SIMPSON THACHER MEMORANDUM

Last Week's FCPA Decision In The Government's Favor Is A Limited Setback For Subjects Of Federal Corruption Inquiries

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As efforts by U.S. regulators to police foreign corruption have dramatically increased in recent years, practitioners have lamented the lack of caselaw interpreting the U.S. Foreign Corrupt Practices Act (the "FCPA"). The primary source of guidance about the FCPA's scope and application has been settlement agreements between subjects of corruption investigations and federal regulators. In these settlements, however, defendants often implicitly agree to an expansive view of the FCPA in return for putting FCPA-related problems behind them. One of the lurking questions about the meaning of the FCPA has been the scope of the definition of "foreign official" as used in the FCPA and whether it covers officers and employees of state-owned entities. In a highly anticipated opinion last week in *U.S. v. Noriega, et al.*, 10-CR-01031 (C.D. Cal. 2010), a federal judge in the Central District of California answered this question in favor of the government, ruling that a state-owned corporation may qualify as an "instrumentality" of a foreign government and, therefore, officers of these corporations may qualify as "foreign officials" under the FCPA. But a close review of the court's reasoning suggests this decision might not be as significant a setback for subjects of FCPA inquiries as the outcome might suggest.

Background to the Case

In *Noriega*, the DOJ filed FCPA charges against the Lindsey Manufacturing Company, a privately held U.S. company that manufactures equipment used by electrical utility companies, and two of its employees (the "Lindsey Defendants").[1] The indictment alleged that these defendants paid bribes through a third party to two high-ranking employees of the Comisión Federal de Electricidad ("CFE"), an electric company wholly-owned by the Mexican government, in order to obtain business from CFE. The FCPA, of course, prohibits the corrupt payment of anything of value to or intended for foreign political parties, candidates for foreign political office, and, most relevant here, "foreign officials." The FCPA defines "foreign official" as "any officer or employee of a foreign government or any department, agency, or instrumentality thereof."

The Lindsey Defendants moved to dismiss these charges on the grounds that employees of state-owned corporations are not "foreign officials" under the FCPA. They argued, first, that CFE could not be a "department" or "agency" of the Mexican government given the ordinary

[1] The DOJ also filed charges against two employees of a third party agent who allegedly made the improper payments on behalf of Lindsey Manufacturing Company. These defendants did not join in the motion to dismiss.

meaning of those words and, second, that the correct definition of "instrumentality" – particularly in light of Congressional intent at the time the FCPA was drafted – excludes state-owned corporations such as CFE. As a result, according to the defendants, the CFE employees who allegedly received the bribes are not "foreign officials" under the FCPA. The government countered that "CFE is part of the Mexican government, mandated by its constitution, formed by its laws, owned in its entirety by the people of Mexico, and constituted to serve the public." On this analysis, the government concluded that CFE is an instrumentality of the Mexican government and thus officers of CFE are "foreign officials" under the FCPA.

The Decision

On April 20, 2011, Judge Howard Matz of the federal district court in the Central District of California denied the Lindsey Defendants' motion to dismiss. In a written decision, he addressed the arguments made by the parties in some detail and provided his view concerning the correct definition of "foreign official" under the FCPA. Like the litigants, the judge reviewed traditional canons of statutory construction, the Mexican Constitution, the nature of CFE, everyday dictionary definitions, and the FCPA's legislative history, which the judge determined was inconclusive. Judge Matz declined to hold as a matter of law that state-owned corporations can *never* be an "instrumentality" of a foreign government under the FCPA. He reasoned that the definition of "foreign official" must include some category of instrumentalities that are different and apart from government agencies and departments because the term "instrumentality" otherwise would be mere surplusage in the definition of foreign official.

The judge went on to consider whether CFE fell within the group of entities that may properly be considered an instrumentality under the FCPA. In ruling that CFE as a matter of law *may* be an instrumentality of the Mexican government, the judge provided five non-exclusive factors that tend to suggest that a state-owned entity is an government instrumentality: (i) the entity provides a service to many or all citizens of the jurisdiction; (ii) the key officers and directors are, or are appointed by, government officials; (iii) the entity is financed, at least in large part, through governmental appropriations or government-mandated revenues; (iv) the entity is vested with and exercises exclusive or controlling power to administer its designated functions; and (v) the entity is widely perceived and understood to be performing official (*i.e.*, governmental) functions.

Applying these factors to the facts alleged in the Indictment, the judge ruled that CFE could be an instrumentality because it has all of these characteristics. For example, the Mexican Constitution provides that the provision of electricity is solely a government function; CFE supplies power to most of Mexico; CFE was created as a public entity by and is owned by the Mexican government; its Director General is appointed by the Mexican president; and its board consists of various government secretaries. Presumably, at the conclusion of the trial now underway, the jury will be instructed along these lines.

Looking ahead: Implications for Other FCPA Investigations

The ruling is not a whole-hearted endorsement of DOJ's broad interpretation of the FCPA's definition of "foreign official." The judge did not rule that employees of state-owned entities necessarily fall within the definition of "foreign official." Rather, he merely left open the *possibility* that employees of state-owned entities – depending on the specific facts in play – will be "foreign officials."

Indeed, while the judge ultimately ruled that the CFE officers in question may be "foreign officials," he did so only after a close analysis of factual circumstances that many practitioners might agree presented an easy case for this conclusion. For instance, unlike other types of state-owned businesses, CFE provides a service that is constitutionally mandated as an exclusive state function; and CFE even describes itself as a government "agency" on its own website. It remains an open question as to whether employees of other state-owned enterprises that do not share these features – such as a state-owned steel company – would be found to fall within the definition of foreign official. Nonetheless, the judge provided some new guidance for FCPA practitioners seeking to determine whether an entity might be an instrumentality of a foreign government.

In the end, the decision leaves ample room for litigants in other situations to dispute whether state-owned enterprises are covered by the FCPA. In the next few months, that could change. Courts in two other pending FCPA cases – one also in the Central District of California and the other in the Southern District of Texas – are also expected to rule on challenges to DOJ's definition of "foreign official."[2]

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[2] The cases are *U.S. v. Carson, et al.*, 09-CR-00077 (C.D. Cal. 2009) and *U.S. v. O'Shea*, 09-CR-00629 (S.D. Tex. 2009).

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