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UNITED STATES

Companies May Face SEC Sanctions for Their Distributors' Actions

Companies must be aware that they may now face sanctions in the United States if their distributors pay bribes. A December 22, 2008 Securities and Exchange Commission (SEC) release notes the penalties imposed on Fiat S.p.A. and its subsidiaries for bribes paid in connection with the United Nations' Oil for Food program. We believe this may be only the second instance of a company being sanctioned for working with a distributor who was paying bribes (the *InVision* case seems to be the first). Based on general agency principles, some have thought a principal could clearly be Foreign Corrupt Practices Act (FCPA) liable for bribes paid by its sales agent. However, if foreign transactions were with a distributor, absent direct wrongdoing by the manufacturer/seller, a question remained as to whether a covered seller was insulated from bribery in the distributor's contracts.

The SEC claimed Fiat's subsidiary, IVECO S.p.A., used its office in Egypt to enter into four contracts with various Iraqi government ministries during the Oil for Food program for the sale of commercial vehicles and parts. IVECO's Egypt-based agent submitted invoices with inflated commissions, and despite the unusually large commissions, IVECO paid the invoices. IVECO paid about US$1.8 million in kickbacks or after-sales services fees (ASSFs).

In 2000 IVECO changed its method for doing business, and the Egypt-based agent became its distributor in Iraq. The distributor in turn purchased equipment from IVECO and sold it to the UN, again using inflated contracts. With this approach IVECO hoped to distance itself from any involvement with possible kickbacks.

According to the SEC, Fiat did not maintain a system to detect and prevent ASSFs and, from its direct sales to Iraq, IVECO knew or should have known that the agent's sales included ASSFs. Without admitting or denying the SEC's allegations, Fiat disgorged US$5.3 million in profits, almost US$1.9 million in prejudgment interest and a civil penalty of US$3.6 million. In addition, Fiat will pay a US$7 million penalty pursuant to a deferred prosecution agreement with the US Department of Justice's Fraud Section.

The FCPA applies to all US individuals and corporations, non-US corporations with securities registered on US stock exchanges and any person or corporation acting in the United States. While the FCPA does not directly apply to non-US subsidiaries of US legal persons, a US entity can be liable for the acts of its foreign subsidiary, such as when it approves or authorizes those acts, and US and other firms with securities registered with US exchanges are required to exert adequate financial controls over their more than 50-percent controlled foreign subsidiaries and to ensure their books and records accurately report expenditures including any improper foreign payments. As

companies expand or operate in parts of the world where bribery and corruption are common, the *Fiat* decision highlights the need to develop strong compliance programs to avoid sanctions similar to those described above.

Corporate Officer Duties: Officers Held to Have Same Fiduciary Duties as Directors, but Are More Exposed to Personal Liability for Lack of Due Care

Summary

The Delaware Supreme Court recently expressly held that officers and directors of Delaware corporations owe essentially the same fiduciary duties of care and loyalty to corporations and their stockholders. However, while Delaware statutes permit corporations to eliminate directors' personal liability for most breaches of the duty of care through so-called "exculpatory" charter provisions, Delaware law does not extend similar protection to officers from such liability.

Except in cases of specific acts of malfeasance or defalcation, claims against officers for breach of fiduciary duty have not been the subject of extensive litigation. However, in light of this recent Delaware Supreme Court ruling, it is possible that claims against officers challenging business decisions could now become more common.

Officers of Delaware corporations should be aware that the statute permitting corporations to provide exculpation to their directors for breaches of the fiduciary duty of care does not extend to them. Accordingly, as discussed below, we recommend that concerned officers seek indemnification agreements and appropriate insurance arrangements to provide protection in the event that such a claim is brought against them.

The Ruling

In *Gantler v. Stephens,* stockholders of a Delaware corporation sued certain officers and directors of the corporation, alleging that they violated their fiduciary duties by rejecting an opportunity to sell the corporation. The stockholders claimed that the officers and directors instead decided to reclassify the corporation's shares to benefit themselves and disseminated a materially misleading proxy statement to gain shareholder approval for the reclassification.

The Delaware Chancery Court dismissed the complaint, holding that the stockholders ratified the reclassification following full disclosure, which was sufficient to protect the decision to reclassify the benefit under the business judgment rule. However, on appeal, the Delaware Supreme Court reversed the lower court's ruling, holding that the complaint pled facts sufficient to overcome the business judgment presumption and to state fiduciary duty claims.

In reaching that decision, the Delaware Supreme Court expressly held that "officers of Delaware corporations, like directors, owe fiduciary duties of care and loyalty, and the fiduciary duties of

officers are the same [as those of] directors." Although this proposition has been implied in the past, the Delaware Supreme Court for the first time expressly held so in this case.

The Court also made clear that the consequences of a fiduciary breach by directors or officers would not necessarily be the same. Specifically, Section 102(b)(7) of Delaware corporation law provides that corporations may include provisions in their certificates of incorporation that would avert personal liability for a director's breach of his or her duty of care. Currently, there is no similar provision that would so limit an officer's liability, and viability of legislation extending that protection to officers in the current political environment is uncertain.

Critical Role of Indemnification Agreements and Officer Insurance

The *Gantler* ruling clearly establishes that officers of Delaware corporations owe the same fiduciary duties as their directors, but that they cannot rely on Delaware's exculpation statute to allow the corporation to limit their liability through charter provisions.

As a result, at least until any new legislation amends the current Delaware statute, concerned officers should consider insisting that indemnification agreements and officer insurance are in place to offer them protection against liability should they face a claim that they breached their fiduciary duties.

Contribution provisions in such an agreement could also provide additional protection if indemnification is unavailable for public policy or other reasons. Such a provision would provide for contribution based on the relative economic benefit of the challenged transaction to the corporation and the officers. In a case where the officer derived little or no economic benefit, a contribution provision could dramatically reduce an officer's exposure to liability.

Further, officers may wish to consider requesting that these agreements contain covenants not to sue for personal liability for breaches of duty of care (subject to the same exceptions contained in director exculpatory provisions), where governing state law would permit such an advance covenant to be enforced.

New Trade Enforcement Legislation Introduced at Start of New Congress

On January 14, 2009 House Committee on Ways & Means Chairman Charles Rangel (D-N.Y.) and Trade Subcommittee Chairman Sander Levin (D-Mich.) introduced a bill to reform US international trade policy. The Trade Enforcement Act of 2009 (the Act), HR 496, has four main objectives: (1) strengthening trade remedy laws; (2) opening markets to US exports by eliminating foreign trade barriers; (3) protecting US borders from imports violating US health and safety laws and regulations; and (4) enforcing intellectual property rights at US borders.

Nearly identical bills were introduced in both the Senate and House in the 110th Congress. Squire Sanders of counsel David M. Spooner (at the time, Assistant Secretary for Import Administration at the US Department of Commerce) testified in hearings before the House Subcommittee on Trade on matters related to these bills. Although previous versions failed to reach the floor of the House or Senate, the prospects for the Trade Enforcement Act may be more promising under the Obama administration and 111th Congress.

Reforms to Trade Remedy Laws

The Act amends US antidumping and countervailing duty law to:

- Codify the application of countervailing duties (CVD) to nonmarket economy (NME) countries, such as China;
- Permit the Department of Commerce to use alternative methods of identifying and calculating countervailable subsidies in CVD proceedings against China;
- Provide Congress with a role in determining when a country's NME status should be revoked;
- Request that Commerce reverse its decision to implement the World Trade Organization (WTO) Appellate Body decision mandating that the United States abandon "zeroing" in investigations; and
- Permit the International Trade Commission (ITC) to evaluate material injury from dumped imports without regard to whether they will be replaced by imports from other countries or whether any benefit to domestic industry will occur (overturning *Bratsk Aluminum Smelter v. United States*).

The Act also limits the discretion of the president in denying relief under the China Safeguard Provision, which permits temporary relief when products imported from China cause or threaten market disruption to US-based producers.

Reduction of Foreign Barriers to US Exports

The Act strengthens the United States Trade Representative's (USTR) annual obligation under current law to identify "priority foreign country practices" – those practices that if eliminated would have the most potential to increase US exports. If consultations prove unsuccessful, the USTR must initiate an investigation to determine whether the practice is actionable under Section 301. Section 301 actions permit the imposition of retaliatory measures, subject to exceptions, for foreign country practices that violate US rights under a trade agreement.

The legislation specifically implements an annual obligation for the USTR to identify countries that impose unfair technical barriers to trade and unfair sanitary and phytosanitary measures on US agricultural exports. The consultation and investigation provisions also apply subsequent to the USTR's reviews of such barriers.

The Act creates the Office of the Congressional Trade Enforcer, which is authorized to investigate violations of foreign country obligations under the Uruguay Round Agreements or any bilateral or

regional free trade agreement to which that country is a party with the United States. The Congressional Trade Enforcer will also possess the power to recommend that the USTR initiate dispute resolution proceedings against countries for such violations.

Ensuring Imports Comply With US Health and Safety Laws

The Trade Enforcement Act establishes a governmentwide, uniform data system to uniquely identify all goods imported into the United States in order to ensure that cargo imported into the United States complies with US health and safety laws and regulations. It also creates a voluntary import safety program that will qualify eligible entities for expedited movement through the border inspection process.

Moreover, the Act provides sanctions for those entities in repeated noncompliance with US health and safety laws.

Enforcement of Intellectual Property Rights at US Borders

The proposed legislation creates the position of Director of Intellectual Property Rights (IPR) Enforcement within the Department of Treasury as well as an advisory committee to advise on IPR enforcement issues. Moreover, the bill enlists Customs and Border Protection (CBP) with the responsibility of preparing a plan for a "Watch List" database for parties posing a risk of importing or exporting pirated or counterfeit goods and to provide for additional scrutiny at the border for such parties. The Act also limits CBP's ability to mitigate fines and expands the prohibitions on exportation or importation of pirated or counterfeit goods including trebling the fines when these goods are intended for sale or public distribution.

The bill has been referred to the House Committees on Ways and Means, Rules and Homeland Security.

DHS Announces Final Rule Expanding US-VISIT Program to Lawful Permanent Residents and Other Categories of Non-US Citizens

DHS announced a final rule on December 18, 2008 that expands the categories of non-US citizens required to provide finger scans, photographs or other biometric data upon entry to the United States through the US-VISIT program. Our May 2008 *Immigration Alert* discussed the US-VISIT program in detail. The final rule took effect on January 18, 2009.

Under the final rule, the following classes of individuals have been added to the categories of non-US citizens that must provide biometric data upon entry to the United States:

- Lawful permanent residents (LPRs);
- Persons seeking admission on immigrant visas;
- Refugees and asylees;
- Certain Canadian citizens who receive a Form I-94 at inspection or who require a waiver of inadmissibility;
- Persons paroled into the United States; and

- Persons applying for admission under the Guam Visa Waiver Program.

Exceptions to the final rule include Canadian citizens seeking short-term admission for business or pleasure under B visas and individuals traveling on A and G visas.

Recently, Paul Morris, executive director for admissibility and passenger control for Customs and Border Protection, stated that LPRs entering through land ports of entry are required to provide fingerprints only if they are referred to secondary inspection. As of January 2009, not all land ports had 10-print finger scan capability, but installation at all ports was expected to be completed soon.

The final rule has been the subject of much criticism, especially concerning the collection of biometric data from LPRs, who, in some cases, have been living in the United States for many years. Litigation challenging the implementation of this rule may be on the horizon.

EUROPEAN UNION

Record Fines Totaling Nearly €1.4 Billion Against Car Glass Cartel

On November 12, 2008 the European Commission (EC) imposed the largest cartel fines in its history against four automobile glass producers for illegal market sharing and exchanging commercially sensitive information in the European Economic Area for an approximately five-year period (early 1998 to early 2003). The cartel participants, Asahi Glass Co., Ltd. (Japan), Pilkington Group Limited (United Kingdom), Saint-Gobain (France) and Soliver (Belgium), controlled roughly 90 percent of the €2 billion market for glass used in new cars and for original branded replacement glass.

According to the EC, the four car glass manufacturers engaged in discussions regarding target prices, production levels, market sharing, customer allocation and renegotiations of ongoing contracts. The companies intended to allocate their products in a manner so that they could each maintain the stability of their market shares in Europe. The EC initiated this investigation upon receiving “reliable information provided by an anonymous informant.” After a series of unannounced inspections, Asahi filed a leniency application.

Due to its full cooperation with the investigation, the EC reduced Asahi’s fine by 50 percent, resulting in a €113.5 million fine. Pilkington and Soliver were fined €370 million and €4.3 million, respectively, while Saint-Gobain received the largest fine ever imposed by the Commission – €896 million. This record-setting fine was the result of a 60-percent penalty increase imposed on Saint-Gobain for previous cartel offenses in Flat Glass Italy (1984) and Flat Glass Benelux (1988).

The New German Limited Liability Company Act

The new "Act aimed at modernizing the Limited Liability Company Act (GmbHG) and combating abuses" came into force on November 1, 2008 and modernizes the old GmbH law in the following key areas:

- The GmbH establishment procedure has been modified to (a) simplify the processes of share division, merging and transfer and (b) facilitate the easy provision of share capital. Furthermore, modernization of the registration system will accelerate the registration process at the commercial register (*Handelsregister*).
- In stark contrast to the old law, the new law permits a GmbH to locate its headquarters outside Germany. It assists the acquisition process by requiring greater transparency in relation to share ownership and codifies rules relating to group financing. This new legal footing will enable the GmbH to wholly participate in cash pooling systems that are common in other countries.
- The new law tackles the issue of deceptive and fraudulent business practices in a number of ways. It simplifies the procedure for filing legal claims, removes the possibility of artificial and vexatious delays in insolvency proceedings and imposes higher standards on those able to become managing directors of companies.

The government's aim is to strengthen the GmbH as a corporate form in Europe through the simplification of GmbH founding and administration procedures, in the following manner.

Formation

The new law allows for a totally new type of legal GmbH to be formed, with a minimum nominal share value of only €1. This new variant of German GmbH has to be named *Unternehmergesellschaft* (*haftungsbeschränkt*), and this (or the abbreviation "UG") must form part of the company name until the general minimum nominal share capital of €25,000 is achieved. In addition, the UG must place 25 percent of its annual profit into a new capital reserve until this minimum nominal share capital is reached. This reserve can be used only for increasing nominal share capital or for balancing losses or loss-carry-forwards of the UG. Unlike the still traditional type of GmbH, a UG may not make contributions in kind during formation or as part of later capital increases.

Cash Pooling

German law relating to capital contribution and maintenance (derived mainly from case law of Germany's Federal Court of Justice (BGH)) is currently obstructive in the context of GmbH participation in internationally recognized and authorized cash pooling structures for group financing. The capital contributions made by a shareholder to the GmbH, when paid directly into a group account under a cash pooling structure, are considered invalid under principles of German

case law, which deems that these payments do not fall under the direct control of the GmbH. However, the new law codifies and modifies such BGH case law by making these payments valid upon satisfaction of the condition that an adequate repayment claim is guaranteed. Upstream loans in cash pooling structures are permitted and available under the new law, even to companies experiencing negative equity. Problems remain, however, as the burden of determining the adequacy of the repayment claim falls upon the managing director, who may be personally accountable for damages suffered by the company or its creditors. What is legally adequate in terms of a repayment claim has yet to be clearly defined.

Transfer of Shares

The new law differs from the old (in particular with respect to the transfer and acquisition of shares) in that it places greater importance on the list of existing shareholders filed with the commercial register (*Handelsregister*). The acquisition of any shares from an individual or corporate entity listed as a shareholder at the commercial register shall be judged to be effective even in circumstances for which the seller had no authority to make the disposal. Therefore, in relation to the shareholder list, the Act allows, in contrast to the old law, the acquisition *bona fide* of GmbH shares. The statutory assumption of ownership outlined above is, however, subject to a number of conditions. The assumption will not apply if (a) the share(s) do not exist, (b) the buyer was aware of any defect in title or (c) the seller has been listed on the shareholder list for less than three years. Under the new law, the need to perform due diligence investigations and verification exercises and to obtain seller's warranties as to ownership of shares will be reduced.

Authorized Share Capital

The GmbH has been afforded greater flexibility in raising capital. The new law enables the GmbH to have authorized capital, similar to that enjoyed by the German stock corporation (*Aktiengesellschaft*). The benefit is that, for a period of up to five years, the shareholders can authorize the managing directors to increase the stated share capital against contributions.

Capital Maintenance Rules

Unlike the old law, the new law relating to capital maintenance (*Eigenkapitalersatzrecht*) is comprehensive and digestible. As previously outlined, the commercial practice of cash pooling has been facilitated through the removal of the assumption that loans to shareholders are a prohibited repayment of stated share capital as long as certain conditions are met (a fully recoverable payment claim and only an accounting exchange on the asset side of the balance sheet). Furthermore, capital maintenance law now forms a part of insolvency law, and loans to shareholders are now in all circumstances subordinate to the claims of other creditors.

Extended Management Liability

The regulations regarding management liability have been modified and tightened in a significant

manner. The focus of liability has shifted away from the shareholders to fall on the managing directors of a GmbH. The new regime legislates that a managing director must accept personal liability for the payment of dividends to shareholders if those payments result in the insolvency of the GmbH (this remains the case even if he or she acted on shareholder instruction). Managing directors also are personally liable for any losses incurred as a result of erroneous information contained in the shareholder list, as they are responsible for the accuracy of this list. The extent of such personal liability also covers issues relating to capital maintenance. Furthermore, managing directors are personally liable if, in connection with cash pooling arrangements, they fail to negotiate an adequate termination option and the failure results in unacceptable levels of indebtedness or insolvency. In this regard, they have a duty to make assumptions necessary to determine whether the repayment claim of the company for loans to the cash pool remains at full value, and as a consequence they are personally liable for any losses resulting from these assumptions.

The modifications to the GmbH law offer easier access to this corporate status, and time will tell whether the new status will be more common used in Europe.

JAPAN

JFTC Files Criminal Charges Against Galvanized Steel Sheet Cartel

On November 11, 2008 the Japan Fair Trade Commission (JFTC) filed a criminal accusation with the Prosecutor-General against three major steel sheet companies, Nippon Steel & Sumikin Coated Sheet Corporation, Nisshin Steel Co., Ltd. and Yodogawa Steel Works, Ltd., on suspicions of violating Article 3 of the Antimonopoly Act ("Unreasonable Restraint of Trade"). This the first time in 17 years and the third time since World War II that the JFTC has filed a criminal accusation for a price-fixing cartel.

According to the JFTC, during the period between April 2006 and June 2006, employees of the accused companies agreed to raise the sale price of hot-dip 55-percent aluminum-zinc alloycoated steel sheets and strips shipped after July 1, 2006 by ¥10 per kilogram.

A fourth steel manufacturer, JFE Galvanizing & Coating Co., also participated in the cartel. It was nevertheless excluded from the JFTC's criminal accusation filing because it applied for leniency (i.e., reduction or exemption of a surcharge) and notified the JFTC of the cartel voluntarily before the JFTC started its compulsory investigation. In this case, the leniency system helped to reveal a cartel. The first to notify the JFTC of a cartel can avoid a criminal accusation by the prosecutor's office (as a matter of fact) as well as any applicable surcharges by the JFTC (as a matter of law). The JFTC hopes that such treatment will

keep the leniency system effective. Although Japan's law does not specifically provide for such exemption from criminal accusation by the prosecutors office, the prosecutors have also taken a position supporting the JFTC's policy regarding the leniency system.

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