



Managing anti-bribery and corruption risk in the financial services sector

Anti-bribery and corruption procedures should now be a key area of focus for all financial institutions, given recent regulatory and legal developments. The Financial Services Authority (FSA) has recently published a report that considers the adequacy of commercial insurance brokers' anti-bribery systems and controls, with particular emphasis on controls to address the risk of illicit payments to third parties. It has expressly stated that many of the issues covered in the report, as well as examples of good and poor practice, are relevant to firms in other sectors.

Introduction

Anti-bribery and corruption procedures and controls should now be a key area of focus for all financial institutions, given recent regulatory and legal developments in this area, not least for the following reasons:

- The Financial Services Authority (FSA) has indicated that it intends to carry out thematic work on anti-bribery procedures at investment banks later this year. This follows the completion of similar work in relation to commercial insurance brokers.
- The Bribery Act, which is currently expected to come into force later this year, introduces a new criminal offence for corporates of failing to have in place adequate procedures designed to prevent acts of bribery being committed by persons associated with them.
- Prosecuting authorities around the world are stepping up significantly levels of enforcement activity for bribery and corruption-related offences. Commercial organisations now face the prospect of huge fines from multiple regulators in the event of bribery and corruption violations.

Against this backdrop, the FSA has recently published its report, *Anti-bribery and corruption in commercial insurance broking* (the report). The report considers the adequacy of commercial insurance brokers' anti-bribery systems and controls, with particular emphasis on controls to address the risk of illicit payments to third parties.

However, the FSA also expressly states that many of the issues covered in the report, as well as examples of good and poor practice, are relevant to firms in other sectors. This is particularly important given that one of the FSA's statutory objectives is to prevent and deal with financial crime. The objective has real political impetus at present, as the financial crisis seems now to be blamed, at least in part, on a failure of risk management and misconduct of one type or another in financial markets.

This briefing highlights the points in the report of general application to financial services firms' anti-bribery procedures, particularly to the anti-bribery procedures of firms using third parties to obtain or retain business.

Anti-bribery procedures: general expectations

- Governance and senior management responsibility: the FSA suggests that responsibility for anti-bribery and corruption should be apportioned to either a single senior manager or a committee with appropriate terms of reference and senior management membership, reporting to the Board. The Board should receive accurate management information (MI) that enables it to assess and manage bribery risks. This MI should include information about the third parties used by firms, including (but not limited to) new third party accounts, their risk classification and unusually high commission paid to third parties.

- Risk-based approach: the FSA expects firms to adopt a risk-based approach to the development of anti-bribery procedures, applying more stringent procedures to higher risk business. Firms are expected to use tools such as the Transparency International Corruption Perceptions Index to analyse the risks arising from doing business in particular countries and to identify types of business where the risk of bribery is high (for example, business with state or state-owned counterparties).
- Response to bribery and corruption events: firms should reassess the adequacy of their anti-bribery systems in light of significant bribery and corruption events. This includes considering the implications for firms' systems and controls, of changes in the law and regulatory action such as the awaited publication, under the Bribery Act, of the Ministry of Justice's guidance on anti-bribery procedures. Firms are expected to establish clear plans to implement improvements, including updating policies, procedures and staff training.
- Compliance and audit monitoring of anti-bribery systems: the FSA believes that compliance and internal audit are 'key lines of defence in the fight against bribery'. The report identifies as good practice regular compliance and internal audit assurance work on the operation and effectiveness of anti-bribery systems. This work should focus on the areas of highest risk and should entail an assessment of business decisions, not just a check that paperwork is in order.
- Staff vetting: firms should have vetting arrangements in place to ensure that staff (including temporary or contract staff), particularly those in higher risk positions, are appropriate persons to discharge their responsibilities. The FSA regards criminal record, financial soundness and regulatory disciplinary history checks and the use of fraud databases as examples of good practice. It recommends that firms adopt a risk-based approach to dealing with adverse information raised by vetting checks.
- Staff training: this is crucial to the success of firms' anti-bribery systems. The report recommends that firms give staff practically-focused training tailored to the bribery risks they are likely to encounter, use testing to ensure staff understanding, and use the results to assess individual training needs and the overall quality of training.
- Remuneration structures: the FSA is concerned that pay structures that are focused entirely on income or profit generation can encourage risk-taking and negligence and increase the risk of bribery and corruption. It recommends that firms adopt a 'balanced scorecard' approach to remuneration, which takes several factors into account (including good compliance practice) in determining the amount of remuneration an individual receives. The report also recognises that deferred bonuses and bonus clawback arrangements for staff in higher risk positions may assist in incentivising employees to conduct business in a compliant as well as profitable way.
- Control of expenses: the FSA is concerned that expense accounts may be used to make inappropriate payments, for example through excessive entertainment, gifts and hospitality and cash payments. It recommends that firms limit payments to third parties from expense accounts to genuine business-related costs and reasonable entertainment that is unlikely to be construed as an inducement and ensure that the reasons for such payments are clearly documented and approved. The report also states that allowing staff to travel to countries with a high perceived risk of bribery with large amounts of cash is poor practice.

Anti-bribery procedures relating to the use of third parties

- Due diligence: the FSA recommends that firms do not rely on informal market views of third parties when entering into relationships, but instead undertake appropriate due diligence. The report suggests that firms adopt a risk-based approach to due diligence checks, applying more detailed checks to higher-risk third parties such as those operating in high-risk jurisdictions or connected with counterparties. It recommends that the due diligence process should include the preparation of a documented business case demonstrating the need to use the third party. The due diligence process should also involve independent checking by someone outside the relevant business area (for example, by compliance).
- Size of payments: firms should put systems in place to ensure that payments made to third parties are

commensurate with the services they provide. The FSA also recommends that firms regularly review payments made to third parties with a view to identifying unusual payments.

- Destination of payments: the FSA is concerned about the practice of making payments on the instructions of a third party to persons other than that third party. Firms should have systems in place to verify third parties' bank details (for example, by obtaining copies of bank statements) and to ensure that payments due to a third party are not made to persons other than that third party without appropriate investigation and approval.
- Reviews: firms should regularly review their relationships with third parties to ensure that changes to their nature or risk profile are identified and subject to appropriate approval. The report also suggests that firms review third party relationships inherited when teams or businesses are acquired.
- Records: the FSA believes that firms should maintain accurate and accessible records of the third parties they use to obtain or retain business, including the due diligence conducted on the relationship and evidence of periodic reviews.

anti-bribery and corruption in other sectors. There is therefore a real risk of enforcement action for firms across the financial services sector that ignore the report's recommendations. Furthermore, the introduction of the Bribery Act means that there is an increased risk that firms which fail to introduce adequate anti-bribery and corruption procedures will find themselves subjected to criminal prosecution if bribes are paid on their behalf.

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Conclusion

The report serves as a clear warning for firms in all parts of the financial services sector that they need to put their anti-bribery procedures into good order now.

The consequences of failing to do so are significant. The FSA has already announced that it is considering enforcement action against a number of insurance brokers in connection with anti-bribery procedures. This follows its high-profile action against Aon in January 2009 (in which Freshfields Bruckhaus Deringer represented Aon). The FSA fined Aon for failing to establish and maintain effective anti-bribery systems and controls. The FSA has also stated that it believes that many firms are not currently in a position to demonstrate adequate procedures to prevent bribery – the only defence to the Bribery Act's new criminal offence for corporates of failing to prevent bribery.

The FSA is about to embark on thematic work on investment banks' anti-bribery procedures. It has also stated in its report that it may do further work on