



Adequate Procedures: The Relevance of Anti-corruption Legislation to the Private Equity Industry

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Overview

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Part I: Overview

Tone from the Top?

From the political leadership all the way down to local administrations, we are hampered by corruption.

In your countries in Europe, drivers don't automatically pull out their wallets when stopped by a traffic policeman

President Dmitri Medvedev

The Current Landscape

- Newly enacted UK Bribery Act
- Aggressive enforcement of FCPA
- Changes to Russian legislation—while corruption continues to increase
- Private equity firms and portfolio companies increasingly at risk

Part II: How the Laws Touch Russia

The Laws

- Leading foreign laws with global reach
 - US: Foreign Corrupt Practices Act 1977 (FCPA)
 - UK: Bribery Act 2010 (UKBA)
- Various Russian anti-corruption laws
 - Criminal Code of 1996
 - Administrative Code of 2001
 - Code of Administrative Offences of the Russian Federation (“CAORF”)
 - Civil Code of 1994
 - Law on State Civil Service in the Russian Federation of 2004
 - Law on Municipal Service in the Russian Federation of 2007
 - Anti Money Laundering Law of 2001
 - Law on Fighting Corruption of 2008

Foreign Corrupt Practices Act

- The law:
 - Prohibits corrupt payments or transfers of things of value to non-US government officials, directly or through third parties, for the purpose of obtaining or retaining business or a business advantage
- Two parts:
 - Anti-bribery provisions
 - Accounting provisions
- Punishment
 - Fines up to twice illicit gain
 - Prison up to 5 years

UK Bribery Act

- Four offences
 - Giving a bribe (sec 1)
 - Receiving a bribe (sec 2)
 - Bribing a Foreign Public Official (FPO) (sec 6)
 - Failing to prevent bribery (the “corporate offence”) (sec 7)
- One defence to corporate offence
 - Adequate procedures to prevent bribery
- Punishment
 - Unlimited fine
 - Prison up to 10 years

Russian Anti-bribery Laws

- Bribery of public officials:
 - Criminal Code, arts 290, 291, 291(1) and CAORF, art 19.28
 - Giving and receiving, aiding and abetting, banned
 - Recently amended to criminalise foreign bribery
- Commercial bribery
 - Criminal Code, arts 204(1) and 204(2) and CAORF, art 19.28
- No corporate criminal liability
- Punishments:
 - Fine up to 500m rubles
 - Prison up to 15 years

Jurisdiction: US

- FCPA's jurisdiction is wide but relatively simple
 - Acts done in US – very broadly prosecuted (mailings, correspondent banks etc)
 - Issuers (any listing in US)
 - Even after delisting, companies remain covered for 5 years
 - Domestic concerns

Jurisdiction: UK

We intend to adopt an aggressive interpretation of the Act's jurisdictional reach

Chris Walker, SFO Head of Policy

- Corporate offence covers any commercial organisation “carrying on a business or part of a business” in the UK
 - Unlike FCPA, this is entirely untested
- Other offences require a “close connection”
 - Acts done in UK
 - UK citizens and residents

Jurisdiction: UK (cont.)

- Ministry of Justice says this requires a “demonstrable business presence” in the UK:
 - UK subsidiary alone not enough, if it acts “independently”
 - UK listing alone not enough (more than 100 Russian companies listed in the UK)
- But SFO director warns against relying on “over-technical interpretations of the Act” and provides examples of presence:
 - Raising finance (through equity or bonds)
 - Regular business meetings
 - Carrying out corporate functions

How Wide Is it?

- Russian company with British and Uzbeki subs. Uzbeki sub pays a bribe in Uzbekistan. Can Russian company be prosecuted?
 - Probably, unless British sub is “wholly independent”
- British company has Russian sub. Russian sub employs Russian consultant. Consultant pays bribe. Can Russian company be prosecuted?
 - No, not unless it carries on business in UK; mere ownership by a British company is insufficient
- Russian company is listed on LSE, but has no business operations in UK. Can it be prosecuted for bribes in Russia?
 - It depends: Did it raise money in the UK? Does it hold regular business meetings there?

Part III: How Private Equity Firms Are at Risk

Liability for Portfolio Companies

- Successor liability for pre-acquisition FCPA violations
- Possible liability under FCPA and UKBA for violations or benefits that continue post-acquisition
- Portfolio companies may be “associated persons” under UKBA, making PE manager/owner liable for their acts
- Anti-corruption due diligence is critical
 - Proportionality: Tailor due diligence to the business to be acquired and the countries in which the target does business
 - Assess risks of the industry and people involved
 - Identify and address any red flags

Fundraising and Obtaining Business

- Two main areas of potential liability in raising capital or soliciting customers:
 - Payments, offers, gifts, travel or entertainment to employees of state-owned enterprises, sovereign wealth funds or public pension funds for purpose of inducing investments or obtaining business
 - Use of placement agents, consultants, or other third parties to solicit investments or obtain business from SOEs, SWFs or foreign public pension funds
- Because the Bribery Act captures commercial bribery too there is a risk of liability from the same activities with respect to private investors.

Part IV: Foreign Prosecutors' Interest in Russia

SFO Statement of Intent

The most difficult cases will be those involving companies (whether UK or foreign) operating in a range of challenging environments that want to continue to use corruption in order to undermine ethical companies. Our [UK] ethical companies want to see fair competition. They can compete on equal terms because of the quality of what they produce. They cannot though compete properly when there is corruption. They want me to do something about that and I certainly want to do that when the foreign companies are within our jurisdiction. This will be a high priority for the SFO and we should be actively looking for these cases”.

- Richard Alderman, Director of the SFO

SFO and Russia

- Director Alderman has shown particular interest:
 - November 2010: Addresses Anglo-Russian business community
 - March 2011: Speaks at Russia and CIS Summit on Anti-Corruption Conference, Moscow

If you carry on business or part of your business in the UK, then bribery that is committed by somebody in your corporation or by somebody who provides services to your corporation anywhere else in the world is within the jurisdiction of the SFO. It does not matter that this bribery is committed outside the UK and Russia. It also does not matter that the bribery had nothing to do with your UK business presence. All that is needed to trigger the jurisdiction is, as I have said, that you carry on business or part of your business in the UK

- May 2011: Meets Russian Ambassador Alexander Yakovenko
- June 2011: Speaks at US-Russia Business Council, London

The US and Russia

- DOJ investigations involving Russia:
 - August 2011: Deere & Co
 - November 2010: Panalpina
 - August 2010: Hewlett-Packard
 - April 2010: Daimler
- Globally, “FCPA enforcement is stronger than it’s ever been—and getting stronger” (Assistant US Attorney General Lanny Breuer). US government collected more than \$1 billion in FCPA sanctions in 2010

Russia and Russia?

- Lots of legislation
- Russia has joined OECD Working Group on Bribery and is a party to various conventions
- But resources are minimal, and there is no real enforcement

Part V: What You Should Do to Protect Yourself

Compliance Programme

- The Bribery Act provides a defence to the corporate offence: “adequate procedures” to prevent bribery
- Similarly, US and other authorities look to companies’ compliance programmes to determine how to proceed and what punishment to assess
- Ministry of Justice Guidance presents six principles. These distil international best practice

1. Proportionate Procedures
2. Top-level Commitment (“Tone at the Top”)
3. Risk Assessment
4. Due Diligence
5. Communication (Including Training)
6. Monitoring and Review

Best Practice for PE Companies

1. Implement adequate procedures at your company
 - a) Risk assessment
 - b) Policies and procedures
 - c) Training
 - d) Testing
2. Require that majority-owned or controlled portfolio companies implement adequate procedures
3. For minority investments, funds of funds etc, recommend, propose, suggest the implementation of adequate procedures; invoke your contractual rights where necessary

You are not required to do the impossible, but you must do what you can

Thank you!

Questions?

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