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BRIBERY

Who Is a 'Foreign Official' in China: The FCPA After *Noriega* and *Carson* Cases

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For many years, the United States government has interpreted the definition of ''foreign official'' in the Foreign Corrupt Practices Act very broadly, meaning that the payment of any remuneration to a wide range of individuals abroad could violate the act. Despite the fact that this broad definition makes compliance difficult, it long went unchallenged until defendants in a few recent cases disputed the government's position. While the government prevailed in these first skirmishes, the opinions in its favor have begun to suggest some potential limits on the range of individuals who might qualify as ''foreign officials.''

These potential limitations provide the first glimmer of hope that the government's broad reach might be curtailed, but it will take a while to determine whether these opinions will make it easier to operate in China without running afoul of the FCPA. Even if the ''foreign official'' limitations do become settled law, it will not always be readily apparent whether specific individuals whom American businesses encounter in China fall within those limitations. Any business hoping for easier compliance with the FCPA in China will need to proceed carefully and with considerable local insight in making those determinations.

American companies doing business in China all seem to be grappling with certain legal challenges. There is an elaborate culture of giving gifts, providing hospitality, and paying bribes; the Chinese government has a role—often not immediately identifiable—in a significant percentage of the businesses; and there is increased enforcement of both domestic and foreign anticorruption laws, particularly the FCPA.

This article seeks to offer insight into identifying and limiting the risk of violating the FCPA by examining which of the individuals in China with whom American companies regularly deal may qualify as ''foreign officials'' and therefore fall within the statute's proscriptions.

The FCPA

The FCPA is President Carter-era legislation designed to halt bribery of public officials in foreign countries and to restore confidence in the integrity of American businesses. It was enacted after several embarrassing bribery scandals involving a number of companies in various countries around the world. The FCPA prohibits the corrupt offer, payment, promise to pay, or authorization for any remuneration to any foreign official for the purpose of inducing the official to use his influence in order to obtain, retain, or direct business.[1]

''Foreign official'' is defined in part as ''any officer or employee of a foreign government or any department, agency or instrumentality thereof.''[2] The FCPA does not refer specifically to state-owned entities, and it does not define ''instrumentality.''

For many years, the Justice Department and the Securities and Exchange Commission have interpreted the FCPA's definition of ''foreign official'' to include employees of state-owned enterprises (SOEs), on the theory that SOEs qualify as ''instrumentalities.'' The result has been that some American companies doing business in China were surprised to learn, after the fact, that their Chinese counterparts in a seemingly nongovernmental business may in fact have been SOEs, subject to the FCPA.

Because historically the vast bulk of the government's investigations focused on companies rather than individuals, and because companies generally have settled rather than contested allegations once the gov-

[1] 15 U.S.C. § 78dd-2(a).
[2] 15 U.S.C. § 78dd-2(h)(2)(A).

 ISSN 1559-3185

ernment decided to pursue them, the government's interpretation was not tested in court. Due to the relative lack of judicial challenges, the SEC and DOJ have been able to take the position that any Chinese company that is state-owned in any way constitutes an ''instrumentality,'' and that any business dealing with its employees is therefore doing business with a ''foreign official.'' The government has gone so far as to take that position under certain circumstances where the Chinese government was a minority owner.[3]

Two Recent Decisions

With the expansion in enforcement activity and with the government's recent emphasis on prosecuting individuals (who are more likely to fight the charges), the government's broad interpretation of ''foreign official'' was recently tested—twice in 30 days—on motions to dismiss indictments. The first case was *United States v. Noriega*[4] and the second was *United States v. Carson*.[5] In both cases, the courts declined to dismiss the indictments. As the only two full opinions addressing the definition of ''foreign official'' under the FCPA,[6] *Noriega* and *Carson* permit a more careful analysis of the issue.

[3] *See SEC v. Meza*, No. 09-cv-01648 (D.D.C. Aug. 28, 2009) (complaint alleging FCPA violations based on ''referral fees'' to employees of Chinese SOEs). As an example of the government's position toward minority government ownership, in a recently filed criminal action, DOJ alleged violations of the FCPA based on payments to officials of Telekom Malaysia, an entity owned 43 percent by the Malaysian ministry of finance. See *United States v. Alcatel-Lucent France SA*, No. 1:10-cr-20907 (S.D. Fla. Dec. 27, 2010) (05 WCR 925).

[4] *United States v. Noriega*, No. 2:10-cr-01031 (C.D. Cal. April 20, 2011) (06 WCR 1060).

[5] *United States v. Carson*, No. 8:09-cr-00077 (C.D. Cal. May 18, 2011) (06 WCR 402).

[6] Two other decisions also went in favor of the government, but they were either summary, see *United States v. Nguyen*, No. 2:08-cr-00522 (E.D. Pa. Dec. 30, 2009) (05 WCR 700), or had a very cursory discussion, see *United States v. Esquenazi*, No. 1:09-cr-21010 (S.D. Fla. Nov. 19, 2010) (07 WCR 242).

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Noriega. The *Noriega* prosecution focused on the allegations that Lindsey Manufacturing Co. and two of its executives paid bribes to two high-ranking employees of the Comisión Federal de Electricidad (CFE), an electric utility company wholly owned by the Mexican government.[7] The defendants moved to dismiss the indictment, contending that a state-owned company could never qualify as ''a department, agency or instrumentality of a foreign government.'' Shortly before trial, the district court denied the motion to dismiss, and later the jury found the defendants guilty.

As required on a motion to dismiss the indictment, the defendants did not contest the allegations in the indictment that under the Mexican constitution the supply of electricity was solely a government function and that CFE was a company created and controlled by the Mexican government. They instead presented a legal argument asserting that when read in context, the term ''instrumentality'' in the FCPA should be interpreted to describe entities that have characteristics like those that are the sine qua non of both ''departments'' and ''agencies,'' which are the two terms that appear before ''instrumentality'' in the statute.

While questioning the defendants' analysis, the district court offered what it called a nonexclusive list of characteristics of government agencies and departments that fall within the standard proposed by the defendants. Those characteristics are:

- The entity provides a service to the citizens—indeed, in many cases to all the inhabitants—of the jurisdiction.
- The key officers and directors of the entity are, or are appointed by, government officials.
- The entity is financed, at least in large measure, through governmental appropriations or through revenues obtained as a result of government-mandated taxes, licenses, fees, or royalties, such as entrance fees to a national park.
- The entity is vested with and exercises exclusive or controlling power to administer its designated functions.
- The entity is widely perceived and understood to be performing official (i.e., governmental) functions.

The court then determined that CFE possessed all these characteristics.

The significance of the district court's analysis of these characteristics is uncertain. The court did not expressly endorse these characteristics (or any analysis of characteristics) as the definitive test for whether a state-owned entity is an ''instrumentality'' for purposes of the FCPA. Moreover, the court went on to analyze the legislative history of the FCPA (which it found inconclusive) and found convincing the government's reliance on a 200-year-old case, *Murray v. Schooner Charming Betsy*,[8] which directed that when fairly possible, stat-

[7] Although Noriega's name is in the case caption, he was a fugitive. He therefore did not participate in the motion to dismiss the indictment that led to the court's decision or in the trial. At trial, the jury convicted the defendants, but the court ultimately vacated the convictions and dismissed the indictments with prejudice based on government misconduct. See 06 WCR 1060, order granting motion to dismiss (Dec. 1, 2011).

[8] 6 U.S. (2 Cranch) 64, 117-18 (1804).

  WCR ISSN 1559-3185

utes should be read not to conflict with international agreements of the United States. The court noted that the Organization for Economic Co-operation and Development (OECD) Convention on Combating Bribery, which Congress ratified in 1998, defines a foreign public official to include anyone working for ''any enterprise, regardless of its legal form, over which a government or governments may, directly or indirectly, exercise a dominant influence.'' As a result, the *Noriega* decision could be read to support either a test based on characteristics of the entity, or a much more easily satisfied test focused on whether the government may directly or indirectly exercise a dominant influence on the entity.

Carson. According to the indictment, Stuart Carson, chief executive officer of valve manufacturing company Control Components Inc., and other company executives paid nearly $5 million in bribes to employees of state-owned customers in China, Korea, Malaysia, and the United Arab Emirates. The motion to dismiss in *Carson* was similar to that in *Noriega*, including the argument that employees of state-owned enterprises could never be foreign officials under the FCPA. In its opinion, the district court cited the *Noriega* decision, which had been decided only a few weeks earlier.

Rather than listing potential standards based on the argument proffered by the defendants, the *Carson* court constructed its own independent interpretation of the statute. Concluding that the meaning of the statutory text is clear, the court determined that whether a state-owned company qualifies as an instrumentality for the purposes of the FCPA is a question of fact. It then offered a series of nonexclusive factors to use in determining whether a business entity qualifies as an instrumentality. Without explicitly making the connection, the factors appear to relate at least in part to the court's view that the term ''instrumentality'' was ''intended to capture entities that are not 'departments' or 'agencies' of a foreign government, but nevertheless carry out government functions or objectives.''

The factors identified by the court as relevant to the ''foreign official'' inquiry are:

- the foreign state's characterization of the entity and its employees;
- the foreign state's degree of control over the entity;
- the purpose of the entity's activities;
- the entity's obligations and privileges under the foreign state's law, including whether the entity exercises exclusive or controlling power to administer its designated functions;
- the circumstances surrounding the entity's creation; and
- the foreign state's extent of ownership of the entity, including the level of financial support by the state (e.g., subsidies, special tax treatment, and loans).

The court did not apply these factors, instead declaring that the motion was ''not entirely segregable from the evidence to be presented at trial.'' At the end of its opinion, the court referred to the ''substantial evidentiary burden'' on the government to establish that a business qualifies as an instrumentality for the purposes of the FCPA.

While the meaning of these factors and how they are weighed against each other to reach a conclusion remain to be decided, the court's presentation of the factors and its reference to the government's burden suggest that employees of state-owned entities could be foreign officials. However, equally important, particularly for China, is the possibility that in certain circumstances such employees may not qualify as foreign officials. The court explained that ''a mere monetary investment in a business entity by the government may not be sufficient to transform that entity into a government instrumentality,'' but where an investment is ''combined with additional factors that objectively indicate the entity is being used as an instrument to carry out government objectives, that business entity would qualify as a government instrumentality.''

Combined Lessons Of *Noriega* and *Carson*

The two cases offer somewhat similar standards for determining whether entities qualify as instrumentalities, with the possible exception of *Noriega*'s reference to reading the OECD's broad definition of foreign official into the FCPA.[9] If subsequent cases attempt to apply the *Noriega* and *Carson* standards, a combination from the two cases would yield the following factors:

- the purpose of the entity, including (i) whether it provides a service to citizens, or all of the inhabitants, of the jurisdiction, and (ii) whether it is perceived and understood to be performing official (i.e., governmental) functions;
- how the government characterizes the entity and the entity's employees;
- how the entity was created;
- whether key officers and directors of the entity are, or are appointed by, government officials;
- the extent of the government's ownership or financial support of the entity, including whether it is financed in large measure through revenues obtained from government-mandated taxes, licenses, fees, or royalties, or through other government support such as subsidies, special tax treatment, or loans; and
- the extent of the entity's powers, including whether the entity has exclusive or controlling power to administer its designated functions.

[9] The principle that the FCPA should be read broadly to harmonize it with a treaty is potentially in conflict with the principle known as the rule of lenity, which requires that ambiguous criminal laws be interpreted in favor of the defendants subjected to them. See, e.g., *United States v. Bass*, 404 U.S. 336, 347-49 (1971); *United States v. Gradwell*, 243 U.S. 476, 485 (1917). The rule of lenity ''not only vindicates the fundamental principle that no citizens should be held accountable for a violation of a statute whose commands are uncertain'' but also ''places the weight of inertia upon the party that can best induce Congress to speak more clearly and keeps courts from making criminal laws in Congress's stead.'' *United States v. Santos*, 553 U.S. 507, 514 (2008) (03 WCR 379). But more recent cases limit the rule of lenity to statutes that contain a ''grievous ambiguity or uncertainty.'' See *Dean v. United States*, 129 S. Ct. 1849 (U.S. 2009).

Applying *Noriega* and *Carson* To Business Entities in China

Understanding the Various Types Of Officials by the Type of Enterprise

In analyzing whether an official in China would qualify as a foreign official under the FCPA, it is necessary to first determine the type of enterprise with which the individual is associated. This determination will inform the level of government ownership and control over the enterprise and hence whether the official is likely to be covered by the FCPA.

To illustrate the different types of SOEs and relevant enterprises in China, we begin by identifying the ''administrative organs'' of the Chinese government that are typically encountered by businesses and then examine the status of enterprises owned, at least in part, by the Chinese government, including businesses that American companies may not expect to be state-owned. We then consider whether all Chinese companies that are wholly or partially state-owned should be considered government instrumentalities in light of the *Carson* and *Noriega* standards.

1. Administrative Organs of the Chinese Government

When American companies conduct business in China, interactions with the government are unavoidable. Any company seeking to establish a business presence in China will necessarily have to engage administrative organs of the Chinese government. The administrative organs in China include those of the central government and various subordinate local governments through the provincial levels, city levels, and often neighborhood levels. The State Council is the chief organ in China, the functional center of state power, and the clearinghouse for government initiatives at all levels. The departments directly under the State Council, and their local branches under the supervision of local governments, are all considered administrative organs of the Chinese government, and most of the people working in these authorities are considered ''state functionaries'' under Chinese law.[10]

Every business in China, domestic or foreign, interacts with administrative organs, whether to receive approval to conduct business from the Ministry of Commerce or its local branches, to obtain a business license from the State Administration of Industry and Commerce or its local branches, or to pay business taxes to the State Administration of Taxation and its local branches. Companies in certain industries may also have to interact regularly with the specific administrative organs that regulate their industry. For example, pharmaceutical and life science companies must obtain special approval from the State Food and Drug Administration or the Ministry of Health before they can distribute or manufacture their products in China. For manufacturing enterprises, the key supervisory authority is the General Administration of Quality Supervision, Inspection and Quarantine, which monitors product quality concerns. Companies engaged in postal services, internet, wireless, broadcasting, communications, electronic and information business, or software industries are subject to approval and scrutiny by the Ministry of Industry and Information Technology. There is little doubt that these administrative organs qualify as government ''instrumentalities'' under the FCPA, and people working for these administrative organs are ''foreign officials.''

2. State-Owned Enterprises Under Chinese Law

SOEs in China can be wholly or partially owned or controlled by the Chinese government. This ownership and control is generally exercised through the State-Owned Assets Supervision and Administration Commission of the State Council (SASAC) and its local branches established by local governments. Chinese SOEs come in all shapes and sizes, span a broad range of industries, and have different levels of government control. However, in construing all such Chinese enterprises to be government instrumentalities, the SEC and DOJ have lumped them together. Knowing the SEC's and DOJ's approach when applying the new standards articulated in *Carson* and *Noriega* can help identify which Chinese enterprises should be deemed a government instrumentality.

Chinese law does not provide a fixed definition of the term ''state-owned enterprise'' or SOE. Therefore, it is necessary to understand the regulatory regime governing Chinese SOEs. SASAC administers the state's investments or enterprises, assuming the role of investor (either as sole investor or co-investor with other private parties). As the government ''investor,'' SASAC is charged with collecting the proceeds of investments, participating in business decisions, and appointing senior management personnel in accordance with its proportional investment.

At least in principle, SOEs are not meant to serve a public function. Rather, SOEs are meant to operate just as private business entities, with the sole difference being the government's involvement as an investor or shareholder of the company. SOEs have no sovereign immunity and are not meant to have any greater influence than any other private business entity. SOEs are intended to give the central government and local governments some control over key sectors of the national economy and to ensure economic development and stability in China.

Under *Noriega* and *Carson*, one factor to consider would be the definition and characterization of SOEs under Chinese law. While Chinese law has not expressly defined the term ''state-owned enterprise,'' the courts and agencies that deal with state investments have issued ''guidances''[11] that characterize SOEs by the degree of control by the state. Under such guidances, SOEs may include wholly state-owned enterprises, state-controlled companies, and partially state-owned enterprises. Enterprises in which the state holds fewer than 50 percent of shares are generally not con-

[10] In Article 93 of the People's Republic of China Criminal Law, state functionary is defined as a person (i) who performs administrative services in a government agency; (ii) who performs administrative services in a state-owned enterprise, state-funded public institution, or state-funded society association; (iii) who is assigned by a government agency, state-owned enterprise, or state-funded public institution to perform administrative services in a non-state-funded enterprise, institution, or society association; and (iv) other people who perform administrative services according to the law. In other words, a ''state functionary'' is essentially the Chinese equivalent term for a government official. Payments to state functionaries constitute ''official bribery'' under Chinese law.

[11] The term of art in China for guidance is ''guidances.''

   ISSN 1559-3185

sidered SOEs under Chinese law. Conversely, enterprises with 50 percent or more state ownership are considered SOEs. Employees who are appointed by government authorities to work in SOEs, and who undertake certain official functions including leadership, supervision, management, and organizational roles, are considered to be ''state functionaries.'' Government investment contributions in SOEs are considered ''state assets.''

3. Closely Controlled SOEs: China Mobile, CNOOC, and other Vital Enterprises

There are a number of large-scale SOEs recognized by the State Council as enterprises that influence the economic lifeblood of the country by implicating national security issues, key infrastructure, or vital natural resources. For these enterprises, the State Council will directly supervise the government's investment. In contrast, for less critical SOEs, the government's investment will be managed by the local SASAC. Currently, SASAC oversees 120 large, centrally owned companies, including China Mobile (the largest cellular phone service provider in China), China National Offshore Oil Corp. (CNOOC) and Shanghai Baosteel Group Corp. (Baosteel).[12]

Closely controlled SOEs, such as China Mobile and CNOOC, are likely to be considered government instrumentalities under the FCPA. Both China Mobile and CNOOC are established and wholly owned by the Chinese government through SASAC. Major business decisions are required to be approved by SASAC, and the senior management personnel of both companies are appointed by SASAC, including, but not limited to, the chairman and vice-chairman, the general manager and deputy general manager, assistant manager to the general manager, and the officers of the Communist Party of China (CPC)[13] of the companies. All these members of senior management are deemed to be state functionaries under Chinese law. Indeed, Zhang Chunjiang, the former deputy general manager and Party Secretary of China Mobile, was recently convicted of ''official'' or ''public'' bribery and sentenced to death with a two-year reprieve for taking 7.46 million RMB in bribes between 1994 and 2009 while holding official positions.[14]

Further supporting the conclusion that such companies should be deemed ''government instrumentalities,'' most enjoy either monopoly status or extremely limited competition in their respective industries as they administer the relevant resources of the state. For example, CNOOC was incorporated and authorized by the Chinese government in 1982 to assume overall responsibility for the exploitation of offshore oil and gas resources in cooperation with foreign partners.

Although SOEs in China are not meant to serve a public function in principle, SOEs such as China Mobile and CNOOC often do share certain public functions, including optimizing the allocation of public resources, improving strategic development and industrial infrastructure, ensuring balanced economic development in different regions, ensuring the country's security, and implementing key government policies. Applying the standards established by the *Noriega* and *Carson* cases, SOEs that are controlled by the government as closely as China Mobile and CNOOC will almost certainly be deemed government instrumentalities.

4. Minority Government-Invested Enterprises: Entities Such as BNAASS

The analysis is considerably more complicated for enterprises in which the state holds only a part or a minority of shares. Still more complicated are situations in which an enterprise may have started out as a wholly owned state enterprise but the state has subsequently ''privatized'' or spun off a majority interest to the private sector. These minority-invested enterprises generally will not be authorized by the state to perform any official function or have any exclusive or controlling power to administer their designated functions. Beijing Wohua Biotechnology Co. (Wohua) is one example of such an enterprise. Wohua is not considered an SOE in China, even though one of its shareholders, Beijing Double-Crane Pharmaceutical Co., is itself an SOE. The reason for this is that Beijing Double-Crane owns only 20 percent of the shares of Wohua and does not have absolute supervision over the enterprise.

While it is relatively easy to assess whether or not a wholly state-owned enterprise or a partially state-owned enterprise is a government instrumentality under Chinese law,[15] it is much more difficult to make that assessment under the FCPA. For instance, take Baosteel-NSC/Arcelor Automotive Steel Sheets Co. (BNAASS). BNAASS is a Sino-foreign joint venture established by Nippon Steel Corp. (Nippon), Baoshan Iron & Steel Co. (Baoshan Iron) (a wholly owned enterprise of Baosteel, a Chinese SOE) and Arcelor. Baoshan Iron, Nippon, and Arcelor have a 50 percent, 38 percent, and 12 percent interest in BNAASS, respectively.

Applying the *Noriega* and *Carson* standards, it is a close question whether BNAASS, despite its government investment, would qualify as a government instrumentality. First, BNAASS was not established by the state and, indeed, two other key investors are foreign parties. Second, BNAASS was not established to provide services to Chinese citizens or perform any official functions. Third, BNAASS enjoys no special treatment nor does it have any exclusive or controlling power to administer its designated functions. Baosteel (as the sole shareholder of Baoshan Iron) is entitled to appoint certain directors but only in accordance with its investment share. Taking into account all the considerations in *Noriega* and *Carson*, it seems that BNAASS operates like any other private enterprise with the only difference being that an SOE is the largest shareholder in the

[12] The list of 120 companies is available in Mandarin on SASAC's website at http://www.sasac.gov.cn/n1180/n1226/n2425/index.html.

[13] Many companies in China will have one or more management positions that are meant to serve as liaisons to the Communist Party, such as the ''Party Secretary.''

[14] Under Chinese law, death with a two-year reprieve means that the defendant is given a death sentence but the sentence is put on hold for two years. After that two-year period, if the defendant has been well behaved, the death sentence is typically commuted. Think of it as a deferred prosecution agreement on steroids.

[15] Enterprises with less than majority control by the government are generally not considered SOEs in China. Where the state holds minority shares in an enterprise, it is much more difficult under Chinese law to say that the state has established the enterprise and actually controls its operation since the key officials are generally not appointed by the state and the state as a minority shareholder is not granted the exclusive veto power to control the development of the enterprise by law.

company and receives proceeds from it. In this circumstance, there is at least a reasonable argument that, under *Noriega* and *Carson*, BNAASS should not be deemed a government instrumentality under the FCPA. In this sense, BNAASS is typical of many entities in which the state is only a partial or minority owner—entities which to date the SEC and DOJ have sought to treat as government instrumentalities for the purposes of the FCPA.

5. Public Institutions: Hospitals

Public institutions in China are organizations established by the government in the cultural, educational, sporting, and medical care sectors for the purposes of providing social services and welfare to citizens. These institutions usually include media, publishing houses, public schools, and hospitals.

It may not be immediately evident to American businesses that such public institutions are considered state instrumentalities. Take hospitals, for instance. The vast majority of hospitals in China are publicly funded. Although the day-to-day practice of medicine may not involve much government control, these publicly funded hospitals and all the health care professionals they employ can create a huge FCPA risk for American companies that are not properly educated on the role of hospitals in China.

Public hospitals in China are run and funded by the Chinese government and are considered ''public institutions'' under Chinese law. In China, public hospitals are distinguished from private hospitals in terms of the hospital's business objectives, missions, various tax and pricing policies, and financial accounting systems. Public hospitals differ from private ones in that they:

- are established and operated by the Chinese government to serve public interest. Their aim is not to make profit, but rather, to operate on a break-even basis. Any surplus income can be used only for its own development, such as medical instrument upgrades, technology imports, or the development of new medical services;

- generally provide basic medical services to the public and carry out other tasks assigned by the government[16];

- are entitled to financial grants from the government and must implement medical-service guideline prices specified by the government. In exchange, they enjoy tax exemption[17];

- implement rules and policies issued by the Ministry of Finance and the Ministry of Health, such as the financial systems of the hospital and the accounting systems of the hospital[18]; and

- have the government appoint key officials, who are deemed to be state functionaries. For physicians and other health care professionals who work for public hospitals and are not state functionaries, their remuneration comes from government fiscal appropriation.

The SEC and DOJ have generally considered public hospitals to be government instrumentalities for purposes of FCPA enforcement.[19] Although this interpretation has never been confirmed by a court, a number of characteristics of public hospitals in China strongly support the SEC/DOJ position. The fact that public hospitals in China are established by the Chinese government for the purpose of providing medical services to citizens is compelling. So is the fact that public hospitals are entitled to financial grants and tax exemptions and are run by key officials appointed by the Ministry of Health. Even under Chinese law, public hospitals are considered ''public institutions,'' and officials working for public hospitals are considered ''state functionaries.'' All these factors support the SEC's and DOJ's interpretation. Accordingly, any business with a public hospital in China, whether it is supplying pharmaceuticals, providing other supplies or services, or even making a charitable donation, puts a company at heightened risk of an FCPA violation.

6. Society Associations

Society associations are another significant risk for American companies operating in China, primarily because their government association is often not evident. Society associations in China generally refer to nonprofit social organizations voluntarily composed of Chinese citizens that perform activities in accordance with the articles of association for the realization of the common desires of the membership. Although by law society associations in China are nongovernmental organizations, they are quasi-governmental organizations in practice. Chinese law requires all society associations to provide an approval letter from the supervising government agency of the relevant industry when filing an application to be established, and many society associations in China are monitored or directed by the central and local governments.

Currently, China has approximately 2,000 national society associations, 200 of which perform some form of government function and receive some level of government fiscal appropriation. The tasks of these society associations are assigned by the government, and the allocation of staff and appointment of key officials are decided by the staffing administration department of the central government. These society associations also enjoy tax-exempt status.

For instance, the All-China Federation of Trade Unions, Communist Youth League of China, and All-China Women Federation are society associations established by the CPC that perform quasi-governmental functions to maintain a connection between the CPC and the populace. These three associations, together

[16] Private hospitals are allowed to decide the scope of their own medical services according to market demand, except in the event of a major disaster, accident, epidemic, or any other exceptional circumstances. In such circumstances, medical institutions are required to follow the instructions of the government.

[17] Private hospitals may set their own medical-service prices and operate without government guidance in accordance with the law. They must, however, pay taxes in accordance with the law.

[18] In China, private hospitals implement generally accepted financial and accounting principles.

[19] See, e.g., DOJ press release No. 05-090, *Micrus Corporation Enters Into Agreement To Resolve Potential Foreign Corrupt Practices Act Liability* (March 2, 2005) (alleged bribes involved payments to doctors at public hospitals in France, Turkey, Spain, and Germany); *United States v. AGA Med. Corp.*, No. 08-cr-00172 (D. Minn. June 3, 2008) (criminal information charges that government-owned and -controlled hospitals in China are instrumentalities of the Chinese government).

  WCR ISSN 1559-3185

with five other associations, can attend the Chinese People's Political Consultative Conference. There are 14 other society associations under the leadership of the State Council, including the China Federation of Literary and Art Circles, Chinese Writers Association, All-China Journalists Association, All-China Federation for Returned Overseas Chinese, and the Red Cross Society of China. Many employees of these society associations are deemed to be state functionaries under Chinese law, and their salaries come from fiscal appropriation.

In addition to the society associations that are under the leadership of the CPC and the State Council, there are certain society associations that are under the leadership of central administrative organs or their local branches. For example, the All-China Sports Federation (ACSF) claims to be a national, nongovernmental, nonprofit sports organization. In practice, it is under the supervision of the State General Administration of Sports (SGAS).[20] Its main responsibilities are to draft sports laws, regulations, strategies, and plans; arrange sports activities and promote sports development in China; examine the qualification of other national sports associations; and perform other tasks assigned by the State Council. Key officials of the ACSF are also officials of the SGAS. In practice, the ACSF and the SGAS are really one organization under two different names.

ACSF has more than 60 society association members, including the Chinese Basketball Association, Chinese Football [Soccer] Association (CFA), Chinese Swimming Association, and all associations for Olympics and non-Olympic sports programs. All these sports associations are under the leadership of SGAS, and their key officials also work for the SGAS. For example, the CFA is a member of ACSF. It is funded by the Chinese government and enjoys tax-exempt status. Its key officials are all from the Football Administration Center of the SGAS. Currently, the full-time vice chairman of the CFA, who is responsible for overseeing the development of soccer in China, is also the head of the Football Administration Center of the SGAS.[21] Its main responsibilities are soccer management, including drafting relevant regulations and policies, developing plans and strategies, managing the national soccer teams, organizing soccer activities, and handling other tasks relevant to soccer development. In practice, the CFA and the Football Administration Center of the SGAS share the same workforce. Thus, American companies that do business with sports teams at either a national or local level may be unknowingly interacting with government-related entities. This business can include anything from team sponsorships to hiring an athlete for commercials or endorsements.

Likewise, it is a very common practice for journalists to demand payment to cover an event or media story (in essence a form of payola) or for companies to sponsor journalists to report on some form of promotional event (i.e., a film festival or fashion show). If an American company makes such a payment, it may be unwittingly interacting with government officials, as journalists in China are typically members of the All China Journalists Association. Similarly, an American company that wants to make a donation to a relief agency, such as the Red Cross Society of China, may not be aware that the organization is a society association in China.

The Journalists Association, the Red Cross Society of China, and all the other quasi-governmental society organizations discussed above share certain characteristics that satisfy the standards offered by *Noriega* and *Carson*, such as:

- funding by government parties or organizations and being subject to their leadership;
- fiscal appropriations from the Chinese government and tax-exempt status;
- key officials who are state functionaries and sometimes also work for government administrative organs. In addition to being state functionaries, many employees receive remuneration from the Chinese government; and
- performing government functions or tasks assigned by the Chinese government.

Because of these characteristics, quasi-governmental society organizations may very well be regarded as ''instrumentalities'' under the FCPA, and their employees might be considered ''foreign government officials.'' This is a special concern not so much because the application of the FCPA to these organizations presents a difficult legal issue, but because as a practical matter it is often difficult to identify when a counter-party in a business transaction is a society organization. Additionally, many American companies do not appreciate that society associations may create risk under the FCPA. This is a significant misunderstanding, because these organizations span such a wide array of industries—from publishing to the arts to sports leagues.

Questions Remain

While the SEC and DOJ can be expected to continue to proceed as if every SOE is an instrumentality (and all of its employees are public officials) for purposes of the FCPA, a court applying the *Noriega* and *Carson* standards may not find the decisions quite so simple.

So where does this leave an American company seeking to do business in China? Unfortunately, the hard-to-determine nature of these quasi-governmental society organizations, compounded by the continuing uncertainty of U.S. law, means that there is no easy answer. American companies can only hope that the courts give further elaboration of exactly who should be considered a government official and, in the meantime, apply heightened scrutiny to their business practices in China.

Noriega and *Carson* are a first, small step in that process. Despite the traditional position of the SEC and DOJ that all Chinese companies with state ownership, potentially including even companies with less than 50 percent government investment, should be regarded as government instrumentalities, a full application of the *Carson* and *Noriega* standards could support a different conclusion.

It is too soon to tell whether the *Noriega* and *Carson* standards will become widely accepted or if a broader, OECD-based definition will win the day. If application of the *Noriega* and *Carson* factors gains wide acceptance, they will help identify—and potentially limit in a

[20] SGAS is a subordinate national government agency of the State Council responsible for sports in China.

[21] The Chairman of the CFA is merely the titular head of the CFA and does not undertake any daily administrative responsibilities.

meaningful way—the enterprises that qualify as instrumentalities for purposes of the FCPA.

WCR ISSN 1559-3185