

By Tara Cummins and Louise Pennington

## Meet the New 800 Pound Gorilla

In many countries, bribes are viewed as a practical and accepted means of securing new business. But the consequences of these long-standing practices are changing as the desire for a more equitable business climate becomes a global priority. Internationally, collaborative efforts to detect and deter bribery, collusion, price-fixing, insider trading and other fraudulent practices are on the rise. Increased regulatory investigations and record-breaking settlements have resulted in more than \$1 billion in fines and penalties in the U.S. alone this year, marking one of the most significant periods in anti-corruption history.

Prolific efforts by regulators and increased incentives for whistleblowers indicate a burgeoning sea change in anti-corruption enforcement. Companies must therefore address this evident, growing risk and review strategies accordingly.

## The Tools of Enforcement

### ➤ Legislation

- **The Foreign Corrupt Practices Act of 1977 (“FCPA”)** stands as the most prominent means of enforcement to date. The Act was established to combat illegal bribery of foreign officials and similar activities threatening the integrity of the U.S. business system. The FCPA organizes its enforcement through two means: 1) anti-bribery provisions which prohibit illicit activities and 2) accounting provisions which require accurate record-keeping and controls. Willful bribery violations carry civil and criminal fines and the potential for prison.

The FCPA was mostly dormant until enforcement resurgence began in mid-2000. Recent significant FCPA-related settlements include \$400 million (BAE), \$365 million (Snamprogetti), \$338 million (Technip) and \$185 million (Daimler AG). These represent some of the largest anti-corruption settlements in history, and all signs indicate significant settlements will continue in the future.

While the FCPA does not grant a private right of action, the potential for FCPA-related litigation exists in allegations of fiduciary breach or lack of oversight. In this sense, the FCPA may be seen as a catalyst for additional, downstream responses to corruption.

- **The UK Bribery Act** is broad-reaching legislation that is scheduled to take effect in April 2011. The Act covers active and passive bribery, as well as the failure to prevent illegal activity. Fines under the U.K. statute are unlimited, and violators may be jailed.

Certain distinctions exist between the breadth of the U.K. Bribery Act and the FCPA. Whereas the FCPA applies to bribery of foreign public officials, the U.K. Act encompasses commercial bribery as well. The U.K. Bribery Act has broader territorial reach, encompassing acts occurring outside U.K. borders where the violator is a U.K. resident or business incorporated in the U.K. While the FCPA affords an exception for small “facilitation payments,” these are not a defense under the U.K. Act.

- **International Efforts**

The Organization for Economic Cooperation and Development (“OECD”) Anti-Bribery Convention has been ratified by nearly 40 nations globally. As a result, anti-bribery laws have been established in numerous countries.

While enforcement of anti-corruption abroad admittedly is disproportionate to U.S. and U.K. efforts, international pressure may change the landscape. Consider, for example, a sampling of recent anti-corruption measures that have occurred overseas:

- Liberia recently passed a law that provides a 5% reward for anyone who gives information that leads to public monies being recovered, and offers to transfer employees who fear they may face retaliation.
- Bahrain will establish an office to combat corruption with a hotline for informants.
- Angola, one of the largest oil-producing countries in the world, announced they would pursue legislation to end corruption and embezzlement.
- Nigeria signed a pact with the European Union to combat corruption.
- In February, the U.S and E.U. signed agreements that improve facilitation of cross-border investigations.

The breadth of nations involved in large corruption cases is also significant:

- An Italian company was ordered by a Milan court to pay \$1.1 billion (750 million Euros) in a civil case that followed an unsuccessful criminal bribery case.
- A German truck maker paid a \$223 million fine (150.6 million Euros) by a Munich court for kickback payments in several countries.
- A U.S. telecommunications company agreed to pay \$10 million to settle a corruption case brought in Costa Rica.
- A large U.S. oil company settled an FCPA investigation for \$559 million. The investigation involved authorities in the U.S., France and Nigeria.
- Europe’s largest engineering company paid a total of \$1.6 billion to U.S. and European authorities to settle bribery investigations that spanned nearly 30 countries.

## Why Anti-corruption Efforts Will Increase

### ➤ US Enforcement Will Serve As a Catalyst

A recent report on global enforcement indicates that the U.S. leads foreign bribery enforcements by a three-to-one ratio over all other countries. These efforts appear to be having an impact. Though signatories of the OECD have been lacking in enforcement, recent improvements are showing. For example, the number of “active” enforcing countries nearly doubled last year (rising from 4 to 7) and since the mid-2000s, countries tagged with “moderate” enforcement doubled from 8 to 16.

In comments to the OECD this year, U.S. Attorney General Eric Holder noted that since 1994, the U.S. has repatriated more than \$156 million in proceeds from corruption to victims abroad, and is likely to repatriate an additional \$68 million. He urged countries with little or no anti-corruption enforcement to “deepen their commitment” to global anti-enforcement efforts by dedicating resources and prioritizing prosecutions.

### ➤ Individuals Will Respond to Incentives and Protections

The Dodd-Frank Wall Street Reform and Consumer Protection Act creates incentives for whistleblowers to report corruption. Specifically, the Act offers awards from 10% to 30% of recovered funds for recoveries of more than \$1 million. Potential rewards are considerable. Consider, for example, the recent SEC settlement with Goldman Sachs for \$550 million. Had the incentive provisions been in effect, a whistleblower would have stood to collect a range of \$55 million to \$165 million. It is no surprise, therefore, that response to the whistle-blowing provisions has been immediate and strong, with the SEC said to be receiving ‘a tip a day’ since passage. With \$452 million set aside for bounties, it is reasonable to expect increased allegations of corrupt activities and a commensurate increase in expense for those companies defending themselves.

## Considerations for Your Risk Strategy

The failure to prevent, detect, or adequately respond to corruption within your organization can have severe consequences. Consider:

- **Civil and criminal fines and penalties**
  - FCPA anti-bribery violations: Criminal fines of \$250,000 for individuals, \$2 million for organizations. Civil penalties of up to \$10,000 may apply.
  - FCPA accounting violations: \$5 million for individuals, \$25 million for organizations. Civil penalties of up to \$500,000 for organizations and \$100,000 for individuals may apply.
  - Alternative criminal fines of up to twice the illegal monetary gain may apply if the alternative fine exceeds the maximum FCPA fine.

- **Imprisonment**
  - FCPA anti-bribery violations: Up to 5 years
  - FCPA accounting violations: Up to 20 years
  - U.K. Bribery Act: Up to 10 years
- **Follow-on litigation**
  - In 2010, nearly 30 companies disclosing FCPA investigations have been the subject of follow-on shareholder litigation in the form of either class actions or derivative suits.
- **Disgorgement**
  - Though it is clear that the SEC is using disgorgement increasingly as a tool in FCPA settlements, predicting the amount of disgorgement is an inexact science. A company may consent to an elevated disgorgement figure simply to avoid protracted litigation. This may have significant implications with respect to uninsured costs.
- **Defense costs and settlements**
  - Anti-corruption settlements have reached historic peaks just as global collaboration is beginning. It is therefore reasonable to expect this trend to continue or even escalate. Defense costs associated with anti-corruption activities must be contemplated not only within the course of the investigation, but also with respect to additional investigations or civil actions that may occur.
- **Internal investigations**
  - The price of internal investigations can be substantial, even if the alleged corrupt activity does not involve significant payments. Consider, for example the case of a U.S. industrial services company which disclosed potential investigatory costs of \$3 million surrounding alleged bribes of \$50,000.
- **Reputational damage, lost business and customer attrition**
  - The fiscal loss associated with reputational damage is hard to quantify, but in a challenging global economy, any lost business is particularly painful. As consumers continue to save more and spend less, retaining current clients and customer loyalty is vital to a business.
- **Management Distraction**
  - Management is already substantially burdened with day-to-day operations and what may feel like a leviathan of regulations, responsibilities, and accountability. The time and effort involved in defending or investigating allegations of corrupt activities may detract from other weighty issues.

## How Should You Respond to This Risk?

It is important to re-examine current risk management strategies in light of growing anti-corruption enforcement. Consider these following questions:

- Has your management sent a clear message concerning corruption and behaviors that are prohibited?
- Do policies and procedures to detect and deter fraud and corruption exist as a part of your risk management strategy? Are third parties that your organization may deal with aware of compliance procedures or mandates? Do you distribute training or guidance materials to staff or business associates?
- How would you respond to an FCPA investigation or allegations of corruption? How would your insurance policies respond?

FCPA investigations can be lengthy, expensive, and complicated. In response to the growing trend of anti-corruption enforcement, certain insurance underwriters now offer limited coverage for defense costs. But policy exclusions must be carefully examined to fully understand the extent of your policy's response to an FCPA or anti-corruption scenario. Often internal investigations may not be covered when they are not precipitated by a shareholder demand or government inquiry. Work carefully with your broker to understand fully how your policy is prepared for various scenarios associated with the growing trend of anti-corruption enforcement.

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