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UK Case Mabey & Johnson Ltd. Continues to Set Anti-Corruption Enforcement Precedent

BY THE GLOBAL COMPLIANCE & DISPUTES PRACTICE

Landmark Recovery Places UK Company Back in the Spotlight

Mabey & Johnson Ltd. ("M&J"), the first company to be convicted in the UK for acts of bribery overseas, continues to set anti-corruption enforcement precedent in this latest chapter of the British bridge-builder's legal saga. On January 12, 2012 the UK's Serious Fraud Office ("SFO") announced that it would recover £131,201 (roughly USD $200,000) in dividends paid to the shareholders of M&J's parent, Mabey Engineering (Holdings) Ltd., that were derived from the subsidiary's illicit activities (the "Mabey Settlement"). The High Court of Justice's order to disgorge the share dividends marks the end of a case that began with M&J's self-referral to the SFO in early 2008 and the first time that the SFO has compelled a parent company, rather than the company itself or individuals responsible for its management, to forfeit profits under Part V of the Proceeds of Crime Act of 2002 ("POCA"). Comments by Richard Alderman, the Director of the SFO, indicate that the SFO plans to leverage this power broadly to recover shareholder dividends resulting from corrupt activities, which could have far-reaching implications for institutional investors in UK companies worldwide.

Unprecedented Recovery Makes Dividends Fair Game

M&J first made anti-corruption headlines in 2009 when it pled guilty to charges of corruption and breaching UN sanctions. While the SFO acknowledged that M&J's parent company was "totally unaware" of the violations,[1] such lack of knowledge ultimately was deemed irrelevant. Actions under POCA[2] do not require any proof of intent. Part V of POCA does not require that the investor or parent company have any tie to the UK so long as the property is obtained through "unlawful conduct"."Unlawful conduct" is broadly defined, and POCA's authority is "exercisable in relation to any property…whether or not any proceedings have been brought for an offence in connection with the property."[3]

The landmark case is significant for two reasons. First, the Mabey Settlement marks the first time that the SFO has sought payments *already* issued to investors, as compared to funds designated for, but not yet distributed to, investors. Second, whereas the dividends in this case involved payments to companies within the same group as the target of the investigation, SFO statements made in connection with the Mabey Settlement suggest that it does not view group membership as a prerequisite to recovering the proceeds of corruption from shareholders. On the contrary, when announcing the recovery of the funds Mr. Alderman emphasized that all investors have an obligation to familiarize themselves with the business practices of the companies in which they invest, especially

"institutional investors who have the knowledge and expertise to do it." Mr. Alderman continued: "The SFO intends to use the civil recovery process to pursue investors who have benefited from illegal activity…Where issues arise, we will be much less sympathetic to institutional investors whose due diligence has clearly been lax in this respect."[4] The SFO has not issued any advice or guidance on determining what would constitute sufficient due diligence in this context.

Broad Implications for Institutional Investors

The Mabey Settlement raises important questions about the extent to which shareholders will be held liable for the criminal conduct of their often far-flung subsidiaries. It also raises the issue of whether institutional investors such as pension funds and private equity firms will be held to a different standard from other investors. Should shareholders expect their sophistication and financial resources to figure negatively into a regulator's consideration of how to pursue illicit proceeds? Judicial approval of the Mabey Settlement set off alarm bells among institutional shareholders who question the ability of non-executive directors to monitor their portfolio companies sufficiently closely to mitigate corruption risks.[5]

Observers of UK anti-corruption enforcement trends will be watching closely to see whether the Mabey Settlement proves to be an outlier or the first instance of a new enforcement paradigm. They also will be watching the reaction of U.S. enforcement agencies and courts to this case. It is possible to imagine the U.S. Department of Justice ("DOJ") borrowing a page from the SFO and seeking to reclaim dividends distributed by a portfolio company to a private equity shareholder. Echoes of Mr. Alderman's assertion that investors have an affirmative duty to conduct adequate due diligence on the targets of their investments can be heard in the 27-page appellate ruling denying leather goods magnate and philanthroper Frederic Bourke, Jr.'s request for a new trial.[6] Issued just days after the Mabey Settlement was announced, the U.S. Court of Appeals for the 2nd Circuit refused to overturn Mr. Bourke's 2009 conviction for participating in a corrupt oil deal in Azerbaijan. Despite alleged governmental misconduct, the two-judge panel found that "a rational juror could conclude that Bourke deliberately avoided confirming his suspicions" that his business partner was bribing Azeri officials.[7] Considering that last year marked the beginning of the first FCPA-related investigation of the financial services sector by the Securities and Exchange Commission ("SEC") with its industry-wide probe of sovereign wealth funds, institutional investors have much to consider as anti-corruption legislation is enforced on both sides of the pond.

It is worth noting that, while the conduct in the Mabey Settlement predates the UK Bribery Act of 2010, which came into effect in July 2011, POCA would allow recovery of dividends resulting from activities violative of the Bribery Act, Given the SFO's seemingly aggressive new enforcement stance, as well as the DOJ's and SEC's actions implicating investors, it is critical that institutional investors press for the implementation of effective anti-corruption policies at the companies they own. Such policies must consider the specific risk factors of the company, i.e., the industry, its business model, the countries in which it does business, the volume of business conducted through third parties or with government end users, etc. An anti-corruption policy that fails to assess the company's particular risks at the outset will not be effective in deterring or detecting potential misconduct. If the Mabey Settlement is any indication of things to come, such blind spots pose increasing risk for institutional investors.

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[1] SFO Press Release (January 13, 2012), available at http://www.sfo.gov.uk/press-room/latest-press-releases/press-releases-2012/shareholder-agrees-civil-recovery-by-sfo-in-mabey--johnson.aspx.

[2] Proceeds of Crime Act of 2002, available at http://www.legislation.gov.uk/ukpga/2002/29/part/5/chapter/1. The Act provides for "the recovery of property which is or represents property obtained through unlawful conduct or which is intended to be used in unlawful conduct." Chapter 29.

[3] *Id.* at Part 5, Chapter 1, Art. 240(2).

[4] *Id.*, SFO January 13, 2012 Press Release.

[5] *See*, Caroline Binham and Kate Burgess, "Investors Alarmed by SFO Warning," *Financial Times* (January 12, 2012), available at http://www.ft.com/intl/cms/s/0/fd890d34-3d17-11e1-8129-00144feabdc0.html.

[6] *United States v. Kozeny*, --- F.3d ---, No. 09-4704-cr(L), 2011 WL6184494, at *15 (2d Cir. Dec. 14, 2011).

[7] *Id.*