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New FCPA Cases Heighten Scrutiny of Intermediaries in China

AGA Medical Corporation (AGA), a privately-held, US medical device manufacturer, and Faro Technologies Inc. (Faro), a public company specializing in computerized measurement devices and software, have agreed to pay \$2 million and \$1.1 million in criminal penalties, respectively, in connection with corrupt payments to Chinese government officials in violation of the Foreign Corrupt Practices Act (FCPA) according to press releases issued by the US Department of Justice (DOJ). The DOJ's enforcement actions against AGA and Faro highlight the FCPA risks of doing business with intermediaries in China.

AGA

According to the DOJ, between 1997 and 2005, AGA's distributor in China made improper payments to physicians employed by government-owned hospitals in exchange for purchases of AGA's products. Senior AGA employees approved improper "discounts" and "commissions" paid to the Chinese doctors who controlled purchasing decisions at these state-owned hospitals. In addition, between 2000 and 2002, AGA senior employees authorized payments through the company's Chinese distributor to government officials employed by China's State Intellectual Property Office to ensure patent approval of several AGA products.

DOJ has charged AGA, in a criminal Information filed in US District Court in Minnesota, with one count of conspiring to make corrupt payments to Chinese officials to obtain and retain business and one count of violating the FCPA by authorizing improper payments to government officials in China. AGA has entered into a deferred prosecution agreement with DOJ, requiring cooperation, an enhanced compliance program, and engagement of an independent corporate monitor. If AGA abides by the agreement for three years, DOJ will dismiss the charges.

[Click here for full DOJ press release](#)

Faro

Beginning in 2003, Faro used its subsidiary in China to sell products directly to the Chinese automotive, aerospace and consumer goods industries. In 2004 and 2005, a Faro employee authorized "referral fees" as payments by other Faro employees to employees of state-owned or controlled Chinese entities to secure contracts for Faro. In 2005, Faro used an intermediary to make these improper payments to "avoid exposure." Faro also falsely described these bribe payments in its books and records as referral fees. DOJ has agreed to enter into a non-prosecution agreement with Faro for a two year term. The company also has agreed to engage an independent corporate monitor.

[Click here for full DOJ press release](#)

Lessons Learned

Under the FCPA, US individuals and companies are prohibited from making improper payments to foreign officials for the purposes of influencing their decisions in order to obtain or retain business. These cases

highlight several important compliance lessons. First, the AGA enforcement action is one of the few FCPA cases involving company liability for independent distributors. Second, while US businesses often retain distributors and other intermediaries to navigate the Chinese market, these cases highlight the substantial FCPA risk in using third parties. Companies that knowingly use intermediaries for bribing government officials in China to secure product sales will be prosecuted. Third, identities of “foreign officials” in China are broadly defined and include physicians employed by government-owned hospitals. Fourth, the AGA case confirms that the DOJ remains focused on the medical device industry. Fifth, AGA and Faro highlight the DOJ’s heightened focus on business operations in China.

Minimizing FCPA Risks In China

As the AGA and Faro actions illustrate, compliance with the FCPA presents significant challenges to US companies conducting business in China. Minimizing FCPA risks in relationships with third parties, including distributors, requires a robust compliance program, due diligence prior to retention, contractual provisions, certifications, training and post-retention oversight. The AGA and Faro enforcement actions provide an opportunity for companies operating in China through intermediaries to review their FCPA practices to make appropriate improvements.

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