

**No.: 10-02**

**Date: July 16, 2010**

## **Foreign Corrupt Practices Act Review**

### **Opinion Procedure Release**

The Department has reviewed the Foreign Corrupt Practices Act (“FCPA”) Opinion request of a U.S. nongovernmental organization (the “Requestor”) that was submitted on May 17, 2010, as well as supplemental information received on June 16, 2010. The Requester is a “domestic concern” within the meaning of the FCPA and thus eligible to request an Opinion of the U.S. Attorney General, pursuant to 28 C.F.R. Section 80.4, regarding whether certain specified, prospective – not hypothetical – conduct conforms with the Department’s present enforcement policy regarding the antibribery provisions of the FCPA. The Requestor represents that the facts and circumstances are as follows.

#### Relevant Facts and Circumstances

The Requestor is a non-profit, U.S.-based microfinance institution (“MFI”) whose mission is to provide loans and other basic financial services to the world’s lowest-income entrepreneurs. It operates in many countries around the world. It receives grants and investments to support its mission from a broad range of donors, including the United States government, other governmental and quasi-governmental aid agencies and development banks, nongovernmental organizations (“NGOs”) and private investors. Its Code of Conduct, which is applicable to all of its employees worldwide, requires full compliance with laws, including the FCPA.

The Requestor is in the process of converting all of its local operations to commercial entities that are licensed as financial institutions, in order to permit them to attract capital and expand their services to include offerings such as savings accounts, microinsurance and remittances. One of these operations is a wholly owned subsidiary in a country in Eurasia (the “Eurasian Subsidiary”) that was founded with startup capital from a foreign aid source. The Eurasian Subsidiary became a self-sustaining institution several years ago and no longer receives grant support for its work in the Eurasian country. The Eurasian Subsidiary is currently organized as a limited liability company under the laws of the Eurasian country and operates under a special non-banking financial institution license from the Central Bank of that country. The activities of the Eurasian Subsidiary are currently overseen by an agency of the Eurasian country (the “Regulating Agency”).

For some time now, the Eurasian Subsidiary has been seeking to transform itself from its current status as an institution regulated by the Regulating Agency into an entity that would permit it to apply for regulation by the Central Bank of the Eurasian country, with the ultimate goal of acquiring a license as a bank. Transformation to bank status would allow the Eurasian Subsidiary to offer additional services that can assist its borrowers, such as savings accounts, and would facilitate its ability to attract capital that could support increased growth in the loan

portfolio. This process would also allow the Eurasian Subsidiary to avail itself of a predictable and detailed regulatory regime that is designed specifically for financial institutions.

The Regulating Agency has taken a skeptical view of such transitions, expressing concern that allowing MFIs to transition from “humanitarian” status (under which MFIs cannot distribute dividends to shareholders) to commercial status could result in grant funds and their proceeds that originally were intended for humanitarian assistance in the Eurasian country either being withdrawn from the country or being used to benefit private investors.

As part of its oversight of the Eurasian Subsidiary and the Eurasian Subsidiary’s proposed transition to commercial status, the Regulating Agency has pressed the Eurasian Subsidiary to take steps to “localize” its grant capital to ensure that it remains in the Eurasian country. Among other things, the Regulating Agency has insisted that the Eurasian Subsidiary make a grant to a local MFI in an amount equal to approximately 33 percent of the Eurasian Subsidiary’s original grant capital. The Regulating Agency has provided a list of local MFIs in the Eurasian country and has stated that the Eurasian Subsidiary could not fulfill its localization obligation unless it provided grant funding to one or more of them. Like the Eurasian Subsidiary, all of those organizations are members of the Eurasian country’s association of MFIs (the “MFI Association”).

The Requestor is concerned that compelled grants to an institution on a short list of institutions – without appropriate safeguards – raise red flags under the FCPA. The Requestor has resisted the Regulating Agency’s efforts to compel it to make such grants, offering alternative proposals to ensure that its original grant capital remains in the Eurasian country. The Regulating Agency rejected those proposals as inconsistent with its policy. The Regulating Agency stated, however, that the Eurasian Subsidiary could engage in due diligence of the local MFIs and could establish and impose controls on the use of grant funds.

To meet the Regulating Agency’s requirements, the Eurasian Subsidiary proposes to contribute a total of \$1.42 million to expand the loan and technical capacity of a local MFI (the “Local MFI”), which previously has received grant funding from the foreign aid community. Of the \$1.42 million, \$1.07 million would be used to increase the Local MFI’s loan capital – to more than triple its current loan capital. The remaining \$350,000 would be used in support of the grant: (a) \$50,000 to pay for loan tracking and reporting management system software; (b) \$120,000 for capacity-building services and support, including hiring six additional staff members and retaining vendors to provide training and other technical assistance; and (c) \$180,000 for the engagement of two independent organizations to monitor and audit the use of the proposed grant (the “Proposed Grant”), as discussed in detail below.

The Eurasian Subsidiary undertook a three-stage due diligence process to vet the potential grant recipients and select the proposed grantee. First, it conducted an initial screening of six potential grant recipients by obtaining publicly available information and information from third-party sources. Based on this review, it ruled out three of the six MFI candidates as generally unqualified to receive the grant funds and put them to effective use. Second, the Eurasian

Subsidiary undertook further due diligence on the remaining three potential grant recipients. This due diligence was designed to learn about each organization's ownership, management structure and operations; it involved requesting and reviewing key operating and assessment documents for each organization, as well as conducting interviews with representatives of each MFI to ask questions about each organization's relationships with the government and to elicit information about potential corruption risk. Based on the information obtained during this second-stage review, the Eurasian Subsidiary ruled out two of the three remaining potential grant recipients: one for conflict of interest concerns, the other after the discovery of a previously undisclosed ownership change in the entity.

As a third round of due diligence, the Eurasian Subsidiary undertook targeted due diligence on the remaining potential grant recipient, the Local MFI. This diligence was designed to identify any ties to specific government officials, determine whether the organization had faced any criminal prosecutions or investigations, and assess the organization's reputation for integrity. Specifically, the Eurasian Subsidiary took the following steps: requested and reviewed more detailed information concerning funding, ownership and control of the Local MFI's 100 percent shareholder (the "Local MFI's Parent Organization"), which is an NGO; requested and reviewed more detailed information concerning the officers, directors and owners of the Local MFI and the Local MFI's Parent Organization and their ties to government officials; requested and reviewed information about whether any family members of officers, directors or employees of the Local MFI are government officials; performed internet searches, including searches of news sources, on the Local MFI and its principals, as well as on the Local MFI's Parent Organization, to look for news stories or other reports suggesting that either entity or persons affiliated with either entity may have engaged in illegal or unethical conduct; met in person with representatives of the Local MFI and the Local MFI's Parent Organization to learn about each organization's ownership and control; interviewed references provided by the Local MFI; and confirmed that the Local MFI was willing to comply with anti-corruption provisions and controls.

According to the Requestor, this final round of due diligence did not identify information of potential corruption in connection with the Proposed Grant. The last round of due diligence, though, did uncover that one of the board members of both the Local MFI and the Local MFI's Parent Organization is a sitting government official in the Eurasian country and that other board members are former government officials. The sitting government official, however, serves in a capacity that is completely unrelated to the microfinancing industry. In addition, under the law of the Eurasian country, sitting government officials may not be compensated for this type of board service, and the Local MFI confirmed that neither its own board members nor the board members of the Local MFI's Parent Organization receive compensation for their board service. The proposed grant agreement would expressly prohibit the Local MFI from transferring any of the grant funds to the Local MFI's Parent Organization or otherwise using the grant funds to compensate board members of either the Local MFI or the Local MFI's Parent Organization.

The Proposed Grant is subject to significant controls proposed by the Requestor. It would, if made, be governed by a written grant agreement with the recipient (attached in draft form to the present Request). The grant would be subject to the following controls, among others:

- Staggered Payment of Grant Funds. Rather than paying the Proposed Grant as a lump sum, the Eurasian Subsidiary would pay the grant funds in eight quarterly installments, in order to allow interim monitoring and to assist the Local MFI in effectively managing the inflow of capital. Each successive installment would be retained by the Eurasian Subsidiary until the satisfactory completion of a quarterly monitoring review and/or semi-annual audit, as discussed below.
- Ongoing Monitoring and Auditing. Each quarter, the Local MFI's use of grant funds would be reviewed by an independent monitor, which would share the results with the Requestor. The Requestor has proposed to engage the MFI Association to perform this monitoring function because its personnel have extensive knowledge of the microfinance sector in the Eurasian country. In addition, every six months, the Local MFI's use of the donated funds would be audited by an accounting firm selected by the Eurasian Subsidiary. The Eurasian Subsidiary would use an earmarked part of the grant funds to pay the third party monitor and auditor directly, rather than paying the Local MFI to engage these vendors. The monitoring and audits would continue for a period of five years, i.e., three years beyond the disbursement of the final installment of loan capital. Results of the monitoring reviews and audits would be shared with the Eurasian Subsidiary.
- Earmarked Funds for Capacity-Building. As noted above, a portion of the grant funds would be dedicated to capacity-building to help the Local MFI develop the organizational infrastructure to make effective use of the new loan capital it would receive. First, funds would be earmarked to engage qualified third-party service providers to provide training and other technical assistance in several areas, including the development of microlending procedures and processes, portfolio and risk management, and planning and financial management. The service providers would be selected by the Eurasian Subsidiary. Payments would be made directly to the vendors. Second, funds would be dedicated to funding six new staff positions at the Local MFI to help manage the anticipated increase in loan volumes made possible by the additional loan capital.
- Prohibition on Compensating Board Members. As already noted, the grant agreement would expressly prohibit the Local MFI from transferring any of the grant funds to the Local MFI's Parent Organization or otherwise using the grant funds to compensate board members of either the Local MFI or the Local MFI's Parent Organization.

- Anti-Corruption Compliance Provisions. The proposed grant agreement would include a series of other compliance provisions: (a) prohibiting the Local MFI from paying bribes or giving anything else of value to benefit government officials personally; (b) requiring the Local MFI to keep and maintain accurate records concerning the use of the donated funds and to provide the Eurasian Subsidiary’s representatives access to the organization’s books, records and accounts; (c) requiring the Local MFI to adopt a written anti-corruption compliance policy; (d) requiring the Local MFI to certify its compliance with these obligations upon request by the Eurasian Subsidiary; (e) prohibiting the Local MFI from undergoing a change in ownership or control, upon penalty of forfeiting the grant; and (f) permitting the Eurasian Subsidiary to terminate the agreement and recall the grant funds if the Eurasian Subsidiary received evidence that reasonably suggests a breach of these compliance provisions.

### Analysis

In accordance with the facts and circumstances recited in the request, the Department does not intend to take any enforcement action with regard to the proposed transaction, for the reasons that follow.

The FCPA prohibits any domestic concern from corruptly giving or offering anything of value to any “foreign official” in order to assist “in obtaining or retaining business for or with, or directing any business to, any person . . . .” 15 U.S.C. § 78dd-2(a)(1). As an organization that is organized under the laws of a U.S. State and that has its principal place of business in the United States, the Requestor is a “domestic concern” within the definition of 15 U.S.C. § 78dd-2(h)(1)(B), and is, therefore, subject to the anti-bribery provisions of the FCPA.

The Eurasian Subsidiary’s Proposed Grant to the Local MFI is for the purpose of obtaining or retaining business (nonprofit business, to be followed by for-profit business) in the Eurasian country; that is, the Proposed Grant would be made as a condition precedent to obtaining a license to operate as a financial institution. The issue presented is whether the Proposed Grant would amount to the corrupt giving of anything of value to any officials of that country in return for obtaining or retaining business. Based on the due diligence that has been done and with the benefit of the controls that will be put into place, it appears unlikely that the payment will result in the corrupt giving of anything of value to such officials.

As an initial matter, it is important to note that the expressed motivation of the Regulating Agency here is to ensure that grant money given to the Eurasian Subsidiary for humanitarian purposes in the Eurasian country continues to be used for humanitarian purposes in that country. The Requestor was concerned, nevertheless, that without due diligence and appropriate controls, such a grant could carry a significant risk that the result might be the transfer of things of value to officials of the Eurasian country.

The Department is satisfied, however, that the Requestor has done appropriate due diligence and that the controls that it plans to institute are sufficient to prevent FCPA violations. As noted above, the Requestor conducted three rounds of due diligence. The controls that the Requestor proposes would ensure with reasonable certainty that the grant money from the Eurasian Subsidiary would not be transferred to officials of the Eurasian country. As noted, these controls include the following: the staggered payment of grant funds; ongoing monitoring and auditing; the earmarking of funds for capacity-building; a prohibition on the compensation of board members; and the institution of an anti-corruption compliance program.

Three prior opinion releases have dealt with charitable-type grants or donations:

- In FCPA Opinion Release 95-01 (Jan. 11, 1995), the Department approved a \$10 million donation to support the construction of a medical facility near a plant that the requester was building in a foreign country. The donation was to be made through a charitable organization incorporated in the United States and through a public limited liability company located in the foreign country.
- In FCPA Opinion Release 97-02 (Nov. 5, 1997), the Department approved a \$100,000 donation to support the construction of a school. The donation was to be made directly to the government entity responsible for the school.
- In FCPA Opinion Release 06-01 (Oct. 16, 2006), the Department approved a \$25,000 grant to be used to fund incentive payments for customs officials in order to promote the enforcement of anti-counterfeit laws and rules. That grant was also made directly to the government agency that ran the program.

Each of these opinion releases included a discussion of the due diligence and/or controls that had been built into the transaction. Those controls included the following:

- FCPA certifications by the recipient (95-01);
- due diligence to confirm that none of the recipient's officers were affiliated with the foreign government at issue (95-01);
- a requirement that the recipient provide audited financial statements (95-01);
- a written agreement with the recipient restricting the use of funds (97-02, 06-01);
- steps to ensure that the funds were transferred to a valid bank account (06-01);
- confirmation that contemplated activities had occurred before funds were disbursed (06-01); and
- ongoing monitoring of the efficacy of the program (06-01).

The Requestor has undertaken each of the above due diligence steps and controls, and has gone further – adding additional controls to minimize the likelihood that anything of value will be given to any officials of the Eurasian country. The Proposed Grant thus is consistent with the Department’s past approach to grant-related requests.

Based on the representations made by the Requestor in its request and attachments, the Department does not presently intend to take any enforcement action with respect to the proposal described in this request.

This FCPA Opinion Release has no binding application to any party that did not join in the request and can be relied upon by the requestor only to the extent that the disclosure of facts and circumstances in its request is accurate and complete and continues to accurately and completely reflect such facts and circumstances.