



# Mandatory exclusion for corporate offences

THE UK PROCUREMENT REGULATIONS AND RECOGNITION OF SELF-CLEANING

The new Bribery Act in the UK introduces a corporate offence of failure to prevent bribery. If a company is convicted, mandatory exclusion from public sector and utility procurement will follow under the Procurement Regulations as they currently stand. This is a material and critical risk for companies providing works, supplies and services throughout Europe and heightens the need to address compliance programmes to ensure adequate procedures are in place to prevent bribery and to ensure that appropriate remedial measures are taken if wrongdoing is discovered.

## Background

In March 2010, the Office of Government Commerce (OGC) published guidance on the mandatory exclusion of bidders under the procurement regulations. The publication of this guidance, and the recent enactment of the new Bribery Act, highlights the potential risks to companies bidding for public procurement contracts of not effectively minimising the risk of corrupt practices.

A recent report by Transparency International identifies widespread corruption in the following sectors: real estate, oil and gas, mining, heavy manufacturing, pharmaceuticals, power generation and transmission, arms and defence, civilian aerospace and utilities. For companies operating in developing economies where the incidence of corrupt practice is high, the associated risks are likely to be greater still.

## The risks – mandatory exclusion

The Public Sector Directive and the Utilities Procurement Directive, as implemented in the UK by the Public Contracts Regulations 2006 and the Utilities Contracts Regulations 2006 (together 'the Procurement Regulations'), include a mandatory requirement for economic operators to be excluded from bidding on public or utilities contracts if they have been convicted of certain offences ('mandatory exclusion').

An economic operator will be ineligible to bid on a public contract if its directors or any other person with powers of representation, decision or control have been convicted of offences including participation in criminal

organisations, corruption, fraud, money laundering or bribery. Although the issue is as yet untested, it seems probable that a company will be ineligible to bid on a public contract where a director or any other person with powers of representation, decision or control has been convicted of one of the relevant offences even if that conviction is otherwise unrelated to the company.

## OGC guidance

A significant concern raised by the OGC's recently published guidance on the mandatory exclusion provisions in the Procurement Regulations relates to the assertion that, because convictions for corporate offences do not currently become spent, 'a corporate conviction that requires mandatory exclusion could therefore result, currently, in permanent exclusion from public procurement contract opportunities'.

Further, although the Procurement Regulations provide that an exemption from the mandatory exclusion may be made if the contracting authority 'is satisfied that there are overriding requirements in the general interest', the OGC guidance recommends that this exception should be used only in the most serious of circumstances – eg a case of national emergency. Accordingly, it is unclear at present how a convicted company might avoid mandatory exclusion.

The OGC's guidance also suggests that there may be circumstances in which the 'sensitivities surrounding the specific contract are such' that the contracting authority may seek disclosure of spent, as well as unspent,

convictions by directors or any other person who has powers of representation, decision or control.

## The risks – the Bribery Act 2010

Why is the risk posed by mandatory exclusion about to increase materially when the exclusion provisions in the Directives and Regulations have been around since 2006?

The answer lies in one of the new offences created by the Bribery Act – namely a strict liability corporate offence of ‘failing to prevent bribery’. Under the new provisions, a company will commit an offence if an associated person performing services on its behalf bribes another person to obtain or retain a business advantage for the company.

It seems likely, though not certain, that this new corporate offence will be a ‘bribery offence’ for the purposes of the mandatory exclusion provisions in the Procurement Regulations and that a company convicted of this offence could be permanently excluded from tendering for public procurement contracts. During the Act’s passage through parliament, a justice minister stated that ‘active consideration’ was being given to whether the corporate offence would trigger the mandatory exclusion but that there remained ‘a number of complex points’ under consideration. The minister further stated that ‘the government’s position will be clear before any of the offences are brought into force’. Clarification is still awaited.

### Defence of ‘adequate procedures’

The only defence to the new corporate offence is to show that the company had in place ‘adequate procedures’ designed to prevent bribery from being committed by those performing services on its behalf. The new Act is unclear on what would amount to adequate procedures, but the government is required to publish non-statutory guidance on this at least three months before the Act comes into force. It is unlikely that this guidance will be prescriptive, the government’s preferred approach appearing to be to leave the courts to decide what a proportionate response should be for a given firm, in view of its size, resources and degree of risk.

In the interim, to the extent companies do not have such measures already in place, careful consideration should be given to how to implement compliance systems and controls that will prevent corruption across the organisation.

## Self-reporting as a fail-safe?

It was also thought that UK corporates could potentially avoid criminal conviction by self-reporting any potential misconduct to the Serious Fraud Office (SFO). Under the SFO’s guidelines, there is some capacity for the wrongdoing to be treated as a civil matter following self-reporting. However, the reliability of this approach is now uncertain following the recent comments made by the courts in *R v Innospec* and *R v Dougall*. These cases indicate that negotiations with the SFO should result in nothing more than an objective statement of mitigating factors that the court may take into consideration in sentencing but that ‘in all cases it is for the court to decide on the sentence’.

In the meantime it appears that the SFO does not intend to alter the terms of the settlement agreement it has agreed with BAE Systems, which is due to come before the courts for consideration in coming months. The view that the judges take towards this plea agreement is likely to be instructive on how future cases of large-scale (and particularly transatlantic) corruption will be dealt with.

In light of these uncertainties the SFO has identified the following issues as requiring resolution:

- global settlements in cases of concurrent jurisdiction;
- plea bargaining – the SFO ‘remains committed to using the plea negotiation framework as the basis for dealing with suitable cases’;
- self-reporting – the SFO has confirmed that ‘there will be appropriate cases where we will want to reach a civil settlement by way of civil recovery’ while acknowledging that in light of *Innospec* there may also be cases to be dealt with criminally; and
- the future of the SFO – the coalition government has stated its commitment to establishing a single Economic Crime Agency, which would include the SFO, Financial Services Authority and Office of Fair Trading (OFT).

## Self-cleaning

The application of an indefinite exclusion under the Procurement Regulations for a bribery conviction is not uniformly applied across the EU. In some EU member states (eg Germany), contracting authorities are required to admit companies that would otherwise be subject to mandatory exclusion if they have undergone

adequate 'self-cleaning'. Industry representatives in the UK, including the Confederation of British Industry, continue to lobby the government to address the uncertainty surrounding this issue in an attempt to ensure that the promised clarification of the government's position on mandatory exclusion reflects the concerns that have been raised.

'Self-cleaning' refers to the concept that a firm convicted of an offence will not be precluded from participating in a procurement process if it can show that it has implemented effective measures to redress the circumstances that gave rise to the offence and ensure that the proscribed conduct will not recur.

The arguments in favour of self-cleaning assert that effective measures – which comprehensively examine and remedy offensive conduct – both positively support the objectives behind the exclusions and may be more effective in promoting those objectives than a mandatory exclusion. Arguably the fundamental principles of EC law – free movement, proportionality and equal treatment – require contracting authorities to give due consideration to effective self-cleaning measures. Moreover, uneven treatment across member states whereby some recognise self-cleaning and permit rehabilitation while others do not in respect of the same offences appear to undermine the same fundamental EU Treaty freedoms.

#### **Lack of consistency across Europe**

The new EU Defence Directive recognises the inconsistent approach adopted across member states and provides that the European Commission should review the equivalent mandatory exclusion provisions in that Directive, 'investigating in particular the feasibility of harmonising the conditions for the reinstatement of candidates or tenderers with prior convictions excluding them from participation in public procurements, and shall, if appropriate, bring forward a legislative proposal to that effect'. This review may influence a separate amendment of the position under the Procurement Directives.

The difficulties of an inflexible application of the exclusion provisions were highlighted in the OFT's decision on bid rigging in the construction industry in September 2009. Alongside that decision, the OFT issued a guidance note setting out a joint recommendation of

the OFT and the OGC that parties to the decision should not be excluded automatically from future tenders. It was observed that to exclude all those who had participated in the bid rigging would materially restrict competition in the UK market. It was said that:

- cover pricing is endemic in the construction industry and it would be wrong to assume that bidders not named in the decision were not involved in bid rigging;
- the parties had received significant financial penalties appropriate to the infringement findings in the decision;
- the parties to the decision could be expected to be particularly aware of the competition rules and the need for compliance and, if anything, would be more likely to be compliant; and
- many of the parties co-operated fully with the OFT's investigation and a significant proportion took measures to introduce or reinforce formal compliance programmes and to ensure that their staff were made aware of competition law obligations.

The OFT investigation involved the discretionary (rather than the mandatory) exclusion provisions under the Procurement Regulations. As currently drawn the UK regulations as interpreted by the OGC guidance do not permit the flexibility to address such factors in the context of a corruption conviction and the effectiveness of self-cleaning measures has not been tested in the UK courts. Accordingly, there is no certainty over how stringently or otherwise contracting authorities will interpret the OGC's guidance, even if a bidder with a conviction has implemented an internal cleansing programme. The remediation steps entailed in a self-cleaning process would, however, be expected by US authorities in corruption investigations under the US Foreign Corrupt Practices Act and are likely to be taken into account as mitigating factors in a UK criminal case.

#### **Effective self-cleaning**

The question of what might constitute effective self-cleaning measures will depend on the particular circumstances of a given case, including the seriousness of the wrongdoing and the nature of the measures adopted. Effectiveness, in all cases, is likely to be determined by the extent to which future occurrences of wrongdoing are rendered, as far as is practicable, impossible. Effective self-cleaning measures are also likely to involve a substantial process requiring significant

investments of time and money without any guarantee that the efforts will be recognised.

Possible elements of a successful self-cleaning process may include:

- clarifying the facts surrounding the wrongdoing;
- repairing the financial damage;
- removing implicated personnel; and
- adopting structural and organisational policies to prevent serious misconduct from occurring in the future.

## International sanctions

Companies with overseas operations also need to be aware of the various sanctions that can be imposed by global organisations.

For instance, the World Bank's sanctions procedures enable debarment of a company engaged in fraud or corruption for either a limited or an indefinite period, with scope for penalties to be reduced for voluntary disclosure, co-operation or other mitigating behaviour. One aim of the World Bank's ongoing process of updating its procurement guidelines is to harmonise the Bank's fraud and corruption policies and procedures with those of other financing partners.

Further, in April 2010, five multilateral development banks (the World Bank, the Asia Development Bank, the African Development Bank, the European Bank for Reconstruction and Development and the Inter-American Development Bank) signed a cross-debarment agreement applying to debarments exceeding one year, which points to a growing 'internationalisation of punishment'. The European Investment Bank is considering how it can join the agreement while ensuring compliance with EU principles.

### Other briefings

- For further details on the new Bribery Act, see our briefings *The UK Bribery Bill* dated April 2010 and [The UK Bribery Act](#) dated May 2010.
- For further information on the decisions in *R v Innospec* and *R v Dougall* see our briefing [Co-operation with the Serious Fraud Office following Innospec and Dougall](#) dated May 2010.
- For further information on international sanctions, see our briefing [Sanctions investigations by the World Bank and other multilateral development banks](#) dated June 2010.

## Conclusion

The extent of sanctions that may be imposed for corrupt or fraudulent practice, in a global context, is considerable and, at present, there is little clarity on how such conduct will be dealt with by the UK authorities. For companies engaged in tendering on public contracts in the UK, it is possible that a mandatory exclusion may result from conviction for a specified offence. Whether such an exclusion would be permanent and non-negotiable, or whether self-cleaning measures may be taken into consideration, is yet to be tested in the UK courts. It is advisable for any compliance programme (to the extent it does not already do so) to address not only adequate procedures to prevent bribery but also steps to take if bribery is discovered so that opportunities to avoid or limit periods of exclusions are maximised.

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