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## Legal Issues in International Philanthropy

Wednesday, May 29, 2013  
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Association of Corporate Counsel Nonprofit Organizations Committee Webcast

**Moderator:**

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# Tax Considerations of International Grantmaking in Today's World

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# Recent Developments in International Philanthropy – Best Practices

- PRIVATE FOUNDATION DISTRIBUTION RULES
  - Private Foundations are required annually to make “Qualified Distributions” equal to 5% of their assets
  - Grants to “non-charities” are deemed to be taxable expenditures subject to penalty taxes unless expenditure responsibility is exercised

## Grants to Foreign Charities

- Grants to foreign charities will be deemed qualified distributions and will not be treated as taxable expenditures if:
  - The foreign charity has been recognized by the IRS as a 501(c)(3) public charity
  - Donor foundation makes a good faith determination that the foreign grantee is the equivalent of a US public charity by either:
    - Exercising expenditure responsibility, or
    - Making an equivalency determination

## Expenditure Responsibility

- Pre-grant inquiry – limited inquiry concerning potential grantee
- Requires written agreement with grantee that
  - Requires repayment of amounts not used for grant purposes
  - Annual reporting
  - Make books and records available
  - Prohibit activities not consistent with 501(c)(3) status
- Donor must report expenditure responsibility grants on its annual Form 990-PF

## Equivalency Determination

- Grantor private foundation makes a good faith determination that the foreign grantee is the equivalent of a US public charity based on either:
  - An affidavit of the grantee
  - An opinion of counsel (of the distributing foundation or the donee organization) – “old law”
  - Written advice from an attorney, CPA or enrolled agent that the organization is the equivalent of a US public charity – proposed regulations issued 9/24/12

## Affidavit of Grantee

- Must be in English
- Requirements set out in Rev. Proc. 92-94
- Requires fair amount of information
- Grantee may find it difficult to provide



## Opinion of Counsel

- Under “old law” was very expensive
- Proposed regulations permit advice from “any” attorney, CPA or enrolled agent (not just counsel to the distributing foundation or donee organization) – should lower costs of equivalency determination
- Opens door to possibility of creating a “repository” of equivalency determinations available to any foundation

## When to Use Expenditure Responsibility

- Grantee's governing documents are in a foreign language and not easily translated
- Grantee has poor recordkeeping
- Hard to determine if grantee is a public charity
- One-time grant to grantee
- Need to make grant quickly – e.g. disaster relief

# When to Make an Equivalency Determination

- Grantee is a church, school or hospital
- Grantor anticipates making multiple grants to grantee over a period of years
- Grant is for capital equipment or for endowment
- General support grants, rather than support of a specific program
- Grantee will find it difficult to do annual reporting

## What's Next

- Comment period on proposed regulations just ended
- Treasury looking at continued viability of affidavits from grantee and putting an “expiration date” on equivalency determinations
- Continued move to standardizing and simplifying process
- Will also help public charities (e.g. community foundations) making foreign grants

# The FCPA and Anti-Corruption Enforcement

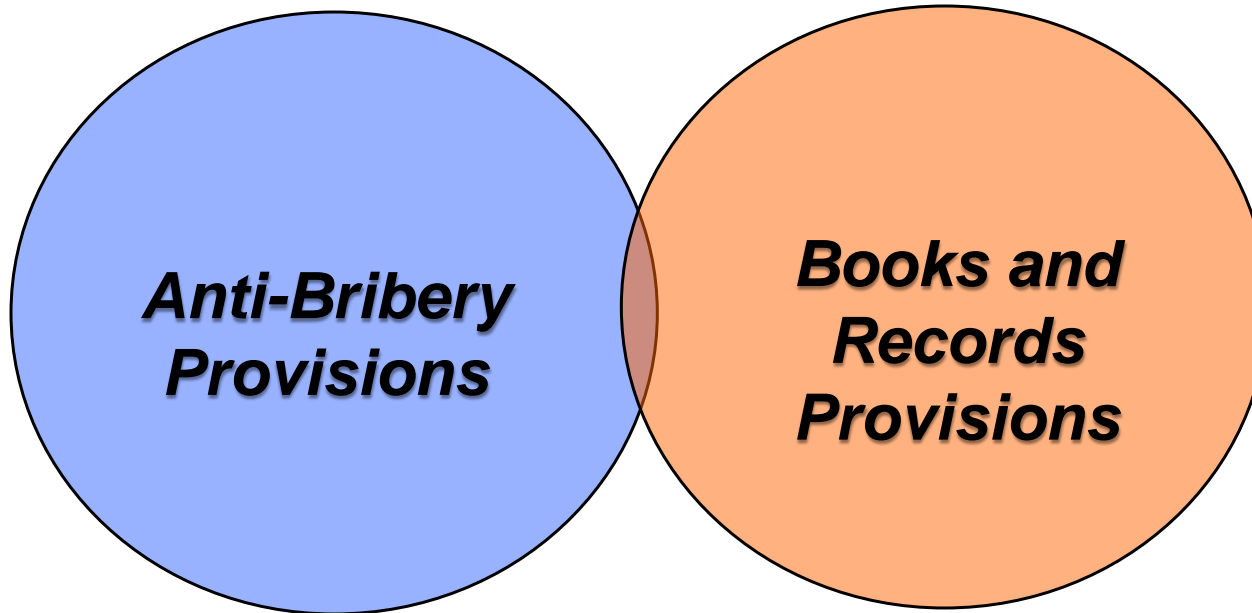
*Robert L. Waldman*

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# What Is the FCPA?

- Enacted by Congress in 1977 to halt practice of bribing foreign officials
- Two main provisions:



- Jointly enforced by the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC)

# The Anti-Bribery Provisions

## 15 U.S.C. § 78dd-1

- Prohibit paying, or offering or promising to pay (or authorizing to pay or offer) money or “anything of value,” directly or indirectly, with corrupt intent,
- To a “foreign official,” political party, political party official, or a candidate for political office,
- For the purpose of influencing an official act or decision, or
- Causing the official to fail to perform his lawful duty, or
- To secure any improper business advantage,
- To assist in obtaining or retaining business for or with any person,
- Limited exceptions and affirmative defenses exist.



# The Books and Records Provisions

## 15 U.S.C. § 78m

- Require “issuers,” *i.e.*, any company, including non-U.S. companies, that publicly trade on a U.S. exchange:
  - To make and keep books and records which “accurately reflect” business transactions, and to make and keep accounts of all payments; and
  - To devise and maintain reasonable, “effective” internal controls for preventing and detecting FCPA violations.





# The Devil Is in the Details...

- “Anything of value”
- “Directly or indirectly”
- “Foreign official”
- “Obtaining or retaining business”



# Who Is Subject to the FCPA?

- **All U.S. companies conducting business abroad, most non-U.S. subsidiaries of U.S. companies, and U.S. subsidiaries of non-U.S. companies**
- **Non-U.S. companies whose securities trade on U.S. exchanges *via* American Depository Receipts (“ADRs”)**
- **Territorial Jurisdiction: Both DOJ and the SEC take an extremely broad view of U.S. FCPA jurisdiction. According to DOJ and the SEC, any contact with the U.S. in furtherance of the corrupt scheme—no matter how fleeting—e.g., e-mails, telephone calls, use of U.S. accounts to clear dollar-denominated transactions (“correspondent bank accounts”)—gives rise to FCPA jurisdiction**
  - For example: In 2011, DOJ accused JGC, a Japanese corporation, of bribing Nigerian government officials to obtain business related to designing and building a liquefied natural gas plant. The criminal information against JGC applied a “territorial jurisdiction” theory, which resulted from JGC’s co-conspirator’s use of correspondent bank accounts to transfer alleged bribes between two foreign banks. JGC agreed to pay a \$218.8 million criminal penalty as part of a two-year deferred prosecution agreement with DOJ
  - For example: Also in 2011, Magyar Telecom was accused of entering into a secret agreement with high-ranking Macedonian officials to delay the license applications of competitor telecommunications companies. Magyar Telecom agreed to pay approximately \$63.9 million in criminal penalties to DOJ, and approximately \$95 million in civil penalties to the SEC, where DOJ’s and the SEC’s only claim to jurisdiction was a foreign government official’s U.S.-based e-mail address, which he allegedly used in furtherance of the scheme

## Who Is Subject to the FCPA? (cont.)

### ■ ***Respondeat Superior Liability:***

- Companies subject to the FCPA are vicariously responsible for the actions of their employees, agents, independent sales representatives, distributors, and other service providers, so long as they are acting on the company’s behalf and joint-venture partners
  - Willful Blindness
  - “Directly or Indirectly”
    - For example: BAE made unlawful payments to “market advisors” to facilitate sales of defense articles to European and Middle Eastern governments. BAE “failed to conduct adequate due diligence into these advisors” who were acting as BAE agents. BAE paid \$400 million and £30 million in penalties

### ■ **All U.S. Persons**

# Willful Blindness

- **FCPA applies only to knowing violations, in other words payments made with corrupt intent.**
- **BUT:**
  - Turning a blind eye where there is a probability that an illegal payment is likely may equate to “willful blindness,” which satisfies the knowledge or corrupt intent requirement.
- **Examples where “knowledge” might be found:**
  - Doing business in a country with rampant corruption without vetting suppliers and representatives
  - Hiring a foreign representative with a history of making illegal payments without properly supervising or vetting the representative
  - Hiring an agent whose function is unclear
  - Building into a subcontractor’s contract price extra costs for “greasing” the wheels
  - In the 2009 Bourke case in the U.S. District Court for the Southern District of New York, the jury was instructed that “knowledge may be established if a person is aware of a high probability of its existence and consciously and intentionally avoided confirming that fact.” Bourke was found guilty and sentenced to 1 year in jail.



# Affirmative Defenses and Exceptions

- **Extremely limited**
- **When the payment is lawful under the written laws of the foreign government official's country**
  - There are no such written laws
- **When the payment is a reasonable and *bona fide* expenditure, such as travel and lodging expenses, incurred by or on behalf of a foreign government official and directly related to:**
  - The performance, demonstration, or explanation of products or services; or
  - The execution or performance of a contract with a foreign government or agency
- **Facilitation Payment Exception – A narrow exception for nominal payments**
  - Action sought to be facilitated must be ministerial
  - It must not involve any discretion on the part of the foreign government official
  - The amount paid must be modest
  - Tension with “business nexus concept”
  - Contrary to OECD Treaty
  - Violates the U.K. Bribery Act
  - Violates the national law of most nations

# Criminal and Civil Penalties

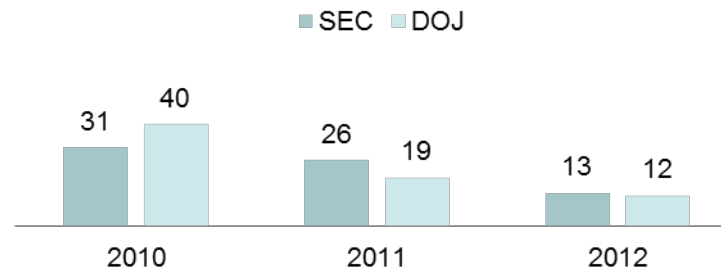
- **Criminal Penalties**
  - For corporations, up to \$2 million per violation or twice the pecuniary gain, whichever is higher
  - For corporate officers, directors, stockholders, employees and agents, up to \$100,000 and imprisonment up to five years
- **Civil Penalties**
  - Disgorgement;
  - Injunction;
  - A fine of \$10,000 per violation; and/or
  - Enhanced penalties of up to \$500,000
- **Private Lawsuits**
  - Currently, the FCPA does not contain a private right of action
  - Nevertheless, civil litigation involving or stemming from alleged FCPA violations is rampant



# Increasingly Vigorous Enforcement Landscape

- Since 2004, DOJ and the SEC, combined, have brought more than 250 enforcement actions against individuals and corporations. This is more than the total number of enforcement actions brought between 1977 and 2004
- 2010 was the most prolific year in the history of FCPA enforcement. In 2011 and 2012, enforcement activity for both DOJ and the SEC was down, but still significant.

**Total SEC/DOJ Enforcement Actions by Year**



- The total amount of sanctions imposed in FCPA cases in 2010 was a staggering \$1.7 billion. DOJ and the SEC, combined, collected approximately \$500 million in penalties in 2011, and approximately \$260 million in penalties in 2012.

# Increasingly Vigorous Enforcement Landscape (cont.)

- Industry Initiatives: Technology/Telecommunications, Government Contracting, Logistics, Tobacco, Health Care, Financial Services, and “Life Sciences” (especially medical device manufacturers)
- Increased governmental resources focused on FCPA
- Increased cooperation with non-U.S. governments and increased non-U.S. prosecutions
- Dodd-Frank Wall Street Reform and Consumer Protection Act
- Successor Liability/Importance of conducting due diligence in M&A transactions



## Corporate Penalties

**Marubeni**  
CORPORATION

*(\$54.6 million)*



*(\$60 million)*

**Allianz** 

*(\$12.3 million)*



Schering-Plough

*(\$500,000)*

*Lilly*

*(\$29.4 million)*

The average penalty paid by corporate defendants in 2012 was  
over \$17 million.

# Enforcement Against Individuals

- In 2012...
  - **Jean Rene Duperval**, sentenced to 9 years in prison for his involvement in the *Haiti Telecom* case. Duperval is the first foreign official to stand trial in connection with an FCPA case.
  - **Albert Jack Stanley**, sentenced to 30 months in prison for his involvement in the *KBR/TSKJ* case.
  - **Manuel Caceres**, sentenced to 23 months in prison for his involvement in the *Latin Node* case.
  - **Fernando Basurto**, sentenced to time served after spending 22 months in prison for his involvement in the *ABB* case.
  - **Jeffrey Tesler**, sentenced to 21 months in prison for his involvement in the *KBR/TSKJ* case.



# UK Bribery Act

- Took effect July 1, 2011
- Guidance issued March 2011
- Companies with a U.K. presence (e.g., a subsidiary, an office, or operations) are exposed to U.K. criminal prosecution for bribes occurring anywhere in the world
- Unlike the FCPA, the Bribery Act has no exception for facilitation payments, prohibits commercial bribery, and reaches the bribe recipient
- It creates strict corporate liability for failure of a corporation to prevent bribery
- Affirmative defense that company had a comprehensive anti-corruption compliance program
- Individual criminal penalties of up to 10 years imprisonment
- Debarment, asset confiscation, and unlimited fines for corporations

# ***Organization for Economic Cooperation and Development***

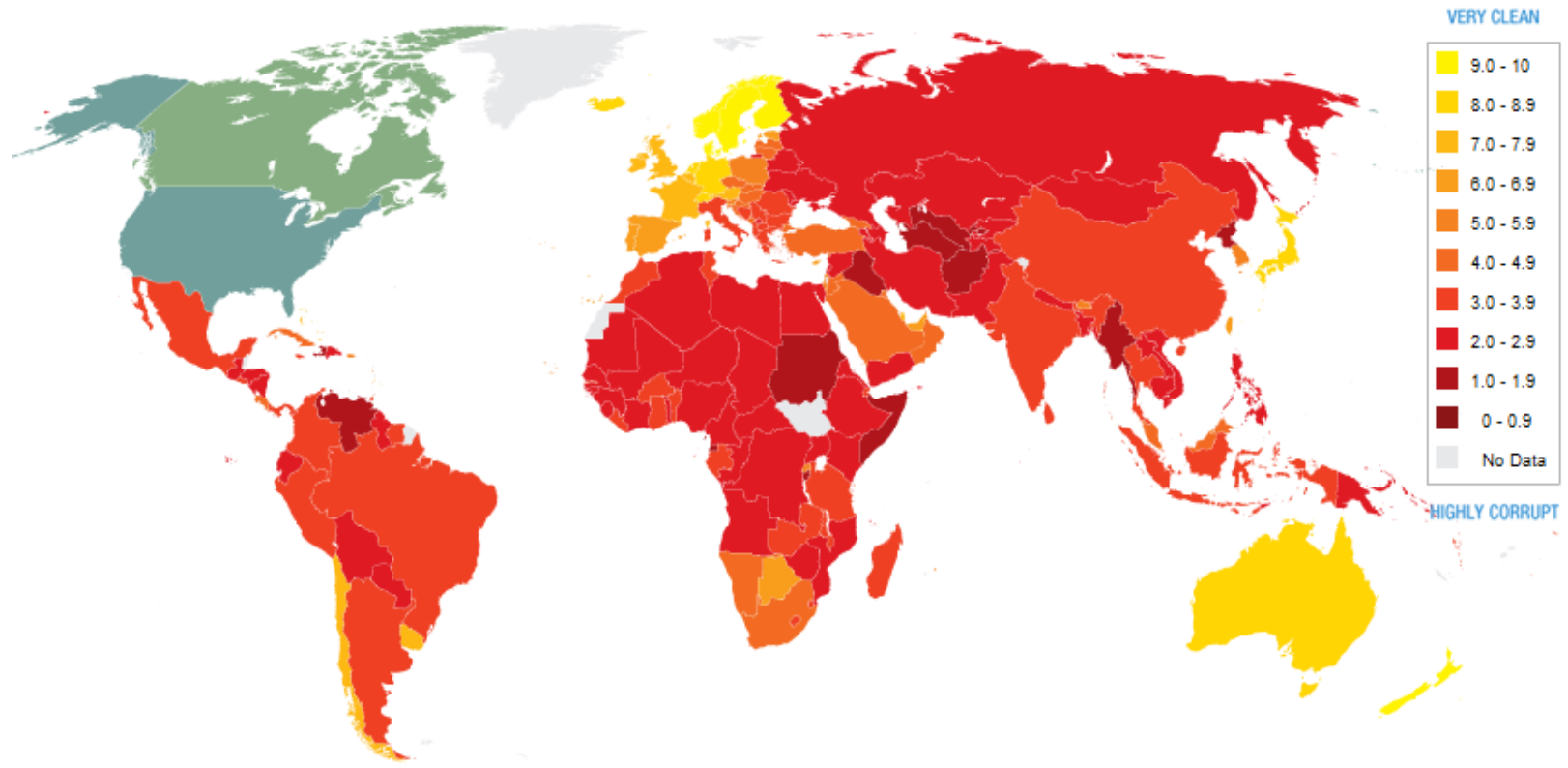
- **38 countries have adopted the OECD Anti-Bribery Convention, requiring national legislation criminalizing the bribery of foreign officials to gain advantages in international business transactions**
  - Including Canada, Brazil, Spain, Germany, Italy, Japan, U.S., and the U.K.
- **Key Provisions**
  - Scope: Applies to both individuals and companies, as well as third party intermediaries
  - Accounting: Establish laws, as necessary, on maintenance of books and records, financial statement disclosures, and accounting and auditing standards
  - Facilitation payments: Prohibited
  - Monitoring: Establishes systematic monitoring of countries' implementation of the Convention
- **China is not a member of the OECD, but does have a strong working relationship with the OECD and its member countries. Recently, China revamped its anti-corruption laws, which criminalize payments made to non-Chinese government officials and to officials of international organizations for any illegitimate commercial benefit**



## FCPA “Red Flags”

- The transaction is in, or involves, a country identified as being a high corruption risk (e.g., Indonesia, China, India, Iraq, Afghanistan)
- Sales representative or agent is requesting an unusually high “commission” or fee
- The entertaining of, or giving gifts to, government officials or their relatives
- Unusual contract terms or payment arrangements, such as requests for payments in cash or “special” invoices
- *The use of shell companies*
- *The foreign customer’s insistence that a particular agent be used*
- *Role or function of an agent or middleman is unusual or not clear*
- *Extraordinary payments*
- *Charitable donations*
- *Payments via third countries without sound commercial reasons*





RANK	COUNTRY/TERRITORY	SCORE
1	New Zealand	9.5
2	Denmark	9.4
2	Finland	9.4
4	Sweden	9.3
5	Singapore	9.2
6	Norway	9.0
7	Netherlands	8.9
8	Australia	8.8
8	Switzerland	8.8
10	Canada	8.7
11	Luxembourg	8.5
12	Hong Kong	8.4
13	Iceland	8.3
14	Germany	8.0
14	Japan	8.0
16	Austria	7.8
16	Barbados	7.8
16	United Kingdom	7.8
19	Belgium	7.5
19	Ireland	7.5
21	Bahamas	7.3
22	Chile	7.2
22	Qatar	7.2
24	United States	7.1

25	France	7.0
25	Saint Lucia	7.0
25	Uruguay	7.0
26	United Arab Emirates	6.8
29	Estonia	6.4
30	Cyprus	6.3
31	Spain	6.2
32	Botswana	6.1
32	Portugal	6.1
32	Taiwan	6.1
35	Slovenia	5.9
36	Israel	5.8
36	Saint Vincent and the Grenadines	5.8
38	Bhutan	5.7
39	Malta	5.6
39	Puerto Rico	5.6
41	Cape Verde	5.5
41	Poland	5.5
43	Korea (South)	5.4
44	Brunei	5.2
44	Dominica	5.2
46	Bahrain	5.1
46	Macau	5.1

RANK	COUNTRY/TERRITORY	SCORE
46	Mauritius	5.1
49	Rwanda	5.0
50	Costa Rica	4.8
50	Lithuania	4.8
50	Oman	4.8
50	Seychelles	4.8
54	Hungary	4.6
54	Kuwait	4.6
56	Jordan	4.5
57	Czech Republic	4.4
57	Namibia	4.4
57	Saudi Arabia	4.4
60	Malaysia	4.3
61	Cuba	4.2
61	Latvia	4.2
61	Turkey	4.2
64	Georgia	4.1
64	South Africa	4.1
66	Croatia	4.0
66	Montenegro	4.0
66	Slovakia	4.0
69	Ghana	3.9
69	Italy	3.9
69	FYR Macedonia	3.9

69	Samoa	3.9
73	Brazil	3.8
73	Tunisia	3.8
75	China	3.6
75	Romania	3.6
77	Gambia	3.5
77	Lesotho	3.5
77	Vanuatu	3.5
80	Colombia	3.4
80	El Salvador	3.4
80	Greece	3.4
80	Morocco	3.4
80	Peru	3.4
80	Thailand	3.4
86	Bulgaria	3.3
86	Jamaica	3.3
86	Panama	3.3
86	Serbia	3.3
86	Sri Lanka	3.3
91	Bosnia and Herzegovina	3.2
91	Liberia	3.2
91	Trinidad and Tobago	3.2
91	Zambia	3.2
95	Albania	3.1

RANK	COUNTRY/TERRITORY	SCORE
95	India	3.1
95	Kiribati	3.1
95	Swaziland	3.1
95	Tonga	3.1
100	Argentina	3.0
100	Benin	3.0
100	Burkina Faso	3.0
100	Djibouti	3.0
100	Gabon	3.0
100	Indonesia	3.0
100	Madagascar	3.0
100	Malawi	3.0
100	Mexico	3.0
100	Sao Tome and Principe	3.0
100	Suriname	3.0
100	Tanzania	3.0
112	Algeria	2.9
112	Egypt	2.9
112	Kosovo	2.9
112	Moldova	2.9
112	Senegal	2.9
112	Vietnam	2.9
118	Bolivia	2.8
118	Mali	2.8

120	Bangladesh	2.7
120	Ecuador	2.7
120	Ethiopia	2.7
120	Guatemala	2.7
120	Iran	2.7
120	Kazakhstan	2.7
120	Mongolia	2.7
120	Mozambique	2.7
120	Solomon Islands	2.7
129	Armenia	2.6
129	Dominican Republic	2.6
129	Honduras	2.6
129	Philippines	2.6
129	Syria	2.6
134	Cameroon	2.5
134	Eritrea	2.5
134	Guyana	2.5
134	Lebanon	2.5
134	Maldives	2.5
134	Nicaragua	2.5
134	Niger	2.5
134	Pakistan	2.5
134	Sierra Leone	2.5
143	Azerbaijan	2.4

RANK	COUNTRY/TERRITORY	SCORE
143	Belarus	2.4
143	Comoros	2.4
143	Mauritania	2.4
143	Nigeria	2.4
143	Russia	2.4
143	Timor-Leste	2.4
143	Togo	2.4
143	Uganda	2.4
152	Tajikistan	2.3
152	Ukraine	2.3
154	Central African Republic	2.2
154	Congo Republic	2.2
154	Côte d'Ivoire	2.2
154	Guinea-Bissau	2.2
154	Kenya	2.2
154	Laos	2.2
154	Nepal	2.2
154	Papua New Guinea	2.2
154	Paraguay	2.2
154	Zimbabwe	2.2
164	Cambodia	2.1
164	Guinea	2.1
164	Kyrgyzstan	2.1
164	Yemen	2.1

168	Angola	2.0
168	Chad	2.0
168	Democratic Republic of the Congo	2.0
168	Libya	2.0
172	Burundi	1.9
172	Equatorial Guinea	1.9
172	Venezuela	1.9
175	Haiti	1.8
175	Iraq	1.8
177	Sudan	1.6
177	Turkmenistan	1.6
177	Uzbekistan	1.6
180	Afghanistan	1.5
180	Myanmar	1.5
182	Korea (North)	1.0
182	Somalia	1.0

# OFAC: Office of Foreign Assets Control

- **Part of the Office of Intelligence and Terrorism Finance, U.S. Treasury**
  - “Economic Warriors” of the US
- **Mission is to enforce economic sanctions programs imposed by the President or Congress against:**
  - Countries (e.g., Iran, Sudan, Cuba, North Korea)
  - Foreign Groups of Persons
    - Terrorist Organizations and individual terrorists
    - Political parties
    - Drug kingpins & traffickers
- **Private Sector Responsibilities:**
  - Private Sector as government agent
  - “Specially Designated Nationals List” (SDN List)
  - Civil and criminal fines, jail terms
    - Greater of \$250,000 or 2x transaction amount
- **Responsibility for compliance may not be delegated**
- **Down (and up) stream due diligence required**

## AML

- **Know your recipient**



# FCPA Guidance: Charitable Contributions

- In November 2012, DOJ and the SEC jointly released their much-anticipated FCPA Guidance, which describes in detail the agencies' enforcement priorities and explains their interpretation of key FCPA provisions
- The Guidance acknowledges that companies engage in charitable giving as part of legitimate local outreach and that the FCPA does not prohibit charitable contributions, or prevent corporations from acting as “good corporate citizens”
- However, the Guidance emphasizes DOJ's and the SEC's underlying concern that corporations will use charitable contributions as a way to funnel bribes to government officials
- Accordingly, the Guidance outlines due diligence measures and controls, which companies should strive to use whenever they contemplate a charitable contribution. Companies should ask:
  - 1) What is the purpose of the contribution?
  - 2) Is the contribution consistent with the company's internal guidelines for charitable contributions?
  - 3) Is the contribution at the request of a foreign official?
  - 4) Is a foreign official associated with the recipient and, if so, can the foreign official make decisions regarding your business in that country?
  - 5) Is the contribution conditioned upon receiving business or other benefits?

# FCPA Opinion Procedure Releases: Charitable Donations

- **95-01** – Requestor, a U.S.-based energy company, sought to acquire and operate a plant in southern Asia. If the acquisition was successful, the Requestor planned to donate \$10 million to a nearby, public medical complex, which was then under construction. The company’s employees and affiliates would be able to use the complex. The donation was to be made through (1) a U.S. domestic charitable organization and (2) a foreign public LLC, located in the southern Asian country. DOJ decided not to take enforcement action because:
  - The Requestor planned to require FCPA/anti-corruption certifications from all officers of the charitable organization and the public LLC;
  - No one at either the charitable organization or the public LLC was affiliated with a foreign government; and
  - The Requestor required audited financial reports, accurately detailing the disposition of the \$10 million donation.
- **97-02** – Requestor, a U.S.-based utility company, planned to construct a plant in a country that lacked primary-level educational facilities. As such, Requestor planned to donate \$100,000 to a government entity to fund an elementary school construction project near the new plant. DOJ decided not to take enforcement action, noting that the Requestor:
  - Required a written agreement from the government entity receiving the donation that the funds would only be used to construct/supply the elementary school
  - Made the donation directly to the foreign government, as opposed to any individual foreign government official

# FCPA Opinion Procedure Releases: Charitable Donations (cont.)

- **06-01** – Requestor, a DE corporation headquartered in Switzerland, wanted to contribute \$25,000 to a regional customs department in an African country, as part of a pilot move to improve local enforcement of anti-counterfeiting laws. The money would be used to fund incentive award to local customs officials, since counterfeiting had become such a serious issue in that country. DOJ declined to take any enforcement action, citing the fact that the Requestor planned to execute a formal memorandum of understanding (“MOU”) with the regional customs department, in order to encourage the mutual exchange of information related to trade in counterfeit products, and the proposed MOU was a “sufficient safeguard” against corrupt activity.
- **10-02** – Requestor, a U.S. non-profit microfinance institution, was in the process of converting its local operations from non-profit organizations to commercial financial institutions, e.g., banks. One such operation was a Eurasian subsidiary of the Requestor that had been started with capital from governmental and quasi-governmental foreign aid sources. A foreign agency that regulated the Eurasian subsidiary became skeptical of the transition and pressured the Eurasian subsidiary to “localize” its grant capital by donating to local microfinance institutions (“LMFIs”) on a pre-approved list from the foreign agency. Requestor was concerned that compelled grants to institutions on a short list provided by foreign officials would raise concerns under the FCPA. DOJ approved the grants, however, provided that the Requestor:
  - Conducted appropriate due diligence of the LMFIs; and
  - Instituted controls designed to ensure with reasonable certainty that no funds given to the LMFIs would find their way into the pockets of the foreign officials.
- **Others:**
  - **09-01**
  - **81-02**

# No Good Deed Goes Unpunished...



## ■ SEC v. Schering-Plough

- From 1999 to 2002, Schering-Plough’s Polish subsidiary paid more than \$75,000 to the Chudow Castle Foundation, a charitable organization that restores ancient castles in Poland. According to the SEC, these payments were made in order to influence the Foundation’s president, who was also the Director of a regional Polish health authority and, therefore, a foreign government official, to purchase Schering-Plough pharmaceutical products.
- According to the complaint, none of the payments to the Foundation were accurately reported in Schering-Plough’s books and records.
  - The SEC alleged that the “charitable contributions” at issue were falsely justified for internal purposes as supporting “medical research”; in reality, the payments went towards restoring local historic buildings
- Additionally, Schering-Plough’s internal accounting controls allegedly failed to detect and prevent the improper payments.
- Schering-Plough paid a \$500,000 civil penalty to the SEC and consented to an injunction/cease and desist order in order to resolve the claims against it
  - Curiously, the SEC did not charge Schering-Plough with any violation of the FCPA’s foreign bribery provisions—only the books and records provisions. As a result, some commentators have accused the SEC of “overreaching” in this enforcement action

# Key Takeaways

- Know your recipient and any downstream beneficiaries
- Require anti-corruption compliance certifications from your recipient(s) and, in appropriate cases, downstream beneficiaries
- Require that the recipient(s) provide audited financial statements showing precisely how the charitable contribution is used
- Require a written agreement with the recipient restricting the use of funds to agreed-upon purposes
- Take specific steps to ensure that the charitable contribution (if money) is transferred to a valid bank account
- Confirm that the recipient's commitments (if any) are met before disbursing any funds
- Monitor, monitor, monitor

# Questions?

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