MARSH

ACADEMY OF RISK

DEVELOPMENTS IN ANTI-BRIBERY AND CORRUPTION

THE IMPETUS FOR AUSTRALIAN COMPANIES TO TAKE ACTION

SOLUTIONS...DEFINED, DESIGNED, AND DELIVERED.

MARSH & McLENNAN COMPANIES

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INTRODUCTION

The World Economic Forum currently estimates the annual cost of corruption to be more than 5% of the global gross domestic product (equal to US$2.6 trillion); meanwhile the World Bank estimates that in excess of US$1 trillion is paid in bribes per annum.

In recent years, the fight against bribery and corruption involving foreign officials has gathered momentum, and there has been an increase in investigatory activities, as well as enforcements through legislation and prosecution.

Bribery and corruption activities can arise in various aspects of a company's operations – sales, marketing, distribution, procurement, payments, international operations, expense claims, taxes, compliance, and facilities operations.

A major area of exposure is with regards to third party providers (TPPs), which can implicate a company by association. While, in the past, an organisation may have been able to absolve itself from responsibility for the activities of its TPPs, this is no longer an effective defence.

Sales is one specific area where bribery and corruption risks are particularly pronounced, as the pressure to "expedite matters" is strong, such as in cases where approval to market a new product line rests in the hands of an official. In some locations, despite domestic laws against it, bribery may be an expected and common practice as the laws may not be enforced as strongly as they are in the more developed markets.

With growing international trade, particularly in markets where corruption is more endemic and legislative enforcement is weak, the risk exposures for international organisations transacting in these markets are naturally higher. These organisations may be subject to the laws of multiple jurisdictions, such that a single event of bribery can result in multiple offences under the laws of various jurisdictions. For this reason, organisations need to ensure that effective risk management frameworks are in place and that every effort is made to ensure compliance with anti-bribery and corruption (ABC) legislation. In recent years, a number of organisations have been investigated and prosecuted. The fines handed out have constituted a significant percentage of each company's annual turnover, and, in some cases, exceeded them.

THE AUSTRALIAN CRIMINAL CODE ACT OF 1995
(SECTION 70.2)

Section 70.2 of the Australian Criminal Code Act deals with the bribery of foreign officials. The law makes it an offence to bribe a foreign public official, even if the bribe is perceived to be "customary, necessary or required in the situation," and even if there is "official tolerance of the bribe."

It places the responsibility squarely on organisations to ensure their employees do not engage in conduct that constitutes an act of bribery. The onus is on organisations to be familiar with the laws and to be aware of the types of activities that are legal and illegal when interacting with foreign officials. In addition, the offence will apply "regardless of the outcome of the bribe or the alleged necessity of the payment."

Paul Wenk and Jacqui Wootton of legal firm Herbert Smith Freehills (HSF), say: "The Australian Criminal Code takes a broad approach to bribery and corruption. Australian law prohibits the offer or provision of a benefit not legitimately due, if offered or given with the intention to influence a foreign official in the exercise of their duties in order to win or retain business or a business advantage". Wootton adds: "The provision of benefits by or to a third party can also be caught by the law – provided the other elements of the offence exist. In addition, benefits extend far beyond money, and can include items such as scholarships, training, and many other benefits."

In 2010, the penalties for bribery offences under Australian law were increased. An individual perpetrator can now be imprisoned for up to 10 years or fined up to a maximum of A$1.7 million. For a business entity, the fine could be three times the value of the benefits obtained (if these can be ascertained), 10% of the company's annual turnover (in cases where the value of the benefit cannot be ascertained) or A$17 million, whichever is higher.

Under the Proceeds of Crime Act 2002, any benefits obtained through bribery can be forfeited to the Australian government.

In addition, companies should be aware that they may be liable for the actions of their employees and TPPs under foreign bribery laws. This may include circumstances in which there was a tolerance of bribery, or if the company did not create a culture of compliance.

WHAT CONSTITUTES A BRIBE?

For an act to be considered a bribe under Australian law, it must meet the following criteria:

1. The person provides a benefit to another person, offers or promises to provide a benefit to another person, or causes a benefit to be provided, offered or promised to another person.
2. The benefit is not legitimately due to the other person.
3. Step 1 was carried out with the intention of influencing a foreign public official (who may or may not be the other person) in the exercise of the official's duties as a foreign public official in order to obtain or retain business or obtain or retain a business advantage which is not legitimately due.

The offence will apply regardless of the outcome of the bribe or the alleged necessity of the payment.

Paul Wenk says: "It is important for organisations to do their due diligence upfront. This does not just extend to business transactions but it includes due diligence in relation to new employees, in-country agents and new business partners. It is equally important to ensure that the risk management framework that is put in place reflects the level of risk that exists in a specific circumstance."

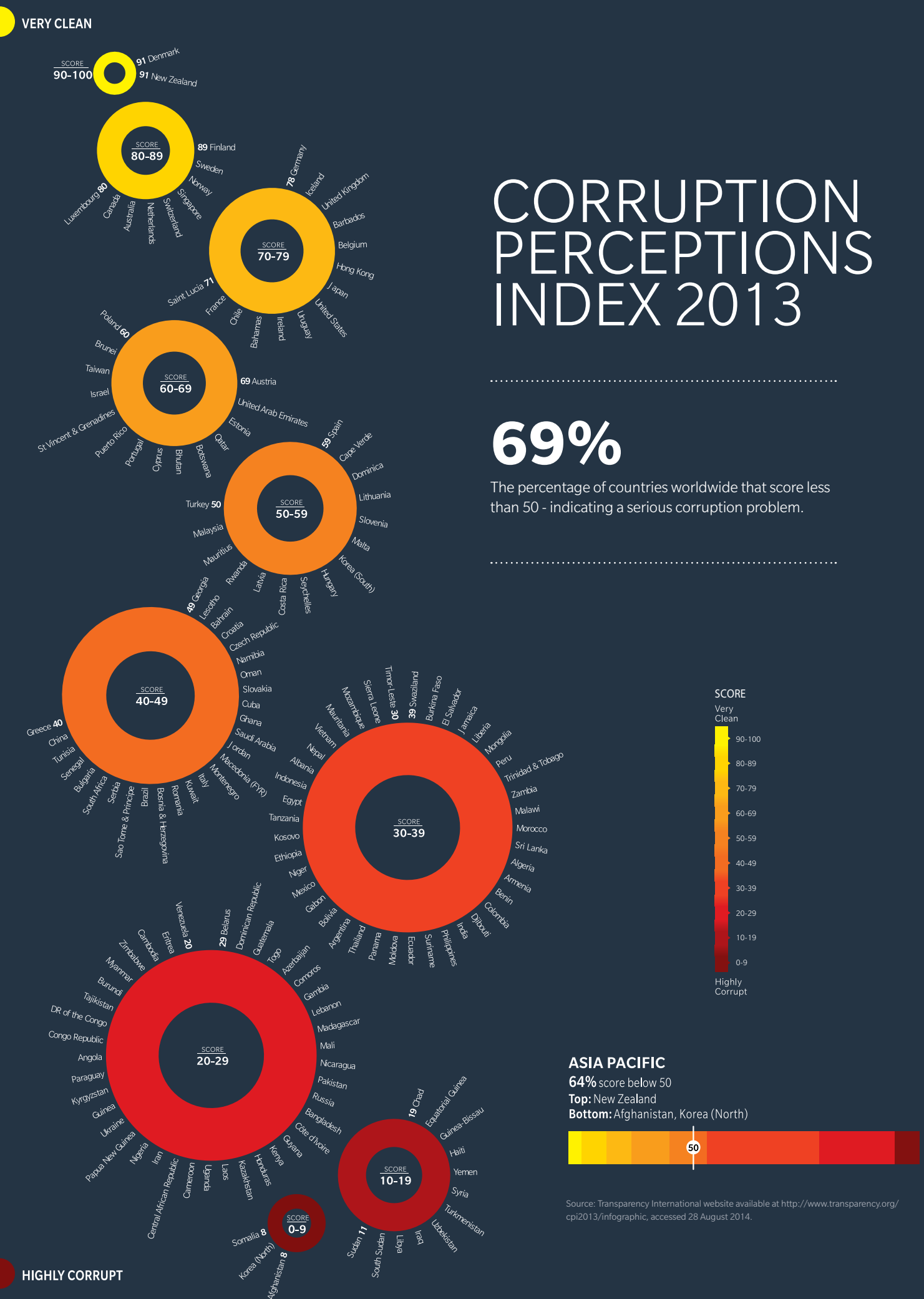
He adds: "It is critical that the benefits offered to third parties – particularly public officials – are consistent with local law and practice, but the overriding consideration must be whether they comply with all laws relevant to the organisation.

One potentially troublesome area of the law is what is called facilitation payments. These are minor benefits provided to expedite or secure performance of a minor routine government function. According to Australian law, if the intent of the facilitation payment was solely to influence the timing rather than influence the outcome (in the latter case it would be a bribe) of the minor routine function, and if the value of the payment was minor, and a proper record made of it, then it would be legal.

However, such conduct may still be illegal under local laws in the country where the payment was made. This invariably creates a confusing situation for companies. The Australian government is currently assessing the possibility of repealing the facilitation payment defence. In addition, the Australian Federal Police (AFP) notes the following in a 2013 fact sheet: "Even if a benefit constitutes a legitimate facilitation payment under Australian law, people making these payments may be liable for bribery under the laws that govern the foreign public official or the laws of other countries, such as the UK Bribery Act. The Australian government recommends that individuals and companies make every effort to resist making facilitation payments."

More than **1 in 4 business people** worldwide believe that they have **lost business** because a competitor paid a bribe.

Source: Transparency International website available at http://www.transparency.org/research/bps2011, accessed 14 August 2014.



CORRUPTION PERCEPTIONS INDEX 2013

69%

The percentage of countries worldwide that score less than 50 - indicating a serious corruption problem.

ASIA PACIFIC

64% score below 50
Top: New Zealand
Bottom: Afghanistan, Korea (North)

Source: Transparency International website available at http://www.transparency.org/cpi2013/infographic, accessed 28 August 2014.

INTERNATIONAL LEGISLATION AND CONVENTIONS

A growing number of countries have been reviewing their laws and regulations and have prosecuted perpetrators in recent times. Australian organisations operating overseas can expect no immunity. An organisation committing an act of bribery or corruption could well face prosecutions in multiple jurisdictions.

Australia is a party to the Organisation for Economic Cooperation and Development (OECD)'s Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (the Anti-Bribery Convention). Australia is also a party to the United Nations Convention Against Corruption (UNCAC). Australia's obligations under these two conventions include making bribery of a foreign public official an offence and prosecuting individuals and companies that engage in it.

Jacqui Wootton of HSF observes that while considerable action is already being taken at a domestic level to combat bribery, there is also growing international cooperation between regulatory authorities and the police: "The Australian Federal Police (AFP) are also a part of an international foreign bribery task force, together with agencies from the UK, Canada and US. Globally and across Australasia, there is increasing focus on instituting or enhancing anti-bribery and corruption laws, coupled with strengthening enforcement and prosecution structures."

Wootton adds there has been increasing impetus in the last five years to identify and prosecute breaches of Australia's foreign bribery laws. In February 2014, the AFP testified in the Senate Estimates Committee that it currently has 13 active investigations underway and 60 dedicated members working on fraud and corruption matters.

The following is a summary of legislative developments in key markets that Australian businesses deal with:

- The anti-bribery provisions of the US Foreign Corrupt Practices Act of 1977, as amended, 15 U.S.C. §§ 78dd-1, et seq. (FCPA) now also apply to foreign firms and persons who cause, directly or through a TPP, an act in furtherance of such a corrupt payment to take place, within the territory of the United States. The FCPA also requires companies whose securities are listed in the United States to meet its accounting provisions. These accounting provisions, which were designed to operate in tandem with the anti-bribery provisions of the FCPA, require corporations covered by the provisions to:

  (a) Make and keep books and records that accurately and fairly reflect the transactions of the corporations, and

  (b) Devise and maintain an adequate system of internal accounting controls.

- Under Section 7 of the UK Bribery Act 2010, a commercial organisation will be liable to prosecution if a person associated with it (which could be an employee or a TPP) bribes another person, intending to obtain or retain business or gain an advantage in the conduct of business for that organisation. However, the Act goes on to state that a "commercial organisation will have a full defence if it can show that despite a particular case of bribery it nevertheless had adequate procedures in place to prevent persons associated with it from bribing." Importantly, failure to prevent bribery is an offence under the act and organisations are criminally responsible for bribes on their behalf by 'associated persons' whether they know about them or not.
- Across Asia, all countries except North Korea have signed the UNCAC. Since then, the majority of countries including China and India have either enacted or made progress towards enacting new legislation to combat the bribery of foreign officials. Countries that have not enacted legislation, such as Hong Kong and Singapore have argued that while bribery of foreign public officials is not expressly referenced in their laws, their existing legislation is broad enough to cover it.

In 2013, a major pharmaceuticals company was investigated by Chinese authorities for paying RMB3 billion in bribes to doctors and government officials. Executives of the company subsequently confessed to offering bribes to boost sales and to raise the price of their company's drugs. As a direct result of the scandal, the company's sales in China reportedly suffered a 61% dive in the third quarter of 2013.

Unless political issues derails it, India in 2014 is expected to pass the Prevention of Bribery of Foreign Public Officials and Officials of Public International Organisations Bill, 2011. Notwithstanding the bill's passing, in 2013, the Central Bureau of Investigation started investigations of a number of Indian military officials and several companies including an Italian based organisation, for participating in a Rs360 crore bribing conspiracy involving the sale of a fleet of helicopters.

WHAT IS A BENEFIT?

A benefit can be non-monetary or non-tangible. It does not need to be provided or offered to the foreign public official; it can be provided or offered to another person. A benefit can also be provided or offered by an agent of the company.

Benefits can take many forms – they can include offers, gifts, promises to give, or authorisation of the giving of anything of value. This could include cash payments, scholarships, travel and entertainment, rebates and commissions, favourable loans, offers to pay off obligations, charitable donations, overpayments, jobs, political contributions, investments, and discounts.

SIEMENS CASE STUDY

IMPLEMENTING BEST PRACTICES AFTER A SCANDAL

The 2006 Siemens corruption scandal was a landmark case that exposed a network of corruption within the multinational company, that spanned across several countries. For years, a considerable number of senior executives had been paying illegal commissions to public servants in these countries, in return for their support in negotiating multimillion dollar contracts.

The investigation that followed, while no different from any other in nature, was one of the largest ever, due to the size and complexity of Siemens' operations. Siemens employed close to 400,000 people, with businesses in 190 countries. The company's products and services were also one of the most diverse, ranging from light bulbs to power plants. The investigation therefore needed to be focused on the business areas that presented the highest risks of corruption.

Siemens commissioned US auditors and consultancies to review its internal measures and investigate what went wrong – a massive project involving 34 markets. As part of the investigation, 1,750 interviews, around 14 million documents, 38 million financial transactions, as well as 10 million bank records were reviewed.[1]

Siemens' measures to institute governance and compliance at the company were nothing less than groundbreaking. In early 2007, Siemens employed a handful of legal experts at corporate headquarters and around 60 compliance officers who performed work in these roles as a secondary activity. Today, several hundred employees work full time as part of the Siemens Compliance Organisation. Reporting lines were streamlined considerably, with the implementation of a global functional reporting structure, whereby all finance officers reported directly or indirectly to the company's CFO, and all legal counsels reporting directly or indirectly to the company's general counsel. The chief compliance officer now reports directly to the general counsel and the CEO.

All employees were issued with a compliance handbook. To help employees report compliance-related concerns, Siemens created a 24-hour hotline and engaged an external ombudsman. The internal audit function at Siemens was streamlined – all audit functions were combined into a single 450 employee unit, called the Corporate Finance Audit (CF A) under the control of a former partner of PricewaterhouseCoopers, who came with extensive international anti-corruption experience. This division instantly initiated a recruitment process for hundreds of qualified auditing staff from outside the company. The CF A also redesigned the internal audit methodology at Siemens, giving weighting to concerns such as financial reporting integrity, risk management, internal control systems, and adherence to compliance.

Internal controls at Siemens were also reviewed, and an interdisciplinary task force was put in place to address weaknesses in controls over the use of funds, bank accounts and IT-based accounting systems, which had earlier contributed to the improper use of Siemens' funds. Perhaps the most important and strategic move to create a culture of compliance within the organisation was the tone set at the top, one which was non-tolerant of future breaches. A corporate disciplinary committee was formed to impose discipline on employees found to have violated anti-corruption laws or company policies.

Although Siemens had for some time already had business conduct guidelines in place, it had to rebuild its compliance processes and culture. Siemens also became a strong public advocate for anti-corruption, committing US$100 million through the World Bank in the fight against corruption via various international non-government organisations. The complexity and extent of the investigation illustrates the challenges inherent in aspiring for a compliance and risk framework that was 100% foolproof.

In a letter to employees, former CEO Peter Löscher stated: "We only do clean business. And only clean business is sustained business. This holds true always and everywhere. Please attend to our clients and our business with this attitude and great commitment. Then we are on the right track."

1 Siemens Press Release, Statement of Seiners Aktiengesell Schaft: Investigation and Summary of Findings with respect to the Proceedings in Munich and the US, Munich, Germany, 15 December 2008.

HOW CAN AUSTRALIAN ORGANISATIONS PROTECT THEMSELVES?

HSF's Paul Wenk emphasises that beyond putting in place the appropriate risk management frameworks, Australian organisations also need to create a culture of compliance, and this starts with senior management.

He adds: "It is critical that company policies and procedures clearly stipulate the kind of conduct that is prohibited, along with mechanisms to identify early the transgressions if these have taken place. Beyond systems and procedures, key performance indicators and remuneration structures must also encourage the right behaviour. Finally, there should be strong and regular communications of the policies and procedures, and the ramifications of non-compliance."

Companies that discover an incident of foreign bribery by their employees or agents face delicate questions about whether to report these incidents. One factor in that equation is that if they don't report they face increased liability and allegations of encouraging a corporate culture that tolerates corruption. Strong awareness of the in-country regulations and a culture of integrity are other important priorities in developing a holistic approach to anti-bribery and corruption.

Even if senior management is fully confident that the risk framework they have put in place can prevent a violation, as businesses become more internationalised, and as they increasingly do work with TPPs, companies' abilities to ensure the integrity and practices of these TPPs are made more difficult. There is also the possibility that a company that has been recently acquired may have violated the law. In addition, the acquired company has its own distributors and TPPs, whose risk management and compliance with regards to ABC may not be of a desirable standard.

Wenk adds: "Increased globalisation, joint ventures, corporate partnerships, public-private partnerships, emerging markets and increased sophistication of international financial arrangements all mean that it is critically important that businesses carry out due diligence of new activities, transactions and markets. This is now a core part of any modern risk management framework."

HOW CAN DIRECTORS AND OFFICERS PROTECT THEMSELVES?

Marsh is often asked to comment on the extent of cover afforded by a client's D&O liability policy for loss, costs, and expenses that may arise out of bribery investigations.

The key types of loss, costs, and expenses that may arise from bribery investigations can be summarised as follows:

- Legal fees and other expenses of a company's directors and officers (both in relation to an investigation, prosecution, or follow-on civil litigation).
- Legal fees and other expenses of the company (both in relation to an investigation, prosecution, or follow-on civil litigation).
- Fines and penalties (civil and criminal).
- Disgorgement of profits.
- Civil recovery orders.

The better D&O liability policies should provide coverage to directors and officers of a company for reasonable costs and expenses incurred in respect of formal investigations by legally authorised bodies and claims which may result from ABC allegations in any jurisdiction worldwide.

Importantly, in today's climate a D&O liability policy should provide cover to a company's directors and officers for:

- Legal representation expenses in relation to investigations.
- Defence costs in relation to prosecutions or follow-on civil suits.
- Civil fines and pecuniary penalties awarded (to the extent insurable at law).

A company itself has far more limited cover in relation to ABC allegations. This is not unusual. Coverage may be available if the allegations form part of (or give rise to) a "Security Entities" claim.

Notwithstanding this, coverage appears to be unlikely in relation to criminal fines and penalties, disgorgement orders, and civil recovery orders. However such restrictions on coverage are common place in D&O insurance on the basis that such losses appear to be uninsurable on public policy grounds and/or would enliven the dishonesty exclusion found in most if not all D&O liability policies.

Please note, that whether or not and to what extent a particular bribery investigation related loss is covered depends on the specific facts and circumstances of the loss and the terms and conditions of the policy as issued.

For further information on how D&O liability insurance can help to reduce and contain the cost and impact of a regulatory investigation, and protect a company's bottom line as well as non-financial loss, please refer to the Marsh report, *Investigations and Outcomes: Managing the Crisis with a D&O Policy.* This paper can be accessed via marsh.com.au or by contacting Marsh on **1800 194 888**.

AUSTRALIA'S FIRST FOREIGN BRIBERY CASE

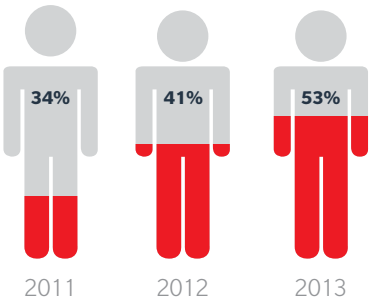
Securency International Pty Ltd, Note Printing Australia Limited, and six of their senior executives were charged by the AFP in 2011 with offences relating to bribery of officials in Malaysia, Vietnam and Indonesia. The charges are the first to be levelled against a company and its employees for alleged foreign bribery acts since Australia's Criminal Code incorporated provisions for it.

The companies had employed commercial agents in pursuing contracts with foreign entities in relation to the printing of national currency. While the case is ongoing, David Ellery, the CFO of Securency, pleaded guilty to a charge of false accounting of a payment to Securency's Malaysian agent. It was alleged that the payment was used for bribes to the Malaysian bank officials to help win a contract to print five ringgit polymer bank notes.

In the context of Ellery and the prosecution agreeing to certain facts, the judge said Ellery had been "acting within the culture which seems to have developed within Securency, whereby staff were discouraged from examining too closely the use of, and payment arrangements for, overseas agents ... The primary motive behind [Ellery's] offending was to assist [his] employer in its commercial activities, by assisting it to gain the benefit of future contracts."[2]

It remains to be seen what the outcome of the other prosecutions will be.

2 R v Ellery [2012] VSC 349



In 2013, **53%** of CEOs surveyed reported being concerned about bribery and corruption

Source: PwC 2014 Global Economic Crime Survey

MARSH RECOMMENDS

There is no "one size fits all" approach to creating an ABC compliance program. Any program needs to appreciate the local landscape and employees must be motivated to behave in an ethical fashion. To facilitate this, integrity and compliance should be values that are embedded in the organisation's mission statement.

Organisations need to be aware of the risk exposures with regards to TPPs. All TPPs engaged by the company should be screened to ensure that they are not associated with politically exposed persons, and there is no evidence of financial instability.

Due diligence for TPPs should include requesting anti-bribery representations and warranties, requiring them to complete ABC training, and to be audited if necessary. TPPs can also be requested to achieve annual certifications of compliance for ABC policies. Subsequently they should be monitored.

While many companies have policies addressing ABC, where they often fail is in the implementation of an awareness program to ensure that employees understand and acknowledge their responsibilities. One way to address this is through mandatory training for all employees, with requirements for them to achieve a certificate of completion on an annual basis.

PRECAUTIONS WHEN APPOINTING A THIRD PARTY PROVIDER:

- Ensure that the TPP is screened for criminal associations, evidence of financial instability and/or improper associations with government entities.
- Have a clear understanding of what service the TPP is being appointed to provide and ensure that the underlying contract ensures that payment terms are appropriate.
- The TPP should provide anti-bribery representations and warranties.
- The TPP should have completed ABC training.
- The TPP should be open to audits being conducted on them.
- The TPP should have achieved an annual certification of compliance with approved ABC policies.
- Ongoing monitoring of the TPP for compliance with approved ABC policies.

Within the organisation, an officer or committee should be designated to be accountable for ABC, with a reporting line to the board. Organisations should regularly perform risk assessments and there should be processes in place for detecting breaches. A risk-based approach to identify the higher risk TPPs may also be warranted.

In the event of a bribery case, a response mechanism should be in place, which includes a proper investigation, evidence identification and preservation, data collection, electronic document reviews, forensic accounting analyses, and interviews, all of which must be documented.

After the investigation, an action plan should be formulated addressing remedial actions against the employee or TPP, potential reporting to external bodies including law enforcement, and if necessary and appropriate, press releases. Additionally, an official response to create internal awareness of the event may be warranted, and existing training and controls may also need to be reviewed for adequacy.

ANTI-BRIBERY AND CORRUPTION RISK MANAGEMENT PROGRAM – KEY AREAS TO ADDRESS:

- What is the "tone at the top" regarding ABC? How is this communicated?
- Is there a documented employee code of conduct in place?
- Are all employees provided with ABC training?
- How does the organisation promote ABC? Are there relevant resources that are available to employees? Does this extend to customers and TPPs?
- What program is in place to monitor transactions and detect potential ABC anomalies?
- To what extent are the whistleblower hotline and other reporting mechanisms for ABC reports utilised?
- How would the organisation respond to an ABC event? What actions would be undertaken, and who would the incident be reported to?
- Who in the organisation is responsible for ABC?
- Are allegations and incidents tracked and is there a regular reporting process for them in place?
- Have the risks of doing business in partnership with joint ventures been carefully considered?
- How are TPPs informed of the organisation's policy on ABC and are they screened for compliance?

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NEXT STEPS

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