
ACC DOCKET

INFORMED. INDISPENSABLE. IN-HOUSE.

Joint Ventures and FCPA Risk Management

Compliance and Ethics



CHEAT SHEET

-
- **Good faith efforts.** Under FCPA accounting requirements, a non-controlling JV partner is held to a lesser standard than its majority holders so long as they establish “good faith efforts” to meet compliance regulations.
 - **The fatal four.** All four elements of anti-bribery provisions must be present to impose liability under the FCPA: the act, the intent, the recipient, and the purpose behind the underlying act.
 - **Watchful eye.** Prior to entering a joint venture, due diligence processes should be put in place by each potential JV partner on its counterparty to evaluate their reputation and FCPA compliance record.
 - **Set the standard.** By negotiating the compliance framework in the JV agreement, non-controlling JV partners can manage FCPA counterparty risk and address compliance early.

The continuing trend of expanding enforcement of the Foreign Corrupt Practices Act (FCPA) creates a heightened risk for businesses participating in international transactions. Often overlooked is the liability present for a non-controlling, minority investor in a joint venture project (a non-controlling JV partner). Despite their lack of authority, a non-controlling JV partner can be “on the hook” for any FCPA violation made during the process. This threat accentuates the necessity of proactive risk mitigation efforts and must be considered against the potential economic benefit of participating as a non-controlling JV partner. This article discusses strategic considerations for FCPA compliance from the perspective of a non-controlling JV partner.

FCPA implications in joint ventures

The legislative and enforcement history of the FCPA is well known. The US Congress enacted the FCPA to combat corrupt practices by US companies involving foreign government officials. Both the US Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) enforce the FCPA. Although a domestic non-controlling JV partner may avoid contact with foreign representatives, FCPA regulations can impose liability to the minority party based solely on the actions of either the non-controlling or the controlling JV partner. Moreover, if a parent company exercises a sufficient amount of control over its JV subsidiary partner, the subsidiary’s liability can be imputed to the parent company. Consequently, JV partners must engage in their own compliance practices — often a challenging role for non-controlling parties.

The FCPA has two categories of offenses: (1) the accounting provisions that require companies to maintain adequate books and records and internal controls, and (2) the anti-bribery provisions that prohibit covered actors from bribing or otherwise influencing “foreign officials” in order to obtain or retain business.

Accounting provisions

The FCPA accounting provisions apply to entities with securities that are registered for trading on the US exchange or are otherwise required to file reports with the SEC. This extends to an entity’s wholly owned and majority-controlled subsidiaries as well. Thus, theoretically, one joint-venturer (and the parent of the joint-venturer) could be subject to FCPA regulations while the other venturer is not. In context, the standard for liability under these provisions is dependent on whether the joint-venture partner is the majority or minority interest holder. While a majority holder is strictly liable for the JV’s books and records, a non-controlling JV partner is subject to a lesser standard. A noncontrolling JV

partner is presumed to comply with accounting provisions so long as it demonstrates “good faith efforts” to meet with FCPA requirements. For this reason, it is critical that non-controlling JV partners establish effective compliance protocols before entering into the joint venture and insist on contractual obligations through the process.

These FCPA accounting requirements apply to all joint venture business dealings, and are not exclusive to transactions with foreign officials. More importantly, there is no materiality requirement, meaning that even the most trivial transactions can result in liability if not accurately recorded. Because the accounting provisions operate independently of the FCPA’s anti-bribery provisions, a transaction that may be legal from an anti-bribery perspective must still comply with the accounting provisions. For example, even though a payment made to a government official may fall outside the jurisdiction of the anti-bribery provision, there is still a potential for FCPA culpability if the payment is mischaracterized, or if the joint venture has maintained an inadequate internal control system.

Anti-bribery provisions

Nearly all US joint ventures are subject to FCPA anti-bribery provisions. This includes business entities, as well as individual actors, such as officers, directors, employees, and shareholders. Unlike the accounting provisions, FCPA anti-bribery provisions are the same for both majority and minority JV parties. There is no strict liability due to the requirement for active participation in or knowledge of the unlawful circumstance. A robust FCPA compliance program is critical for any company to manage counterparty FCPA risk prior to entering into a joint venture.

The standard for liability of a domestic actor is low, as the use of any means of interstate commerce (i.e., using mail, email, telephone, text message, fax, wire transfer, or methods of transportation from, to, or through the United States) in furtherance of any payment to a foreign official is considered corrupt. These provisions cover actions occurring both within and outside the United States. For a foreign actor, this interstate commerce requirement is removed.

All four elements of the anti-bribery provision must be present to impose liability under the FCPA: the act, the intent, the recipient, and the purpose behind the underlying act. Each element is applied broadly by enforcement agencies. In essence, the anti-bribery provisions cover inducements offered or tendered for the purpose of obtaining an unfair business advantage.

Exceptions and affirmative defenses to the anti-bribery provisions

The FCPA anti-bribery provisions provide a narrow exception for payments made in furtherance of routine governmental action. Whether or not a governmental action is routine depends on whether discretion is involved with the action. The amount of the payment is irrelevant. Accordingly, examples of non-discretionary acts by foreign officials include obtaining permits or licenses to do business in a foreign country, processing visas, and scheduling inspections.

The FCPA includes two additional defenses. There is no FCPA liability for actions that are lawfully committed under the standards of another country (the “local law” defense), or where the payment is related to the promotion of the products, services, or performance of a contract with a foreign government (the “reasonable and bona fide business expenditure” defense). To be clear, the absence of written laws in a foreign country does not, by itself, sufficiently satisfy the “local law” defense; in fact, this defense is rarely available. Under the “reasonable and bona fide business expenditure” defense, the DOJ has suggested that the following acts are permissible: travel and expenses related to visiting company facilities, training, product demonstrations, and promotional

activities. Again, these actions still must comply with the accounting provisions.

Mitigating FCPA risks in JV transactions

Effective compliance policy and procedures

Prior to considering a joint venture investment, companies should adopt an internal FCPA compliance program. Any potential joint venture counterparty will expect one to be in place and will establish best practices that can be imposed on the joint venture. An effective FCPA program should create a culture for preventing, detecting, remediating, and reporting misconduct. Establishing an effective compliance program at both the parent and the subsidiary JV level will make it easier to manage the compliance program through the process. Even if a potential violation occurs, having an effective program in place can decrease and even eliminate DOJ and SEC charges related to the violation. Although compliance programs will be customized for each unique joint venture, fundamental elements of an effective compliance program include:

- Specific FCPA policies and practices;
- Training officers, directors, and employees on FCPA policies;
- Appointing FCPA compliance officers for the JV;
- Creating a system for reporting potential infractions;
- Establishing accounting procedures in line with GAAP;
- Including FCPA language in all JV contracts;
- Updating the board of directors periodically on FCPA compliance; and,
- Executing continued due diligence as necessary.

Due diligence

Prior to entering into a joint venture, exhaustive due diligence should be performed by each potential JV partner on its counterparty. It is vital to evaluate a potential partner's reputation and historical FCPA compliance record, including how the partner came to acquire its assets, licenses, and contracts to ensure that each was properly obtained. Additionally, there should be an examination of the potential partner's anti-bribery policies in comparison to FCPA standards. Due diligence should cover the potential partner's relationship with foreign officials, including any third party intermediaries and consulting agreements. Red flags discovered during the diligence process should not be ignored. Non-controlling parties will be held liable for unlawful circumstances they should have known about. Documenting the due diligence effort is critical to showcasing a party's efforts to prevent FCPA violations.

Contractual protections in the JV agreement

The governing agreements for the joint venture can mitigate the risk of future potential liability. Often, formation of the joint venture will be the only opportunity for a non-controlling JV partner to establish obligations that the joint venture owes to it. The noncontrolling JV partner should demand the following:

- Membership on the board of directors or governing body;
- Covenants for ongoing due diligence (on assets added to the JV after formation);
- Audit rights (allowing either partner to request audits of the JV);
- Exit strategies (termination rights and put options);

-
- Business conduct (covenants prohibiting payments to foreign officials; representations and warranties that improper payments have not been made in the past); and,
 - Covenants implementing an FCPA compliance program.

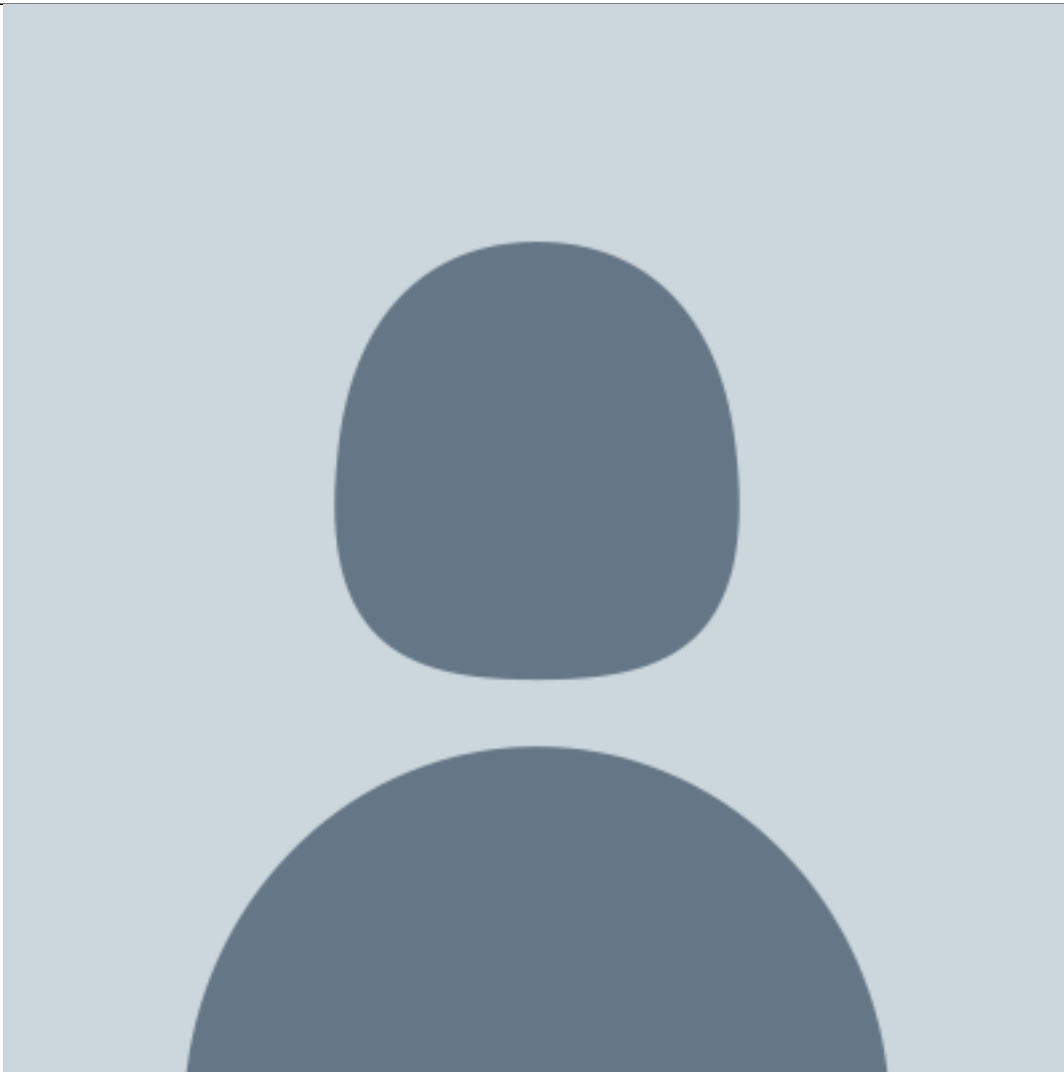
Negotiating for a compliance framework in the JV agreement allows non-controlling JV partners to manage the FCPA counterparty risk that's inherent in joint ventures. A noncontrolling JV partner should address compliance early in the negotiation process while leverage is at its peak. Exploring compliance issues early will complement the due diligence process and provide a better understanding of the potential JV counterparty.

Conclusion

In some cases, non-controlling JV partners need to perform more research on their controlling partners than they do on their typical acquisition target. A non-controlling JV partner must demonstrate "good faith efforts" to use its influence to cause the joint venture's books and records to meet FCPA requirements. In other words, a non-controlling JV partner has an affirmative obligation to be involved with the JV's accounting processes and, though not strictly liable for compliance, ambivalence will increase the liability risk. Under the anti-bribery provisions, a non-controlling JV partner can be liable for its own actions, as well as the acts of its JV counterparty, even including acts related to the JV occurring both before and after the joint venture's formation. This standard establishes the necessity of rigorous due diligence before and during the operation of the joint venture. As an additional risk, international JV counterparties may not be subject to the FCPA, making it even more crucial to develop and implement FCPA compliance protocols for the joint venture. Overall, each JV partner should be cognizant of the FCPA's impact on the timing, risk exposure, and potential investment return of the transaction as a whole.

Non-controlling JV partners should not take the risks associated with the FCPA lightly. In order to strengthen risk mitigation efforts when establishing a joint venture, the parties should anticipate FCPA compliance as a necessary component of the transaction.

[John L. Rudy](#)

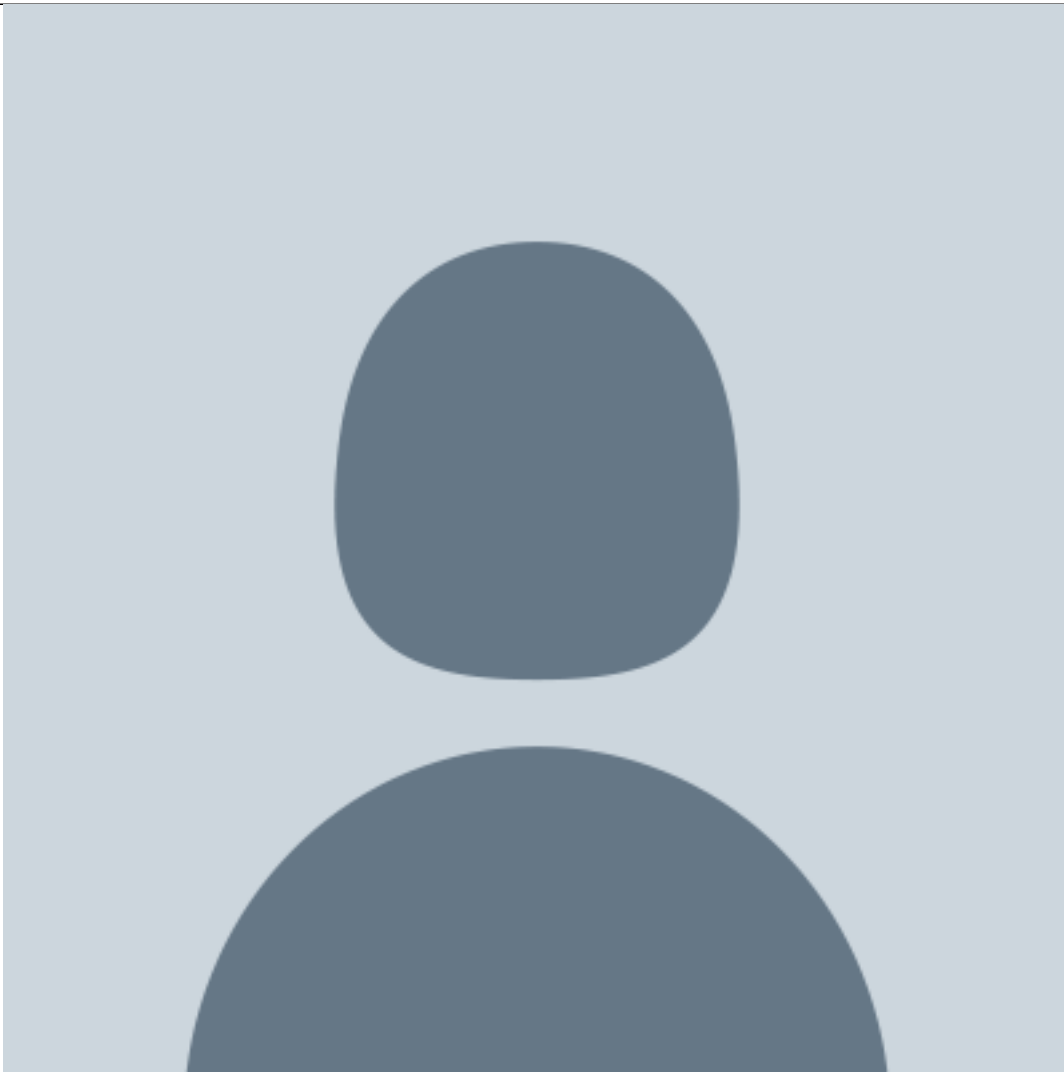


Senior Counsel

the SEC/finance group at Deere & Company

He supports the corporate secretary. He serves as the primary lawyer for investor relations and his responsibilities include proxy disclosure, pension fund support, securities, corporate governance, and compliance.

[Anshu Pasricha](#)



Partner

Koley Jessen, PC, an Omaha based law firm

He has a broad, multidisciplinary practice that includes counseling strategic corporate and private equity sponsors in domestic and international M&As, joint ventures, divestitures, and general corporate matters