February 13, 2009

INTERNATIONAL TRADE ALERT

HALLIBURTON CO., KBR, INC. AND KBR LLC AGREE TO LARGEST COMBINED SETTLEMENT OF FCPA CHARGES BY U.S. COMPANIES

Kellogg, Brown & Root LLC (KBR), a Houston-based global engineering, procurement and construction services firm, its parent company, KBR, Inc., and its former parent company, Halliburton Co. have agreed to pay a total of $579 million to the U.S. Department of Justice (DOJ) and the U.S. Securities and Exchange Commission (SEC) in connection with KBR's participation in a scheme to bribe Nigerian government officials, including officials of an entity in which the Nigerian government held less than a 50 percent ownership stake, in order to obtain construction contracts in violation of the U.S. Foreign Corrupt Practices Act (FCPA). In U.S. District Court on Wednesday, February 11, 2009, KBR pled guilty to one count of conspiring to violate the FCPA and four counts of violating the anti-bribery provisions of the FCPA. In a related civil complaint filed by the SEC, the SEC charged KBR with violating the FCPA's anti-bribery provisions and charged KBR, Inc. and Halliburton with books and records and internal controls violations related to the bribery. KBR, Inc. and Halliburton settled the civil charges without admitting or denying the SEC's allegations.

According to U.S. enforcement officials, KBR's predecessor entities (Kellogg, Brown & Root Inc. and the M.W. Kellogg Company) formed a joint venture with three other multinational engineering construction companies in 1991 ("the TSKJ joint venture") for the sole purpose of bidding on and, if successful, performing a series of engineering, procurement and construction (EPC) contracts to design and build liquefied natural gas production facilities on Bonny Island, Nigeria (the "Bonny Island Project"). The joint venture was awarded four EPC contracts (valued at more than $6 billion) by the Nigerian government between 1995 and 2004 to undertake the Bonny Island Project.

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THE DOJ CASE

The DOJ's complaint against KBR describes KBR's scheme to bribe Nigerian officials to secure the EPC contracts, as well as its attempts to insulate itself from FCPA liability for its corrupt payments. According to the DOJ, officers of KBR and the other joint venture members held so-called "cultural meetings" at which they discussed, among other things, the use of particular agents to pay bribes to Nigerian government officials in order to secure the officials' support for the TSKJ joint venture in obtaining and retaining the construction contracts.

The DOJ's complaint alleges that the TSKJ joint venture operated through three Portuguese special purpose corporations (SPCs) based in Madeira, Portugal. The TSKJ joint venture used one of these SPCs ("Madeira Company 3") to enter into sham consulting agreements with two of the joint venture's agents (a solicitor based in the United Kingdom (the "UK Agent") and a Japanese trading company (the "Japanese Agent")), who, in turn, funneled their consulting fees of more than $180 million to Nigerian officials. According to the DOJ, evidence of KBR's intentional efforts to insulate itself from FCPA liability includes the fact that KBR held its interest in Madeira Company 3 indirectly through M.W. Kellogg Ltd. Further, while the board managers of the other SPCs included U.S. citizens, KBR avoided placing U.S. citizens as board managers of Madeira Company 3.

The DOJ notes that KBR admitted that, from 1994 to 2003, its former CEO, Albert "Jack" Stanley, and others involved in the joint venture met with high-ranking Nigerian government officials and their representatives to arrange the bribe payments and to seek approval of the agents who would serve as conduits for the bribes. In a related criminal case, Stanley pled guilty in September 2008 to conspiring to violate the FCPA for his participation in the bribery scheme. Stanley's sentencing is currently scheduled for May 6, 2009.

THE SEC CASE

The SEC's complaint alleges that Halliburton (the parent company of KBR's predecessor entities from 1998 to 2006) failed to detect any bribe payments and failed to "devise and maintain adequate internal controls to govern the use of foreign sales agents and failed to maintain and enforce internal controls it had." For example, while conducting minimal due diligence on the UK Agent, Halliburton never learned the names of the beneficial owners of the UK Agent's company and did not seek to determine how the UK Agent would or could carry out his duties under the consulting contract from the United Kingdom, or how he was carrying out his duties under the then-existing $60 million contract in connection with the initial phases of the Bonny Island Project. In addition, Halliburton did not check all of the references provided by the UK Agent, some of which were false. The SEC complaint also alleges that Halliburton conducted no due diligence on the Japanese Agent. The complaint also states that,

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in numerous KBR and Halliburton company records, the payments to the UK and Japanese agents were falsely characterized as legitimate "consulting" or "services" fees, when, in fact, they were bribes. KBR's books and records containing the false information were incorporated and reflected in Halliburton's corporate books and records.

THE SETTLEMENTS

KBR agreed to pay a $402 million criminal fine to the DOJ, while KBR, Inc. and Halliburton agreed to pay $177 million in disgorgement to settle the SEC charges. The total penalty ($579 million) represents the largest combined settlement ever paid by U.S. companies since enactment of the FCPA and the second largest fine ever paid in an FCPA prosecution. The total penalty in this case is second only to the $800 million combined settlement paid to DOJ and SEC by Siemens AG, a German company, in December 2008.

Under its plea agreement with DOJ, KBR is required to retain an independent monitor for three years to review the design and implementation of KBR's compliance program. Similarly, the SEC settlement requires KBR, Inc. to retain an independent monitor for a three-year period to monitor its FCPA program, and Halliburton is required to retain an independent consultant to perform a 60-day initial compliance assessment and, approximately one year later, a 30-day follow-up review and evaluation of its policies and procedures as they relate to FCPA compliance. The proposed SEC settlement is subject to court approval.

IMPLICATIONS OF THE KBR AND HALLIBURTON CASE

This case demonstrates that the FCPA is able to penetrate convoluted company structures and payment schemes devised to insulate corporate executives and their companies from FCPA liability. The case also highlights the desire of U.S. enforcement officials to (a) seek penalties that they believe are "commensurate with, and will deter," FCPA violations, and (b) aggressively investigate violations of the FCPA, often with the assistance of non-U.S. law enforcement authorities.

In addition, the case further diminishes a commonly-held view that U.S. companies are insulated from FCPA liability when bribery involves foreign companies in which the state owns less than a fifty percent stake. Here, Nigerian National Petroleum Corporation (NNPC)—itself a government-owned entity—had a 49 percent ownership stake in Nigeria LNG Limited (NLNG). DOJ deemed that ownership stake sufficient, along with other indicia of control, to reach the conclusion that NLNG employees were "foreign officials" under the FCPA, notwithstanding the fact that the other owners of NLNG were multinational oil companies.

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Finally, this case also shows the importance of conducting adequate due diligence in FCPA compliance. While the FCPA does not have an explicit due diligence requirement, the overall structure of the statute, the basic principles of criminal liability, and established practice under the FCPA, make clear that proper due diligence is a touchstone of effective FCPA compliance and successful defense of FCPA enforcement actions. Robust due diligence in connection with employees, agents, representatives, business partners and potential acquisitions can prevent FCPA violations, avoid assumption of successor liability for violations by others and prevent prosecution for acts of bribery committed by parties for whom the company is legally responsible.

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