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Foreigner Beware

This article is a cautionary tale.

It is directed to attorneys representing non-U.S. clients. Those attorneys and their clients need to know that bribery engaged in by a non-U.S. citizen, entity, or resident who (a) is not an officer, director, or employee of a U.S. entity; (b) is not affiliated with an entity that bribed a U.S. company or individual; and (c) engaged in wrongful conduct directed solely at a non-U.S. individual or entity may be subject to personal jurisdiction in American courts. The perhaps counter-intuitive nature of that conclusion is all the more reason why clients need to know that their conduct may embroil them in American courts.

Watergate and widespread bribery of foreign officials helped create an atmosphere of distrust, which led to a demand for greater honesty and transparency in government and corporate America. One of the consequences of the tawdry atmosphere of the '70's was the 1977 enactment of the Foreign Corrupt Practices Act[1]. At its heart lies the prohibition which forbids "domestic concerns,"[2] "issuers,"[3] and persons subject to "territorial jurisdiction"[4] of the U.S. from making corrupt payments to foreign officials to obtain or retain business. It may have been the paucity of judicial decisions and the resulting lack of clarity as to the reach of the statute which prompted the Department of Justice ("DOJ") and Securities and Exchange Commission ("SEC") in 2012 to publish the Resource Guide to the FCPA.[5] The Guide, however, left vague the threshold issue of personal jurisdiction.

Two recent decisions out of the Southern District of New York came to different conclusions as to the reach of personal jurisdiction. In *SEC v. Straub*,[6] Judge Sullivan denied the defendants' motion to dismiss in which they had argued that they had insufficient contacts to justify jurisdiction. In *SEC v. Sharef*,[7] Judge Scheindlin granted defendant Herbert Steffen's motion to dismiss, finding that the SEC failed to establish that Steffen had met the minimum contacts standard to justify jurisdiction. The question thus arises, are there meaningful factual differences between the two and will the Second Circuit, when called upon, agree with either or both of the holdings?

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[1] 15 U.S.C. §§ 78dd-1 *et seq.* ("FCPA").
[2] Domestic concerns include U.S. persons and businesses.
[3] Issuers are those U.S. and foreign public companies which are listed on stock exchanges in the United States or are required to file periodic reports with the Securities and Exchange Commission.
[4] Persons subject to territorial jurisdiction include certain foreign persons and businesses acting while in the territory of the United States.
[5] Criminal Division of the U.S. Department of Justice & Enforcement Division of the U.S. Securities and Exchange Commission, *A Resource Guide to the FCPA*, Nov. 14, 2012, at 2.
[6] *SEC v. Straub*, No. 11-CV-9645, 2013 WL 466600 (S.D.N.Y. Feb. 8, 2013).
[7] *SEC v. Sharef*, No. 11-CV-9073, 2013 WL 603135 (S.D.N.Y. Feb. 19, 2013).

The singular glaring difference between the two cases is that in *Straub*, the defendants actually signed certain financial documents. There, Judge Sullivan found that sufficient contacts existed to obtain jurisdiction over Straub. In *Sharef*, Steffen did not sign anything and his motion to dismiss was granted.

Both of these cases involved non-U.S. individual defendants who engaged in conduct which, to one degree or another, was designed to further a non-U.S. corporate employer's financial interests by bribing non-U.S. persons, companies, or governments. To determine whether such a person can be ensnared by the FCPA requires a careful look at the constitutional requirements for a valid acquisition of personal jurisdiction: i) minimum contacts; and, if those are constitutionally satisfied, ii) whether the defendant can present a compelling case that other circumstances render the imposition of jurisdiction unreasonable.

Before analyzing the facts affecting jurisdiction, some basics should be noted.

First, "[a] nonresident defendant sued under the [Securities] Exchange Act [of 1934] need not have minimum contacts with the state seeking to exercise personal jurisdiction; rather the only contacts required are with the United States as a whole, as Section 78 provides for nationwide service of process."[8]

Second, to satisfy Due Process, the plaintiff must show that the claim:

i. Arises out of or relates to, the defendant's contacts with the forum; i.e., the defendant purposely availed itself of the privilege of doing business in the forum; and that

ii. The defendant could foresee being haled into court in that forum.[9]

As to subparagraph i, both *Sharef* and *Straub* agree on the fundamental propositions that: jurisdiction exists where an executive of a foreign securities issuer, wherever located, participates in a fraud *directed* to deceiving U.S. shareholders; and that the signing or directly manipulating financial statements to cover up illegal foreign action, with knowledge that those statements will be relied upon by U.S. investors satisfies that test.[10]

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[8] *Sharef*, at *4, citing *In re Magnetic Audiotape Antitrust Litig.*, 334 F. 3d 204, 207 (2d Cir. 2003).

[9] *Straub*, at *6, citing *Kernan v. Kurz-Hastings, Inc.*, 175 F. 3d 236, 242-43 (2d Cir. 1999); *Sharef*, at *4 n.50, citing *Bank Brussels Lambert v. Fiddler Gonzales & Rodriguez*, 305 F. 3d 120, 127 (2d Cir. 2007).

[10] *Sharef*, at *4; *Straub*, at *6. "Where an executive of a foreign securities issuer, wherever located, participates in a fraud directed to deceiving United States shareholders in violation of federal regulations requiring disclosure of accurate information to holders of securities traded in the United States, such direct consequences have occurred. SEC regulations would be meaningless as applied to foreign issuers of U.S.-traded securities if the United States courts lacked jurisdiction over executives abroad who violate those regulations. The complaint here alleges that [the defendant executive] conceived and implemented a strategy for entering a sham transaction and specifically intended that his work would result in false statements by [his company] in its publicly-filed financial statements in the United States. At least to the extent that this allegation states a claim for violation of the United States securities laws, this Court has jurisdiction over the persons alleged to have committed that violation." *SEC v. Stanard*, No. 06-CV-7736, 2009 WL 196023 (S.D.N.Y. May 16, 2007) (unpublished transcript of ruling, Opp'n Ex. 2, Tr. 3:2–18).

As to subparagraph ii, *Sharef* held that it is foreseeable for a defendant to be subjected to a U.S. court's jurisdiction where the effects of its conduct occur as a direct and foreseeable result of conduct outside of the territory; directly manipulating financial data that a U.S. investor may rely upon is sufficiently direct. Foreseeability alone is not enough to satisfy the Due Process requirements for a finding of jurisdiction.[11] "[A] foreign actor's activity in relation to the United States must be sufficiently extensive and regular to make the possibility of litigation in the United States a foreseeable risk of business."[12] *Straub* held that jurisdiction is proper where "the contacts proximately result from actions by the defendant *himself* that create a substantial connection with the forum."[13] The emphasized word "himself" may hold the key to the distinction between the decisions *Straub* and *Sharef* -- based primarily, if not exclusively, on Steffen's not having "himself" signed any financial documents. As will be noted, Steffen certainly left his figurative fingerprints on the bribery scheme. What he did not do, was leave any ink on a financial document. As Judge Scheindlin said:

> It is by now well-established that signing or directly manipulating financial statements to cover up illegal foreign action, with knowledge that those statements will be relied upon by United States investors satisfies this test. However, the exercise of jurisdiction over foreign defendants based on the effect of their conduct on SEC filings is in need of a limiting principle.[14]

Short of signing a false document, what constitutes manipulation of a financial document sufficient to satisfy Judge Scheindlin's need for a limiting principle? Should a sophisticated business person, who actively engaged in a bribery scheme and who urged and cajoled a financial officer to sign off on financial documents that are false and filed with the SEC, have known that the financial documents would necessarily be falsified to hide the scheme, and, as falsified, would be relied upon by American investors? Is that enough?

As we will note, apparently not for Judge Scheindlin.

The minimum contact analysis is the offensive prong of the FCPA jurisdictional gambit. Assuming it is satisfied, the inquiry shifts to the defensive Due Process review of reasonableness. Here, reasonableness is subjected to a 5 point evaluation:

> (1) the burden that the exercise of jurisdiction will impose on the defendant; (2) the interests of the forum state in adjudicating the case; (3) the plaintiff's interest in obtaining convenient and effective relief; (4) the interstate judicial system's interest in obtaining the most efficient resolution of the controversy; and (5) the shared interest of the states in furthering substantive social policies.[15]

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[11] *World-Wide Volkswagen Co. V. Woodson,* 444 U.S. 286, 295 (1980).

[12] *Straub,* at *6.

[13] *Id.*, quoting *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 475 (1985) (emphasis in original). In a footnote, the *Straub* court noted that a defendant's personal actions needed to proximately *cause* a defendant's contacts, not that a defendant's personal actions need to have proximately caused the injury. *Id.*, at *19 n.6.

[14] *Sharef*, at p.6.

[15] *Straub*, at *10; *Sharef*, at *4; both citing *Asahi Metal Indus. Co., Ltd v. Super. Ct. of Cal.*, 480 U.S. 102, 113-114 (1987).

In *Straub*, the court found the reasonableness defense of no avail to the defendant. In *Sharef*, the court dismissed the complaint, noting that the defense served merely to bolster the more fundamental finding that the SEC failed to establish the required minimum contacts.

These principals, both as to minimum contacts and reasonableness, are the standards by which to measure a defendant's conduct to determine whether he or she is subject to U.S. jurisdiction, and, if so, whether the exercise of that jurisdiction would be offensive to Due Process concerns of fair play and substantial justice. Applying these standards, under what circumstances will jurisdiction be found where the individual is (i) not a U.S. citizen or resident; (ii) not an officer, director, or employee of a U.S. corporation; and (iii) not affiliated with an entity that bribed a U.S. company or individual?

Sharef involved Siemens Aktiengesellschaft ("Siemens"), a multinational corporation headquartered in Germany. The court's decision came on Steffen's motion to dismiss. Between 2002 and 2006, the CFO of Siemens Business Services ("SBS") Bernd Regendantz signed quarterly and annual certifications under the Sarbanes-Oxley Act in which he represented that SBS' financial statements were not false or misleading. On Steffen's motion to dismiss, the allegation of the bribery scheme is accepted as true and the certifications thus are deemed fraudulent. Steffen was a German citizen, CEO of Siemens in Argentina from 1983 to 1989 and again in 1991. Thereafter, he was group president of Siemens Transportation Systems from 1996 until 2003. The SEC allegations set forth a scheme by which Siemens paid an estimated $100 million dollars in bribes to government officials in Argentina. And approximately $31 million dollars of those bribes were paid after March 12, 2001 when Siemens became subject to U.S. securities laws.

Uriel Sharef, a Siemens managing board member, recruited Steffen to facilitate the payment of bribes to Argentinean officials because of Steffen's relationships with them over many years.

In 1998, Siemens was awarded a $1 billion dollar contract in Argentina. After a change in government, Siemens was advised that the contract was not going to be renewed, unless terms -- bribes -- were renegotiated with -- paid – to the new government officials. Those officials demanded that Siemens pay bribes in order to reinstate the contract. The bribes were, in fact, paid using a Siemens front company to cloak the payments. Notwithstanding that the bribes were made, the contracts were cancelled. Distressed that its bribery scheme failed, Siemens initiated an arbitration proceeding in the World Bank's International Center for the Settlement of Investment Disputes to recover lost profits and costs. The evidence of the corruption in the initial contract award would have provided a defense to Argentina and so Siemens doubled down and now bribed officials in Argentina to ensure that they did not disclose the earlier/unsuccessful bribes.

Steffen had met with Regendantz and pressured him to authorize the bribes. Steffen was involved in a phone call initiated by Sharef from the United States in which, in 2003, Steffen allegedly urged Sharef to make the additional bribes. Regendantz sought guidance from "superiors" from Siemens' CFO, its head of compliance, its CEO as well as two members of the managing board who advised him that the bribes were authorized. He then authorized the bribes. Fictitious documents were created, payments routed through an intermediate in Uruguay and wire transfer instructions were sent to a bank account in New York. A second bribe was made after Steffen had retired.

Siemens prevailed in arbitration. Regendantz filed allegedly fraudulent certifications under Sarbanes-Oxley when he represented that the financial statements were not false or misleading.

In dismissing the SEC complaint, Judge Scheindlin observed that,

> . . . Steffen's actions are far too attenuated from the resulting harm to establish minimum contacts. Steffen was brought into the alleged scheme based solely on his connections with Argentine officials. In furtherance of his negotiations with those officials, Steffen "urged" and "pressured" Regendantz to make certain bribes. However, Regendantz did not agree to make the bribes until he communicated with several "higher ups" whose responses he perceived to be instructions to make the bribes. Once Regendantz agreed to make the bribes -- following receipt of instructions from Siemens' management rather than Steffen -- Steffen's alleged role was tangential at best. Steffen did not actually authorize the bribes. The SEC does not allege that he directed, ordered or even had awareness of the cover ups that occurred at SBS *much less that he had any involvement in the falsification of SEC filings* in furtherance of those cover ups. Nor is it alleged that his position as Group President of Siemens Transportation Systems would have made him aware of, let alone involved in falsification of these filings.
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> . . . If this Court were to hold that Steffen's support for the bribery scheme satisfied the minimum contacts analysis, even though he neither authorized the bribe, nor directed the cover up, much less played any role in the falsified filings, minimum contacts would be boundless. Illegal corporate action almost always requires cover ups, which to be successful must be reflected in financial statements. Thus, under the SEC's theory, *every* participant in illegal action taken by a foreign company subject to U.S. securities laws would be subject to the jurisdiction of U.S. courts no matter how attenuated their connection with the falsified financial statements. This would be akin to a tort-like foreseeability requirement, which has long been held to be insufficient.
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> . . . The allegations against Steffen fall far short of the requirement that he "follow a course of conduct directed at . . . the jurisdiction of a given sovereign, so that the sovereign has the power to subject the defendant to judgment concerning that conduct. Absent any alleged role in the cover ups themselves, let alone any role in

> preparing false financial statements the exercise of jurisdiction here exceeds the limits of due process, as articulated by the Supreme Court and the Second Circuit.[16]

If Steffen's conduct can be viewed as attenuated, then jurisdiction, if imposed, might well, as Judge Scheindlin suggests, subject "*every* participant in illegal action taken by a foreign company subject to U.S. securities laws."[17]

Straub presents differently. In it, the individual defendants, executives of the Hungarian telecommunications company, Magyar Telekom, Plc. ("Magyar") jointly moved to dismiss the SEC's complaint which alleged violations of the FCPA. The complaint alleged schemes to bribe public officials in both Macedonia and Montenegro. In 2005, the Macedonian Parliament enacted a new electronic Communications law which would have been unfavorable to Magyar. To mitigate the impact of the law, the defendants began to bribe officials in both political parties, memorializing the scheme in a "secret document" kept on Magyar's computers. A Protocol of Cooperation was entered into between Magyar and the officials which mitigated the effect of the new Law. In exchange, the Macedonian government received €95 million from a former telecom provider, MakTel, jointly owned by Magyar and the Macedonian government. The officials themselves fed at Magyar's own bribe trough.

Magyar's securities were traded through American Depository Receipts ("ADRs") listed on the New York Stock Exchange ("NYSE") and were registered with the SEC. Magyar's executives made certifications to its auditors which were alleged to be false and designed to cover up the bribery scheme. Magyar filed seven quarterly reports on Form 6-K with the SEC which Straub signed.

During the period of the violations, Straub signed false management representation letters to the auditors. Other defendant executives allegedly signed false management sub-representation letters. Judge Sullivan held that it was:

> . . . not only that Magyar traded securities . . . on the NYSE that satisfies the minimum contacts standard but also that Defendants allegedly engaged in a cover-up through their statements to Magyar's auditors knowing that the company traded ADRs on an American exchange and that prospective purchasers would likely be influenced by any false financial statements and filings...The Court thus has little trouble inferring from the SEC's detailed allegations that, even if Defendants' alleged primary intent was not to cause a tangible injury in the United States, it was nonetheless their intent, which is sufficient to confer jurisdiction.[18]

The court went on to note that in *In re CINAR Corporate Securities. Litigation,*

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[16] *Sharef*, at *4-5 (first emphasis added) (citations omitted).

[17] *Id.*, at *1.

[18] *Straub*, at *7.

> the court upheld jurisdiction over a Canadian general counsel defendant who signed an allegedly fraudulent registration statement because she "must have known that the [s]tatement was made to comply with the laws governing securities offerings in American markets and, as such, it would be used and relied upon by American investors".... In other words, '[s]he could have reasonably foreseen that, were there to be litigation concerning the [s]tatement, she would be haled into court in the United States.[19]

On the motion to dismiss, the Court held that the SEC had made out its prima facie case of jurisdiction noting, *inter alia*, that the individual defendants 1) engaged in conduct designed to violate U.S. securities regulations and that this conduct was directed at the United States; 2) the wrongdoing corporations were publicly traded in the US and registered with the SEC; 3) because the companies made regular filings, the defendants knew . . . that any false or misleading financial reports would be given to prospective US investors.

CONCLUSION

The SEC complaint set forth that Steffen: was aware of the reason for the bribing of the Argentine officials; encouraged SBS's CFO, Regendantz, to authorize the bribes; was brought into the scheme precisely because he knew who to bribe; and "urged" and "pressured" Regendantz to actually make the bribes. Steffen certainly signed nothing and Regendantz did seek management-wide authority to make the illegal payments. If management had stopped the scheme, Steffen would have been spared because no act would have been committed. But, to suggest that because he was not the ultimate decision maker or signer and merely the *eminence grise* -- an accessory to the actions, a facilitator or co-conspirator -- seems a thin basis upon which to allow Steffen to escape the reach of personal jurisdiction.

Steffen knowingly participated in the orchestration of a bribery scheme using his contacts with Argentine officials to identify the most vulnerable and susceptible targets to maximize the effect of the scheme. He was sophisticated enough to have been CEO of the Argentine company which later engaged in the scheme. He was the group president of another Siemens company during the time the scheme was implemented. As Judge Sheindlin herself stated in *Sharef*, a "defendant must know, or have good reason to know, that his conduct will have effects in the [forum] seeking to assert jurisdiction over him."[20] Scheindlin continued, "[n]or is it alleged that his position as group President . . . would have made him aware of, let alone involved in falsification of these filings."[21] It is difficult to explain this statement except to the extent that it is based on a pleading defect. It is not his position as group President that would have made him aware; it is his sophistication and active participation in the scheme. The scheme was perpetrated by and on behalf of a company registered with the SEC. In 2003, he urged Sharef to meet the demands of the Argentine officials to make the additional bribes, apparently the ones needed to silence the officials from disclosing the first round of bribes. In April of 2002, while he was still group President, he told the CFO that SBS (the Siemens unit making the bribes) "had

[19] *Id.*, at *8, citing *In re CINAR Corp. Sec. Litig.*, 186 F.Supp. 2d 279, 304-06 (E.D.N.Y. 2002) (emphasis added).
[20] *Sharef*, at *4, quoting *Leasco Data Processing Equip. Corp. v. Maxwell*, 468 F2d 1326, 1341 (2d Cir. 1972).
[21] *Id.*, at *4.

a '*moral duty'* to make at least an 'advance payment' of ten million dollars to the individuals who had previously handled the bribes because he and the other individuals were being threatened as a result of the unpaid bribes."[22] The SEC complaint alleged that "In order to suppress that evidence, [of the bribery from the arbitrators] . . . Steffen . . . continuously urged Siemens management to funnel more money to Argentine officials."[23]

While it is not clear from the *Sharef* decision, it may be that Steffen escaped the clutches of the FCPA because the SEC failed to plead that Steffen knew or should have known that his conduct would have effects in the United States. It is clear that "[t]he Securities Exchange Act permits the exercise of personal jurisdiction to the limit of the Due Process Clause of the Fifth Amendment. . . . To support specific jurisdiction over a defendant based on his or her conduct outside of the United States, minimum contacts analysis will be satisfied . . . if the defendant knew or had good reason to know that the actions would have effects in the United States." [24] Significantly, the court rejected the individual defendant's arguments that various factors should lead the court to conclude that his conduct could not reasonably have been anticipated to have had effects in the United States.

In *Dunn*, a defendant urged that various factors should lead to a finding that he could not reasonably have expected the U.S. consequences, but Judge Preska stated, "[t]hose factors, however, cannot overcome the common-sense conclusion that an accounting fraud by a high ranking Canadian officer of a large Canadian public company traded in the United States would directly and foreseeably have effects in the United States . . . protestations of ignorance notwithstanding, someone in his position should have known as much . . . ."[25]

Nothing suggests that the FCPA would treat this issue differently.

Steffen was spared here because he did not sign any financial statement. But if the SEC had pled that he knew or should have known the consequences of his conduct, the mere failure to sign should not have sufficed to insulate him and his conduct might have led to the common-sense conclusion that he should have known the consequences of his acts. It is inconceivable that the man who had been the CEO of Siemens Argentina, later group president of another Siemens entity did not know or have reason to know that financial documents would be filed which would certainly not disclose the bribes. After all, he was part of the effort to bribe officials to prevent them from disclosing the bribes which, had they been disclosed, would have defeated Siemens arbitration claim for lost profits.

If the logic of *Straub* prevails, and if the SEC pleads that the offending party knew or should have known the consequences of his acts, it is difficult to say that the next Steffen will not be caught up in the same jurisdictional web—with or without his handwriting on a financial document.

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[22] *Id.*, at *2; SEC compl. ¶ 40 (emphasis added).
[23] SEC compl. ¶ 37.
[24] *SEC v. Dunn*, 587 F. Supp. 2d 486, 509 (S.D.N.Y. 2008).
[25] *Id.*. at 509-10.