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The U.S. Foreign Corrupt Practices Act in Theory and Practice: The Case of General Cable

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Abstract

This study examines the 1977 United States Foreign Corrupt Practices Act and its recent re-interpretation by the U.S. Department of Justice. The original motivation for and concerns about the legislation are examined with particular attention to the two competing regulatory approaches at the time of the congressional debate: (1) the Criminalization Approach and (2) the Disclosure Approach. The example of the prosecution of General Cable is a primary application of the Criminalization Approach and its implications for companies that do business outside the United States. A timeline is provided of General Cable's attempts to survive an increasingly competitive global cable marketplace and the subsequent history of the company is provided, with the conclusion that the DOJ used a new and little-advertised change in interpretation of a thirty-year old law to effectively destroy an established American company and oversee the sale of its assets to a European conglomerate.

Keywords: General Cable, Foreign Corrupt Practices Act, Case Study, Business Ethics.

Introduction and Background of the FCPA

The Foreign Corrupt Practices Act (FCPA) was passed in December, 1977, and signed into law by President Carter on the 19th day of that same month. The bill had passed the U.S. House of Representatives by a vote of 349 to 0. The U.S. Senate had passed the bill by unanimous consent (U.S. Congress (1977)). Although there had been spirited debate on the bill and previous versions throughout 1976 and 1977, the final version was passed without a single "nay" vote (Kohler, 2012, pp. 990-998).

The FCPA was born against the backdrop of the doctrine of Corporate Social Responsibility (CSR) (Bénabou & Tirole, 2010; Hess, 2012). Two alternative approaches to dealing with bribery of foreign officials by American companies and individuals were considered during the congressional hearings: (1) the Criminalization Approach and (2) the Disclosure Approach. Democratic majorities in both the House and Senate favored the former, while the Republican Securities Exchange Commission under the Ford Administration favored the Disclosure Approach (Kohler, 2012, *passim*). The final bill, signed into law by the new democratic President Carter, was "the first law in the world governing domestic business conduct with foreign government officials in foreign market(s)." (Kohler, 2012, p. 930).

The charge in favor of the Criminalization Approach was led in the Senate by senior democrats William Proxmire of Wisconsin and Frank Church of Idaho and in the House by democrat Stephen Solarz of New York. Some of the arguments they made were that

- Bribery of foreign officials by U.S. firms or individuals undermined U.S. foreign policy,
- Bribery by a relatively small number of firms undermined honest efforts of other firms,
- Bribery was frequently accompanied by "slush funds" that could be used to influence U.S. domestic affairs (Watergate),
- Bribery would take funds away from shareholders,
- Mere full disclosure of such activities, such as promulgated under the Disclosure Approach,could impose a substantial burden on multinational firms, and
- An outright ban on such activities would give multinational firms "cover" to be able to plausibly rebuff expectations of bribery on the part of foreign officials.

The SEC did not support the Criminalization Approach. Instead, the SEC's emphasis was on disclosure alone. In this, the SEC was performing its traditional role of shareholder protector, following the lead of Milton Friedman's influential paper advocating a pure disclosure approach to CSR (Friedman, 1970). The idea was that disclosure enables shareholders to know about bribery and adjust their holdings of a company's stock (and thereby its value) accordingly. The SEC emphatically distanced itself (and to a large extent has continued to distance itself) from criminalizing international commerce (Black, 2012).

Economic Issues in Enforcement

Enforcement of the FCPA has been spotty, at best. For its first twenty-five years, only 60 cases were prosecuted against corporations (Crites, 2012, p. 1060). Graham (1984) early on noted no negative effect on American exports from FCPA enforcement. However, a later empirical study by Hines (1995) concluded the FCPA had failed to "strike a balance between the benefits of encouraging ethical behaviour and the costs of social responsibility' (p. 21). The first big increase in FCPA enforcement began in 2004 (Crites, 2012, p. 1060), perhaps due to the role of international trade in the worldwide economic boom (p. 1061). The second big change in enforcement of the FCPA occurred in 2010, when the U.K. enacted the Bribery Act in a process that has been called "messy, chaotic, and highly politicized" and explicitly linked to the U.S. FCPA (Alldridge, 2012, p. 1181). While the Bush Administration had committed to using the law under a compliance approach to provide a useful guide for firms to avoid illegal activity (Henning, 2012, pp. 884-888), the subsequent administration was criticized for "overzealous prosecution … leading to uncertainty and injustice" (Henning, 2012, p. 886).

In recent years, the law has had skeptics like Koehler as well as defenders like Stewart (2012) and Urofsky et al. (2012). Similar to enforcement of U.S. Antitrust Law, it seems very much that which party is in control of the administration affects FCPA enforcement (see Boudreaux & DiLorenzo, 1993, and Armentano, 1972, for the claim about Antitrust Law and Koehler, 2010, 2011, for the claim about the FCPA). Chaffee (2012) documented the failure of both the congress and the administration in addressing domestic corruption in financial markets through the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank). Instead, the Obama Administration concentrated its attention on business practices overseas rather than financial intermediation at home.

Koehler (2011) documented how the U.S. Department of Justice made a concerted effort in 2010 to change how the FCPA was interpreted and enforced. The DOJ and SEC jointly announced a $30 million settlement with U.S.-based Universal Corporation and Alliance One International for violations of the FCPA (Riggins & Palos, 2010). In that year alone, between the DOJ and SEC, twenty-two companies paid more than $1.8 billion in FCPA enforcement fines and penalties. Of these companies, a dozen were based in the US, with the other eight headquartered in France, Germany, India, the Netherlands, Switzerland and the UK, but the seven largest fines were levied against foreign companies. Furthermore, many of the actions on which the prosecutions had been based had taken place over a decade earlier (Koehler, 2011, p. 105).

Dodd-Frank established monetary rewards for whistleblowing (from ten to thirty-percent of the amounts a prosecutorial action recovers). These and other incentives served to put FCPA allegations on a high-growth path (Crites, 2012, p. 1061-1062). Voluntary reporting was encouraged, with the hope that DOJ would seek lower penalties and work with the self-reporting company to curb bad practice in the future. The vehicles established for such cooperation were non-prosecution agreements (NPAs) and deferred prosecution agreements (DPAs). NPAs were designed as contracts between DOJ and the company and therefore would not have to receive court approval, while DPAs were reserved for companies that did not "play ball" with authorities and would bring substantially higher fines and penalties. [Ironically, beginning in 2009, DOJ began to go after companies for activity from years earlier, even though such practices had been cleared by previous administrations under the old interpretation of FCPA.] Effectively, however, "there (was) little to no judicial scrutiny of (either) NPAs or DPAs," and a lack of information forthcoming from DOJ so that "companies (had) little bargaining rights and (were) at the mercy of what (would later be) proposed in the NPA or DPA" by the prosecuting agency (Crites, 2012, pp. 1063-1064).

In November, 2011, the DOJ prosecutor who spearheaded the new approach stated that "what's really changed is not so much the legislation, but the enforcement and approach to enforcement by U.S. authorities" (Koehler, 2011, p. 104), presumably referring to the black box approach of NPAs and DPAs. The involvement of the judicial and legislative branch in reviewing the decisions or interpreting the law also appears to have been minimal, as might have been expected by the widespread use of NPAs and DPAs (see also Westbrook, 2011). One of the key issues in enforcement became what was referred to as "grease payments" in the original debate before passage of the FCPA in 1975-77. To understand the role of grease payments and their genesis, it is necessary to first introduce the two "broken window" theories and then analyse the role of corruption in economic development.

The Two Competing Broken Window Theories

There are two influential theories in the social science literature that are both known by the same name and consider the interaction between governmental policy and individual choice. The first is an old theory pioneered by the French economist, Fredric Bastiat, in 1850. Bastiat wrote influential pamphlets before and during his time in the French National Assembly concerning the unseen effects of collective action. In his essay, "What is Seen and What is Unseen," Bastiat (1850) posits a situation in which a vandal breaks a window. According to Bastiat, what is seen by bystanders is the repair of the window and the funds that are paid to the glazier and the resulting uses to which those funds are put. What is unseen are the purchasing opportunities lost by the owner of the broken window from forgoing whatever best use he would have made of the funds had he not had to pay the glazier to repair the window. This is not the "Broken Window" theory that appears in the FCPA literature.

The second theory, which is the one cited in the FCPA literature, is a relatively new theory espoused by Kelling & Wilson (1982) and Kelling & Coles (1997) and questioned by Harcourt & Thacher (2005), Harcourt and Ludwig (2006) and Alford (2012). According to this newer theory, one broken window in a neighbourhood begets more broken windows, until the long-run equilibrium outcome is all broken windows. This idea has been used to justify zero tolerance of any crime, since the tendency of letting one infraction slide is a march toward wholesale anarchy. This theory was influential in the well-received war on crime under the Giuliani administration in New York City throughout the 1990s (Kelling & Coles, 1997, pp. 259-260). However, the idea behind "Fixing Broken Windows," is that of community involvement in "taking back the streets" with a limited role for the criminal justice system (Kelling & Coles,1997, pp. 239-242). [The position of the authors on this theory in general is neutral, since its applicability depends on the situation or institution being considered.]

What Degree of Corruption is Optimal?

As might be expected, the competing broken windows theories have spawned a significant literature on the efficacy of the complete abatement of all infractions. Wholesale eradication of all corruption may be fraught with problems more nearly aligned with Bastiat's view of broken windows. Leff (1964) pointed out that absolute abatement of corruption may not be in the best interests of the public. For example, "corruption is an extra-legal institution used by individuals or groups to gain influence over the actions of the bureaucracy" (p. 8). According to Scott (2009, p. 123), corruption "may be seen as an informal political system." Johnson et al. (1997) used the experience of entrepreneurship in the former Soviet Union to point out the initial path from Feudalism to Capitalism required all sorts of mechanisms that were generally unacceptable at the time, including warfare, to establish efficient commerce and a higher standard of living (p. 233-234). Cheung et al. (2012) seemed to characterize bribery as spanning a market that conventional means left underserved. Their study attempted to measure cost and benefits to firms in cases from around the world. Shleifer & Vishny (1983), Beck & Maher (1989), Baumol (1990), Beck et al. (1991), Mauro (1995), Bardhan (1997), Haddock (2003), Svensson (2005), and Fisman & Svensson (2007) are but a few of the economic papers calling into question the absolute result of zero tolerance enforcement. For example, as noted by Chow (2012), China is at a substantial disadvantage under the FCPA since there are few non state-owned enterprises in China and the FCPA is primarily designed to address bribery of government officials (p. 1017). This illustrates the thesis of D'Souza & Kaufmann (2013), who concluded that "national governance in the country where a firm operates plays an important role in determining a firm's decision to bribe and how much it pays" and "corruption in procurement is highly prevalent around the world" (p. 360). Grimm (2010) noted the inefficiency imposed on potential mergers and acquisitions of the successor-liability aspect of the new approach to FCPA enforcement. In this regard, the economic treatment of corruption is akin to the transactions cost literature begun by Coase (1960) in which a key point is that it is prohibitively costly to society to eliminate all pollution.

But the alternative viewpoint, that even a little corruption taints the entire system, has proved more influential in foreign policy settings. As early as 1997, more than a decade before the Obama Administration's emphasis on re-interpreting the FCPA, the Organisation for Economic Cooperation and Development (OECD) established a Convention on Combating Bribery of Foreign Public Officials that requires signatory countries to implement laws that apply the Criminalization Approach worldwide.

Multiple Jurisdictions

Van Alstine (2012) explored the possibility of double jeopardy for a firm caught between the U.S. FCPA and the OECD Anti-Bribery Convention. The mere existence of multiple jurisdictions does not necessarily imply double jeopardy under the Fifth Amendment to the U.S. Constitution. As Van Alstine (2012, p. 1332) notes, the U.S. Supreme Court ruled in *United States v. Lanza* (1922) that "two sovereignties … deriving power from different sources …may rule that … an act denounced as a crime by both … may be punished by each" without violating the Fifth Amendment. Furthermore, in *United States v. Balsys* (1998), the Court ruled that prosecution by a foreign government generally does not trigger Fifth Amendment rights in a judicial proceeding in the U.S. (Van Alstine, 2012, pp. 1333-1334, fn. 80). The basis for this decision was the very old Supreme Court decision in *United States v. Furlong* (1820), in which the Court's reasoning gave great weight to offenses which were generally against "the Law of Nations," or "against all, and punished by all." Bennedsen et al. (2011) analysed the rent-seeking that has resulted from uneven distribution of fines and subsidies and concluded that financially-strong firms often try to change laws and regulations while financially-weak firms tend to pay bribes. The conflicts from overlapping jurisdictions, rent-seeking, and departure from rights under the U.S. Constitution led Yockey (2011; 2012)) to characterize the selective enforcement of international commerce laws as making a market in "legalized extortion." This is somewhat reinforced by Zeume's (2017) study using U.K. firms, which found that "Imposing unilateral anti-bribery regulations on some firms benefits their unregulated competitors." Presumably, NPAs and DPAs at least have the potential for use as tools of legalized extortion in selective enforcement of international commerce laws, including the FCPA.

General Cable Corporation

General Cable Corporation was formed in New Jersey in 1927. The firm (or any of the many companies it acquired and/or divested over many years) represented successful government, military, and civilian contracting in some of the most important industrial projects of the last 150 years, including Morse's original telegraph lines, the Statue of Liberty, the Chicago World's Fair, the Transatlantic cables, the Hoover Dam project, and the Olympic Games, to name just a few. Throughout its history, General Cable had acquired companies headquartered in other countries such as France, Germany, Great Britain, Mexico, South Africa, and Spain. By the time of its acquisition of General Cable, Prysmian had already become the world's largest cable manufacturer with its 2011 acquisition of number two-ranked Draka.

The following timeline was taken directly from the company website of General Cable Corporation and its successor, Prysmian Group. Some direct quotes are included and exceptions for other sources are noted.

1927 General Cable is incorporated in New Jersey as the result of a merger between Phillips Wire and Safety Cable Company, Rome Wire Company, and Standard Underground Cable.
1979 General Cable changes its name to GK Technologies.
1981 GK Technologies is acquired by Penn Central Corporation.
1994 GK Technologies is acquired by Wassall PLC, a British Holding Company.
1997 General Cable began public trading on the New York Stock Exchange on Friday, *May 16th*, with the ticker symbol BGC.
1999 *April 7* – General Cable announces its acquisition of BICC Energy Cables. The company subsequently changes its name to BICCGeneral.
2001 *September 6* – BGC announces sale of plant assets in Plano, TX, to Georgia-based Southwire.
2002 *March – May 24* BGC announces plant closings in Illinois and California.
2003 *October 28* – BGC announces plant closing in Taunton, MA.
2004 BGC conducts a feasibility study of further plant closings in the face of declining demand for its telecommunications cable products in the wake of the Dot-Com correction.
2005 *June 15* – BGC announces plant closings in Texas and Connecticut, plant expansion in Massachusetts.
December – BGC acquires Silec Cable (France) for $250 million, Helix/HiTemp for $30 million, and BERU SA (Mexico) for undisclosed amount to form General Cable Automotive.
2006 *June 13* – Chicago Board Options Exchange begins listing General Cable options.
August 31 – BGC acquires E.C.N. Cable (Spain)*.
2007 *April 30* – BGC announces the purchase of NSW (Norddeutsche Seekabelwerke GmbH), a German supplier of offshore cable, from Corning for an undisclosed amount.
September 13 – BGC announces the acquisition of Phelps-Dodge (PDIC) from Freeport-McMoRan Copper & Gold Inc. for $735 million.
2008 BGC acquires majority ownership of a joint venture in Algeria and the Philippines.
2009 *August* – BGC acquires the Gepco brand of studio, stage and broadcast AV cables and cable assemblies.
2010 BGC acquires Phoenix Power Cables (S. Africa), Beru SAS (France), BICC Egypt, invests in a joint venture in Oman, and makes an equity investment in Pakistan Cables. These acquisitions are small enough that they are not noted in the financial press and are not counted as material in affecting stockholder reports.
2012 BGC acquires Delphia, Alcon Cable North America, Prestolite Wire, and acquires majority interest in Procables of Columbia, giving it unprecedented access to markets such as automotive wiring in Latin America.
2014 *March 7* – The last day on which BGC common stock closes above $30 per share.
July 9 – BGC announces a 7 percent cut in its global workforce. September – BGC announces that some of its staff had issued payments to officials of Angola government-owned public utilities, possibly violating the FCPA.
December 11 – BGC announces reduction in workforce in Altoona plant (160 jobs).

2015 BGC common stock closes at its lowest price since August 5, 2003: $6.60 per share.
February 26 - BGC announces that it expects to disgorge $24 million in profits as a result of possible FCPA violations in connection with bribery in Angola.
November – BGC announces plant closings in Massachusetts and Pennsylvania, expansion in Lawrenceburg, KY, manufacturing centre.
December 3 – BGC announces plant closure in Malvern, Arkansas.

2016 *February 10* – BGC announces that it may have obtained in excess of $33 million in profits in potential violation of the FCPA.
July 24 – Prestolite plant in Paragould allegedly to be closed
Sept. 6 – Belden Inc. announces that it has purchased the Gepco brand from BGC.
December 29 – BGC announces that it “has agreed to pay $82.3 million to resolve the U.S. government’s investigation into inappropriate payments to government officials in Egypt, Angola, Bangladesh, China, Indonesia and Thailand.” According to DOJ, between “2002 and 2013, General Cable subsidiaries paid approximately $13 million to third-party agents and distributors, a portion of which was used to make unlawful payments to obtain business, ultimately netting the company approximately $51 million in profits.”

2017 *January 5* – General Cable is sued in U.S. District Court for the Southern District of New York in a class action lawsuit brought by investors under 1934 Securities Exchange Act and subsequent SEC rules for stock price manipulation through bribery in violation of the FCPA (consistent with Westbrook, 2012).
March 15 – General Cable is sued in U.S. District Court for the Eastern District of Kentucky in a class action lawsuit (*Eley v. General Cable Corporation et al*) brought by pensioners of the company under the 1974 federal ERISA statute for artificially inflating stock prices through bribery in violation of the FCPA (Wille, 2017).
March 23 – General Cable is sued in State of Delaware Chancery Court by shareholder Michael Quackenbush for fraud connected with its failure to produce records of improper payments related to the $82 million FCPA claims settlement (Boysen, 2017).
December 3 – BGC common stock closes at $21.80 per share.
December 4 – Prysmian Group, a publicly-held Italian company, announces its planned acquisition of General Cable for $30 per share cash (according to Prysmian, a total of $3 billion) (Prysmian Group, 2017). As expected, General Cable stock closes 35 percent higher at $29.45 per share. Presumably, the stock is slightly discounted from the $30 per share offer because of minor uncertainty that the acquisition will go through. From this point on, the stock trades at $29.15 or higher each day until the acquisition is completed.

2018 *June 6* – General Cable formally becomes a wholly-owned subsidiary of Prysmian Group, an Italian conglomerate, and ceases to trade on the NYSE (Prysmian Group, 2018).

Discussion

Fox (2017) quoted former-Assistant Attorney General Leslie Caldwell’s assessment in a DOJ Press Release:

> *General Cable paid bribes to officials in multiple countries in a scheme that involved a high-level executive of the company and resulted in profits of more than $50 million worldwide. But General Cable also voluntarily self-disclosed this misconduct to the government, fully cooperated and remediated. This resolution demonstrates the very real upside to coming in and cooperating with federal prosecutors and investigators. It also reflects our on-going commitment to transparency.*

Unfortunately, for General Cable, voluntary cooperation with DOJ proved fatal. Not only were executives sued personally by shareholders, the corporation was sued and the DOJ imposed large fines relative to General Cable’s size. Only those shareholders who were able to hold out for Prysmian’s successful offer of $30 per share were able to recover some of their investment. A successful, although struggling, eighty-five-year-old American firm was put out of business through aggressive enforcement of a re-interpreted, controversial, thirty-five-year-old law. It was effectively handed over to a European conglomerate that was formed for the purpose of taking those assets out of the United States. General Cable, which had won numerous quality awards during the last twenty years of its existence, laid off thousands of American employees. The widespread use of secret NPAs and DPAs hardly represents an “on-going commitment to transparency” that DOJ representative Caldwell declared. Instead, it is more akin to moving the goalposts after the game has already started. Where is the “upside” to the DOJ’s actions, after all? Is it likely that a large, European, conglomerate will perform any more ethically than did General Cable in its eighty-year existence?

The price history of General Cable common stock over its last twenty years of existence demonstrates that it experienced periods during which it mirrored the U.S. economy as measured by the S&P 500 Index, as well as periods during which it behaved counter-cyclically. This is shown in Figure 1 below (The S&P 500 Index was rescaled so it could appear alongside General Cable’s common price per share for a fair comparison).

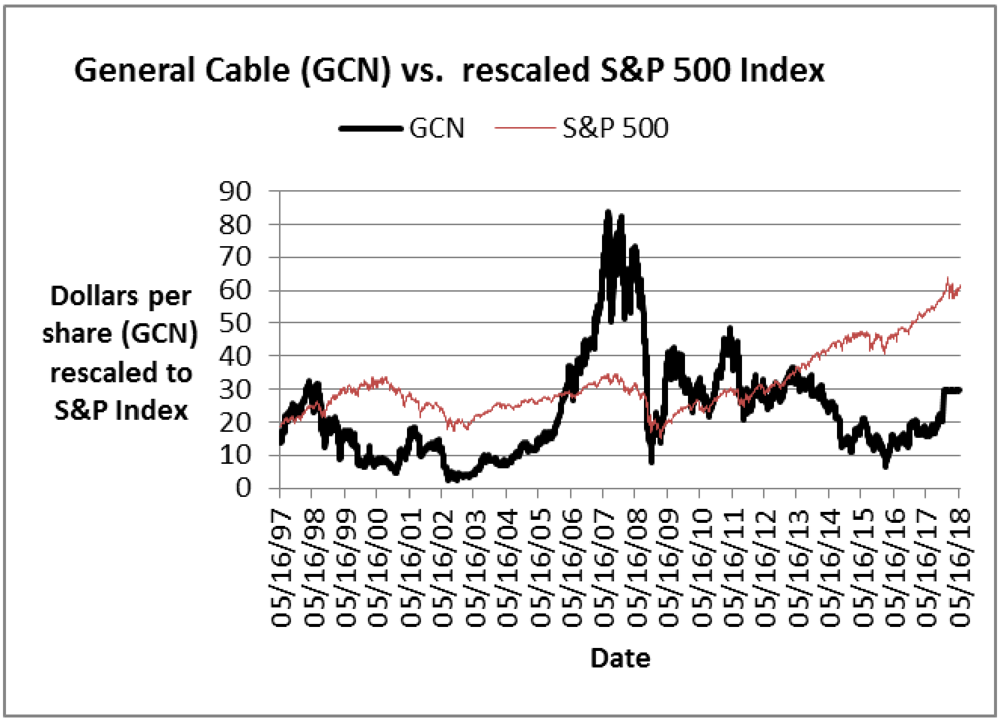

Figure 1: General Cable Common Stock Daily Price relative S&P 500 Index, 1997-2018

What is most striking is that the firm seemed to overcome its sub-par market performance during the period from May, 1998, through May, 2006, just in time to be hit by the Great Recession of 2008-2009. Recovering from recession during the early days of the Obama Administration, General Cable self-reported bribery activity and was never able to recover again. In effect, a large, successful, conscientious (it came forward voluntarily, after all) company headquartered in Kentucky and employing thousands throughout the U.S. was shuttered through aggressive and politicized prosecutorial policy of the U.S. Government. Holm et al. (2017) is among many papers in the regional science literature that try to put dollar amounts to the significant opportunity costs and explicit costs to families and communities when a company such as General Cable is forced to withdraw from a community in which it may be the only substantial employer.

Conclusion

Perhaps the lesson here is that some broken windows are better mended than replaced. The Disclosure Approach, without the subsequent opportunity costs of the Compliance Approach, might have been as effective as the prosecution of General Cable under the FCPA without the attendant millions of dollars of implicit and explicit costs. Rather than destroying a company that self-reported and tried to do the right thing, perhaps the DOJ should have limited its prosecution to those who were solely responsible. Such a signal proves less distortionary to market expectations in labour, output, and financial markets by limiting opportunities for rent-seeking and "legal extortion."

There is perhaps another lesson that should be taken. Drastic revisions in policy tend to have drastic consequences. Larry Kudlow of the Trump administration suggested that the FCPA be abolished. That is extremely unlikely with the White House and both houses of congress in democratic hands for the first time since the heyday of expansive interpretation of the FCPA. With the new Biden administration, some natural questions are "will there be a return to ex post enforcement and will grease payments be treated as bribery?" Perhaps a mid-ground between the Obama administration position of hyper-prosecution of bribery and the Trump administration position of non-prosecution of bribery whatsoever would serve business and stakeholders better, *so long as those subject to the law know the prevailing policy before they are required to comply with it.*

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