Consumer Finance Monitor (Season 3, Episode 27): A Primer on the Foreign Corrupt Practices Act for Consumer Financial Services Providers

Speakers: Chris Willis and Hank Hockeimer

Chris Willis:

Welcome to the Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer financial services and what they mean for your business, your customers, and the industry. I'm your host, Chris Willis. And I'm the practice group leader of Ballard Spahr's Consumer Financial Services Litigation Practice. And I'll be moderating today's program.

Chris Willis:

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Chris Willis:

Today I'm joined by a very special guest, Hank Hockeimer, who is the practice group leader of our firm's White Collar and Government Investigations Group. Hank, welcome to the podcast.

Hank Hockeimer:

Thanks, Chris. How are you doing?

Chris Willis:

We're really glad to have you with us today, Hank, because we're going to be talking about a really interesting and unusual event that happened recently. A large consumer financial services company announced in an SEC disclosure filing that it had set aside a pretty large reserve in anticipation of a potential enforcement action relating to the Foreign Corrupt Practices Act. And that's something that is pretty unfamiliar to a lot of us who practice in the consumer financial services world. So I'm glad you're here to join us, because Hank is an expert on the FCPA. So, Hank, what do we know about the matter that was referenced in this SEC disclosure?

Hank Hockeimer:

Thanks, Chris. Like you mentioned, we don't know a whole lot. By virtue of a SEC filing, as you mentioned, World Acceptance Corporation, the company at issue, announced that it had set aside 21.7 million to resolve a Securities and Exchange Commission investigation into potential violations of the FCPA, the Foreign Corrupt Practices Act.

Hank Hockeimer:

The filing itself is pretty cryptic. It talks about that they commenced an investigation back in 2017 to evaluate the "legality of certain payments relating to loans." All we know is that there appears to be both an SEC investigation, which again, they've set aside a good chunk of money for, and also Department of Justice investigation, and there's no indication that that is on the verge of any kind of settlement, unlike the SEC case.

Hank Hockeimer:

So just to give it a little more color, World Acceptance until 2018 had a business in Mexico, and the allegations relate to payments associated with loans made in Mexico by the subsidiary that it had in Mexico.

Chris Willis:

I think that's very interesting. And if it's true that this is the beginning of a level of interest by the regulators in enforcing the FCPA and the financial services industry, I know that a lot of U.S. financial services companies also have overseas operations. So it probably behooves us to know a little bit about the FCPA. So could you give our audience an overview of what the FCPA is and how does it work?

Hank Hockeimer:

So the statement that World Acceptance made in connection with the set aside for the SEC appears to relate to payments that it made through its Mexican subsidiary relating to loans and also some compensation for employees down there. But other than that, as a factual matter, we don't know a whole lot.

Hank Hockeimer:

What we do know, and this is probably most important for your listeners, is that the government is utilizing the FCPA in connection with consumer finance companies, lenders, other financial institutions that may be operating outside of the United States. We haven't seen a lot of that kind of activity by the Department of Justice and the SEC in connection with financial institutions, but this may be a harbinger of some trend down the road. We'll just have to see. Historically, oil companies, gas companies, utility companies, manufacturing companies, those historically have been in the crosshairs of the FCPA. This seems to be an expansion of that.

Hank Hockeimer:

In simple terms, the FCPA can be defined as follows. Any payment to a foreign official in order to obtain or retain business could be a violation of the Foreign Corrupt Practices Act. Now that deceptively simple definition belies the complexity underneath it. You start then asking, well, what are the payments that are being made to a foreign official? And we'll get to foreign official in a second and how that's defined.

Hank Hockeimer:

But the payments essentially are anything of value. So it could be a bag of money. That's obviously an easy example. It could be some sort of wire transfer, but it also could be giving a foreign official a trip, giving a family member of a foreign official a trip, giving a job to a family member. Anything of value, and the U.S. government will view that fairly broadly, fairly liberally in determining what benefit has been provided to the foreign official. So you start with, first of all, was anything given in order to obtain or retain business?

Hank Hockeimer:

The next question is, is to whom is this benefit been provided? Foreign officials are defined pretty broadly. It's not just simply the equivalent of a secretary of a cabinet level department in the United States. It's anybody who essentially works for the government, who's a public official. And when you talk about a lot of different countries that have different political and other economic systems compared to the United States, often those officials are counter-intuitive. Often those foreign officials could be counterintuitive, meaning that, for example, in Eastern block country, most hospitals are state-owned. And so if a company gives anything of value to an administrator of a hospital, that hospital by virtue of being state-owned, that employee will be considered a public or foreign official under the FCPA.

Hank Hockeimer:

So the reach both in terms of the benefits provided and the foreign officials to whom the benefits were provided are both broadly interpreted or defined by the government, both the Department of Justice and the SEC.

Chris Willis:

When you mention the SEC and the Department of Justice, obviously financial institutions are used to a certain set of regulators. Federally chartered banks and state chartered banks that are federally insured have the FDIC and the OCC. We have the Federal Reserve Board and the CFPB for consumer finance issues and the Federal Trade Commission. And then we've got state banking departments or state departments of financial institutions. But what are the regulators that are responsible for enforcing the FCPA? Where does that enforcement activity come from?

Hank Hockeimer:

So, two things, two sources. One, within the Department of Justice, within the Criminal Division of the Department of Justice, there's the fraud section, and the fraud section has its own FCPA unit. And they enforce the FCPA all over the world for instances of violations of the FCPA.

Hank Hockeimer:

The penalties are pretty severe. You can have up to a $2 million fine, up to five years of imprisonment. You have $2 million fine against the company per violation, up to five years of imprisonment for an employee, and fine them up to $250,000 for individuals. The DOJ can also bring a civil action.

Hank Hockeimer:

The SEC enforces what's known as a books and records violation. And so when I turn back to what I said about the definition of payment or something of value in order to obtain or retain business, payments of a company are obviously memorialized or reflected in accounting records. If those accounting records misstate or don't record a particular payment, that could be a book and records violation of the SEC. There the penalties can be up to a $25 million fine for companies and up to 20 years imprisonment or $5 million fine for individuals.

Hank Hockeimer:

So both of those entities work in tandem, particularly if it's a public company. If it's a public company, then the SEC is not in play. It's the Department of Justice. And then there are other rules about the presence that they have in the U.S. and the relationship between the foreign entity and the United States entity that's probably more subject to another podcast.

Hank Hockeimer:

But suffice to say that the two regulators, so to speak, are the Department of Justice and the Securities and Exchange Commission. The latter focusing on books and records violations, whether the payments or other things of value are accurately memorialized in their accounting and other records maintained by the company.

Chris Willis:

And, Hank, again to draw a comparison with the consumer protection laws that our audience is very accustomed to, we're used to having all the kinds of regulators that I mentioned before do examinations and look for violations of various consumer protection laws. But what's the detection method for FCPA violation? How does the DOJ or the SEC find out enough to start an investigation? How do these cases normally start?

Hank Hockeimer:

Well, that's a great question, and there's no template for how they start. I mean, the World Acceptance investigation, apparently it was prompted by the receipt of an anonymous letter to the company or, I think, to the board. But it's unclear within the publicly filed disclosure statements. That can be an avenue. You could have some other kind of whistleblower, whistleblower hotline that could field a violation or the potential violation that could be communicated on a whistleblower line.

Hank Hockeimer:

It could be a former employee who is disgruntled. It could be a current employee. It could be a company just doing its own routine audit of its books and records, and their internal audit people could come across payments or trips or things like that. We've had cases where an internal auditor saw some trips that seemed out of place to third parties. And it turned out the third parties were foreign officials who were in charge of determining whether the company in a particular country would get business or not.

Hank Hockeimer:

So they can come from a variety of ways. I'm not aware of the SEC performing its own routine audits coming across it, but I'm sure that has happened. But they can be prompted or revealed by a whole host of different ways.

Chris Willis:

Well, given the severity of the penalties that you discussed a few minutes ago, multimillion dollar fines and potentially even criminal charges and jail time for people who are involved in violations of the FCPA, it's obviously of great importance for our audience to know what steps they can take to try to avoid potential FCPA liability. What advice would you have for them in that regard?

Hank Hockeimer:

Sure. And we do that a lot. We do a lot of compliance work for clients both before an issue happens, and frankly, we often revise compliance programs after the problem has materialized. But there's no necessarily a checklist, but there are certain fundamental things that a company should look at.

Hank Hockeimer:

Number one is, where are you operating? Are you operating in a red flag country? And a red flag country is defined as a country where purported or possible corrupt payments are often made in order to get business, in order to keep business. And there's a company, Trace International, that puts out on an annual basis a map that gives the red flag countries that the Department of Justice and the SEC are historically very interested in focusing on those countries. So that's the first thing you should look at is where are you operating. Latin America, Eastern Europe are a lot redder when it comes to red flags then say a Nordic country like Sweden or Denmark or whatever.

Hank Hockeimer:

The second is, are you using any kind of intermediaries, agents, consultants? If so, do you have an agreement with that person or those persons in a particular country? Is there an anti-bribery provision in any consulting or agency agreement you have with someone who's assisting you to get business from a foreign entity?

Hank Hockeimer:

And I should back up for a second. In addition to looking at the geographic issue, who are your customers in those different countries? Do they involve foreign officials? Do they involve government entities that are your customers? Then you really have to, obviously, hone in on the FCPA issue. If you have intermediaries, agents, consultants that are assisting in getting you business, you really have to give a hard look at those individuals in order to make sure that the agreements are airtight.

Hank Hockeimer:

Because if an issue does come down the road, the first thing the government's going to ask, and this is a big area within the last several years, is "Are you using third parties? And if so, are there agreements? And we'd like to see those agreements." And so you might have some cover if the agreements are solid, if there are anti-bribery provisions in the agreements, and then you could potentially make the argument that the agent was off the reservation if he or she did make any kind of payment or provide anything of value to a foreign official to get business.

Hank Hockeimer:

You want to look at the industry that you're in. Here, we're financial services. Historically, there hasn't been a lot of activity, but again, with the World Acceptance issue, and a couple of years ago there were some investment banks that had some FCPA issues because of the hiring practices where they hired relatives of foreign officials. So you want to look and see if in that country there have been historically issues that have maybe impacted your particular industry.

Chris Willis:

Yeah, that is really interesting, Hank, and I can't thank you enough for being on today's podcast and telling our audience about this important development and the potential trend that it may signal in the consumer financial services world. And to give our audience an education about the nuts and bolts of the Foreign Corrupt Practices Act and how it works. I know this is a critically important issue for a number of financial services companies, because many of them based in the U.S. do business overseas, both banks and non-banks. So I'm sure our audience got a lot out of the podcast today. So thank you very much for joining us.

Hank Hockeimer:

Sure. Happy to do it, and thanks for having me, Chris. You take care.

Chris Willis:

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Chris Willis:

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