New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM
An ALM Publication
VOLUME 251—NO. 05
WEDNESDAY, JANUARY 8, 2014

WHITE-COLLAR CRIME

Expert Analysis

Dilemma of Self-Reporting: The FCPA Experience

By **Elkan Abramowitz** And **Jonathan Sack**

One of the most challenging questions faced by white-collar defense counsel and their clients is whether to report voluntarily, that is, to "self-report," information about the misconduct of a client company or individual. The issue is a particularly thorny one for companies which, unlike individuals, cannot resist the production of incriminating information by asserting Fifth Amendment rights, and which are obliged to make decisions based on the interests of shareholders, not current management.

As a practical matter, the decision about self-reporting commonly boils down to an assessment of three issues: (i) whether the client is obligated to report the misconduct—for example, under federal securities laws and the rules of industry self-regulatory organizations;[1] (ii) the likelihood of exposure, through government investigation, journalistic inquiry, whistleblowing or otherwise; and (iii) the possible benefit of self-reporting and, concomitantly, the risk of additional sanction from failing to self-report wrongful behavior if it is later discovered. Because clients and counsel often need to make these assessments with little hard and sure information, the judgments and analysis are sometimes very difficult.

Federal authorities seek to influence private decision-making with a carrot-and-stick approach. The Department of Justice and Securities and Exchange Commission, for example, declare that self-reporting will be rewarded and will yield reduced sanctions and, at the same time, that failing to divulge information voluntarily will lead to enhanced penalties.[2] One of the clearest expressions of this carrot-and-stick policy comes in the field of the Justice Department's criminal enforcement of the antitrust laws, where the department gives complete amnesty to the first party to report a criminal antitrust conspiracy but does not offer leniency to parties that subsequently self-report the same violation.[3] Another high-profile effort to encourage self-reporting—the Internal Revenue Service's voluntary disclosure program for offshore financial accounts—though not offering amnesty, provides explicit and substantial financial incentives to self-report.[4] Yet these programs are the exception; complete amnesty and clear, calculable financial incentives from the government are rarely available when clients consider whether to self-report.

In this article, we address the dilemma of self-reporting in the context of the government's recent focus on criminal and civil violations of the Foreign Corrupt Practices Act (FCPA). Through speeches and publications the government has declared its strong commitment to FCPA enforcement and the dire consequences of failing to self-report violations of the law. At the same time, the benefit received from FCPA self-reporting has been difficult to discern, as illustrated by two recent FCPA investigations in the news, involving Ralph Lauren Corp. and Avon Products Inc. Notwithstanding government pronouncements about the rewards of self-reporting, the dilemma remains quite real: Is it worth it to self-report?

Government's FCPA Message

In November 2012, the SEC and the Justice Department released the Resource Guide to the U.S. Foreign Corrupt Practices Act. The guide refers to the "high premium on self-reporting, along with cooperation and remedial efforts in determining the appropriate resolution of FCPA matters."[5]

Senior government officials have emphasized the importance of self-reporting and the flipside—the danger of learning of misconduct and not telling the government. Charles Duross, deputy chief of the Justice Department's FCPA Unit, recently said that "[t]he risk of getting caught…is greater today than any point previously," and opined that a company's decision whether to self-report potential violations was "kind of a no-brainer."[6] In November 2013, Andrew Ceresney, codirector of the SEC's Division of Enforcement, warned that "if we find the violations on our own, the consequences will surely be worse than if you had self-reported the conduct."[7] These recent remarks echo past statements to the effect that significant credit would be given for a company's self-reporting of FCPA violations.[8]

The written policies of both the Justice Department and the SEC likewise suggest that voluntary disclosure will be viewed favorably when charging decisions are made. In its Principles of Federal Prosecutions of Business Organizations, the Justice Department includes in the analysis whether the company made a voluntary and timely disclosure of relevant information.[9] In the Seaboard Report, a company's self-reporting of misconduct is part of the SEC's determination of whether a company has cooperated and, more broadly, whether a company should be treated with leniency for "good corporate citizenship."[10] In this respect, executive branch policy is consistent with the federal Sentencing Guidelines for Organizations, which, in its discussion of Compliance and Ethics Programs, calls for consideration of "self-reporting and cooperation with authorities."[11]

> Complete amnesty and clear, calculable financial incentives from the government are rarely available when clients consider whether to self-report.

Securing favorable treatment is hardly a trifling matter when facing possible FCPA sanctions. Companies face fines of up to $2 million for each violation of the anti-bribery provisions and additional fines for each violation of the statute's accounting provisions, while individuals too are subject to substantial fines and imprisonment for violations of the anti-bribery and accounting provisions.[12] No wonder so few companies and individuals go to trial on FCPA charges.

Ralph Lauren Corporation

The FCPA case against Ralph Lauren Corporation has been held out as an example of credit being given for prompt, voluntary disclosure. In 2010, the company found evidence of bribes by its Argentine subsidiary to government officials, through intermediaries, to ease getting its goods through Customs without the required paperwork

ELKAN ABRAMOWITZ *and* JONATHAN SACK *are members of Morvillo Abramowitz Grand Iason & Anello. Abramowitz is a former chief of the criminal division in the U.S. Attorney's Office for the Southern District of New York. Sack is a former chief of the criminal division in the U.S. Attorney's Office for the Eastern District of New York.* GRETCHAN R. OHLIG, *an attorney, assisted in the preparation of this article.*

and inspections.[13] Ralph Lauren promptly reported its findings to the government, adopted remedial measures, including firing its customs broker, and cooperated with the government's investigation.

In April 2013, Ralph Lauren entered into a non-prosecution agreement with the SEC and Justice Department, agreeing to pay more than $700,000 in disgorgement and interest to the SEC and $882,000 in penalties to the Justice Department. According to the SEC's Acting Director of Enforcement George S. Canellos, "The NPA in this matter makes clear that we will confer substantial and tangible benefits on companies that respond appropriately to violations and cooperate fully with the SEC."[14]

While, on the surface, the benefit from Ralph Lauren's self-reporting appears substantial, particularly given the massive disgorgement and penalties now routinely imposed on companies, questions have been raised about just how much credit the company was given for promptly going to the government. Critics point out that the government could have declined prosecution altogether. As stated in an alert by Covington & Burling, "it is difficult to imagine a set of facts more deserving of a non-public declination based on the criteria outlined by the SEC and the DOJ late last year in the FCPA Resource Guide."[15]

The facts warranting declination seemed substantial. The misbehavior at issue was isolated in a single foreign operation and limited in scope and duration. According to the non-prosecution agreement filed in the case, the conduct was discovered when the company distributed its FCPA policy to employees—revealing the company's active and real compliance efforts—which elicited concerns in the Argentine subsidiary about the company's third-party customs broker. Despite these mitigating facts, the government opted for an NPA rather than simply declining prosecution, which required Ralph Lauren to publicly acknowledge wrongdoing, and which may expose it to private lawsuits and unfairly harm its reputation.

Law Professor Michael Koehler of Southern Illinois University School of Law, an expert on the FCPA has made a pointed critique of the Ralph Lauren settlement:

> [w]hen the DOJ and SEC take action against one entity (one of the world's most admired companies according to [a] recent Fortune list) that had an isolated instance of conduct that likely did not even violate the FCPA *as Congress intended*, this is not something to praise, it is something to lament. When the DOJ and SEC extract approximately $1.6 million from an entity that acted like a responsible corporate citizen upon learning of an issue…this is not something to praise, it is something to lament.[16]

(emphasis in original). While surely debatable, this viewpoint is important to consider when weighing the likely benefits of self-reporting.

Avon Products

In 2008, Avon Products, the maker and seller of beauty products, commenced an internal investigation into payments to Chinese officials. A primary focus of its investigation was a 2005 internal audit report which had found that Avon employees in China may have paid several hundred thousand dollars to Chinese officials and third-party consultants to help secure a license to conduct door-to-door sales. In October 2008, the company voluntarily informed the SEC and the Justice Department of its internal investigation, and, according to public statements, the company has provided full cooperation with the government's subsequent investigation.[17] Media reports indicate that the government has devoted substantial effort to determine whether current or former executives ignored or sought to suppress the 2005 audit report.[18]

While, on the surface, the benefit from Ralph Lauren's self-reporting appears substantial, particularly given the massive disgorgement and penalties now routinely imposed on companies, questions have been raised about just how much credit the company was given for promptly going to the government.

On the surface, Avon has taken the requisite steps to benefit from self-reporting—at least since its 2008 voluntary disclosure to the government. By the end of 2012, the company had spent approximately $300 million on its internal investigation and disclosed its findings to the government. The company also took clear steps to remedy any problems, including the termination of its chief executive and other members of senior management and adopting enhanced ethics and compliance programs.[19] Yet the benefit to the company for these efforts has been difficult to detect from public statements and reporting.

In June 2013, the company offered to settle FCPA cases initiated by the Justice Department and the SEC on terms that included payment of monetary penalties of approximately $12 million. The government rejected that offer. In September 2013, the SEC proposed settlement for an amount which was, according to Avon, "of a magnitude significantly greater than our earlier offer."[20] Since then, Avon's stock has fallen, and, as stated in public filings, the company "expect[s] to continue to incur costs, primarily professional fees and expenses, which may be significant, in connection with the government investigation."[21]

Conclusion

Against a backdrop of uncertain benefits from self-reporting, proposals have surfaced in recent years for an FCPA amnesty program, harking back to the widespread corporate self-disclosure and amnesty following adoption of the law in 1977.[22] The government has opposed a new amnesty program, arguing that disclosure should not allow companies to "get a pass for those crimes."[23] No change in law or policy is in sight.

Consequently, the question of whether a company should voluntarily disclose wrongdoing will remain a difficult one in the context of possible FCPA violations as well as other areas of federal law enforcement. Statements and policies of government agencies can, in some cases, clarify the issue and give genuine incentives for self-reporting. In the field of FCPA, the government has sought to encourage self-reporting, but its actions arguably are sending mixed signals. The core dilemma of self-reporting—whether the benefits outweigh the costs—will not be going away any time soon.

1. See e.g., Financial Industry Regulatory Authority Rule 4530 (requiring members to report to FINRA certain internal and external findings of misconduct); SEC Press Release, "Xerox Settles SEC Enforcement Action Charging Company With Fraud" (April 11, 2002) (settlement of claims brought regarding company's obligation to report accounting irregularities).
2. United States Attorney's Manual, "Principles of Federal Prosecution of Business Organizations," Title 9, Chapter 9-28.000; SEC Release No. 44969, "Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions" (the Seaboard Report).
3. See Department of Justice, "Frequently Asked Questions Regarding the Antitrust Division's Leniency Program and Model Leniency Letters" (Nov. 19, 2008) (available on Justice Department website); Department of Justice, "Corporate Leniency Policy" (Aug. 10, 1993) (available on department website).
4. See Jeremy H. Temkin, "New Justice Department-Swiss Bank Program Announced," NYLJ (Oct. 28, 2013) (detailing IRS voluntary disclosure programs).
5. Department of Justice and Securities and Exchange Commission, "A Resource Guide to the U.S. Foreign Corrupt Practices Act" at p. 54 (Nov. 14, 2012) (available at http://www.sec.gov/spotlight/fcpa/fcpa-resource-guide.pdf).
6. Andrew Ramonas, "The Perils of Keeping FCPA Infractions Under Wraps," Corporate Counsel (Oct. 29, 2013).
7. Keynote Address at the International Conference on the Foreign Corrupt Practices Act (Nov. 19, 2013).
8. See Andrew Ceresney, Codirector of SEC Division of Enforcement, Keynote Address at the International Conference on the Foreign Corrupt Practices Act (Nov. 19, 2013) ("the Commission has made it clear that it will reward companies or individuals who cooperate, despite the fact that a violation has occurred"); Lanny A. Breuer, Assistant Attorney General, Criminal Division, Department of Justice, Prepared Remarks to Compliance Week 2010—5th Annual Conference for Corporate Finance, Legal, Risk, Audit & Compliance Officers (May 26, 2010) ("If you come forward and if you fully cooperate with our investigation, you will receive meaningful credit for having done so"); Prepared Remarks of Alice S. Fisher, Asst. Attorney General, Department of Justice, at the ABA National Institute on the FCPA (Oct. 16, 2006) ("although nothing is left off the table when you voluntarily disclose, I can tell you in unequivocal terms that you will get a real benefit").
9. United States Attorney's Manual §9-28.300 (A)(4).
10. Resource Guide to FCPA at p. 55.
11. See United States Sentencing Guidelines §8B2.1, Application Note 6.
12. 15 U.S.C. §§78dd-2(g)(1)(A), (g)(2)(A); 15 U.S.C. §78ff(a); 18 U.S.C. §3571.
13. Peter Lattman, "Ralph Lauren Corp. Agrees to Pay Fine in Bribery Case," The New York Times (April 22, 2013).
14. SEC Press Release, "SEC Announces Non-Prosecution Agreement with Ralph Lauren Corporation Involving FCPA Misconduct" (April 22, 2013).
15. Covington & Burling, "The Ralph Lauren Case: Inadequate Rewards for Exemplary Corporate Cooperation" (April 26, 2013).
16. Mike Koehler, "Ralph Lauren Enforcement Action Commentary—Hits and Misses," FCPA Professor Blog (April 29, 2013).
17. Avon Products 10-Q (Nov. 1, 2012).
18. Joe Palazzolo and Emily Glazer, "Foreign Bribe Case at Avon Presented to Grand Jury," The Wall Street Journal (Feb. 13, 2012).
19. Richard L. Cassin, "Feds Reject Avon Settlement Offer," The FCPA Blog (Aug. 1, 2013).
20. Avon 10-Q at p. 14 (Oct. 31, 2013).
21. Id. at p. 15.
22. Jed S. Rakoff and Jonathan S. Sack, Federal Corporate Sentencing 5-10–5-12 (Rev. Ed. 2007); Testimony of Michael Volkov Before the Senate Judiciary Committee, Subcommittee on Crime and Drugs, Hearing on "Examining Enforcement of the Foreign Corrupt Practices Act" (Nov. 30, 2010).
23. Hilary Russ, "DOJ Says No to Amnesty Program for FCPA Cases," Law360 (Nov. 30, 2010); see also Testimony of Greg Andres, Acting Deputy Assistant Attorney General, Before the Subcommittee on Crime and Drugs, Senate Committee on the Judiciary (Nov. 30, 2010).