Speaker 1: [inaudible]

Speaker 2: Welcome to the GT ABC podcast. I'm your host, Cuneyt Akay here. The GT stands for Greenberg Traurig and the ABC stands for anti-bribery [00:00:30] and corruption. In this episode, we're going to turn our attention to the recently passed national defense authorization act or N D A. And first, we're going to start off by discussing what the NDA does in terms of the expansion of the SCCs power to disgorge profits from ill-gotten gains. And we're going to talk about how this relates to FCPA and FCPA violations. And second, we're going to discuss the reasons behind the NDAs corporate [00:01:00] transparency act ban on anonymous shell companies and what those provisions mean and what effects they may have also on FCPA compliance now to talk about the NDA I'm joined on this episode by our guests, Sarah Mathews, Sarah is a senior associate in GTS Denver office for the last decade. Sarah has focused her practice on government investigations of all types, including anti-corruption and anti money laundering investigations. Before joining us in the [00:01:30] Denver office, Sarah lived in DC and worked in the GT DC office for five years. She has a wealth of experience handling client concerns about government enforcement, of anti-corruption and financial statutes and regulations like the ones we're about to discuss in this episode. So, first of all, Sarah, welcome to the podcast. And can you start by explaining to our listeners what the NDA is

Speaker 3: Tonight? Thank you for having me on the ABC podcast. Um, so basically [00:02:00] the NDA is a piece of legislation that's passed to annually that authorizes the countries department of defense budget. It's mostly just an appropriations bill, but sometimes includes, uh, related legislation. And it's usually fairly routine this year. There was a little bit of drama because president Trump actually vetoed the bill that Congress had enough votes to override the veto and delivered its first override of a Trump veto [00:02:30] nearly four years into his presidency on January 1st. So the 2021 NBA is now in effect with the congressional override.

Speaker 2: Well, when we think of FCPA and anti-corruption, we usually don't think of the NDA, but this year was different. And so Sarah, can you kind of walk us through and tell us why this year's NDA was specifically different and how that relates to this podcast?

Speaker 3: Sure. Uh, well this year, in addition to the routine appropriations of [00:03:00] the defense budget, there were some substantive ad-ons to the law and this includes an expansion of the FCCS disgorgement power. And so what the NDA does is explicitly allow for disgorgement as a sec, remedy discouragement is basically a remedy in FA in federal court to recover profits from the company, sound to a violated the exchange act and recover ill gotten gains and disclosure. It can serve a variety of [00:03:30] purposes, but its main purpose is to deter future violations, Ru getting ill, gotten gains in federal district court. So,

Speaker 2: You know, before this year's NDA was passed, what did disgorgement look like? What was the landscape for the SCCs power to, uh, use disgorgement?

Speaker 3: So the FTC had been using discouragement as a remedy for years, but their, their power for discouragement, there was no expressed [00:04:00] statutory provision, allowing them to do this. They mostly use the exchange act power to seek equitable relief. And so a few cases challenged the sec has authority to use the scores meant saying that the scores weren't really isn't an equitable remedy, but it's a, it's a punitive one. So the first case that challenge this discouragement power was a case called [inaudible] versus sec, uh, went up to the Supreme court and they got a partial victory on that front. [00:04:30] Uh, when the Supreme court found the perspective of limitations purposes, discouragement is a penalty. So it's only five years. And then in justice last year, there was a case called Lew versus sec. I actually co-authored a silent alert about this case is if you're interested in more information about that, but the defendant directly challenged the FCCS disgorgement authority and argued that the scorcher in itself is not a proper remedy [00:05:00] under this equitable relief provision of the exchange act. So the Supreme court ultimately upheld that the scores tend to be an equitable remedy and it survived the Lew case, but the Supreme court also limited the FTCs power to use the score judgment. It basically limited the recovery to the amount of net income generated from the unlawful conduct. And it had to follow certain guidelines to sit [00:05:30] within the scope of equitable relief. So while discouragement survived under the case, the FTCs power was limited in that regard.

Speaker 2: Well, Sarah, as you mentioned, and I, and I read and enjoyed the GT alert that you did over the summer on the loo case, and we will certainly make sure that we disseminate that GT alert as we're putting this podcast on our social media platforms as well. But let's talk for a second about you. So we came out of the cook cash and the loo case, [00:06:00] what does the NDA do to expand the SCCs discouragement authority now?

Speaker 3: So the NBA discouragement provisions can be seen as a direct response to loo, but the first thing it does is make it clear that discouragement is a proper remedy. It makes it explicit in the statute without having to rely on this, uh, sort of a more serious, equitable relief provision. And so it's not limited by what's equitable, [00:06:30] um, necessarily. And then the second thing it does is it supersedes co cache by explicitly stating that disgorgement has a 10 year statute of limitations instead of the five year that [inaudible] held.

Speaker 2: Well, I generally hate, and I think most attorneys hate to make predictions. So I won't ask you about predictions, but I will ask you, what do you expect will happen now regarding sec enforcement with this expanded discouragement power that the, uh, the sec has been given in the NDA?

Speaker 3: [00:07:00] So I, I think that the sec will now be emboldened to seek discouragement over a longer period of time through the longer statute of limitations. And, you know, since it's no longer constrained by the equitable relief language of the exchange act, it can go beyond the holding of the loo case and, uh, go into, uh, may go beyond net profits and into punitive territory for particularly egregious violations [00:07:30] here. So tonight, what does this mean from an FCPA perspective?

Speaker 2: This is an interesting development from an FCPA perspective in that, and as listeners to the podcast. Now, you know, the sec is one of the two agencies that enforces the FCPA, uh, in particular, the sec is the agency that enforces the FCPA accounting provisions, which impose requirements on issuers to make and keep accurate books and records as well as maintaining and devising [00:08:00] a system of internal accounting controls. And, uh, those people that follow FCPA enforcement, uh, typically understand that it's been easier for the U S government to prove books and records violations than it has been to prove anti-bribery provision violations. And so when there is a books and records violation, the sec typically imposes two types of penalties. One is a civil penalty and it can also impose a disgorgement of profits along with associated [00:08:30] pre-judgment interest. And what's interesting about discouragement is the sec didn't really use disgorgement in the FCPA context until about the mid two thousands.

Speaker 2: But since the sec started using this as a penalty, it's collected over $5 billion in disgorgement and related interest, and it's become one of the tools that the sec uses in FCPA. You know, I went back and looked at the sec enforcement of [00:09:00] the FCPA over the last couple of years and found that by my account, something like 19 of the 21 sec FCPA cases in the last two years had discouragement. And not only was it used in over 90% of the cases, discouragement also is the largest percentage of the penalties that are imposed by the sec, by my count, uh, roughly 75% of the SCCs penalties were due to discouragement in the related interest. [00:09:30] So not only does the sec routinely seek discouragement, it's also a large financial penalty is often levied in FCPA cases. So, you know, there, there's obviously some question before with the cook and lieu cases about, you know, where disgorgement really stood in terms of, uh, on a legal footing. Uh, the sec certainly has very strong legal grounds right now after the MDAA to continue to use discouragement as a penalty, uh, in FCPA [00:10:00] cases.

Speaker 3: So to know what can companies do to avoid disclosure and penalties for FCPA violations?

Speaker 2: Well, it's basically the same, uh, information in terms of, uh, what companies need to do to make sure that they're not running a foul of the FCPA as a whole, and of course the best way to avoid discouragement of profits. And the best way to avoid large financial penalties is to continue to have a compliance program. And from the discouragement context, the key is [00:10:30] keeping and maintaining internal controls to prevent hopefully, or at worst detect illicit payments, uh, if they happen. And what this really means is that companies can't just rely on anti-bribery compliance, but they must also focus on internal and financial controls to make sure that they're compliant with the FCPA. So now that we've talked about the discouragement piece of this and the NDA context, let's go over other provisions in the NDA that may be relevant [00:11:00] to anti-corruption first, there's a ban on anonymous shell companies in the corporate transparency act attached to the NDA. And Sara, can you explain to us why anonymous shell companies were a problem for the U S government, particularly in its anti money laundering goals, but associated and related to anti-corruption goals as well.

Speaker 3: Formation of Kermit the corporations and other legal entities are mostly governed on a state by state basis. And states don't really standardize what information [00:11:30]

they need for someone to form a corporation before the MBAA. Some states didn't even require that that companies disclosed all of their beneficial owners. That is individuals who exercise significant control or derive a significant benefit from the legal entity. This lack of reporting requirement allowed anonymous actors to launder money through shell companies, to engage in illicit activity. And this has obviously become a money [00:12:00] laundering enforcement nightmare. Prior to the corporate transparency act. There was a patchwork of laws, lack of reporting and the ease of forming anonymous companies, which was utilized to further corrupt activities. And this often goes hand in hand with money laundering. So us financial institutions had an obligation to report beneficial owners for companies. We didn't always have the information they needed to make these verifications that sometimes laid within the companies themselves.

Speaker 2: [00:12:30] Well, Sarah, as you just mentioned, uh, in our listeners to the podcast, you know, we've, we've talked about this frequently when there is corruption, oftentimes there's also money laundering. So you can certainly see the nexus between the two here. So well, what does the corporate transparency act do to address these issues?

Speaker 3: So what the new legislation does is it poses a, an affirmative burden on the companies to do the reporting instead of relying on the financial institution [00:13:00] to do so a company, whether it be a corporation LLC or other similar entities must report its beneficial owners to the financial crimes enforcement network or FinCEN. And that's an arm of the us treasury department that analyzes financial transactions to combat money laundering other financial crimes. So what companies have to need to do is they just need to report the beneficial owners name, date of birth residence, and a identifying number from [00:13:30] something like a passport or a driver's license to just give them the information it needs to identify the beneficial owners. And we should keep in mind that not every company needs to report this legislation is targeted at that company. So there are three major types of companies that are excluded from this reporting requirement excluded from this requirement are companies that employ more than 20 full-time [00:14:00] employees in the United States. I never tied the company is a company that annually reports more than 5 million in gross receipts. And the third type of a company that has an operating presence at a physical office could be within the United States. So basically companies that actually do business and have business operations that are active.

Speaker 2: Sarah, one of the things you mentioned a little earlier was the concept of beneficial owner. And so, uh, you know, for those listening to the podcast [00:14:30] that may not know, you know, w who is a beneficial owner, particularly under the CTA.

Speaker 3: So beneficial owner is defined by the CTA is any individual who owns a 25% equity stake in the company or exercises, quote, unquote, substantial control over the company.

Speaker 2: Thanks, sir. That's helpful to get a better feel for what beneficial owner means. In this context, in this podcast, we often talk about compliance and try [00:15:00] to give companies some helpful suggestions in terms of how they can comply with the law going forward. So as you look at the CTA, what can companies do to make sure that they comply with these new provisions?

Speaker 3: Well, the first thing that you do is make sure that these transparency provisions actually apply to you. Uh, like I said earlier, not every company is a so-called reporting company under the statute, as it's in to combat anonymous shell companies, really. Uh, but [00:15:30] if your business needs is seized without active business operations or without significant revenue, they may qualify as a reporting company. Um, for example, lots of startups trying to raise capital for a new business venture may fall under that umbrella. Um, another example is if you are conducting the merger transaction, uh, some companies use shell companies when those mergers and acquisitions, uh, to transfer assets or wind up business operations. [00:16:00] So would you estimate uses and sell companies, but maybe faced with a new reporting requirement the second way you could do, uh, if you qualify as a reporting company, and it's simply a matter of reporting, your beneficial owners determine who has substantial control over a company, isn't quite defined, but I'm the writer, but this language seems to mirror some other statutes and transparency regulations that apply to financial institutions. So, [00:16:30] uh, those individuals are usually people like an executive officer or senior manager, CEO, CFO, COO, someone like that, or any other individual who perform similar functions at the company. So to me, can you explain how these provisions may factor into an overall anti-corruption compliance program?

Speaker 2: Well, so you, as you mentioned, you know, that this certainly has a much stronger nexus to anti money laundering and anti money laundering and compliance. [00:17:00] And, uh, certainly there's a strong connection between money laundering and anti-corruption, and as we've seen in enforcement cases over the years, uh, oftentimes when there is an allegation of corruption, there is, uh, also an allegation of money laundering and from a compliance perspective, uh, money laundering compliance goes hand in hand with anti-corruption compliance. And so as the DOJ and sec, uh, updated their FCPA resource guide last [00:17:30] summer, we see in the FCPA resource guide, one of the things that the resource guide notes is that many FCPA cases do indeed, uh, involve violations of anti money laundering statutes, because anytime you have engaged in illicit activity like bribery, there's a high likelihood that those ill gotten gains from that will also be laundered.

Speaker 2: So there's definitely a connection. And we've spoken about this in previous podcast episodes between money laundering and anti-corruption from a compliance [00:18:00] perspective, one of the things that companies need to consider when they're conducting anti-corruption due diligence on not only transactions, but third parties is whether a third party has complied with the NDA transparency requirements, uh, going forward under the CTA. Certainly if they haven't, that may be a red flag in the due diligence, particularly regarding money-laundering. And of course, when there is a money-laundering red flag, there's often an anti-corruption red flag as well. [00:18:30] So from a compliance perspective, this is just one more thing that companies who are subject to this, um, need to keep in mind as they are designing and implementing their compliance program. So a few key takeaways from, uh, our discussion in this podcast episode regarding the NDA this year is number one.

Speaker 2: Uh, we typically don't think of the NBA and anti-corruption together. And that's one of the things we like to do in this podcast is to discuss, uh, [00:19:00] anti-corruption

maybe from a perspective that most people aren't thinking about. And this year the NBA was certainly different, not only because of the presidential veto, but as Sarah mentioned, uh, earlier on the discouragement of profits, a component of the NDA was certainly unique. And the biggest takeaway from an FCPA and anti-corruption standpoint is the discouragement of profits is here to stay. It's certainly become a large [00:19:30] part of what the sec does to enforce the FCPA. Not only in terms of what percentage of the cases involve a discouragement of profits, but also how large the disgorgement of profits typically is in FCPA cases. So, uh, the new statutory language in the NDA certainly, uh, seems to embolden the sec to continue to use disgorgement of profits. And the last takeaway is the, the corporate transparency act, [00:20:00] certainly add some new wrinkles in terms of reporting and potentially adds some new compliance requirements from a money-laundering standpoint. And as we all know, money laundering, and anti-corruption typically go hand in hand from a compliance perspective. So those are the key takeaways from this year's NDA. Sarah, thank you for joining us on this episode of the podcast

Speaker 1: And thank you for tuning in [inaudible].