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# Navigating FCPA Risks Of Minority-Owned Joint Ventures

By **Ben Kimberley and Addison Thompson** (November 5, 2021, 4:09 PM EDT)

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On Oct. 28, Deputy Attorney General Lisa Monaco stated that the U.S. Department of Justice would would further invigorate efforts to combat corporate crime.[1]

While practitioners will likely focus on Monaco's comments regarding topics such as emphasizing individual accountability — i.e., a return to the Yates Memo — it is important not to lose sight of existing risks that are most likely to result in investigations and enforcement actions.

One area that the DOJ and the U.S. Securities and Exchange Commission will no doubt continue to focus on is third-party risks under the U.S. Foreign Corrupt Practices Act. These risks are myriad, ranging from third-party consultants to agents to majority-owned joint venture partners.

An area frequently mentioned among FCPA practitioners relates to minority-owned joint ventures. But due to a relative dearth of regulatory guidance and past enforcement actions, discerning regulators' expectations and the fault lines regarding these common commercial arrangements presents challenges.

What are the FCPA-related risks faced by U.S. issuers that have minority-owned joint ventures? And what should companies do to mitigate those risks? This article seeks to distill key lessons learned for each of these questions.

**Theories of Liability for Minority JVs**

At the outset, we note that there are several potential ways in which regulators may assert FCPA liability associated with minority-owned JVs.

First, while not an independent theory of liability, we note that a minority owner's direct participation in corrupt conduct involving the JV's business can violate the FCPA's anti-bribery provisions, assuming that a jurisdictional basis for such a violation exists.

Perhaps the best known example involves four companies — Technip SA, Snamprogetti Netherlands BV, Kellogg Brown & Root Inc. and JGC Corp. — none of which had a majority interest, involved in a JV to secure natural gas contracts in Bonny Island, Nigeria. The DOJ charged each of the four companies with conspiring to violate the FCPA in connection with paying millions of dollars to Nigerian government

officials, resulting in total enforcement-related penalties of more than $1 billion.

Second, the FCPA's anti-corruption provisions apply to the acts of any agent of an issuer. In that regard, a company potentially could be held liable for the conduct of a minority-owned JV if the JV were an agent of the issuer.

A finding of an agency relationship, in turn, depends on control. In particular, the elements of an agency relationship are (1) mutual assent between the principal and agent, that (2) the principal will control the agent for the benefit of the principal.[2]

Third, the FCPA's accounting provisions — including the internal controls provision — apply to joint ventures, including those that are minority-owned. There are important fault lines in terms of potential enforcement liability and enforcement risk depending on the level of ownership and control in the JV.

On the one hand, an issuer is responsible for "ensuring that ... affiliates under its control, including foreign subsidiaries and joint ventures, comply with the accounting provisions," as articulated by the DOJ and SEC in an FCPA resource guide.[3]

On the other hand, where an issuer holds 50% or less of the voting power, the FCPA

> require[s] only that the issuer proceed in good faith to use its influence, to the extent reasonable under the issuer's circumstances, to cause [the joint venture] to devise and maintain a system of internal accounting controls.[4]

If the issuer "demonstrates good faith efforts to use such influence [it] shall be conclusively presumed to have complied with" to have complied with the accounting provisions.

In that regard, so long as a minority owner does not exercise control over its JV, the obligation to proceed in good faith effectively operates as an affirmative defense to potential violations of the FCPA's internal controls provision.[5]

**Ownership Versus Control**

While owning more than 50% of a joint venture provides a more clear line for liability under the accounting provisions, a company that holds a minority interest in a joint venture also may have enforcement risk similar to a majority-owned issuer if the company exercises control over the joint venture.

Enforcement authorities consider a number of factors to evaluate control, including:

- A large ownership interest among a plurality of owners, i.e., a significant shareholder in a consortium of owners;

- Majority board or leadership representation, i.e., the right to appoint a majority of the board or leadership;

- Consolidated operational management, i.e., most or all key leaders at the joint venture are drawn from or report to the same company;

- Unique veto rights over an entity's actions, i.e., the ability to exercise control of the joint venture through powerful voting rights;

- Commercial arrangements between the parties that affect control, e.g., an operating agreement or other arrangement that confers control on one party; and

- Consolidated books and records between the company and the joint venture.

While no single factor is dispositive, each factor that exists increases the likelihood that a regulator would conclude that the minority owner effectively controlled the joint venture, akin to a majority owner, and thus expect to cause the entity to comply with the FCPA's accounting provisions, just like with a majority-owned affiliate. This is an important risk area to watch for companies structuring joint ventures.

Two enforcement actions involving violations of the FCPA's accounting provisions — BellSouth Corp. in 2002 and ENI SpA in 2020 — demonstrate how FCPA risks are higher for minority JV owners that exercise control over a joint venture.

In BellSouth, the SEC concluded that although the company owned 49% of a Nicaraguan JV, Telefonia Celular de Nicaragua SA, it exercised "operational control [and] had the ability to cause Telefonia to comply with the FCPA's books and records and internal controls provisions."[6]

As evidence of BellSouth's control, the SEC pointed to facts including:

- Via an indirect, wholly-owned subsidiary, BellSouth appointed four of the six JV board members; and

- The operational agreement for the JV made BellSouth responsible for daily operations and long-term planning.[7]

As an added wrinkle, Nicaraguan law prevented foreign companies like BellSouth from acquiring a majority interest in a telecom company. This is another area to watch — i.e., those situations in which an issuer might be required under local law to limit ownership to less than 50%, yet exercise control over the JV.

More recently, in Eni SpA, the SEC brought an enforcement action based on the FCPA's accounting provisions despite the fact that ENI only owned a 43% interest in the JV, Saipem SpA.

While the SEC described Eni as the controlling minority shareholder in its administrative order, the SEC did not elaborate on the specific factual bases upon which it concluded that control existed, though we note that Eni was the largest shareholder.[8]

The SEC instead focused on the fact that Saipem's chief financial officer — who was involved in approving allegedly improper payments to a third party — later became Eni's CFO, and continued to facilitate the payments to the third party in his new role.

The SEC noted that because the CFO was "aware of and participated in Saipem's conduct, Eni failed to proceed in good faith to use its influence to cause Saipem to devise and maintain a system of internal accounting controls."[9]

In sum, Eni and BellSouth illustrate that regulators will pressure test both whether a company exercises control over a minority-owned JV and whether it acted in good faith.

**What Good Faith Requires**

In those cases where a minority owner does not control the JV, a company can focus on proceeding in good faith to influence the JV to comply with the FCPA's internal controls provisions.

However, "good faith" is not defined in the FCPA, and regulatory guidance and enforcement actions provide only limited guidance.

Establishing that an issuer exercised good faith efforts to influence its minority-owned JV entails a fact-intensive inquiry focused, at a minimum, on "the relative degree of the issuer's ownership of the domestic or foreign firm and the laws and practices governing the business operations of the country in which such firm is located," as stated in FCPA.[10]

The FCPA's legislative history also makes clear that this is not an exhaustive list, and that other factors may also be important in evaluating whether the issuer has made good faith efforts to cause its minority-owned subsidiary to devise and maintain adequate internal accounting controls.[11]

Eni provides one instructive example where regulators concluded that the requirement to proceed in good faith was not met. There, according to the SEC, the minority, controlling owner's CFO participated in conduct that circumvented the JV's controls in order to execute improper contracts with a third party.

In that regard, Eni could be said to have acted with bad faith with respect to the JV's internal controls, leaving little doubt that Eni could not satisfy the good faith requirement.

In addition to the CFO's specific conduct underpinning this enforcement action, the SEC highlighted a number of alleged deficiencies as examples of programmatic failures falling short of the good faith requirement, including in the areas of third-party diligence, contract execution, internal reports follow-up, audit thoroughness, and various procurement and financial review-related controls and policies.

**Practical Tips for Minority, Noncontrolling Owners**

As a practical matter, companies will have a number of opportunities to demonstrate good faith during the formation, design and operation of the joint venture.

The specific steps that a company should take will, of course, depend on facts, such as the level of ownership in the JV — i.e., the greater the ownership, the greater the expectation in terms of what good faith requires, given the expectation that the company will have more influence.

The following steps provide a foundation upon which to build:

- Joint venture compliance diligence: Engage, when possible, in preacquisition integrity due diligence on JV transactions.

- Compliance leadership: Drive compliance as a key agenda item through board representation and the appointment of personnel, as appropriate for the size and risk of the JV.

- Programmatic building blocks: Encourage the creation of the foundational scaffolding of a risk-based compliance program, such as a Code of Conduct and key policies and controls for relevant risk areas.

- Training and awareness: Train majority partner personnel of JVs on compliance issues, in addition to supporting and encouraging efforts to train JV personnel.

- Audit rights: Obtain and exercise audit rights where necessary or appropriate. Consider conditioning the audit right on a triggering event.

- Seek influence to address the greatest risk areas: Seek to obtain veto-approval rights in higher-risk compliance areas, such as use of third-party intermediaries — see BellSouth and Eni, both of which involved third parties — and procurement.

- Issue identification and remediation: Emphasize issue escalation, and promptly and robustly respond to any corruption-related issue that comes to light.

Minority owners should take steps to ensure that these efforts are directed at the greatest risk areas.

While compliance-focused risk assessments are a best practice in designing and fine-tuning compliance programs, the reality is that a minority owner may have limited access to JV personnel, thus limiting opportunities for risk assessments. One solution is to encourage the majority owner to do so, and to offer support or participate in a listening mode.

Moreover, it is important to ensure that there are open communication channels between the company's compliance team and company personnel with the greatest direct visibility into the JV's operations.

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[1] See https://www.justice.gov/opa/speech/deputy-attorney-general-lisa-o-monaco-gives-keynote-address-abas-36th-national-institute.

[2] See, e.g., Fisher v. Townsends, Inc., 695 A.2d 53, 57 (Del. 1997).

[3] A Resource Guide to the U.S. Foreign Corrupt Practices Act, Second Edition, p. 43.

[4] 15 U.S.C. § 78m(b)(6).

[5] Id.

[6] See https://www.sec.gov/litigation/admin/34-45279.htm.

[7] Id.

[8] See https://www.sec.gov/litigation/admin/2020/34-88679.pdf.

[9] Id.

[10] 15 U.S.C. §78m(b)(6).

[11] H.R. Rep. No. 100-576, at 917 (1988).