



Market Outlook 2010

For this annual feature, Financier Worldwide has again gathered the opinions of the corporate advisory and dealmaking community to explore their insights into current and emerging trends as we enter the new year.

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 +44 (0)845 345 0456 or by email: james.lowe@financierworldwide.com

FRAUD & CORRUPTION

SHARI A. BRANDT AND JAMES Q. WALKER,
 RICHARDS, KIBBE & ORBE LLP

REGULATORY CHALLENGES FOR PUBLIC COMPANIES

Examination of US regulatory enforcement actions and criminal investigations and prosecutions in 2009 suggests that the Securities and Exchange Commission (SEC) and United States Department of Justice (DOJ) have intensified their focus on senior executives and are targeting them even in the absence of evidence of actual participation in any misconduct.

For example, the SEC recently settled cases finding the respondents liable as “control persons” – persons who directly or indirectly controlled the conduct of the wrongdoer – for misconduct that was committed by others, even though there was little to no showing of participation by the control person in the misconduct. Former AIG CEO Hank Greenberg settled with the SEC this past year on a control person liability basis agreeing to pay \$15m in fines and disgorgement in connection with AIG’s violations of the antifraud and other provisions of the securities laws.

Although the SEC stated that Greenberg was a “culpable participant” in the misconduct, it is notable that they did not charge him with either violating or aiding and abetting AIG’s violations. The SEC’s settlement with Nature’s Sunshine Products, Inc. went even further. In that settled action, the SEC charged the COO and CFO with violating the Foreign Corrupt Practices Act (FCPA) on the grounds that they were control persons who had failed to supervise the company personnel who were in charge of maintaining the company’s books and records and internal controls. The SEC did not suggest that the COO and CFO failed to address red flags that were brought to their attention, but rather that they should be held responsible solely by virtue of their positions in the company.

Recent cases have demonstrated that the US government may more aggressively exploit its ability to prosecute executives where there is evidence that they consciously avoided knowledge of misconduct. For example, in *United States v. Kozeny*, 643 F. Supp. 2d 415 (S.D.N.Y. 2009), the DOJ convicted an investor, Frederic Bourke, for conspiracy to violate the FCPA by demonstrating that Bourke consciously avoided knowledge of bribes paid to Azeri government officials in connection with

privatisation of an oil company. It is particularly astounding that the evidence that led to Bourke’s conviction was merely that Azerbaijan was known to be a corrupt environment and that Bourke was concerned that the head of the investment consortium might have paid bribes. With the number of open FCPA investigations hitting a record high of 130 in 2009 (according to a speech by Mark Mendelsohn, Deputy Chief at the DOJ, Fraud Section), the conviction of Bourke should serve as a warning to investors operating in jurisdictions with a reputation for corruption that they must conduct thorough due diligence, monitor the activities of third parties, and document and remediate any FCPA concerns.

In sum, corporate entities, executives, and investors must remain vigilant in 2010 in investigating and remediating any lapses in internal controls and books and records that could expose them to regulatory liability. ■

Shari A. Brandt and James Q. Walker are partners at Richards, Kibbe & Orbe LLP. Ms Brandt can be contacted on +1 (212) 530 1874 or by email: sbrandt@rkollp.com. Mr Walker can be contacted on +1 (212) 530 1817 or by email: jwalker@rkollp.com



Shari A. Brandt
 Partner
 T: +1 (212) 530 1874
 E: sbrandt@rkollp.com
www.rkollp.com

Shari A. Brandt focuses on complex civil litigation, regulatory proceedings, internal investigations, and white collar criminal defense. She often represents clients in matters that proceed simultaneously in regulatory, white collar defense, and civil litigation forums.

Ms. Brandt represents international and domestic clients in the finance, accounting, pharmaceutical, retail, computer software/hardware, telecommunications, and education industries, among others. She also represents individuals. She works on behalf of plaintiffs and defendants in civil litigations at the federal

and state level, arbitrations, and mediations. She also represents individuals, institutions, securities professionals, accountants, and corporate officers who are under investigation by the SEC, FINRA, United States Attorney, and other governmental and self-regulatory bodies.



James Q. Walker
 Partner
 T: + 1 (212) 530 1817
 E: jwalker@rkollp.com
www.rkollp.com

James Walker concentrates in internal investigations, white collar criminal defense, civil litigation, professional liability and legal ethics. Mr. Walker represents audit committees, audit committee directors, corporate officers, and securities industry and other professionals

in United States Attorney, New York State Attorney General, New York District Attorney, SEC, and FINRA investigations of potential violations of the securities laws and Foreign Corrupt Practices Act. He represents law firms, lawyers, and other professionals in government

and internal investigations of potential criminal, regulatory and/or professional misconduct, and in related criminal and civil litigation and regulatory proceedings.