

# U.S. Directors Abroad at Greater Risk of FCPA Violations

Written by: Douglas Mancill

According to The Delaware Court of Chancery's comments in the recent headline case of *In re Puda Coal, Inc. Stockholders Litig.* (Puda Coal), directors of U.S. corporations are at greater risk now of personal liability for FCPA violations and other acts of corporate malfeasance abroad. Although Puda Coal involved an improper sale of assets in China, the court's comments about the obligations of directors to protect the interests of shareholders of Delaware corporations in foreign jurisdictions are equally applicable to Thailand.

There is no reason why the obligations imposed upon directors in the Puda Coal case should not also apply to directors in Foreign Corrupt Practices Act (FCPA) cases and other cases involving corporate malfeasance abroad. Here is what Chancellor Strine, the judge in Puda Coal, had to say:

"If you're going to have a company domiciled for purposes of its relations with investors in Delaware and the assets and operations of the company are situated in China that, in order for you to meet your obligation of good faith, you better have your physical body in China an awful lot...You better have the language skills to navigate the environment in which the company is operating. You better have retained accountants and lawyers who are fit to the task of maintaining a system of controls over a public company."

Because so many corporations in the U.S. are incorporated in Delaware and because so many other state courts take their lead from Delaware courts on matters of corporate law, this decision could be game changer for directors of U.S. companies with operations abroad. For example, if a U.S. parent corporation has a subsidiary in Thailand, the directors of that Delaware company need to ensure that robust measures are in place to prevent that subsidiary from violating the FCPA. Chancellor Strine observed:

"Independent directors who step into these situations involving essentially the fiduciary oversight of assets in other parts of the world have a duty not to be dummy directors. I'm not mixing up care in the sense of negligence with loyalty here, in the sense of our duty of loyalty. I'm talking about the loyalty issue of understanding that if assets are in Russia, if they're in Nigeria, if they're in the Middle East, if they're in China, that you're not going to be able to sit in your home in the U.S. and do a conference call four times a year and discharge your duty of loyalty. That won't cut it."

Just as a U.S. company cannot put its head in the sand when there are red flags of corruption nor can the independent directors of company do so either. That won't cut it. Indeed, Chancellor Strine's comments strongly suggest that directors must go one step further: they must independently

ensure measures are in place to ensure compliance with the FCPA and proactively ferret out corruption when evidence of corrupt dealings come to their attention. If they fail to do this, they may be personally liable to the shareholders of the corporation for any damages that corporation suffers from, say, FCPA charges that could have been avoided if there was an effective system of controls in place. If an independent director fails to do this, and an FCPA violation occurs as a result of such failure, the shareholders who lose money as a result of that compliance failure may recover directly against the corporation's directors.

Since fines in FCPA cases often amount to tens of millions of dollars, and sometimes run into the hundreds of millions of dollars, this is no small risk to directors of U.S. companies, particularly since the Puda Coal decision also suggests that directors lose their corporate indemnification rights when they fail to meet these obligations. The FCPA is a U.S. federal criminal law, but this Delaware state court decision on corporate law substantially increases the financial risks on the directors of all U.S. corporations by putting them at risk for substantial civil damages when such corporations are charged by the federal authorities with violating the FCPA. ■

*Douglas Mancill is a partner in PriceSanond and Chair of AMCHAM's Legal Committee; he can be reached at: [dmancill@pricesanond.com](mailto:dmancill@pricesanond.com).*



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