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ARTICLES

Cautionary Lessons in Analyzing Foreign Misconduct

How to navigate claims involving potential extraterritorial white-collar crime.

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Despite a recent turn toward economic protectionism in the United States, the global commercial activities of U.S.-domiciled companies continue largely unabated—whether via the operations of foreign affiliates or the commercial trade activities of U.S. producers. International operations have long exposed U.S. companies to commercial claims filed in U.S. courts based on those activities abroad. The successful litigation of these claims requires a deep understanding of the legal environment in those foreign jurisdictions, including the characterization or, conversely, mischaracterization of events abroad by opposing counsel.

The extraterritorial nature of such disputes can pose significant and often unanticipated challenges to commercial litigants and their U.S. attorneys who often are unfamiliar with the language, local norms and customs, and regulatory rules and bodies—not to mention the political, social, and economic milieu—in the foreign jurisdiction required to properly identify, interpret, and ultimately prove the underlying facts. These challenges can be compounded when the underlying behavior involves putative criminal activity in the foreign jurisdiction, potentially subjecting the parties to foreign regulatory and legal authorities ancillary to the U.S. litigation.

In particular, the advent of global anticorruption legislation, accompanied by increased local enforcement around the world, has led to significant overlapping investigations and prosecutions by different governmental authorities and scrutiny from varied regulatory agencies within the foreign jurisdiction. This article identifies and discusses just a few touch points to help U.S. commercial litigators anticipate, identify, and strategize with these international obstacles in mind. Our insights are based on our recent experience with commercial claims filed in U.S. courts that involved alleged criminal activity in several Latin American countries.

Don’t Take Their Word for It

Our recent experience working on disputes in Latin America has reinforced our belief that deep scrutiny of civil complaints and criminal allegations arising from activities in foreign jurisdictions must be thoughtfully analyzed to be understood by U.S. courts. Here are a couple of examples.

> **Tax evasion structures or corruption?** In a merger and acquisition dispute involving the sale of a business, Latin America’s onerous and byzantine taxation rules—from decentralized and variable value-added taxes to complicated labor taxes—can lead to

questionable and misleading third-party invoices. A seller's practices may have been overlooked in high-level or sample-based due diligence but can come into focus once the new owner takes control. Local tax maneuvers in foreign jurisdictions are particularly common in family-owned businesses in which internal controls are not particularly robust. However, many large public and private organizations also engage in or abet tax avoidance or evasion as well. What at first glance may appear to be outright fraud or corruption in an alleged vendor kickback scheme may, in truth, reflect rogue or, alternatively, owner-complicit avoidance of labor, local content, or other local taxes. While the latter is still an issue to contend with in a dispute, it may be the source of a misinterpretation of transactions rather than the more serious legal complication of corruption or fraud. Adequate, country-specific, and experienced investigation will pay dividends.

Reports from foreign government agency audits and reports. Local Latin American governmental bodies and their published investigatory audits and reports can be the source of helpful evidence or seemingly crippling accusations. There may be local, state, or federal governmental institutions in the region that have no direct corollary in the United States. Hence, making a strict comparison to the U.S. regulatory and enforcement landscape can prove difficult and possibly misleading.

For example, Brazil has an audit body called the Tribunal de Contas da União (TCU), or National Accounts Court (if translated literally). Its title is deceiving because it is not a court, nor does it issue legal opinions. Rather, it is a federal accounting institution that audits government contracts of all sizes. The tone, characterization, and legal force in Brazil of its publicly available reports require close scrutiny.

Understanding the role and judicial standing of an agency or tribunal like Brazil's TCU could prove critical when formulating arguments that use its findings of fact or, alternatively, criticize conclusions from it.

Economics and Accounting Issues: White-Collar Investigations and Damages

In addition to the challenges identified above, white-collar investigations into foreign transactions could involve business customs and practices in foreign jurisdictions that may vary from those in the United States. Accordingly, transaction evidence, already less accessible if it is written in a language other than English, is more difficult to analyze.

Further, forms and labeled calculations may vary widely from U.S. practice because of institutional structures such as supply chain value-added taxes or complex regulations. The paper and electronic versions of orders, invoices, payment records, receipts, and correspondence transmitting them, acknowledging them, or replying to them may lead to factual narratives that

are inconsistent with the actual intent of their authors. We have seen transactional evidence grossly misinterpreted by U.S. and other non-native investigators, as a result of their failure to understand the author's intent in the context of local business practices.

In addition, the foreign economic environment may present seasonal variations and business cycles that are different from those in the United States. Depending on their materiality, those differences may have to be separately considered in the course of testing hypotheses about the foreign events and behaviors, and carefully evaluated in relation to the economic environment embedded in the U.S. claims. The implications for investigating liability through event-study statistics or calculating damages from alleged employee or executive negligence, gross negligence, or fraudulent behaviors can either be missed or, alternatively, mask the otherwise discoverable operational or financial effects.

Conclusion

U.S. commercial litigators should be wary of the characterization of events abroad especially when litigants in U.S. courts are faced with the challenge of educating judges and juries with granular explanations based on local circumstances. Awareness of alternative descriptions of those circumstances and experienced investigative vigilance in a search for alternative explanations to corporate or employee behavior, including alleged criminal behavior, may be pivotal to your ability to creatively evaluate your legal strategies involving events in foreign jurisdictions.

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