

EFFECTIVE USE OF LEGAL AND ASSET-TRACING REMEDIES FOR CORRUPTION:

CIVIL LEGAL REMEDIES

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I. Overview of Legal Remedies for Corruption

A. Example based on an actual case of corruption by a foreign contractor

In 1990, Big Tex Energy Incorporated, which is doing limited business in Ruritania, learns of a potentially lucrative opportunity to enter into a joint venture with the government of Ruritania to explore and develop oil reserves. The joint venture is to be called Ruritanian Energy. To increase the likelihood of being awarded the contract, Big Tex hires Frantz Schwartz, an individual with close ties to the Ruritanian government. With the assistance of Schwartz, Big Tex sets up meetings with members of the Ruritanian government, including the Energy Minister. At those meetings, the president and vice-president of Big Tex bribe the Energy Minister and two other officials \$5 million to award the joint venture to Big Tex. The money is wired to a Swiss bank account, and the new joint venture agreement is signed in 1991. The agreement contains a number of favourable terms for Big Tex, and provides for arbitration in New York in the event of a dispute. During the next four years, Big Tex makes a number of smaller payments to other government officials to ensure that the terms of the contract continue to be favourably interpreted. For example, under contracts signed pursuant to the joint venture agreement, New Ruritanian Energy must buy expensive oil development equipment from subsidiaries of Big Tex in the United States.

In 1995, New Ruritanian Energy discovers new oil reserves. In 1997, Big Tex sells its share of Ruritanian Energy at a substantial profit. Big Tex then moves all of its assets out of Ruritania and into Texas and New York.

B. Legal issues to be considered

Prior to determining what legal action, if any, it wants to pursue, the government (or any potential claimant) must consider certain key legal issues.

1. What is the legal harm suffered?

The Ruritanian government claimant has suffered various types of legally cognisable harms, including:

- unfair contract terms (for example, deadlines and payment schedules)
- unfair contract price
- unnecessary purchase of products or services
- lost profits from sale of product and sale of business

Damages in other cases may include compensation for shoddy performance or for defective product(s) which cause injury to others.

2. Does the contract contain a valid dispute resolution mechanism?

The two basic types of dispute resolution clauses are:

- an arbitration clause
- a forum selection agreement

Big Tex's contract with the Ruritanian government contains an arbitration clause. Therefore, if the clause is still valid and applicable, the parties should be required to arbitrate their disputes.

3. What are the potential remedies?

- criminal (punishing the offenders)
- administrative remedies (e.g., banning company or country from doing business in the state as a result of governmental investigations)
- civil (getting compensation for damages)

Effective civil remedies may change the economic priorities in the fight against corruption. Criminal penalties seek to deter and punish individuals who have engaged in corruption. Although civil suits may have this effect, as well, they focus on a different economic dynamic: getting back lost money and recovering compensation for harm done. For purposes of this conference, I will primarily consider available civil legal remedies. Of course, civil remedies should be pursued in parallel with criminal and administrative penalties, where appropriate.

4. Where are the assets located?

- where the assets are no longer located in the jurisdiction, then arbitration or a suit in the contractor's home court may be more likely

Big Tex has moved all of its assets outside of Ruritania. Therefore, the Ruritanian government should compare the availability of damages from a lawsuit brought locally versus arbitration or a suit brought in the contractor's home jurisdiction.

5. Who are the parties that may be sued?

- bribing company (Big Tex)
- bribe recipient(s) (Minister of Energy and other officials)
- directors and officers of bribing company in their individual capacities
 - Director and Officer insurance may exclude dishonesty
- professionals involved in drafting documentation (e.g., the attorneys representing Big Tex).

6. What are the sources of potential legal remedies?

The potential civil legal remedies will depend on choice of law clauses, if any, conflicts of law principles, and the jurisdiction in which the suit is brought. Therefore, a potential claimant may seek relief based on:

- domestic law
- law of foreign contractor
- public and private international law
 - But note that most multilateral treaties generally provide for criminal and not civil penalties

II. Potential Avenues for Civil Remedies

One of the most important decisions that a potential claimant faces in evaluating its civil remedies is to decide where, and by whom, the dispute will be decided. There are three fundamental choices: 1) arbitration, 2) litigation in the courts of the host country, and 3) litigation in the contractor's home country. This choice often determines the dispute's eventual outcome. See Gary B. Born, *International Arbitration and Forum Selection Agreements: Planning, Drafting and Enforcing* (Kluwer 1999).

A. Actions Pursuant to Arbitration Provisions in Underlying Contract Against Foreign Contractor

Increasingly, international contracts provide for arbitration as the dispute resolution mechanism. This may be due to a number of reasons, including the parties' desire for a neutral forum, considerations of cost and speed, the perception of competence of and control over the decision-makers, concerns about confidentiality, and the ease of enforceability under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention"), to which more than 120 countries are now members.

1. Scope of arbitration agreement and the choice of law clause. The remedies available to a party invoking an arbitration clause may depend on the scope of the arbitration clause and which law the parties have provided for in their agreement.

- a. Scope of the arbitration clause. Critical to the arbitration agreement is the "scope" of an arbitration clause. For example, will the parties submit disputes bearing any conceivable connection to their contractual relations or will they limit the arbitration only to disputes over the express terms of the parties' agreement? This can be especially important because a "narrow" arbitration clause may prevent a party from bringing claims of fraud and corruption in arbitration. Subject to local law, a clause which may catch both contract and tort claims linked to a commercial contract may read:

"The parties shall submit to binding arbitration, under the Rules of Arbitration of the International Chamber of Commerce in force at the date of the request for arbitration, for the resolution of any disputes relating to this contract. The tribunal shall consist of [a sole/three arbitrators]. The place of the arbitration shall be [town/city]. The language of the arbitration shall be [language]."

- b. Choice of law clause. Remedies will depend on the law the parties have chosen, if any. U.S. courts increasingly allow arbitration of most civil claims. *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 238, 242 (1987) (RICO claims arbitrable). A typical choice of law clause might read:

"This contract and all issues relating to it shall be settled in accordance with the laws of [country or state]."

2. Possible legal obstacles to arbitration

- a. Separability of arbitration clause. The law of the United States, like the law of most jurisdictions, provides that "*except where the parties otherwise intend . . .* arbitration clauses are 'separable' from the contracts in which they are embedded...." *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 402 (1967).

- In *The Republic of the Philippines v. Westinghouse Electric Corp.*, 714 F.Supp. 1362 (D.N.J. 1989), the U.S. District Court held that the Philippine government's claims against Westinghouse, an American corporation, arose out of a contract for construction of a nuclear power plant and were subject to arbitration. The fact that the company allegedly bribed the Marcos regime to get the construction contract did not constitute fraud that invalidated the arbitration clause.
- b. Non-arbitrability doctrine. Some countries' courts may refuse to allow arbitration of corrupt transactions. However, a Swiss arbitral tribunal held that it had jurisdiction to deal with bribery claims in a case involving the Marcos family. See Gary Born, *International Commercial Arbitration in the United States* (Kluwer 1994).
- c. Cost of arbitration proceedings. A claimant must pay administrative expenses and arbitrator(s)' fees up front. But he may recover those costs if he wins (See, e.g., ICC Rules, Article 31(3)).

B. Actions in Host Country's Courts Against Contractor

1. Possibility of civil suit in local courts of country where project is located. Depending on the issues discussed below, a government or government entity may bring a civil suit in the local courts of the country where the project is located. As noted above, however, litigation against contractor in host country courts may violate an arbitration agreement or the forum clause in the underlying contract.
2. Possible Civil Remedies in Host Country's Courts. As discussed above in II.A.1.b. and III below, civil remedies depend on choice of law (or, in the absence of a clause, conflicts of law principles). The principles for these remedies may, in certain cases, be similar to the U.S. principles discussed below (although punitive damage awards are unlikely). For example, in Germany, the Federal Supreme Court has held that contracts resulting from bribery actions are null and void under section 138 BGB, the German Civil Code, as conflicting with "bonos mores." 94 BGHZ 268, 271.
 - Compensatory damages for poor performance/shoddy product. One reason to bring a suit in local courts (as opposed to in arbitration) would be to include claims for damage to third parties, perhaps from personal injury or products liability. For example, a state or state entity might claim damages for collapse of buildings in an earthquake due to failure to comply with standards as a result of corruption.
 - Forfeiture statutes. Compare 28 U.S.C. § 2514 ("A claim against the United States shall be forfeited to the United States by any person who corruptly practices or attempts to practice any fraud against the United States in the proof, statement, establishment, or allowance thereof."); *U.S. v. ACME Process Equip. Co.*, 385 U.S. 138, 87 S.Ct. 350 (1966) (a government may, as a matter of public policy, avoid a contract that is tainted by fraud, kickbacks, conflicts of interest, or bribery).

3. Possible obstacles to bringing a suit in the host state's courts. When deciding whether to bring a suit in its own courts, a host state should consider a number of legal and non-legal factors. The most important, of course, is whether the contract with the foreign contractor included an arbitration or forum selection clause (as discussed above). Other significant considerations include political issues such as publicity and politisation, and legal issues such as court delays or lack of judicial expertise. In addition, a host country should consider the ease or difficulty in enforcing its local judgement in another country's courts, if there are assets located abroad.
 - Without a multilateral treaty such as the Brussels and Lugano Conventions or a bilateral treaty, a local judgement may be difficult to enforce. Although the United States is a member of the New York Convention, it is not a party to any international treaties on enforcement of judgements. Thus, a foreign party seeking to enforce a foreign judgement must meet the requirements of the law of the state in which it seeks enforcement.

C. Actions Against Contractor in Contractor's Home State

1. Possibility of civil suit against contractor in its "own back yard." A key reason why a foreign party may want to bring a suit in the contractor's home state is because the defendant's assets are located there. (See example in section I. above).
2. Choice of law principles. As discussed in II.A.1.b. above, civil remedies depend on a choice of law clause (or, in the absence of a clause, conflicts of law principles). A foreign party bringing a suit in a contractor's home state courts should note that mandatory laws of that jurisdiction may apply. In the United States, for example, courts may apply certain mandatory rules of law or public policy even where the parties have agreed to non-U.S. law. *See Govett American Endeavor Fund Ltd. v. Trueger*, 112 F.3d 1017 (9th Cir. 1997) (where illegal acts were committed in California, the defendant could not avoid RICO by choosing law of Jersey, a foreign jurisdiction). In addition, although punitive damages are more difficult to obtain in breach of contract cases, a U.S. court is generally more likely to award exemplary damages than an arbitrator.
3. Possible civil remedies. Potential civil remedies under U.S. law are discussed in more detail in section III below. However, U.S. courts have faced civil RICO suits predicated on the Foreign Corrupt Practices Act on at least two occasions:
 - In *Dooley v. United Technologies Corp.*, 803 F.Supp. 428 (D.D.C. 1992), the District Court held that the FCPA does not apply to foreign corporations, and therefore the FCPA could not serve as a predicate act in a civil RICO case.
 - In *Environmental Tectonics v. W.S. Kirkpatrick, Inc.*, 847 F.2d 1052 (3d Cir. 1988), *aff'd on other grounds*, 493 U.S. 400 (1990), a U.S. competitor of another U.S. company who allegedly bribed the Nigerian government to obtain a foreign military contract brought RICO claims which were

predicated in part upon violations of FCPA. The court determined, in a conclusory paragraph, that the competitor had standing to bring RICO claims against the U.S. company.

4. Possible legal and other obstacles. There are a number of legal and other obstacles which may discourage a foreign government or entity from bringing a suit in U.S. courts, including:
 - Litigation against contractor in host country courts may violate arbitration agreement/forum clause in underlying contract.
 - Home court bias v. advantages of some local tribunals (e.g., no jury).
 - Cost (contingent fees or creative fee structures; opportunity for substantial success).
 - Waiver of immunity and exposure to counterclaims under the Foreign Sovereign Immunities Act (28 U.S.C. §§1602 – 1610).
 - Other judicial costs, such as extensive discovery.

5. Related party litigation: suits by third parties. Third parties other than the government contractor have brought suits in U.S. courts on various occasions. The courts have generally been reluctant to allow these suits to proceed.
 - Suit by distributor or employee of bribing company. A distributor of GE products in Peru could not bring RICO claim against GE due to the distributor's alleged refusal to co-operate with GE in its scheme to secure and retain contracts through bribery and extortion of public officials. *J.S. Service Center Corp. v. GE Technicial Services Co.*, 937 F.Supp. 216, 226 (S.D.N.Y. 1996); *Dooley v. United Technologies Corp.*, 803 F.Supp. 428 (D.D.C. 1992) (employee sued his employer, its parent corporation and others, alleging that they engaged in a bribery scheme to sell helicopters to Saudi Arabia and that he was demoted due to his refusal to participate).
 - Suit by individual in government. Minister of Tourism and Information of Jamaica could not bring RICO claims against advertising firm for alleged injury to reputation and status resulting from dissemination of false information regarding bribery. *Abrahams v. Young & Rubicam Inc.*, 79 F.3d 234, 237 (2d Cir.), *cert. denied*, 519 U.S. 816 (1996).

D. Actions Against Recipient of Bribe

1. Possible fora
 - a. Probably not possible to invoke arbitration agreement
 - Third parties (i.e., the recipient of the bribe) not generally bound by arbitration clause
 - b. Host state's courts
 - Local law
 - Local attitudes
 - Political will
 - c. Place where bribe was deposited
 - Possible locations
 - d. Elsewhere
 - Depends on local jurisdictional powers
2. Possible claims (Depends on applicable law)
 - a. Forfeiture
 - b. Disgorgement/conversion
 - c. Damages for breach of duties
3. Possible legal and practical obstacles
 - a. Locating assets that can be enforced against
 - b. Political issues
 - c. Subjecting state to foreign jurisdiction

III. Potential Civil Remedies Under U.S. Law

Under U.S. law, a claimant might be able to seek the following legal remedies for corruption:

1. Foreign Corrupt Practices Act ("FCPA"). Although the FCPA provides for criminal and civil provisions, there is no private right of (civil) action under the FCPA's anti-bribery or accounting provisions. *Lamb v. Philip Morris, Inc.*, 915 F.2d 1024, 1027-30 (6th Cir. 1990), *cert. denied*, 498 U.S. 1086 (1991) (anti-bribery provision; no private right of action in favor of domestic tobacco producers); *Citicorp Int'l Trading Co. v. Western Oil & Refining Co.*, 771 F.Supp. 600, 606-07 (S.D.N.Y. 1991)

(antibribery provision; no private right of action for shareholders allegedly injured by corporation's attempt to bribe foreign officials); *J.S. Service Center Corp. v. GE Technical Services Co.*, 937 F.Supp. 216, 226 (S.D.N.Y. 1996); *Shields ex rel. Sundstrand Corp. v. Erickson*, 710 F.Supp. 686, 688 (N.D. Ill. 1989) (accounting provision); *Eisenberger v. Spectex Indus., Inc.*, 644 F.Supp. 48, 50-51 (E.D.N.Y. 1986) (accounting provision).

2. Rescission/setting aside of contract (on theories of fraud, illegality, etc.). A contract is invalid and may be set aside where it was product of a bribe or other corruption. *Chuidian v. Philippine National Bank*, 734 F.Supp. 415, 418 (C.D.Cal. 1990) citing California Civil Code § 5111 (contract invalid or rescinded where tainted with corruption, illegality or fraud); *Banker's Trust Co. v. Litton Systems*, 599 F.2d 488 (2d Cir. 1979) (contract illegal and unenforceable where contract obtained through bribery). In addition, a party may seek the forfeiture of paid and unpaid proceeds of contract. *S.T. Grand, Inc. v. City of New York*, 38 A.D.2d 467, 330 N.Y.S.2d 594 (N.Y.Ct.App. 1st Dep't. 1972) (but note violation of established mechanism for bidding).
 - International standards. Council of Europe's Multi-Disciplinary Group on Corruption: proposal requiring the parties to adopt national legislation which would treat as null and void any contract made in order to facilitate the receiving of illicit payments or other illicit advantages. New Criminal Law Provisions Against the Corruption of Public Officials, Council of Europe: Multidisciplinary Group on Corruption (GMC), 14th Sess. 1, 18 (1995); Paolo Bernasconi, About the Necessity of an International Convention Preventing and Combating the Corruption of Public Officials (Draft Summary), arts. 2, 6, 8, 10 (Nov. 1993).
3. Reformation of unfair terms of contract. A party may seek to reform certain terms in a contract where that contract was induced by fraud. *Hartman v. Prudential Insurance*, 9 F.3d 1207, 1209 (7th Cir. 1993). Alternatively, a party may seek compensatory damages for unfair terms or excessive price of a contract where there have been fraudulent representations by the other party. The damages may be measured by the difference between the fair price without the bribe and the bribe-induced price. *Schank v. Schuchman*, 212 N.Y. 352, 106 N.E. 127 (N.Y.Ct.App. 1914).
4. Compensatory damages for poor performance/shoddy product. Where the foreign contractor poorly performed the contract (but got away with it due to corruption) or where the foreign contractor produced a shoddy product, the contractee could seek compensatory damages for the damages.
 - However, since there must be a valid arbitration agreement before compelling a party to arbitrate, it is unlikely that tort damage to third parties could be submitted to arbitration.
5. Equitable claims such as restitution, accounting, or a constructive trust.

- a. The bribe-payor and bribe recipient may both be liable for repayment of the amount of the bribe. *Continental Management, Inc. v. United States*, 208 Ct.Cl. 501, 527 F.2d 613, 620 (1975) (common law right of government to sue bribors for amount of bribes paid to government employees; "the amount of the bribe provides a reasonable measure of damage, in the absence of a more precise yardstick."); *City of New York v. Joseph L. Balkan, Inc.*, 656 F.Supp. 536 (E.D.N.Y. 1987) (city stated common law cause of action against contractors for alleged bribery of city sewer inspectors); *United States v. Cripps*, 460 F.Supp. 969 (E.D.Mich. 1978).
 - b. In most states, a claimant would be able to ask for the establishment of "constructive trust" for the proceeds of bribes. *Chicago Park District v. Kenroy, Inc.*, 78 Ill.2d 555, 402 N.E.2d 181 (Ill. 1980); see *Jackson v. Smith*, 254 U.S. 586 (1921) (party who participates in breach of fiduciary duty must disgorge all profits made as a result of wrongful conduct, without regard to whether the plaintiff suffered a corresponding loss). Party could then trace the proceeds of the bribe.
 - c. Similarly, a claimant may ask for an accounting for the proceeds of the bribe. *County of Cook v. Barrett*, 36 Ill.App.3d 623, 344 N.E.2d 540 (Ill.Ct.App. 3rd Div. 1976); *United States v. Carter*, 217 U.S. 286 (1910).
 - d. Since the United States does not allow tax-deductibility for bribes, any benefits gained must also be returned. See *Carter v. Berger*, 777 F.2d 1173 (7th Cir. 1985) (defendants must surrender tax benefits received as a result of bribing public officials); *People ex. rel. Daley v. Warren Motors, Inc.*, 500 N.E.2d 22 (Ill.App. 1986).
6. Remedies from breach of a statutory duty/breach of claims under international treaties
- a. The OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions lacks any specific civil enforcement mechanisms. However, Article 3(3) of the OECD Convention does possess a civil principle – the forfeiture/disgorgement/restitution of the benefits of a bribe. It provides

"Each party shall take such measures as may be necessary to provide that the bribe and the *proceeds of the bribery* . . . or property the value of which corresponds to that of such proceeds, are subject to seizure and confiscation or that monetary sanctions of comparable effect are applicable." (emphasis added).
 - b. "Proceeds of the bribery" is defined as "profits or other benefits derived by the briber from the transaction or other improper advantage obtained or retained through bribery." Commentary 21.
 - c. Forfeiture under the OECD is not necessarily consistent with the FCPA, because it could result in civil fines that exceed the US\$10,000 maximum civil penalty under the FCPA.
 - d. Difficulty with tracing and measuring the "benefits" attributable to the bribe, and

when such benefits are to be measured (early in the project or later?).

7. Exemplary/punitive damages. Under certain statutes, a claimant has a right to triple damages as a matter of law. (E.g., RICO, 18 U.S.C. § 1964(c)). Likewise, under the common law, a claimant may be entitled to punitive damages. However, international arbitral tribunals are less likely than U.S. courts to award exemplary or punitive damages against a party.

IV. Importance of Proper Preparation and Organisation

A. Litigation Realities

- Time consuming, expensive, mere possibility of success

B. Need for Focussed, Disciplined Client Representatives as Part of Team

- Possesses confidence of superiors and with authority to act
- Identifying/organising witnesses and documents
- Realistic assessment of chance of success
- Likelihood of publicity

C. Selecting and Managing External Advisers

- Knowledgeable of law of forum and dispute resolution options
- Knowledgeable of international law
- Knowledgeable of local and international political realities
- Prepared to deal with publicity concerning matter