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E-ALERT | Anti-Corruption

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THE UK BRIBERY ACT 2010: FOCUS ON PRIVATE EQUITY INDUSTRY

Recent pronouncements by the Serious Fraud Office ("SFO"), the body tasked with enforcing the UK Bribery Act 2010 ("UK Bribery Act"), which entered into force on 1 July 2011, have sought to highlight the exposure that private equity firms face as a consequence of the UK Bribery Act.

Under the UK Bribery Act, companies that do business in the UK will be liable for bribes by "associated" persons -- those performing services for or on behalf of the company -- unless they are able to demonstrate that they have implemented "adequate procedures" to prevent bribery. Unlike the US Foreign Corrupt Practices Act, the UK Bribery Act covers bribes paid in the private as well as the public sectors.

In a speech delivered recently to members of the private equity community entitled "Private Equity and the Bribery Act," Richard Alderman, the Director of the SFO, has made it clear that private equity firms need to ensure that they have implemented adequate procedures to mitigate the risk of bribes being paid on their behalf and for their benefit. Specifically, Director Alderman stated that –

> *[w]e are stressing the responsibility of the owners of companies to ensure proper standards of governance and a proper anti-corruption culture. Owners should not stand aside and say this is nothing to do with them but is an operational issue for the company. It is not. As owners of companies, private equity (as well as the big institutional shareholders) has a responsibility to society to ensure that the companies in which they have a shareholding operate to the right standards. It may even be that it is a condition of investment by fund managers allocating funds to you to invest that you invest only in companies that are FCPA and Bribery Act compliant. This is something you will need to bear in mind. You may also need to look at your exposure * * * if you are directors (whether executive or non-executive) in the companies in which you invest.*

Director Alderman emphasized in the same speech that private equity firms that violate the UK Bribery Act also should be cognizant of their potentially consequent exposure under the UK Proceeds of Crime Act 2002 – the primary UK statute addressing money laundering. According to Director Alderman:

> *[Let me turn to the issue of] your responsibility if any of the companies that you own pays bribes. You might at first think that this is nothing to do with you as the owners of the company. It might be that as portfolio owners you are not committing an offence of failing to prevent bribery. But it does not end there. First of all we will be looking at money laundering in order to see what money has been laundered as a result of the criminal conduct and to whom it has gone. It may be indeed that the owners have some knowledge of the contract that was obtained through bribery. We will be thinking about money laundering.*

Even if there was no knowledge within a private equity firm of the bribery that occurred in a portfolio company, the SFO nonetheless would be able in many instances under the UK Proceeds of Crime Act 2002 to seek to recover from the private equity firm the benefit the firm had realised as a result of the bribery. Director Alderman noted in that connection that –

> *[a] feature of the SFO's work that you may hear about in due course is what happens when something goes wrong and the company gets involved in bribery. The owning company or partners may know nothing about this although they will have received the benefit through dividends or other distribution. We are looking at how we recover the benefit.*
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> *This is something I care about very much because I want to ensure that companies have built a true anti-corruption culture. I am seeing this in many companies at the moment. What I am also seeing is that these companies are ensuring that those who do business with them are also building up that anti-corruption culture * * *.*

Comments

There is no special, or distinguishing, treatment for private equity firms or investors under the UK Bribery Act. However the nature of the private equity industry is such that there are certain special issues and complexities which arise. Within the private equity community, private equity managers making direct investments will likely face the broadest set of issues.

- Apart from issues arising out of ordinary operations, managers will need to focus on UK Bribery Act compliance in the raising of funds, in the sourcing of deal flow, the undertaking of acquisitions and investments and in relation to the operation of the businesses of underlying portfolio companies.
- Buy-out funds, and other funds taking controlling interests in companies, will be most likely to face issues relative to portfolio companies; venture funds perhaps less so.
- Secondary investors and fund-of-funds investors who make use of intermediaries to source deals may need to give particular attention to these arrangements.
- Private equity firms and investors alike will need to review due diligence procedures as well as organise effective compliance programs. With many private equity transactions taking place in a very competitive environment with often demanding time frames, it is especially important to determine appropriate due diligence procedures in advance.

The vast majority of the largest and most sophisticated private equity firms, particularly those operating or investing in the US, already have implemented policies and procedures to address their exposure under the US Foreign Corrupt Practices Act ("FCPA"). Many private equity firms also already have reviewed and updated their FCPA related policies and procedures in light of the UK Bribery Act.

The private equity firms and investors that have not done so already, despite their UK presence or UK related investments, will need to review their existing policies and procedures to take account of their potential exposure under the Bribery Act and other legislation such as the UK Proceeds of Crime Act 2002. The following steps should be undertaken as swiftly as possible:

- Assess your risk - identify the corruption risks that arise by virtue of the nature of your global business activities, portfolio companies and other investments.
- Design and implement an appropriate compliance program or modify an existing program to ensure compliance with the Bribery Act. You will need to pay attention in that connection to the principles set out in the "adequate procedures" guidance issued recently by the UK Ministry of Justice. As part of that process, private equity firms should --
  - seek to identify the bribery related risks that actually are facing as a result of their operations and the operations of portfolio companies;
  - develop targeted approaches to mitigating such risks;

- develop an appropriate due diligence program for use in connection with proposed acquisitions and investments;
- review commercial agreements with third parties (such as intermediaries) whose actions may create liability for them;
- develop a clear policy for dealing with bribery related issues that have been reported to them, whether the information comes from a whistleblower or some other source;
- make sure that those within the firm that can affect the firm's bribery related risk profile understand their legal responsibilities and the firm's expectations of them; and
- periodically reevaluate their bribery related policies and procedures to ensure that they are, and will be deemed to be, fit for purpose in the event their adequacy is called into question.

Covington has developed a large and sophisticated cross-office practice relating to bribery and other related forms of corruption. Our experience includes designing compliance programs for individual companies, investigating possible wrongdoing and conducting compliance GAP analyses with the goal of identifying deficiencies in the policies and procedures individual companies have implemented to ensure compliance with measures such as the US Foreign Corrupt Practices Act, UK Bribery Act 2010 and companion measures in other countries.

Approximately 25 Covington lawyers -- working from our offices in Beijing, Brussels, London, New York, San Francisco and Washington -- spend all or a very substantial part of their time working on bribery related matters. Our lawyers in London include Robert Amaee, until January of this year the Head of the Anti-Corruption and Proceeds of Crime Units at the UK Serious Fraud Office. Robert joined a group of lawyers in our London office who already had been widely recognized for their anti-bribery expertise.

Covington's anti-bribery lawyers work closely with lawyers in the firm's private equity and funds practices in assessing the particular needs of private equity clients.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our white collar group:

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