

China Eastern Airlines Case: Ruling and its Implications

On February 1, 2013, the Seoul High Court affirmed the lower court's decision, finding two individuals who bribed the CEO of the Korean subsidiary of China Eastern Airlines not guilty in Korea's first-ever trial under the Act on Preventing Bribery of Foreign Public Officials in International Business Transactions ("FBPA"). This case is noteworthy not only as the first court trial of a FBPA violation, but also for addressing the scope of "foreign public official" for purposes of the FBPA.

1. China Eastern Airlines Case

The CEOs of a logistics company and a travel agency allegedly bribed the CEO of the Korean subsidiary of China Eastern Airlines, requesting more shipments at more favorable freight fees and more flight tickets for sale, respectively.

One of the main issues was whether China Eastern Airlines' CEO constitutes a "foreign public official" under the FBPA.

Article 2 of the FBPA defines "foreign public official" similarly with the OECD Convention on Bribery, encompassing not only government officials but also individuals performing a public function such as employees of government-controlled companies or state owned enterprises.

Specifically, in Article 2(2)(c) of the FBPA, the term "foreign public official" is defined to include:

[A]n executive or employee of a company in which a foreign government contributed more than 50% of the paid-in-capital or with respect to which a foreign government exercises de facto control over its overall management including major business decisions and the appointment or dismissal of its executives (however, this sub-paragraph shall not be applicable if a company conducts business on a competitive basis with other private-sector companies without receiving preferential subsidies or other benefits from the government).

The lower court found that even though there is some evidence to show that the CEO would fall within the definition of a “foreign public official” under the FBPA, the evidence presented did not rise to the level of satisfying the burden of proof. The court, however, did not specify which prong of the above provision the prosecution failed to prove.

On appeal, the prosecution sought to prove that the CEO is a foreign public official for purposes of the FBPA by arguing that the Chinese government exercises de facto control over China Eastern Airlines on the grounds that (i) a company wholly owned by the Chinese government owns more than 50% of China Eastern Airlines’ capital and (ii) the Chinese government appoints and dismisses the CEO of China Eastern Airlines. Furthermore, the prosecution also presented the following reasons for finding that China Eastern Airlines does not conduct on a competitive basis with private-sector companies: (i) the Chinese government is in charge of mergers and spin-offs of the company; (ii) such misconduct as embezzlement by an executive or employee of the company should be reported to the relevant Chinese local governments; (iii) a Chinese government agency monitors the performance of the company; and (iv) the company receives large amounts of government subsidies.

Despite the arguments put forth by the prosecution, the appellate court affirmed the lower court’s holding without providing any additional reasoning. It is regrettable that the appellate court did not provide clearer guidance on this issue.

2. Comparison with the FCPA

The China Eastern Airlines case reveals an interesting parallel between the FBPA and the United States’ Foreign Corrupt Practices Act (“FCPA”) in connection with the scope of foreign public official.

The FCPA defines “foreign official” to include:

[A]ny officer or employee of a foreign government or any department, agency, or instrumentality thereof, or a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.

While it is usually clear what constitutes a government department or agency, the FCPA does not provide guidance on what type of entities are “instrumentalit[ies]” of a foreign government. In general, though, state-owned or controlled enterprises are regarded as “instrumentalities”. Nevertheless, uncertainty remains as to the exact percentage of government ownership or voting rights required to constitute an instrumentality within the meaning of the FCPA.

With regard to this issue, *United States v. Esquenazi*, a recent FCPA case currently on appeal before

the 11th Circuit, sheds some light. This well-publicized case (primarily due to the record 15-year sentence) involves a federal investigation into activities of a company called Terra Communications and its relationship with the national telecommunications company of Haiti (“Haiti Teleco”). The allegation was that Terra’s executives used intermediaries to make illegal payments to Haiti Teleco’s executives in exchange for lower rates and other business advantages. Before the trial, the defense moved to dismiss, arguing that the defendants were not foreign officials and that Haiti Teleco was not an instrumentality of the Haitian government.

Denying the motion to dismiss, the trial court in Miami instructed jurors to consider the following factors in deciding if Haiti Teleco was a government instrumentality under the FCPA:

1. Whether it provides services to citizens and inhabitants of Haiti;
2. Whether its key officers and directors are government officials or are appointed by government officials;
3. The extent of Haiti ownership of Haiti Teleco, including whether the government owns a majority of the company’s shares or provides financial support, including subsidies and tax breaks;
4. Haiti Teleco’s obligations and privileges under Haitian law such as a government-granted monopoly; and
5. Whether Haiti Teleco is widely perceived to be performing governmental functions.

The approach taken by the court implies that not all of the above is required to be met and none of the factors alone would be determinative. The Eleventh Circuit’s forthcoming decision in *Esquenazi* will provide some guidance as to the definition of foreign official in the FCPA and thus should be closely monitored.

3. Implications for Korean Companies and Multinational Companies in Korea

As seen from above, the exact definition and scope of foreign public official is yet to be delineated not only in Korea but also in the United States. Needless to say, the standards should be clarified so that companies who transact business with foreign counterparties can do so without the fear of prosecution. Such uncertainty is further exacerbated when dealing with foreign companies in developing countries that undertake various forms of privatization, making it more difficult to evaluate the degree of government control.

In case of Korea, it should be noted that both the district and appellate courts in the China Eastern Airlines case ruled against the prosecution not because the CEO does not constitute a “foreign public official” but because the prosecution had not met its evidentiary burden of proof showing that China Eastern Airlines was an “enterprise” within the meaning of Article 2(2) of the FBPA. Furthermore,

as the courts acknowledged that “there is some evidence that China Eastern Airlines might be an enterprise within the meaning of Article 2(2) of the FBPA,” it remains to be seen how the Supreme Court of Korea will decide on this issue.

If there is any question regarding the above, please contact us as set out below.

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| ● Taek Rim (Terry) Oh | TEL : 02 316 4020 | E-Mail: troh@shinkim.com |
| ● Myong-Hyon (Brandon) Ryu | TEL : 02 316 4276 | E-Mail: mhryu@shinkim.com |
| ● Seungmin Lee | TEL : 02 316 4639 | E-Mail: smilee@shinkim.com |
| ● Suh-Young (Claire) Shin | TEL : 02 316 1601 | E-Mail: syoshin@shinkim.com |
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