Hogan Lovells Newsletter

An Annual Reminder:
United Kingdom's First Deferred Prosecution Agreement and United States' Recent Enforcements Underscore Risks Associated with Third Parties

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The Risks associated with Third Party Intermediaries

The UK's recently announced Deferred Prosecution Agreement (**DPA**) between Standard Bank plc (**Standard Bank**) [1] and the Serious Fraud Office (**SFO**) is an unequivocal and timely reminder to companies operating around the world of the significant risks posed by third-party service providers and intermediaries.

All commercial organisations, regardless of their size, use third parties to obtain business opportunities, retain customers, and provide services on a regular basis. This is often due to needing a physical presence in far flung places or because third parties possess key contacts in particular territories.

However, this comes with significant risk. Under English [and U.S.] law the actions of a third party contractor or agent can give rise to liability for the person who contracted the services. Indeed, the SFO [and the DOJ] recently reminded us that, while there are often good reasons for appointing local agents or third parties, prosecutors are aware that the model is frequently used to perpetuate or hide corruption.

The DPA, the first of its kind in the UK, and other similar resolutions in the United States, demonstrate how costly mistakes in dealing with third parties can prove to be. Nevertheless, they also highlight the potential benefits that can be gained if a company takes steps to conduct internal reviews, make self-disclosures, and effectively remediate compliance gaps.

The UK's First DPA

The DPA relates to bribes paid to a third party by Stanbic Bank Tanzania Ltd (**Stanbic**), Standard Bank's sister organisation, contrary to section 7 of the UK Bribery Act 2010.

[1] Now known as ICBC Standard Bank plc

The UK Bribery Act imposes strict liability on companies that fail to prevent persons associated with them paying bribes.

As Stanbic is Standard Bank's sister organisation there is no question that it would be considered an 'associated persons'. However, it is important to remember that the definition of 'associated persons' can extend to any person that performs services for or on behalf of a company; and can, therefore, include suppliers, distributors and licensees. Agents will almost always constitute associated persons.

It is a defence to show that "adequate procedures" were in place to prevent bribery.

In the case of Standard Bank, it is unlikely that the bank would have been able to avoid liability. As a result, it applied to the SFO for a DPA, which ultimately required it to pay a fine of US$32.2 million and implement improvements in its compliance systems.[2]

Background to the Standard Bank DPA

The issue arose as part of a sovereign note placement by the Government of Tanzania to support its Five Year Development Plan which was designed to substantially increase Tanzania's growth.

In February 2012 Stanbic (together with Standard Bank) offered to act as manager for the fundraising.

However, the deal lost momentum and did not progress until September 2012, by which time Stanbic had brought in Enterprise Growth Markets Advisors Limited (**EGMA**), a local Tanzanian organisation. Upon EGMA's inclusion, the deal progressed, and the banks' fees increased by approximately $7.7million (much of which was to take account of the $6milion that Stanbic agreed to pay to EGMA).

[2] Standard Bank has also been fined by the U.S. SEC.

According to the facts of the DPA, however, EGMA did not provide any recorded services to either Stanbic or Standard Bank; and, as a result, the only inference that the SFO and the court could draw from the arrangement was that the payment to EGMA constituted a bribe.

EGMA's Relationship with the Government

The SFO's suspicion was no doubt heightened when prosecutors looked into the third party further. EGMA's managing director had been chief executive officer of the Tanzanian Capital markets and Securities Authority until 2011; and the its chairman (and one of its three shareholders), Mr Kitiliya, was the Commissioner of the Tanzania Revenue Authority which advises the government on financing needs and is the main fiscal agency in the country.

Indeed, Mr Kitiliya was so closely connected to the deal that he was actually a part of the government team dealing with the fundraising and made calls to potential investors on behalf of the government.

It is clear that both individuals were likely to be considered public officials, and that there was significant scope for bribery risk.

Inadequate Due Diligence into Agent and Corporate Failings at Standard Bank

Despite obvious bribery red flags and the fact that Standard Bank knew little about EGMA or its role in the deal, the bank failed to either: conduct proportionate or sufficiently targeted due diligence into EGMA; or instruct Stanbic to do so on its behalf.

According to the SFO, the bank's internal policies were unclear on whether it needed to undertake its own due diligence in a situation where it wasn't party to any contract with a third party, and where Stanbic had conducted some limited due diligence into the third party.

It is clear that Standard Bank did not provide the deal team with adequate training on the policies to follow when dealing in high risk jurisdictions, through a sister organisation.

The failings were not limited to pre-contractual issues.

In March 2013, Stanbic paid EGMA roughly US$6million. There is no evidence that the Standard Bank insisted that Stanbic include contractual time limits on EGMA's ability to withdraw the funds, or required EGMA to certify how the funds were spend.

Within 10 days of Stanbic's payment, the vast majority of the $6million had been withdrawn in cash. The cash withdrawals prevented Standard Bank, or prosecuting authorities from any further tracing the monies.

Why a DPA?

The SFO has made it clear that DPAs will not be considered standard practice, and that they will only be applicable where a company can demonstrate that it is an "honest business wanting to trade legally."[3] Indeed, in September 2015 David Green, the Director of the SFO, reminded companies that prosecution was the SFO's preferred option for dealing with bribery and corruption.[4] [5]

Standard Bank was offered a DPA as a result of the actions it took upon discovering the bribes, and its genuine cooperation with the SFO. Such cooperation included: prompt and fulsome self-reporting to the SFO, conducting a detailed internal investigation into the actions of Stanbic (in parallel to the SFO's own investigation), disclosing internal interviews and facilitating the further interviews of employees by the SFO, and providing timely and complete responses to requests for information.

U.S. Parallels

The Standard Bank DPA closely mirrors recent actions taken by the Department of Justice (**DOJ**) and Securities and Exchange Commission (**SEC**) when investigating bribes or improper payments made by third-party agents. Indeed, Standard Bank itself agreed to pay $4.2 million to the SEC as part of a global settlement with US and UK authorities related to the matter at issue here.

In 2015, DOJ resolved two significant corporate FCPA matters, both of which arose from the use of third-party agents. In June 2015, it reached a Non-Prosecution Agreement (**NPA**) with IAP Worldwide Services Inc. (**IAP**) related to conduct in which IAP used a third-party agent to pay Kuwaiti government officials in order to secure a contract to provide surveillance capabilities.

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[3] Ben Morgan, Joint SFO Head of Bribery and Corruption, to the Managing Risk and Mitigating Litigation Conference, 1 December 2015

[4] David Green to the Cambridge Economic Crime Symposium, Jesus College, 7 September 2015

[5] In practice, this assertion may be the result of pressure from non-governmental organisations to ensure that large corporates cannot avoid prosecution by simply paying a fine. Nevertheless, under English law DPAs have to be approved by the court and in his judgment approving the DPA, Lord Justice Leveson made clear that the court would not approve a DPA where it felt that prosecution was more just or where a company had not offered the SFO fulsome cooperation

Due to a variety of factors, including IAP's previous cooperation and a promise of continued cooperation and remediation, DOJ agreed to this NPA. Publicly available materials do not confirm whether IAP self-reported the conduct, although references to its past cooperation suggest that self-disclosure likely occurred.

In July 2015, DOJ and Louis Berger International Inc. (LBI) agreed to a DPA arising from its use of third-party vendors to pay so-called "commitment fees" and "counterpart per diems" to officials in Indonesia, Vietnam, Kuwait, and India in order to secure government contracts. In agreeing to a DPA, the government explicitly referenced LBI's self-disclosure of the conduct, its cooperation and remediation, and its assurances of an ongoing commitment to improve its compliance program and internal controls.

Advice for Companies

It is clear that Standard Bank failed to adopt adequate procedures to prevent bribery. In order to ensure that companies can best avoid incurring liability as a result of the actions of agents, and to ensure that they can best defend themselves against an FCPA or UK Bribery Act action, they should:

1. Have clear, specific policies which deal with the unique risk posed by agents (particularly where agents are contracted through a subsidiary or a sister organisation).

2. Ensure that policies are reinforced through regular communication and training.

3. Always conduct due diligence into agents and never rely exclusively on due diligence undertaken by other organisations over which no control or oversight is exercised. Such due diligence can be proportionate to the risks faced, but that means in certain countries extra, even costly, enquiries must be made.

4. Document the services provided by agents and question the use of agents that provide no material services.

5. Ensure that agency contract terms are reasonable, appropriate, and consistent with fair market value.

6. Remember that transparency on ownership is crucial; and require all agents to confirm that neither their shareholders, nor their directors, employees, or investors are public officials or related to public officials, and to affirm that the agent is aware of and will comply with relevant anti-bribery laws.

7. Remember that these procedures and diligence are an ongoing responsibility. Companies should remain engaged and actively supervise and monitor the actions of the agents, including periodic updates to due diligence and compliance certifications.

Even companies who follow the above steps may unavoidably encounter concerns about the activities of their agents. As the 2015 resolutions with Standard Bank, IAP, and LBI reflect, however, if a company self-identifies potential misconduct, it will want to consider the benefits of an internal investigation and possible self-disclosure to relevant authorities. While an internal investigation and self-disclosure can be time-consuming and costly, it may also allow the company to avail itself to DPAs, NPAs (in the US), or other resolutions which will avoid significantly more costly prosecutions.

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