Insurance in the Wake of the United Kingdom Bribery Act

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While the new United Kingdom Bribery Act 2010 (UKBA), 2010 c. 23, was adopted by royal assent in April 2010, it only came into force on July 1, 2011, as the result of extended consultations over the official governance providing comment on how the UKBA will be interpreted and enforced. The UKBA has serious potential implications for non-UK companies. It applies to any company that has a UK business presence and to acts undertaken by persons of any nationality anywhere in the world. In light of the strict liability nature of the statute and the limited defenses available, companies should review their insurance coverage to make sure that it will respond to this new exposure.

Particular attention should be given to section seven of the UKBA, which establishes a strict liability corporate offense for failure to prevent bribery. The only defense recognized in the UKBA is where a company can show it has in place "adequate procedures" to prevent bribery by its own employees and those associated with it. There is also a specific offense for any director who consents to or participates in such an offense. Directors and officers (D&O) liability insurance policies do not necessarily cover these claims. So what should you do to ensure that your D&O policy will?

Bribery Fuels Business in Many Countries

Transparency International's 2010 *Corruption Perceptions Index,* which ranks countries on a scale from 1–10, ranging from consistently corrupt at level 1 to highly honest or "very clean" at level 10, illustrates quite clearly the problem of corruption endemic in today's global economy. Unfortunately, almost three-quarters of the 178 countries ranked in the index score below 5. For example, Somalia is ranked at the bottom in 178th place with a corruption score of 1.1. Indonesia is ranked 110th with a score of 2.8. European Union members Italy are in 67th place with a score of 3.9, and Greece at 78th place with a 3.5 score. The United States and the UK are respectively at 22nd and 20th place on the table, with scores at 7.1 and 7.6.

While the United States Foreign Corrupt Practices Act (FCPA), codified at 15 U.S.C. §§ 78dd-1, *et seq*., and the vigorous enforcement actions undertaken by the Department of Justice and the Securities and Exchange Commission, have apparently not done much to improve the United States' index ranking, the UKBA is clearly meant to address this situation, respond to mounting pressure over the last 11 years for reform of the law relating to bribery and corruption in the UK—effectively since the 1998 OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions—and improve the UK's standing and ranking as a leader in the fight against corruption.

Why Should U.S. Companies Take Note?

One of the UKBA's more controversial provisions is its sweeping extraterritorial reach: It applies to corrupt conduct committed anywhere in the world as long as the corporate entity carries on any part of its business in the UK. Therefore, even if a company is incorporated and headquartered outside the UK, it may be subject to the UKBA. Moreover, unlike the FCPA, the UKBA imposes strict liability—there is no scienter requirement—and applies not only to governmental bribery but also to corruption between private commercial entities. Thus, even companies that comply with the FCPA may not have adequate procedures in place to comply with the broader scope and different requirements of the UKBA.

For example, assume that a U.S.-incorporated and -based energy company, which has a UK subsidiary, appoints an intermediary to facilitate its business interests in Nigeria, and that the intermediary pays a bribe to a local official in Nigeria. In these circumstances, whether or not the U.S. parent or the UK subsidiary were aware of the actions of the intermediary and regardless of any benefit to the UK subsidiary, the U.S. parent could be liable under the UKBA for failing to prevent bribery. The UKBA may be applicable simply by virtue of the existence of the UK operation. Also, the UK subsidiary is itself at risk of prosecution if a person or company associated with it is involved in bribery, as are any U.S. nationals working for the UK subsidiary and "ordinarily resident" in the UK, if they are found to have paid or received a bribe. Even having just a UK representative office or agent may be sufficient for the purposes of the corporate offense. Comments from the UK agencies responsible for enforcement suggest that a London stock listing without any demonstrable UK business presence will probably not be sufficient to trigger liability under the UKBA. In this respect, the UKBA appears to be narrower than the FCPA, which may be applied simply as the result of a listing on a U.S. exchange. In the other respects just mentioned, however, the UKBA is wider than the FCPA, and remarks from the UK authorities make it clear that an FCPA-compliant company may not be UKBA-compliant.

An individual found guilty of an offense under the UKBA could be subject to a maximum imprisonment of 10 years and/or an unlimited fine. A company convicted of failing to prevent bribery can also be liable for an unlimited fine. To further complicate matters, the benefits of any business obtained by bribery will be considered criminal property bringing into play the UK's Proceeds of Crime Act 2002 (POCA), 2002 c. 29, and its Money Laundering Regulations 2007, 2007 n. 2157. These provisions in turn can carry substantial criminal penalties as well as civil exposure to seizure of assets. The UKBA, therefore, places the obligation squarely on companies that conduct any business in or touching on the UK to ensure that their own anti-bribery procedures are suitably robust and effective. Should a company not have adequate procedures in place, its directors may well face claims in connection with that corporate failure.

Insurance Concerns

Companies with business operations in the UK that also do business in higher risk regions of the world, such as Africa, Russia, Indonesia, India, or China, may now face increased exposure under the UKBA, which will necessarily impact the insurers who cover these risks. U.S. companies can expect that their insurers will now begin to conduct greater due diligence with regard to the operations of insured companies to assess whether the insured's risks have increased as a result of the UKBA, and this scrutiny may have an impact on premium levels and coverage terms.

The implications are particularly important for D&O insurance, which protects companies from securities claims and their directors and officers from a wide range of claims of wrongdoing. Some insurers have already started adding blanket exclusions to their D&O policies for all claims arising under the UKBA and FCPA while offering to provide limited optional coverage for an additional premium. For companies with UK operations that do business internationally, it is important to scrutinize these new exclusions carefully and either purchase adequate additional limits to protect against UKBA and FCPA claims or consider switching to an insurer that does not rely on one of these exclusions.

It is possible that insurers may decide to exclude certain established business activities that are permitted under the FCPA but potentially illegal under the UKBA, such as claims arising out of facilitation payments or hospitality, either generally or in certain identified jurisdictions, or may impose premium surcharges for such coverage. Some D&O policies already exclude claims arising out of the payment of commissions or gratuities to foreign government officials, but until now companies have often been able to negotiate to have such exclusions removed—in part, no doubt, because such conduct does not necessarily give rise to liability under the FCPA. Given the UKBA's more stringent prohibition on such payments, it may become more difficult for U.S. companies that do business internationally to persuade insurers to drop these exclusions.

FCPA fines and penalties are already often expressly excluded from a D&O policy's definition of covered "loss," but many companies have been able to negotiate policy enhancements that provide coverage for FCPA civil fines and penalties awarded against individual directors and officers or for non-willful FCPA penalties. U.S. companies doing business internationally should now try to ensure that fines and penalties awarded against individual directors and officers under the UKBA are also included within the definition of covered "loss." Because the UKBA imposes strict liability regardless of intent, however, it may become more difficult for some companies to obtain coverage for innocent violations, though it is more important than ever to negotiate for it.

Most D&O policies also exclude coverage for claims arising out of fraudulent, dishonest, or criminal acts. Companies facing potential FCPA claims have commonly negotiated "final adjudication" language into these exclusions, so that they and their directors and officers will not be deprived of defense coverage merely because someone alleges that they have committed an FCPA violation. Such "final adjudication" language also ensures that policyholders have coverage for settlements of claims.

The same strategy is now recommended for companies facing potential liability under the UKBA. It should be noted, however, that it is not clear to what extent the UK enforcement agencies will be free to negotiate settlements: The UK court jealously guards its prerogatives on sentencing, and the UK court has held that insurance cannot be used to lessen the punishment for criminal activity. Courts in some U.S. jurisdictions have held similarly. Likewise, depending on whose law applies to the insurance policy, it is possible that no coverage will be available for fines and penalties either, even if the insurance policy expressly promises to cover them. Furthermore, where a fraud and dishonesty exclusion is later triggered, the insurer may argue under the law of some jurisdictions that it is entitled to recover any defense costs already paid, although this is certainly not a winning argument in every U.S. jurisdiction.

U.S. experience also shows that many FCPA actions are resolved during the investigation phase, and that the costs of responding to such investigations can be exorbitant. Many D&O policies, however, do not include investigations within their definition of covered "claims," or if they do include "investigation" coverage, limit it to circumstances in which an individual director or officer is the target of the investigation. As with companies facing potential FCPA exposure, it is now important for companies affected by the UKBA to ensure that their policy's definition of "claim" includes bribery investigations. In light of the increased focus on anti-corruption enforcement, it is also crucial for companies to ensure that they are purchasing adequate D&O indemnity limits. Otherwise, the costs of responding to an investigation can exhaust the policy limits, leaving nothing to indemnify the individual directors and officers for settlements, fines, or penalties, or to respond to follow-on securities lawsuits brought by unhappy investors.

It is likely that insurers, especially D&O and professional liability insurers, will take note of the increased risk of claims relating to individuals charged with a principal offense under the UKBA or senior officers working overseas in high risk areas but with a "close connection with the UK," given the potential for an increased volume of claims for defense costs incurred in relation to civil claims and investigation costs in relation to actions by regulatory authorities.

U.S. policyholders should, therefore, expect that part of their insurer's process of risk reassessment may well involve a more thorough inquiry into whether a prospective or renewing insured with business connections to the UK has "adequate procedures" in place, what "associated persons" are typically used to perform services for the insured, and whether those persons are covered by the insured's anti-bribery policies and procedures.

The fact that insurers will become actively engaged in reviewing whether business practices, protective measures, and compliance procedures are adequate and appropriate in light of the potential for increased exposure and the nature of the potential risks and penalties under the UKBA should provide additional incentive for U.S. companies with a UK presence to take the new law seriously.

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