All Facially Good Deeds May Not Go Unpunished

Hyperdynamics Corporation Investigated For Charitable Contributions

On March 13, 2014, Tullow Oil ("Tullow") announced that it was suspending further funding and activities related to a drilling concession in Guinea until the resolution of an investigation into potentially corrupt activities by its partner – Hyperdynamics Corporation ("Hyperdynamics"). Tullow's actions follow a September 30, 2013 announcement by Hyperdynamics that the United States Department of Justice ("DOJ") is investigating whether the company illegally obtained and retained certain drilling concession rights in Guinea, with particular focus on charitable contributions made by the company, in potential violation of the U.S. Foreign Corrupt Practices Act ("FCPA") or U.S. anti-money laundering statutes. The company has publicly disclosed that the U.S. Securities and Exchange Commission ("SEC") has also issued a subpoena in connection with the investigation. While not the first case in which the DOJ or SEC have questioned charitable contributions, it serves as a useful notice and warning of the significant commercial and legal hazards that exist in connection with charitable contributions.

In general terms, the FCPA, as is typically the case around the world, prohibits not only monetary contributions to a government official but also the giving of anything of value (directly or indirectly) to an official to influence their official behavior or to use their influence to affect the behavior of another government official.[1] Similarly, the determination to characterize a payment as a charitable contribution when it should have been properly considered something else (especially in the face of insufficient due diligence) can be considered a books and records and/or internal control failure subject to sanction, including by the SEC (in the case of issuers).[2] In the normal course of business, companies routinely engage in charitable undertakings or community development in the jurisdictions in which they operate. Such undertakings are often considered appropriate (and sometimes necessary) activities to assist the local population in the jurisdiction where the company is engaging in business activities. Notwithstanding the public good served by such contributions, companies are well advised to proceed with great caution when agreeing to or making these commitments.

Charitable contributions can be challenged as running afoul of the FCPA where, for example, (1) the charity is not *bona fide* but is a disguised economic vehicle for the government official (or a friend or family member of the government official); or (2) the charity is considered to have particular significance to the government official (such as might be the case if development of a local school would have an impact on the government official's election).

For example, in its December 2012 settlement with the SEC, the SEC found that Eli Lilly and Company ("Eli Lilly") had failed to implement sufficient internal controls and had improperly recorded charitable contributions made to the Chudow Castle Foundation (the same organization implicated in Schering-Plough's 2004 settlement with the SEC).[3] The SEC variously claimed that in connection with certain of the contributions, Eli Lilly had: (1) failed to conduct appropriate due diligence on the charitable entity to assess (a) the identity of the founder of the charity and his role as a government official; and (b) the legitimacy of the charitable organization's services; (2) failed to understand the timing of requests made by the government official for the contributions; and (3) failed to articulate a coherent basis for why it chose the particular charity. In commenting on Eli Lilly's internal control environment, the SEC stated that "Lilly and its subsidiaries primarily relied on assurances and information provided in the paperwork by . . . intermediaries or by Lilly personnel rather than engaging in adequate verification and analyzing the surrounding circumstances of the transaction." In a similar vein, in October 2013, the SEC instituted an administrative proceeding against Stryker Corporation ("Stryker") for books and records and internal control violations relating to improper payments made in Mexico, Poland, Romania, Argentina and Greece. In describing a "sizable and atypical" donation that Stryker made to fund a university laboratory in Greece, the SEC noted that it was a "pet project" of a government official who was believed to have the ability to influence future sales by Stryker Greece to public hospitals affiliated with the government official.[4]

Taken together, companies should be mindful of a few key practice points when considering or making charitable contributions or donations:

- **Subject Contributions Suggested by a Government Official to Enhanced Scrutiny:** Any charitable contribution specifically requested or suggested by a government official raises a red flag that must be carefully evaluated. Although not *per se* improper, such contributions should be made only after a thorough analysis has concluded that the individual who has requested the contribution is not in a position to influence the award or retention of business.

- **Conduct Sufficient Due Diligence:** Careful due diligence of proposed charitable contributions must be undertaken, particularly regarding the ownership and beneficiaries of the charity, use of proceeds by the charity, and the relationship (if any) of the charity to relevant government officials. As noted by the Eli Lilly resolution above, simply relying on paperwork completed by a charity or local personnel without additional research may not on its own be sufficient depending on the circumstances.

- **Document the Basis for Gift:** Although charitable contributions and donations can serve as the hallmark of responsible behavior, companies must nevertheless be careful to understand and document their basis for making the particular charitable contribution. In circumstances where a contribution or donation is not made for *bona fide* purposes, companies may be subject to books and records and/or internal control violations for failing to properly record such payments or failing to have in place a system that ensures they are made appropriately.

[1] *See* 15 U.S.C. § 78dd-1(a); 15 U.S.C. § 78dd-2(a); 15 U.S.C. § 78dd-3(a).
[2] *See* 15 U.S.C. § 78m(b)(2)(A) and 15 U.S.C. § 78m(b)(2)(B).
[3] U.S. Securities and Exchange Commission v. Eli Lilly Corporation, Case No. 1:12-cv-02045 (Dec. 20, 2012).
[4] In the Matter of Stryker Corporation, Administrative Proceeding File No. 3-15587 (Oct. 24, 2013).

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