

March 15, 2018

Elbit Imaging Settles with SEC in First FCPA Resolution of 2018

On March 9, 2018, the U.S. Securities and Exchange Commission announced a settled enforcement action against Israel-based Elbit Imaging Ltd. and its majority-owned indirect subsidiary Plaza Centers N.V., alleging violations of the internal accounting controls and books and records provisions of the Foreign Corrupt Practices Act.¹ Specifically, the SEC alleges that between 2007 and 2011, in connection with real estate projects in Romania and the United States, Elbit and Plaza paid approximately \$27 million to third-party entities “despite having no evidence that these counterparties actually provided any of the contracted for services.”² Without admitting or denying these allegations, Elbit agreed to pay a civil penalty of \$500,000 to resolve the matter.

Factual Allegations

According to the SEC’s Cease and Desist Order (the “Order”), in 2006 and 2011, at the direction of an unnamed high-level executive at Elbit,³ Plaza engaged two off-shore third-party consultants to assist in obtaining approval from the Romanian government to participate in a real estate development project in Romania.⁴ The SEC alleges that Plaza did not conduct any due diligence on either consultant, and that there was no evidence that the consultants provided services relating to the transactions. In particular, the SEC highlighted the consultants’ failure to attend any meetings and inability to provide any evidence of their consulting work. In connection with this real estate project, the SEC alleges that between 2007 and 2012, Plaza paid the consultants approximately \$14 million.⁵

The SEC also alleges that in 2011, in connection with the sale of a portfolio of 47 real estate assets in the United States, Elbit and Plaza—at the direction of the same executive at Elbit—retained a third-party agent, again without conducting any due diligence, and paid that agent approximately \$13 million in

¹ See In the Matter of Elbit Imaging Ltd., Exchange Act Release No. 82849 (March 9, 2018), available at <https://www.sec.gov/litigation/admin/2018/34-82849.pdf>.

² *Id.* ¶ 18.

³ According to the Order, this executive passed away in June 2016. *Id.* ¶ 3.

⁴ The Order does not provide details about the approvals that were sought from the Romanian government.

⁵ The Order does not discuss the size of the Romanian real estate projects. However, in its consolidated financial statements that were filed with the SEC, Elbit estimated the carrying value of these assets (as of December 31, 2015) to be \$461.2 million. Elbit Imaging Ltd., Current Report (Form 8-K), Ex. 99.1 at 49 (March 31, 2016).

commissions after obtaining \$1.428 billion from the portfolio sale.⁶ The SEC further alleges that \$12.75 million of the \$13 million paid in commissions to this third-party agent was subsequently paid to another entity that was beneficially owned by the Elbit executive.⁷ According to the Order, “the documentation supporting the payments did not identify the services that the consultants provided pursuant to the contracts.”⁸

The Order also notes that Elbit’s and Plaza’s internal accounting controls were “deficient,” for “fail[ing] to identify” the payments to the third-party agents and consultants,⁹ but does not provide details about the state of either company’s internal controls. The Order further notes that both companies “mischaracterized” the payments as legitimate business expenses, “even though some or all of the funds may have been used to make corrupt payments to Romanian government officials or were embezzled.”¹⁰ Similarly, the Order does not describe how the payments were actually characterized in Elbit’s or Plaza’s books and records, or why the SEC concluded the entries were “mischaracterized.”

The SEC recognized that, once the conduct was discovered, Elbit self-reported to Romanian and U.S. authorities.¹¹ Moreover, according to the Order, Elbit subsequently conducted an independent investigation of its and Plaza’s business, fully cooperated with the SEC, and implemented revisions to both companies’ internal accounting controls and anti-bribery policies.¹²

Implications of the Resolution

This FCPA enforcement action, the first by the SEC in six months,¹³ reflects a recurring fact pattern that the SEC has been examining more frequently in recent years, *i.e.*, where payments to third-party vendors or consultants have been identified with little or no evidence that the purported services were legitimate and/or actually provided and, yet, there is also insufficient evidence to conclude whether there was actual bribery, embezzlement, or merely poor record-keeping practices. Although the SEC assessed a relatively

⁶ Release No. 82849, ¶¶ 11–17.

⁷ *Id.* ¶¶ 14, 17. The SEC’s Order does not suggest that the funds paid to this entity were subsequently paid to public officials.

⁸ *Id.* ¶ 17.

⁹ *Id.* ¶ 18.

¹⁰ *Id.* ¶ 20.

¹¹ *Id.* ¶ 22. Elbit self-reported to the SEC on March 31, 2016. Elbit Imaging Ltd., Current Report (Form 8-K), Ex. 99.1 at 3, 47 (March 31, 2016).

¹² Release No. 82849, ¶¶ 23–24. The Order does not discuss what, if any, actions the SEC took against the entity controlled by the now-deceased Elbit executive.

¹³ See U.S. Sec. & Exch. Comm’n, *SEC Enforcement Actions: FCPA Cases*, available at <https://www.sec.gov/spotlight/fcpa/fcpa-cases.shtml> (last enforcement action from September 2017).

modest \$500,000 civil penalty, which could be explained by Elbit's inability to pay,¹⁴ this resolution is a reminder that the SEC will use the civil accounting provisions of the FCPA to bring enforcement actions in situations such as this one, even where the evidence might not sustain a charge under the FCPA's anti-bribery provisions.¹⁵ For companies, this settlement highlights several important considerations relating to managing third-party risk: (1) conducting appropriate risk-based due diligence; (2) determining whether third parties are being engaged for genuine and needed services; (3) determining whether the contemplated compensation is commensurate with the services to be provided; (4) ensuring that there is sufficient documentation or other evidence that the contracted services were provided; and (5) approving only those invoices for payment based on proof or reliable confirmation of services.

It is also notable that the SEC's Order is unaccompanied by a corresponding announcement from the U.S. Department of Justice. Given that Elbit self-reported the alleged conduct just as the DOJ's Pilot Program was unveiled,¹⁶ we would expect the matter to have been evaluated under the Program like others that technically pre-dated its rollout.¹⁷ As was the practice under the Pilot Program, under the current Corporate Enforcement Policy, there is a requirement that decisions to decline prosecution will be made

¹⁴ Release No. 82849, ¶¶ 21, 28 (Elbit has been selling its assets and restructuring its debt obligations).

¹⁵ See, e.g., Final Judgment, *SEC v. Oracle Corp.*, No. 12-cv-04310-CRB (N.D. Cal. Aug. 27, 2012) (Oracle Corporation agreed to pay \$2 million to the SEC to settle charges that it violated the FCPA's internal controls and books and records provisions.). In *Oracle*, the SEC did not allege that corrupt payments were made to public officials in exchange for any specific government action or benefit. Rather, the SEC alleged that, at the urging of employees at Oracle's Indian subsidiary, some portions of proceeds owed to Oracle were "parked" and paid to third-party vendors as marketing expenses, and that the parked proceeds "creat[ed] the potential for bribery or embezzlement." Compl., *SEC v. Oracle Corp.*, No. 12-cv-4310, ¶¶ 1, 10–12 (N.D. Cal. Aug. 16, 2012). See also *In the Matter of Cadbury Ltd.*, Adm. Proc. File No. 3-17759 (Jan. 6, 2017); *In the Matter of Las Vegas Sands Corp.*, Adm. Proc. File No. 3-17204 (April 7, 2016); *In the Matter of BHP Billiton Ltd.*, Adm. Proc. File No. 3-16546 (May 20, 2015).

¹⁶ On April 5, 2016, the DOJ introduced the "Pilot Program," which was designed to motivate companies to voluntarily self-disclose FCPA-related misconduct, fully cooperate with prosecutors, and remediate gaps in internal controls and compliance programs. Andrew Weissmann, U.S. Dep't of Justice, Criminal Div., The Fraud Section's Foreign Corrupt Practices Act Enforcement Plan and Guidance (Apr. 5, 2016) (hereinafter, "2016 FCPA Pilot Program Guideline"), available at <https://www.justice.gov/archives/opa/blog-entry/file/838386/download>. On November 29, 2017, the DOJ announced the FCPA Corporate Enforcement Policy, which codifies and builds on the 2016 FCPA Pilot Program. U.S. Dep't of Justice, FCPA Corporate Enforcement Policy 9-47.120 (Nov. 29, 2017), available at <https://www.justice.gov/criminal-fraud/file/838416/download>.

¹⁷ See, e.g., Declination Letter, *In re NCH Corp.*, at 1 (Sept. 29, 2016) (noting that the declination was "[c]onsistent with the FCPA Pilot Program" even though NCH Corp. self-reported before the Program was announced), available at <https://www.justice.gov/criminal-fraud/file/899121/download>; Declination Letter, *In re Akamai Techs., Inc.*, at 1 (June 6, 2016) (same), available at <https://www.justice.gov/criminal-fraud/file/865411/download>.

public.¹⁸ It will be interesting to see if action by the DOJ follows in this matter where there appears to be a clear jurisdictional nexus between certain of the alleged conduct and the United States, there is the apparent knowing involvement of a senior executive (an aggravating factor under the Pilot Program),¹⁹ but there is no definitive evidence—according to the SEC—that bribery exists.

* * *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Mark F. Mendelsohn

+1-202-223-7377

mmendelsohn@paulweiss.com

Alex Young K. Oh

+1-202-223-7334

aoh@paulweiss.com

Farrah R. Berse

+1-212-373-3008

fberse@paulweiss.com

Peter Jaffe

+1-202-223-7326

pjaffe@paulweiss.com

Justin D. Lerer

+1-202-373-3766

jlerer@paulweiss.com

Adam B. Schwartz

+1-202-223-7341

aschwartz@paulweiss.com

Associate H. Bola George contributed to this Client Memorandum.

¹⁸ See U.S. Dep't of Justice, FCPA Corporate Enforcement Policy 9-47.120, at 5 ("Declinations awarded under the FCPA Corporate Enforcement Policy will be made public."), available at <https://www.justice.gov/criminal-fraud/file/838416/download>.

¹⁹ See 2016 FCPA Pilot Program Guideline, *supra* note 16, at 9.