exceed the amount of any illicit payment. Individuals are subject to a maximum of five years' imprisonment and a $100,000 fine for violation of the FCPA's anti-bribery provisions, while those who violate its accounting and record-keeping provisions may be fined up to $5 million and risk imprisonment for up to 20 years. Companies are subject to fines of up to $2 million for knowing violations of the FCPA's anti-bribery provisions and $25 million for willful violations of the internal accounting and record-keeping provisions.

Examples of recent enforcement action under the FCPA include:

- In 2006, Schnitzer Steel Industries, Inc. agreed with the US Department of Justice (DOJ) to a fine of $7.7 million following allegations of improper payments to managers at government-owned steel mills in China and improper accounting for payments made to private steel owners in China and South Korea.
- In 2005, Titan Corporation agreed with the DOJ and SEC to pay $28.5 million – the largest FCPA penalty

Inside This Issue:

Continued from Page 1 — The Foreign Corrupt Practices Act: US Liability for Non-US Companies

in history – following its $3.5 million payment to a business advisor to the President of the African state of Benin in exchange for higher management fees. The payment comprised a criminal fine of $13 million and a civil penalty of approximately $15.5 million.

- In 2004, in a leading example of the FCPA's extra-territorial reach, ABB Ltd (a Swiss company) and two of its subsidiaries incurred $16 million in criminal and civil penalties following payments of $1.1 million to government officials in Nigeria, Angola and Kazakhstan.

Latham & Watkins' White Collar Crime and Government Investigations Practice Group advises on all aspects of the application and potential extra-territorial effects of the FCPA. ■

The New ICSID Arbitration Rules Approach Their First Anniversary

As from 10 April 2006, arbitral proceedings administered by the International Centre for Settlement of Investment Disputes (ICSID) have been subject to new rules of procedure for arbitration proceedings adopted under both the ICSID Convention and the Arbitration (Additional Facility) Rules. Any ICSID arbitration to which the parties have consented after 10 April 2006 is to be conducted in accordance with the new rules, unless the parties to the arbitration agree otherwise. In general, the changes are intended to make the ICSID process both more efficient and more transparent.

The new rules have made two changes to the pre-merits stage of the proceedings. Perhaps most significantly, they have improved the speed at which an arbitral tribunal can grant provisional measures. Rule 29 now permits parties to ask for provisional measures as soon as a Request for Arbitration is registered with ICSID, even before the tribunal has been constituted. The ICSID Secretary-General is then to set time limits for the parties to exchange observations on the request, thus allowing the tribunal to decide on the provisional measures immediately upon constitution.

Rule 41 has been amended to provide an additional ground for a preliminary objection: namely, that the claim is "manifestly without legal merit." A party now has up to thirty days after the constitution of the tribunal to object on this ground. The other party has the right to respond and the tribunal must give its ruling in an expedited fashion.

Other changes are intended to increase the transparency of the ICSID process. To this end, the rules now for the first time allow the tribunal to accept *amicus curiae* briefs even if the parties object, although the tribunal must still consult both parties before deciding to accept such briefs. The Rules specify criteria for the tribunal to take into consideration, such as whether the brief would provide a "perspective, particular knowledge or insight that is different from that of the disputing parties." If an *amicus curiae* brief is accepted, the tribunal must give both parties an opportunity to comment upon it.

Similarly, the new Rule 32 gives ICSID tribunals the authority to allow third parties to attend oral hearings, provided that no party objects. If a hearing is opened to third parties, the tribunal is under an obligation to create procedures to protect proprietary or privileged information.

Another major change relates to publication of awards. Although the ICSID Rules prohibit the ICSID Secretariat from publishing awards without obtaining the consent of the parties, the old Rules allowed ICSID discretion to publish excerpts revealing reasoning. Now, Rule 48 requires ICSID to publish "excerpts of the legal reasoning" of each award in a prompt fashion.

Other changes to the Rules include a clarification that an arbitrator's duty to report a relationship with one of the parties is ongoing and a modification of an arbitrator's declaration of independence in these terms; and the setting of standard daily fees for arbitrators.

The new ICSID rules provide practical aid in streamlining the ICSID process and making it more transparent.

Perhaps the amendments to the rules are most noteworthy, however, for not having included a centralised appeals process, as ICSID had suggested. ICSID apparently rejected the proposal following widespread opposition during consultation. The issue of providing an appeals structure for ICSID decisions may nevertheless be the subject of a future round of proposals, especially since such structures are envisaged in certain bilateral and regional treaties on the protection of cross-border investment.

The rules have already had an impact on various disputes. In at least one case, the Secretary General of ICSID has issued an accelerated briefing schedule for provisional measures prior to the constitution of the tribunal.

In connection with other requests for provisional measures, in at least one case the claimant has invoked two sources of consent: one prior to the changes in rules and one subsequent to the changes. This is potentially significant because the date of consent determines which version of the rules applies. It remains to be seen how tribunals will deal with this issue.

The new ICSID rules provide practical aid in streamlining the ICSID process and making it more transparent. Faced with the burgeoning number of bilateral investment treaties that call for ICSID arbitration, the increased transparency should, it is hoped, allow ICSID case law to develop in a more controlled and predictable fashion.

Lawyers in Latham & Watkins' International Dispute Resolution Practice Group have extensive experience in advising on the ICSID arbitral process and in representing both corporate claimants and sovereign state defendants in all forms of investment dispute. ■

New York Case Signals that Large Punitive Damages in Arbitration Awards Will Receive Closer Scrutiny

Recent developments suggest that New York courts may be less willing to accept disproportionate punitive damage awards in arbitrations, a development that may prove significant in light of the increasing use of arbitration in consumer cases and the emergence of class arbitrations.

In *Sawtelle v. Waddell & Reed Inc.*,[1] the First Department of the Appellate Division affirmed the vacatur of an arbitral award granting a mutual fund broker $25 million in punitive damages against his former employer on the ground that "[a]n award of punitive damages that is some 23 times actual damages is irreconcilable with prevailing authority and can only be construed as arbitrary."

The Court concluded that an excessive award violated New York's public policy and was therefore "manifestly in disregard of the law".

The Court had previously vacated the same award and ordered the arbitration panel to reconsider.[2] On reconsideration, the arbitral panel reiterated that the conduct violated the Unfair Trade Practices Act of Connecticut and granted the same punitive award. It expanded its previous characterization of the employer's conduct as a "campaign of deception" describing it as a "horrible campaign of deception, defamation and persecution." The Appellate Division was unimpressed, calling the change a "pretextual gloss" and ruling that the "arbitral prerogative does not permit a panel to ignore the [previous] ruling and obdurately issue an identical determination."

Both *Sawtelle* decisions applied the "manifest disregard of the law" standard of review. The Court of Appeals had previously rejected this federal standard for arbitral awards governed by the Federal Arbitration Act (FAA) in favor of its own standard, which mandated reversal "if [an award] is totally irrational or violative of a strong public policy."[3] The decision in Sawtelle is in line with a recent string of cases from the First Department which have again begun applying the federal standard to awards governed by the FAA.

The language in both *Sawtelle* decisions suggests that the Court considered the Supreme Court's due process review standards for punitive damage awards. New York courts have traditionally avoided applying due process review (which applies to state action) to arbitration awards. Although it did not apply a due process analysis directly, the Court's evaluation of the punitive award through the lens of public policy was clearly informed by due process standards. The Court concluded that an excessive award violated New York's public policy and was therefore "manifestly in disregard of the law".

Paradoxically, the Supreme Court of Connecticut held that a large punitive damages award under the same legislation governing *Sawtelle* did not violate Connecticut's public policy. In *MedValUSA* an arbitral panel awarded $5 million in punitive damages, despite awarding no compensatory damages. Focusing solely on the public policy issue, the *MedValUSA* Court rejected claims that the award was grossly disproportionate.

Sawtelle's application of the more rigorous "manifest disregard" standard may be a signal that New York courts will more closely scrutinize arbitration awards in future. The invalidation of the award on public policy grounds also suggests that the courts will apply a level of scrutiny similar to the Supreme Court's due process standards when reviewing punitive damages in arbitration awards.

Endnotes

1 801 N.Y.S.2d 286, 288 (App. Div. 2005).

2 *Sawtelle v. Waddell & Reed Inc.*, 754 N.Y.S.2d 264 (App. Div. 2003).

3 *Hackett v Milbank, Tweed, Hadley & McCloy*, 86 NY2d 146, 155 (1995).

4 *See BMW of North America, Inc. v Gore*, 517 US 559 (1996); *State Farm Mut. Auto. Ins. Co. v Campbell*, 538 U.S. 408 (2003).

5 *MedValUSA Health Programs, Inc. v. Memberworks, Inc.*, 872 A.2d 423, 662 (Conn. 2005). ■

News in Brief

- **Canada signs Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID).** On 15 December 2006, Canada signed the so-called ICSID Convention, to which over 150 countries are now signatories. Once it is ratified and enters into force for Canada, the Convention will provide a significant new potential means for resolution of disputes between foreign investors and Canadian authorities, or between Canadian investors and state authorities outside Canada. The ratification process may take some time due to complications arising out of Canada's federal system of government, but a number of provinces (including Ontario) have already enacted implementing legislation.
- **Kyrgyzstan loses appeal against Energy Charter Treaty award.** The Swedish Court of Appeal has rejected an attempt by Kyrgyzstan to overturn an award rendered in 2005 by the Arbitration Institute of the Stockholm Chamber of Commerce under the Energy Charter Treaty (ECT). Pursuant to the award, the UK energy company Petrobart was awarded over US $1 million following a finding that Kyrgyzstan had failed to accord its investment "fair and equitable treatment". In its appeal, Kyrgyzstan argued that the protections of the ECT did not apply to investments made by Gibraltar-based entities and that Petrobart's sales contract with a Kyrgyz state joint stock company was not an "investment" for the purposes of the ECT. The Swedish Court rejected both arguments and ordered Kyrgyzstan to pay the Court's costs.
- **ICSID Tribunal awards German investor US$217 million for violation of Argentina-Germany bilateral investment treaty.** In the fourth recent investment arbitration award against Argentina, Siemens has succeeded in a claim that its investment in Argentina's national identity card programme was expropriated in 2001 by the Argentine Government's attempt to impose new contractual terms. Among other violations of the treaty, Argentina was found to have failed to accord "fair and equitable treatment" to Siemens' investment. A significant number of further investment treaty claims is still pending against Argentina.
- **ICSID Tribunal permits *amicus curiae* submission in Argentine investment dispute.** On 12 February 2007, an ICSID tribunal hearing a bilateral investment treaty dispute about water concessions in Argentina issued an order permitting five non-governmental organisations (or NGOs) to make a joint *amicus curiae* submission in the proceedings. Rejecting the objections of the claimant investors, the tribunal determined that the NGOs' experience with matters of human rights, the environment and the provision of public services meant that their submission could assist the proceedings by providing perspectives that the litigating parties could not provide. The tribunal noted that its decision was consistent with the new ICSID Arbitration Rules, discussed in more detail above. The tribunal denied the five NGOs' request for access to the record of the arbitration proceedings.
- **English Court confirms arbitrators' ability to rule on bribery allegations and related issues concerning validity of contract.** On 24 January 2007, in the case of *Fiona Trust and Holding Corporation and Others v. Privalov and Others,* the English Court of Appeal ruled that arbitrators could decide all allegations relating to the validity of a contract, including allegations that the contract was procured by bribes. An arbitration clause containing standard "arising out of" wording should apply to all disputes except a dispute as to whether there was ever a contract at all. Therefore, only if the arbitration agreement was directly impeached might the arbitrators be prevented from deciding disputes relating to the contract. In general, under the Arbitration Act 1996, it should fall first to an arbitral tribunal to determine whether it had jurisdiction to hear a dispute.

Barcelona
Brussels
Chicago
Frankfurt
Hamburg
Hong Kong
London
Los Angeles
Madrid
Milan
Moscow
Munich
New Jersey
New York
N. Virginia
Orange County
Paris
San Diego
San Francisco
Shanghai
Silicon Valley
Singapore
Tokyo
Washington, D.C.

International Dispute Resolution is published by Latham & Watkins as a news reporting service to clients and other friends. The information contained in this publication should not be construed as legal advice. Should further analysis or explanation of the subject matter be required, please contact the attorneys listed below or the attorney whom you normally consult. A complete list of our publications can be found on our Web site at www.lw.com.

If you wish to update your contact details or customise the information you receive from Latham & Watkins, please visit www.lw.com/resource/globalcontacts to subscribe to our global client mailings program.

If you have any questions about this edition of *International Dispute Resolution*, please contact the co-chairs of our International Dispute Resolution Practice Group: **Mark Beckett** (NY) or **Robert Volterra** (LO). Alternatively, please contact the attorney with whom you normally consult.

The editorial board of this publication consists of Stephen Fietta (LO), Emily Finn (NY), Jeroen Van Kwawegen (NY), Jose Manuel Garcia Represa (PA) and Sebastian Seelmann-Eggebert (HH).

Mark D. Beckett
New York
+1-212-906-1200
mark.beckett@lw.com

Robert G. Volterra
London
+44 20 7710 1000
robert.volterra@lw.com

Complete details of attorney bios can be found on our Web site at www.lw.com/attorney.

Latham & Watkins operates as a limited liability partnership worldwide with an affiliate in the United Kingdom and Italy, where the practice is conducted through an affiliated multinational partnership. Under New York's Code of Professional Responsibility, portions of this communication contain attorney advertising. Prior results do not guarantee a similar outcome. Results depend upon a variety of factors unique to each representation. Please direct all inquiries regarding our conduct under New York's Disciplinary Rules to Latham & Watkins LLP, 885 Third Avenue, New York, NY 10022-4834, Phone: +1.212.906.1200. © Copyright 2007 Latham & Watkins. All Rights Reserved.

Barcelona
+34 902 882 222

Brussels
+32 (0)2 788 60 00

Chicago
+1-312-876-7700

Frankfurt
+49 69 60 62 60 00

Hamburg
+49 40 41 40 30

Hong Kong
+852-2522-7886

London
+44 20 7710 1000

Los Angeles
+1-213-485-1234

Madrid
+34 902 882 222

Milan
+39 02-3046-2000

Moscow
+7-495-785-1234

Munich
+49 89 20 80 3 8000

New Jersey
+1-973-639-1234

New York
+1-212-906-1200

Northern Virginia
+1-703-456-1000

Orange County
+1-714-540-1235

Paris
+33 (0)1 40 62 20 00

San Diego
+1-619-236-1234

San Francisco
+1-415-391-0600

Shanghai
+86 21 6101-6000

Silicon Valley
+1-650-328-4600

Singapore
+65-6536-1161

Tokyo
+81-3-6212-7800

Washington, D.C.
+1-202-637-2200