Published in issue 122 of the Journal of the British Insurance Lawyers Association

The Bribery Act 2010: implications for the insurance industry

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Introduction

On 1 July 2011 the UK Bribery Act 2010 (the ***Act***) comes into force. It will replace the old patchwork of bribery offences with four new statutory bribery offences. In March 2011 the Ministry of Justice published guidance to assist commercial organisations in relation to the procedures they should put in place to prevent bribery (the ***MOJ Guidance***). At the same time the Serious Fraud Office (***SFO***) and Director of Prosecutions published guidance on the manner in which the Act will be enforced (together, the ***Prosecutorial Guidance***). With the publication of this guidance, the new UK anti-bribery landscape is complete.

This article explains the key provisions of the Act and considers its implications for the insurance industry. It covers:

- The three new 'primary' bribery offences created by the Act;
- The new corporate offence of failing to prevent bribery;
- The implications of the Act for the insurance industry in connection with (i) improper payments (ii) the use of coverholders and introducers to procure business (iii) commission arrangements and (iv) corporate hospitality; and
- Conclusions.

2. The Three Primary offences

The Two General Bribery Offences

The Act creates two general bribery offences of:

- Offering, promising or giving a bribe to another person (section 6); and
- Requesting, agreeing to receive or accepting a bribe from another person (section 2).

A bribe is defined, in summary, as a financial or other advantage given or accepted with the intention to induce or reward 'improper performance' of a 'relevant function or activity' (or given in circumstances where the acceptance itself constitutes improper performance of such a function or activity).

A 'relevant function or activity' is, in summary, a function or activity which is:

- Of a public nature, connected with business, performed in the course of a person's employment or performed by or on behalf of a body of persons; and

- Expected to be performed in good faith or impartially, or where the person performing the function or activity is in a position of trust by virtue of performing it. In determining what is expected, the test is what a reasonable person in the UK would expect in relation to the performance of the function or activity in question.

In the insurance sector, it is likely that, (by way of example):

- A placing broker will be treated as performing a 'relevant function or activity', because such a broker is performing a business function and has, in English law, a duty of loyalty to the insured.
- Employees of the insured responsible for deciding what insurance to buy will be treated as performing a 'relevant function or activity'. This is because they perform that activity in the course of employment, and would be expected to perform the function impartially in the best interests of their employer.

'Improper performance' of a 'relevant function or activity' will occur where the function or activity is performed in breach of the expectation of good faith or impartiality, or in breach of an expectation arising from the position of trust. For example:

- If an insurer pays an employee of an insured to place business with it, that payment will constitute bribery. This is because it will have been made with the intent to procure the performance of the employee's duties in breach of the expectation that he would act impartially in the best interests of his employer when deciding which insurer to place business with.
- If a placing broker asks an insurer to make a secret payment to it in consideration of the broker placing business with the insurer, that request will constitute bribery. This is because the request will have been made with the intent to perform the broker's duties improperly by accepting a secret commission to place business contrary to the broker's duty of impartiality.

Bribing A Foreign Public Official

The third primary offence created by the Act is of bribing a 'foreign public official' (section 6). The offence is of:

- Offering, promising or giving a financial or other advantage to a 'foreign public official' (or to another person at a foreign public official's request or with such an official's consent or acquiescence);
- With the intention to influence the 'foreign public official' and obtain or retain business or a business advantage in circumstances where the written law applicable to the foreign public official does not permit or require the foreign public official to be so influenced.

The term 'foreign public official' is broadly defined as any individual who holds a legislative, administrative or judicial position in a country outside the UK, or who exercises a 'public function' on behalf of such a country or any public agency or enterprise of such a country[1]. The term 'public function' is not defined in the Act. However, the Commentary on the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which section 7 of the Act implements, provides helpful clarification. It states that a public function is "*any activity in the public interest, delegated by a foreign country, such as the performance of a task delegated by it in connection with public procurement … an official of a public enterprise shall be deemed to perform a public function unless the enterprise operates on a normal commercial basis in the relevant market, i.e. on a basis which is substantially equivalent to that of a private enterprise, without preferential subsidies or other privileges."* This suggests that, for example, any employee of a state owned insurance company with an insurance monopoly (such as exist in many developing countries) will be a 'foreign public official' for the purposes of the Act.

Jurisdictional Reach of the Three Primary Offences

An individual or a company can be liable for any of the three primary offences if the relevant act or omission either takes place:

- In the UK; or
- Outside the UK, if the defendant has a 'close connection' to the UK. A person will have such a connection if, in summary, he is a British resident or citizen or an overseas British citizen[2], or in the case of a UK company.

Penalties for the Three Primary Offences

The three primary offences carry a maximum penalty of 10 years' imprisonment (for individuals only) and/or an unlimited fine. In England a company will only be liable for the primary offences if the offence is committed by a person who is the 'directing mind and will' of the company (usually a senior executive). Where an offence under sections 1, 2 or 6 is committed by a company with the 'consent or connivance' of such a senior officer, section 14 of the Act provides that the senior officer can also be personally criminally liable for the offence.

Historically prosecutors have struggled to convict companies using the 'directing mind and will' test as English criminal law makes it very difficult to attribute acts of employees to companies. Therefore the primary concern for companies is likely to be the new corporate offence under Section 7.

3. The corporate offence of failing to prevent bribery

The Corporate Offence

Section 7 of the Act introduces a new offence for corporates of 'failing to prevent bribery'. This is the most significant departure from previous law in the Act. A company will

commit the offence if an 'associated person' bribes another person in order to obtain or retain business or a business advantage for the company. A bribe will be treated as having been made where the section 1 or 7 offence has been committed, or where it would have been committed if the Act had no jurisdictional restriction.

Jurisdictional Scope

The new corporate offence applies not only to UK incorporated companies, but also to corporates 'carrying on business, or part of a business, in the UK'. The Act does not define the meaning of this phrase. The MOJ Guidance anticipates that whether a business is carried on in the UK is a question of fact and that "*organisations that do not have a demonstrable business presence in the UK*" will generally not be caught.

In practice, this means that a non-UK broker or insurance company which carries on business in its own right in the UK (e.g. through a branch, office or agency) will be likely to be caught by Section 7. A foreign insurance company which underwrites UK risks and attends meetings in the UK in connection with such risks may also be caught, even if it has no UK branch, office or agency, on the basis that as a matter of fact part of the company's business is carried on in the UK.

Many non-UK brokers and insurers have UK subsidiaries. The MOJ Guidance clarifies that, if a UK subsidiary is performing the same role as a branch or agency on behalf of a non-UK parent company, this may bring the parent within the scope of Section 7, depending on factors such as how the subsidiary operates and is managed. However, the presence of a UK subsidiary should not mean that the parent company (or its affiliates) are automatically 'carrying on business or part of a business in the UK'. The MOJ Guidance also clarifies that the listing of a company's securities in the UK should not, of itself, make a company subject to section 7.

Foreign insurers and brokers should exercise caution before concluding that they are not subject to section 7 of the Act. The Director of the SFO has warned that "*companies should not rely on over-technical interpretations of the Act*"[3]. If the SFO believes that a UK insurer or broker has been disadvantaged because a non-UK competitor has paid a bribe, it may well adopt a wide approach to the interpretation of 'carrying on business or part of business in the UK' in order to create a level playing field.

Meaning of 'Associated Persons'

A person is associated with a company if that person performs services on its behalf. A broker or insurer's employees will be presumed, unless the contrary can be shown, to be an 'associated person'. However, 'associated persons' are not limited to employees. Agents who act on behalf of companies will also be 'associated persons'. For example:

- Coverholders who issue policies on behalf of an insurer or introducers who procure business for a broker are likely to be 'associated persons' of the relevant insurer or broker for the purposes of the Act. Third party loss adjusters or claims handlers may also constitute 'associated persons'.

- Subsidiaries that perform services for an insurer or broker which is subject to section 7 of the Act will be treated as 'associated persons', although the MOJ Guidance makes clear that a subsidiary will not automatically be treated as a person associated with a parent company for the purposes of the Act.
- A joint venture (***JV***) operating through a separate legal entity may constitute an 'associated person'. The MOJ Guidance confirms that JV members will not necessarily be liable because they benefit from a bribe through their investment in the JV, although they could be if a bribe was to benefit their specific business. The MOJ Guidance suggests that the degree of control exercised over a JV will be relevant in deciding whether a person who paid a bribe in the conduct of the JV business was "*performing services for or on behalf of a participant in that arrangement*".

Penalties

The corporate bribery offence is punishable by an unlimited fine. The Government has confirmed that companies convicted of bribery will be subject to discretionary disbarment from tendering for Government contracts[4].

The Adequate Procedures Defence

The only defence available to the company where bribery has been committed by an 'associated person' is to prove that it had adequate procedures in place designed to prevent those associated with it from undertaking such conduct. The company bears the burden of proving that its procedures were adequate.

The Act requires the Secretary of State to publish guidance on the procedures that companies can put in place to prevent bribery. This is contained in the MOJ Guidance, which expands upon 6 principles:

- **Proportionate Procedures:** A company's procedures should be proportionate to the bribery risks that it faces, the nature of its activities and should be clear, practical and effectively implemented and enforced.
- **Top Level Commitment:** The senior management of a company must be committed to preventing bribery by persons associated with it and foster a corporate culture in which bribery is not tolerated.
- **Risk Assessment:** A company should undertake periodic, informed and documented assessment of the nature and extent of its exposure to bribery risks by its associated persons.
- **Due Diligence:** A company should apply due diligence procedures to its associated persons to mitigate the risk of bribery.
- **Communication and Training:** A company should ensure its anti-bribery procedures are embedded through communication and training.

- **Monitoring and Review:** A company should monitor and review its anti-bribery procedures regularly, making improvements where required.

4. Implications of the Act for the Insurance Industry

The Act poses two challenges to insurers and brokers subject to it:

- The first is to re-evaluate their business practices in the light of the Act by considering what bribery risks they entail, and deciding how those practices should be adjusted. Insurers and brokers should not assume that, because they are subject to the US Foreign and Corrupt Practices Act (***FCPA***) and have implemented a global FCPA compliance programme, they need take no further steps in the light of the Act. The Act is in certain respects significantly broader than the FCPA. For example, the FCPA is concerned only with public sector bribery, while the Act also covers private sector bribery.
- The second is to put procedures in place to ensure that their 'associated persons' comply with the decisions made about business practices. This is not only to maximise the strength of an 'adequate procedures' defence in the event that a bribe is paid by an one of their 'associated persons', but also, more importantly, to reduce the risk of bribes being paid in the first place.

We have considered below some practices in the insurance market which brokers and insurers may need to consider as they respond to these challenges.

Improper Payments

Insurers and brokers operating in countries with a high perceived risk of bribery[5] are likely to face requests to make payments to companies or individuals other than their contractual counter-parties and clients.

Even before the Act, such payments involved a very high risk of bribery. Last year Julian Messent, a former reinsurance broker at PWS, was imprisoned for 21 months under the Prevention of Corruption Act 1906 (one of the Act's predecessors). He was convicted of making or authorising corrupt payments of almost US$2 million to officials in the Costa Rican national insurance and electricity and telecommunications companies. The payments were made for the purpose of ensuring that PWS was retained as broker for the reinsurance of the electricity and telecommunications provider's insurance policies from the national insurer to the London market. Had those payments been made when the Act was in force, PWS would have been criminally liable for Mr Messent's actions under the new corporate bribery offence unless it had adequate procedures to prevent such payments.

Brokers and insurers will therefore need carefully to examine their employee training programmes to ensure that staff are able to identify and reject requests for inappropriate payments, and ensure that their internal payment authorisation processes act as a robust second level of protection against such payments being made.

Use of Introducing Agents and Coverholders

Some insurers and brokers use agents to help them procure business. This practice is common in areas such as the Middle and Far East, where local connections are often seen as crucial in doing business. There is nothing inherently improper in such arrangements. However, they involve a risk that the agents will pay bribes to procure business for the broker or insurer for whom they act, giving rise to criminal liability under the new corporate offence.

This risk is illustrated by the enforcement action taken by the FSA against Aon in 2009. Aon was fined £5.25 million for failing to take reasonable care "*to establish and maintain effective systems and controls for countering the risks of bribery … associated with making payments to … overseas third parties who assisted Aon in winning business from overseas clients, particularly in high risk jurisdictions*"[6].

Following the action against Aon, the FSA undertook thematic work on commercial insurance brokers' anti-bribery systems and controls, focusing in particular upon the risk of illicit payments being made through third parties. In the report setting out the results of its work[7] the FSA recommended that firms should:

- Undertake appropriate due diligence on agents (particularly in countries with the highest risk of bribery);
- Ensure that payments to agents are commensurate to the services provided;
- Ensure that payments due to an agent are made only to that agent (and not to some other person on the agent's orders without appropriate investigation);
- Regularly review relationships with third parties to ensure that their risk profile and the nature of the service they provide have not changed; and
- Maintain records of the third parties they use and the due diligence and periodic reviews conducted.

Insurers or brokers using agents to procure business should have careful regard to this guidance. Agents used to procure business are likely to be treated as 'associated persons' of brokers and insurers for the purpose of the Act. In the event such agents pay bribes to procure business, a failure to comply with the FSA's guidance may well (notwithstanding that is does not have formal status under the Act) be regarded as indicating that a firm's procedures are inadequate, leaving the firm criminally liable.

Although the bribery risk is highest for agents whose sole function is to procure business, similar risks arise in connection with other agency relationships. For example, an insurer may delegate to another company (known as the 'coverholder') authority to enter into contracts of insurance on its behalf pursuant to a 'binding authority' agreement. In these circumstances, the coverholder is likely to be treated as an 'associated person' of the insurer for the purposes of the Act. Consequently, insurers should have adequate procedures in

place to ensure that coverholders do not pay bribes to procure business. The key features of such procedures are likely to be similar to those appropriate for introducing agents[8].

Broker Remuneration

Broker remuneration is a subject that has long vexed the market. The Act will add a further layer of complication for insurers and brokers attempting to establish what types of broker remuneration arrangements are appropriate.

The Act is unlikely to affect traditional brokerage paid by insureds. Nor is the Act likely to be relevant to arrangements whereby brokers undertake specific consultancy work for insurers.

The principal area where insurers and brokers will need to consider the implications of the Act is in connection with 'contingent commission' arrangements. These are agreements by which underwriters make payments to brokers calculated by reference to the volume and/or profitability of the business placed with the underwriters by the brokers, in return for the provision of 'market services' by the brokers. Such arrangements were common prior to 2005. In 2005, the leading brokers agreed to stop entering into them following investigations by Eliot Spitzer, the Attorney-General of New York[9]. Mr Spitzer claimed that contingent commission arrangements caused brokers to steer business to the underwriters who paid them the largest commissions, rather than to the underwriters who offered brokers' clients the most favourable terms. Last year, most US states lifted their ban on contingent commission arrangements. Indeed, such arrangements were never banned in the UK. The FSA's Rules merely require a broker to disclose, upon an insured's request, the details of commissions received from an insurer[10].

Concerns have been raised in the market that 'contingent commission' arrangements, and other arrangements by which insurers make payments to brokers calculated by reference to business placed, could be construed as bribery under the Act. The concern is that such arrangements involve the conferring of a financial advantage on a broker with the intention of rewarding or inducing 'improper performance' by the broker by steering business to the paying underwriter, in breach of the expectation that the broker would act impartially and in good faith when advising on the placing of business.

However, the Act does not prohibit all arrangements pursuant to which underwriters make payments to brokers. Whether such arrangements give rise to a significant bribery risk under the Act will depend upon the facts of each arrangement. Key factors relevant to the risk assessment will include:

- **Level of Transparency and Consent:** The clearer the disclosure of a payment arrangement that is made to the insured, and the more explicit the insured's consent to that arrangement, the less likely it is to constitute bribery for the purposes of the Act. First, the Court of Appeal confirmed in *Hurstanger v Wilson*[11] that a payment which is disclosed is incapable of constituting a bribe as a matter

of civil law. Second, as noted above, the FSA's Rules permit brokers to receive commission from insurers provided that they are disclosed upon request. Third, even where the broker is paid by the insured and therefore owes a fiduciary duty to account to the insured for sums received from insurers, that duty does not arise where the insured gives 'informed consent' to the retention of the payment by the broker[12]. It would be odd for the broker to be regarded as having been induced or rewarded for improper performance by a payment which did not involve a breach of fiduciary duty, to which the insured had consented, which accorded with the FSA's Rules and which was not a bribe in civil law.

- **Purpose of the Payment:** If the commercial purpose of a payment arrangement is to reward the broker for services of real value provided to the insurer, or to recognise the collateral benefit the insurer receives from the performance of such services for the insured by the broker (for example in the subscription market, where the broker's role in organising and processing documents and information benefits insurers as well as insureds), the bribery risk is lower. The bribery risk is higher where the services in respect of which payment is made are not of real value.
- **Manner of Calculation of Payment:** The level of any payment, and the manner in which it is calculated, should be commensurate with the value of the services for which payment is made. If a payment is calculated by reference to the profitability of business placed with an insurer by a broker, the bribery risk is highest. Such a payment creates a conflict between the broker's client's interest in securing cover on favourable terms, and the broker's own financial interest. Volume based payments where the level of payments increase the more business is placed with the insurer are also comparatively high risk, because they can be seen as an incentive to steer large volumes of business to an insurer. The payment of a flat rate per contract entails a lower risk.
- **Broker's Systems and Controls:** If a broker has appropriate systems and controls to manage any conflicts of interest that arise from payment arrangements in accordance with the FSA's Rules and the general law, the bribery risk is reduced. This is because it is less likely in these circumstances that the arrangement will give rise to any breach of the broker's legal or regulatory duties.

Insurers and brokers should carefully consider the nature of the payment arrangements that they enter into, and put in place procedures to ensure that they only enter into arrangements that do not involve an unacceptable level of bribery risk.

Corporate Hospitality

The insurance industry is not known for stinting on corporate hospitality, which can give rise to concerns under the Act in circumstances where it can be construed as conferring an 'advantage' on the recipient.

The MOJ Guidance expressly states that the Act does not criminalise bona fide reasonable and proportionate hospitality:

- For the section 1 offence, the MOJ Guidance underlines that the prosecution will need to show that the hospitality was intended to induce conduct that amounts to a breach of an expectation that a person will act in good faith, impartially or in accordance with a position of trust.
- For the section 6 offence, the prosecution will need to show that there is an intention that hospitality amounting to a financial or other advantage will influence the official in his or her official role and secure business or a business advantage. The prosecution will have to show that there is a sufficient connection between each of the advantage, the intention to influence and the business benefit. This will depend on the evidence, which the Prosecutorial Guidance provides can be drawn from a wide range of sources, either documentary or otherwise. The MOJ Guidance warns, however, that *"simply providing hospitality … which is commensurate with such norms*" will not be a defence if there is contrary evidence and/or where the norms are "*particularly extravagant*".

Insurers and brokers should carefully review their corporate hospitality and gifts policies to ensure that they only provide hospitality that is reasonable and proportionate. Practices such as flying key employees of clients and spouses to London for all-expenses paid 'conferences' at which more time is spent at the theatre and on sightseeing trips than at risk management seminars is likely to involve a greater bribery risk than many insurers and brokers are willing to take. By contrast, a meal arranged by a broker to celebrate the successful placement of a risk is, in the absence of unusual circumstances, unlikely to give rise to an issue under the Act.

5. Conclusion

The Act may not radically change the insurance market. However, it will force insurers and brokers to think more carefully about the appropriateness of their business practices, and about the effectiveness of the procedures they have in place to ensure that they do not engage in improper arrangements.

Finally, the Act represents an important opportunity for the UK insurance industry, because it is a significant move towards greater international convergence in anti-bribery regulation. The very wide jurisdictional scope of the Act (similar to that of the FCPA) increases the risk for foreign insurers and brokers of using bribery to win business from

UK competitors which seek to comply with the Act. If the Act is vigorously enforced, this should assist in developing an international market for insurance in which no firm can risk being engaged in bribery and business is secured by the broker or insurer who can offer the best service, price or product.

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Endnotes

1 Officials or agents of public international organisations are also caught.

2 The Act applies to the citizens of British dependencies active in the insurance market (e.g. Bermuda).

3 Daily Telegraph interview, 31 March 2011.

4 See the Justice Secretary's Written Statement of 30 March 2011 at http://services.parliament.uk/hansard/Commons/bydate/20110330/writtenministerialstatements/part009.html.

5 See Transparency International's 2010 Corruption Perspectives Index at http://www.transparency.org/policy_research/surveys_indices/cpi/2010).

6 See the FSA Final Notice of 6 January 2009.

7 See "*Anti-bribery and corruption in commercial insurance broking*", FSA, May 2010.

8 Lloyd's recent Market Bulletin on Bribery and Corruption (Y4492) provides helpful guidance on the management of relationships with coverholders.

9 We acted for Marsh in connection with an investigation into UK contingent commission arrangements in 2005.

10 See ICOBS 4.4.1R.

11 [2007] EWCA Civ 299

12 See *Hurstanger v Wilson*