

The Foreign Corrupt Practices Act and the Financial Services Industry: Towards Enhancing Compliance

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Why should members of the financial services industry, who have traditionally not been the focus of bribery enforcement actions, pay attention to anti-bribery law concerns at this time when compliance budgets are so stretched and the predominant risk focus has drifted further away from compliance because of the financial crisis? And if they do, what kinds of approaches should be explored? There are many reasons for the salience of Foreign Corrupt Practices Act (FCPA) to this industry, and several advantages to be obtained by leveraging longstanding compliance program efforts.

Is There Now A Pronounced FCPA Focus On The Financial Industry?

There are significant indicators that the financial services industry is currently prominent in the minds of persons who enforce bribery and corruption laws. Earlier this year, the Financial Industry Regulatory Authority (FINRA), the Securities Exchange Commission (SEC) and the New York State Insurance Department all announced initiatives to promote compliance with anti-bribery laws. In March 2009¹, FINRA indicated that FCPA issues have become a priority in the examination process. The SEC formally announced the formation of an FCPA enforcement unit in August², and in June³, (Insurance) New York Superintendent Eric Dinallo indicated that, notwithstanding the state's jurisdictional limits, insurance companies are subject to expectations regarding financial criminal activity, including money laundering and FCPA violations.

As if that were not enough, recent highly publicized bribery cases have presented issues that invite application to the financial industry. An example is the case of Frederick Bourke, who was convicted in August (awaiting sentence) in the Southern District of New York of conspiring to violate the FCPA. The trial included a jury instruction on willful blindness. The willful blindness doctrine of liability⁴ provides that a defendant who is aware of circumstances creating a high probability of something and who does not look further, will be equivalent to a defendant with actual (guilty) knowledge. In light of anti-money laundering (AML) law, regulations and guidance, which are replete with references to and application of willful blindness, financial industry members are probably quite familiar with the doctrine. In the *Bourke* case, the government alleged that Bourke made capital contributions to an energy related company and that he (at least constructively) recognized that the company was carrying out its business by bribing foreign (Azerbaijani) officials⁵. There was no allegation that Bourke actually bribed an official or designated specific funds for a bribe, however at least one juror after the trial indicated that "We thought he knew and he definitely should have known" ... "He's an investor. It's his job to know."⁶ Since financial industry members bring about the capitalization and financing of companies as part of their day to day business model, this result is, to say the least, intriguing. Consider that when such funds are provided, whether through a bond

offering, initial public offering or even a large loan, there is usually an intensive practice of due diligence regarding the enterprise that will receive the funds. Banks, brokers and other industry members often conduct and/or are privy to the results of the due diligence. The *Bourke* case shows that an active investor who learns of strong indications of improper activity may become criminally responsible for the activity. If a thorough due diligence on the integrity of the party receiving funds created those indications, the persons or entities providing the funds would begin to look like Bourke in FCPA terms. On the other hand, if the thorough due diligence, properly carried out, supports the opposite conclusion, the resemblance to the *Bourke* case goes away, and the due diligence protects a party from liability. After *Bourke*, however, the party that does not carry out this due diligence, particularly regarding activity in a corruption-prone part of the world, will be vulnerable to the charge that he avoided knowledge that would have been available in the ordinary course, and therefore is potentially criminally responsible as though he had actual knowledge of the wrongdoing.

The *Bourke* facts are noteworthy, potentially involving many millions of dollars in bribes and gifts to induce foreign government officials to activate, and thereby make valuable, previously issued oil development company vouchers, and the result is sobering. The high profile nature of the bribes had already precipitated intense government attention, and given rise to concessions to government charges against an individual and a hedge fund in 2007, although, in the absence of a contested trial, these attracted less attention than the *Bourke* case.⁷

Similarly sobering is the *Nature's Sunshine* case, brought and settled by the SEC at the end of July⁸. There, the SEC sued the company and two senior executives alleging that, with respect to improper payments to Brazilian customs authorities, the company was in violation of the requirement to have reasonably accurate books and records, and to maintain a system of internal accounting controls to permit preparation of adequate financial statements. The executives, the CFO and COO, were not alleged to have actual knowledge of the improper payments, but were alleged to be liable as control persons. If *Bourke* underscored how someone who provided money to a private company and who "should have" known of an improper payment could pick up FCPA related liability, *Nature's Sunshine* demonstrates how corporate executives with no alleged actual knowledge can be held accountable (civilly, in this case) as controlling persons regarding the consequences of improper payments by their company's foreign subsidiary. Because many financial institutions are global in scope and may have a variety of global affiliates, *Nature's Sunshine* could have clear applicability as well to the financial services industry.

And it is not just in the United States that enforcement of anti-bribery laws that may be particularly applicable to the financial services industry has been noteworthy. Earlier this year, the United Kingdom's Financial Services Authority (FSA) fined AON Ltd. 5.25 million pounds with regard to payments made by third party intermediaries to foreign officials that appear to have facilitated AON's reinsurance business⁹. The release by the FSA cited AON as having reported some related payments as suspicious activity, and noted the failure to proactively reassess the control environment in that regard. This approach is consistent with enforcement actions in the AML environment, where companies are criticized for not drawing reasonable inferences based upon the suspicious behavior they have identified and reported.

Also, the UK has pending the Bribery and Corruption Bill¹⁰, which meticulously defines corrupt activity, places especial emphasis on the personal liability of senior management, and includes the bribery of corporate (i.e., non-governmental) officials as part of the same legal framework. Many other countries of course have detailed bribery and corruption laws, with a varying level of enforcement.

Why Is FCPA Enforcement Becoming More Prominent?

The 'why' question is a bit more difficult to answer. Probably a large factor has been the popularization and growing global awareness of the social cost of corrupt payments. Consider for example, the May, 2009 testimony¹¹ of Nuhu Ribadu from Nigeria, before the House Committee on Financial Services, in which he scolds the international banking community for banking the corrupt payments through which international aid to his country has been detoured. Similarly, increasing use is made of the internet by groups such as Global Witness to voice the same message. Global Witness recently circulated a lengthy piece entitled, "Undue Diligence: How Banks Do Business With Corrupt Regimes."¹² These groups also have the ability to spur government attention on the potential movement of corrupt monies, as has been the case with Transparency International, the French government and the Gabon family earlier this year.¹³ One of the logical extensions of this attention is the prospect of civil litigation on behalf of persons alleging they are victims of the lack of compliance, as happened several years ago with Arab Bank¹⁴ regarding alleged irregularities as to its compliance with the OFAC sanctions programs. On a more pedestrian note, legislation has been proposed that would confer a private right of action on U.S. companies that were competitively disadvantaged because of an improper payment by a foreign company to a foreign official.¹⁵

Consider that FCPA enforcement actions have focused on specific industries, such as energy, pharmaceuticals and medical devices, where the specific methodologies of facilitating corrupt payments may lend themselves to the industry, and thus attention to other industries requires the development, in a factual sense, of specific targets for investigation. One factor in turning attention to a particular industry may be the salience of the industry to prosecutors because of other negative attention. Perhaps the financial industry, which has been a steady target of negative media reports of blame for the ongoing global financial crisis, is vulnerable to being one of the next in line in this regard.

FCPA Risks In The Financial Services Industry

Even a cursory review of FCPA requirements makes clear that the financial services industry is exposed to liability under the FCPA. Setting up a new business in a foreign land often requires government licenses or favorable zoning treatment for a new business site. Doing business with sovereign wealth funds presupposes currying favor, legitimately or otherwise, with government officials. Serving as the custodian of assets or making financial transactions for foreign State Owned Enterprises (SOEs) (such as banks, hospitals or utilities), whose employees may be deemed foreign officials under the FCPA, similarly involves dealing with foreign officials, and in this instance, the SOEs can have U.S. branches, and the "officials" can be in the U.S. And, just as for other industries, the ways that improper payments can be effected

are not always obvious. They can involve favorable treatment for real estate transactions that benefit foreign officials, promotional tours with a lavish or predominantly non-business purpose, or the provision of employment to a competent nephew who otherwise would have been rejected in favor of an even more competent stranger with no relationship to a government official.

Taking A Straightforward Approach To FCPA Risk

Industry members should consider a straightforward approach to these risks, to the extent they have not already done so. A company needs to carry out a risk assessment and to consider applicable risk mitigation strategies. To this end, a company should evaluate how FCPA risk fits into its overall approach to risk, and, most importantly, how to leverage existing risk assessment and control processes. This process will require some time, but will put the company on the path to having a realistic and cost effective program. It is essential to identify the nature and extent of resources that are necessary to initiate or enhance an FCPA compliance program.

There is no granular regulatory and examination framework to set out the boundary lines of an FCPA compliance program, as there is for AML, although the FCPA does impose a requirement of internal controls such that books and records are accurate.¹⁶ The key criteria for such a program arises out of the Federal Sentencing Guidelines¹⁷ and various Department of Justice memoranda or opinions, which state that if the company is a potential defendant (including FCPA), the presence of a robust compliance program is a factor in the decision whether to bring a criminal or civil enforcement action, how serious the action will be, and how draconian the penalties sought will be¹⁸. Since most financial services industry companies are already required to have a formal AML compliance program, those programs are a good starting point to look for ways to leverage existing thinking and processes when establishing or enhancing an FCPA compliance program. In this sense, composing or enhancing an FCPA compliance program can draw upon the same effort for compliance programs for the Treasury's Office of Foreign Assets Control (OFAC) requirements. Similar to the FCPA, there is no set of compliance regulations requiring the establishment of an OFAC compliance program, but the financial industry has borne very significant penalties for OFAC sanctions violations.¹⁹ In response, companies have created OFAC compliance programs very similar to those built for AML purposes. If one compares the basics of an AML program, training, appointment of an AML Officer, independent testing and policies and procedures and controls to what the Department of Justice and the SEC have declared as lacking when bringing enforcement actions²⁰ or indicating how to avoid them, the overlap becomes clear.²¹

Leveraging AML Program For FCPA

At last, a piece of luck regarding AML programs: Most members of the financial services industry already have such a program, and, given all the attention by regulators, it is likely to be reasonably rigorous. There may be an AML risk assessment framework established in most financial companies. For example, it is required either directly by regulation (in the insurance industry) or by implication of the Federal Financial Institutions Examination Council (FFIEC) Bank Secrecy Act Anti-Money Laundering Examination Manual (in the banking industry)²² or, in a somewhat

less clear manner, by the implications of FINRA Rule 3013 and the emphasis on complete written supervisory procedures for broker dealers. The AML risk assessment approach a company already has in place can now incorporate FCPA issues, so that a better risk profile, clarifying the nature and extent of risk, can be created. This will include, at a minimum, supplementing the self-assessment questionnaire many firms send to their affiliates or branches on a yearly basis. It may also include more pointed front office and operations interviews to account for practices and local environments that the home office may not have come to know well enough for these purposes. And it may include some analysis of data (some of the same and some different data²³ than for the AML program). Next, there will usually be an AML training program that has risk ranked employees and determined which of them need customized rather than only generic training. The infrastructure already created for that program can be used to identify FCPA training needs and to create new or supplemental FCPA training for employees and senior management.

There will typically already be an AML Officer; the USA Patriot Act requires it for covered financial institutions. A company should consider appointing someone with the same focused responsibility for FCPA issues. It may not be the same person as the AML Officer, but since much of an FCPA compliance program will overlap with AML, the person will most likely at least be part of the same group. Some organizations have already created departments regarding "financial crime," that address fraud, AML, FCPA and like matters collectively. The presence of an appointed person helps streamline governance and escalation issues that any event driven (frauds, bribes, money laundering, insider trading, etc.) compliance program must address.

The core compliance functions in an FCPA program, including policies, procedures and investigation, have significant overlap with AML, and governance and escalation issues should be handled in a similar way. One of the things, however, to be wary of, is that FCPA issues much more frequently involve direct personal criminal or civil liability, so a greater involvement of the general counsel's office is appropriate. As the Office of Thrift Supervision recently noted, this is an area where advice of counsel is paramount.²⁴ Escalation, reporting and investigation issues thus have some different emphases here than for AML.

A financial services company will usually have a Financial Investigations Unit (FIU) or a functional equivalent that investigates alerts and makes reports of potential suspicious activity under the AML regulations, and a transaction monitoring system that creates the alerts. The FIU can be broadened to address FCPA issues in its otherwise generated investigations. Also, the alerts can be broadened in several ways. First, with training and attention, the FCPA aspects of existing alerts can be examined. Second, existing transaction monitoring systems can be programmed to accept new data feeds and new scenarios. In the alternative, a standalone monitoring approach drawing upon related expertise can be employed. FCPA issues will often involve data originating from accounts payable and general ledger entries rather than the customer transaction data that dominates AML transaction monitoring, but, like transaction data, this data can be subject to specific (FCPA) scenario analysis. However, even without going that far, existing surveillance or management information reports regarding gifts and entertainment expenses may effectively be channeled into an FCPA analysis, as many bribes take this format.

Moreover, the AML program should already be identifying Politically Exposed Persons (PEPs) amongst the customer population. PEPs, of course, will often be foreign government officials under the FCPA, or potential conduits to such officials for FCPA purposes. This PEP analysis can be extended to vendors, agents and third party intermediaries. The investigation and surveillance protocols can be extended to identify situations in which PEP customers who are, for example, affiliated with vendors, also have personal accounts with the institution. Such surveillance can isolate instances where favorable treatment by the institution for a customer might otherwise appear a mere irregularity, rather than a potential prohibited payment to a foreign official.

Finally, independent testing of the compliance environment, usually by internal audit²⁵, is critical. This may involve training the auditors for a new set of issues, or revisiting the compliance procedures being put in place to ensure that they create a testable set of requirements. Having an independent tester (from inside or outside the firm) assess the completeness and effectiveness of what is going on for FCPA compliance gives significant additional credence to the program, as seen by regulators, prosecutors, civil claimants, or other potential stakeholders.

There are of course many areas where the FCPA compliance initiative will go well beyond the skeletal requirements for AML programs. Gift and entertainment policies, specific books and records requirements, a code of ethics requirement, an employee hotline, disciplinary procedures for self enforcement of policies and other measures are elements of a relatively complete program²⁶. Different AML programs may have more or less overlap with these specific areas. Similarly, the nature of risk assessments and other aspects of an FCPA program will have their own features distinct from their AML counterparts. The important point is that the AML program is an effective starting point to leverage existing compliance resources to generate a good FCPA program, or enhance a skeletal one.

Conclusion

Anti-bribery compliance is becoming a high priority requirement for financial services companies. A combination of global sensitivities and aggressive enforcement actions, as well as a growing recognition of the risks, makes it now prudent for companies to consider their exposure to bribery and corruption activities and the strategies to control them. There are many existing programs and processes for companies to leverage, particularly arising out of existing AML compliance. The key is to take a deliberate approach and to systematically come to better understand the risks, the stakes and the opportunities to handle these risks in line with the other compliance risks that continue to be found in this focal area for regulators and prosecutors, and which continue to implicate both social duty and exposure to reputational risk.

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¹ March 9, 2009 letter from FINRA to Executive Representatives.

<http://www.finra.org/web/groups/industry/@ip/@reg/@guide/documents/industry/p118113.pdf>

² August 5, 2009 Speech of Robert Khuzami.
<http://www.sec.gov/news/speech/2009/spch080509rk.htm>

The speech announces the formation of the unit, and promises coordination with global authorities, as well as increased investigation: "The Foreign Corrupt Practices Act unit will focus on new and proactive approaches to identifying violations of the Foreign Corrupt Practice Act, which prohibits U.S. companies from bribing foreign officials for government contracts and other business. While we have been active in this area, more needs to be done, including being more proactive in investigations, working more closely with our foreign counterparts, and taking a more global approach to these violations."

³ June 29, 2009 Circular Letter from New York State Insurance Department.
http://www.ins.state.ny.us/circltr/2009/cl2009_11.htm

⁴ The instruction on knowledge includes the following: "When knowledge of the existence of a particular fact is an element of the offense, such knowledge may be established if a person is aware of the high probability of its existence and consciously and intentionally avoided confirming that fact. Knowledge may be proven in this manner if, but only if, the person suspects the fact, realized its high probability, but refrained from obtaining the final confirmation because he wanted to be able to deny knowledge."

⁵ The indictment sets out various alleged acts by Bourke suggestively consistent with his recognition and decision to distance himself from the company's activities. The conviction was described in a Department of Justice Press Release.
<http://www.usdoj.gov/usao/nys/pressreleases/July09/bourkefrederickverdictpr.pdf>
Although Bourke was convicted of conspiracy to violate the FCPA, his role could fairly be characterized as that of an investor with enhanced knowledge.
http://www.australia.to/index.php?option=com_content&view=article&id=12421%3Ainvestor-found-guilty-in-massive-scheme-to-bribe-senior-government-officials-in-the-republic-of-azerbaijan&Itemid=207

⁶ The full quote in the article is: "We thought he [Bourke] knew and he definitely should have known," Murphy said. "He's an investor. It's his job to know. We thought the tape was damning." The tape referenced regards a conversation Bourke had entertaining how to deal with the prospect that the company in which he was investing was engaging in bribery:
<http://www.law.com/jsp/article.jsp?id=1202432210710&hbxlogin=1>

⁷ See the June 6, 2007 Department of Justice Press Release, "U.S. Announces Settlement With Hedge Fund Omega Advisors, Inc." <http://www.usdoj.gov/usao/nys/pressreleases/July07/omeganonprospr.pdf> Omega Advisors entered into a non-prosecution agreement, in which it acknowledged responsibility for the conduct of its agent, Clayton Lewis, who had previously pled guilty and who had indicated that he, acting on behalf of Omega, entered into an investment that was taking advantage of potentially prohibited provision of value to Azerbaijani officials. An additional defendant in the original indictment, David Pinkerton, had allegedly been AIG's investment representative in the same venture; all charges against Pinkerton were dropped by the government in 2008. <http://www.law.virginia.edu/pdf/faculty/garrett/omegoadvisors.pdf>. The case presumes that Lewis, by having acted on behalf of Omega, created responsibility for Omega without necessarily having communicated these circumstances of the investment to Omega. One of the further reasons why Bourke has attracted more attention is that in Omega, is that there was already a guilty plea in which Lewis admitted actually knowing about bribery. In *Bourke*, the culpability was shown in terms of inferences from Bourke's actions and matters he knew which arguably should have drawn him to make an inference, rather than a statement of his (the investor's) actual knowledge. This was an aggressive position taken by the government, and having carried the burden of proof in a full blown criminal trial, the viability of the use of this theory against investors instantly became much more credible than it had been.

⁸ Announced and settled on the same day, the individual defendants and the company agreed to pay, respectively, \$25,000 and \$600,000. <http://www.sec.gov/litigation/complaints/2009/comp21162.pdf> The SEC's description of the settlement is also of note. <http://www.sec.gov/news/digest/2009/dig073109.htm>

⁹ The Final Notice describing the underlying conduct and announcing the fine is revealing. <http://www.fsa.gov.uk/pubs/final/aon.pdf> The FSA (the Financial Services Authority, which is the principal financial regulator in the United Kingdom) described the presence of corruption risk it understood regarding a particular AON business line:

"Some of the business units within Aon Ltd's Aviation and Energy divisions made use of and paid Overseas Third Parties, particularly in connection with reinsurance business carried out by those divisions in overseas jurisdictions. These payments may have been made in order to secure or retain business from clients based in overseas jurisdictions. Some of these clients were state owned entities (either in whole or in part) or otherwise had government connections. Accordingly, although it was not unusual or necessarily inappropriate for Aon Ltd to make payments to Overseas Third Parties, there was a significant risk in some countries that some of the monies involved might be used by Overseas Third Parties to bribe persons connected with the insured, the insurer or public officials, or otherwise be used for potentially inappropriate purposes." *Id.*, at par. 4.3.

¹⁰ <http://www.justice.gov.uk/publications/docs/draft-bribery-bill-tagged.pdf>

¹¹ http://www.house.gov/apps/list/hearing/financialsvcs_dem/ribadu_testimony.pdf

¹²

http://www.globalwitness.org/media_library_detail.php/735/en/undue_diligence_how_banks_do_business_with_corrupt contains the link to the report.

¹³ The group appears to have filed a formal complaint that has led the French government to carry out an investigation of the banking of potentially corrupt

moneys by leaders from several African countries, such as Equatorial Guinea, in France. "The Enrichment of Africa's French Allies" Time, May 8, 2009

<http://www.time.com/time/world/article/0,8599,1896891,00.html>

¹⁴ *Olmag v. Arab Bank, PLC*, CV 04-5564, U.S. District Court (SDNY)

¹⁵ Foreign Business Bribery Prohibition Act of 2009.

<http://www.govtrack.us/congress/billtext.xpd?bill=h111-2152>

At present, the bill would allow actions by U.S. companies that were disadvantaged by foreign concerns.

¹⁶ 15 U.S.C. § 78m

¹⁷ 2007 Federal Sentencing Guidelines.

<http://www.ussc.gov/2007guid/TABCON07.html>

¹⁸ See the Principles of Federal Prosecution of Business Organization, commonly referred to as the Filip Memorandum.

<http://www.usdoj.gov/dag/readingroom/dag-memo-08282008.pdf>

¹⁹ See Lloyds Deferred Prosecution Agreement, CR-009-007 (US District Court, D.DC) \$350 million in 2009; In the matter of ABN AMRO Bank et al, FRB Dkt 05-035-CMP-FB, in which the bank was fined \$80 million to be paid to the Federal Reserve Bank, The New York State Banking Department the Illinois Banking Department and FinCEN, as prominent examples. A further deferred prosecution agreement remains under negotiation regarding the ABN AMRO matter, holding potentially additional fines for its owner.

²⁰ The framework of FCPA compliance is consequently particularly responsive towards problems that have arisen in enforcement actions. These often involve problematic behavior of employees and accounting irregularities. The recent actions against Siemens Aktiengesellschaft and related companies, including the prosecution by the U.S. Government, provide a good example in this regard. See *United States v. Siemens Aktiengesellschaft*, Information, Case 1:08-CR-00367-RJL (2008).

²¹ See, the Department of Justice Opinion Procedures Release 4.02, which indicated that indicates that ABB, Ltd might avoid FCPA enforcement regarding a new company being set up or acquired if it, among other things, would have a clear FCPA policy and clear procedures, independent testing corroborating implementation of its compliance code, due diligence regarding employees and vendors, and assignment of one or more persons with oversight of the policies. The congruence with AML is readily understandable if one keeps in mind that the same sentencing guidelines inform the government's view of how company's can proactively address risks of criminal law violations, so as to be subject to leniency when an issue occurs.

Training is another area where there is an enforcement expectation for FCPA, even though there is no specific regulation. In its 2007 FCPA complaint against Lucent, the SEC noted that Lucent's failure to train its employees was part of the rationale for the complaint:

"Lucent's violations occurred because Lucent failed, for years, to properly train its officers and employees to understand and appreciate the nature and status of its customers in China in the context of the FCPA. Many of Lucent's Chinese customers were state-owned or state-controlled companies that constituted instrumentalities of the government of China and whose employees, consequently, were foreign officials under the FCPA. The Chinese foreign officials who traveled at Lucent's expense were often identified by Lucent in its internal documents as "decision makers" with respect to awarding new business." Complaint at paragraph 3,. *SEC v. Lucent Technologies* (D.DC 2007). <http://www.sec.gov/litigation/complaints/2007/comp20414.pdf>

²²The manual provides that if a bank does not have a risk assessment when the examiners arrive, they (the examiners) should draft one. 2007 Bank Secrecy Act Examination Manual, Federal Financial Institutions Examination Council, at p. 18.

²³Payments by financial service companies to vendors and for gifts and entertainment is usually not part of an AML transaction monitoring system data warehouse.

²⁴ <http://files.ots.treas.gov/74847.pdf>

In particular, the 2009 OTS Examination Handbook counsels as follows: "The FCPA also requires the establishment of internal controls to ensure that organizations execute transactions according to management's authorization and properly record the transactions so as not to disguise corrupt payments. Anyone acting on behalf of a savings association, in any transaction with a foreign official, should have benefit of legal counsel to ensure compliance with the far-reaching provisions of the FCPA."

²⁵As with any new testing program, an institution should insure that the testing personnel involved are adequately trained and can bring the appropriate judgment and experience to bear in designing their program and interpreting the results.

²⁶A starting point for a more complete FCPA menu is the Department of Justice ABB statement, Opinion Procedure Release 04-02 regarding ABB Lt in 2002. <http://www.usdoj.gov/criminal/fraud/fcpa/opinion/2004/0402.html>