SLAUGHTER AND MAY

Slaughter and May Podcast

Bribery and corruption and successor liability in distressed M&A: assessing risk in times of COVID-19

Tim Blanchard	Hello and welcome to the Slaughter and May podcast. My name is Tim Blanchard and I'm a partner in our Disputes and Investigations team.
David Green	I'm David Green, I'm a consultant with Slaughter and May and was Director of the Serious Fraud Office.
Ella Williams	And I'm Ella Williams, an associate in the Disputes and Investigations team working with David and Tim.
Filippo de Falco	And I'm Filippo de Falco, a corporate partner at Slaughter and May
Tim Blanchard	So over the next 15 minutes or so we will be sharing our views on how to identify and assess possible bribery and corruptions risks in distressed M&A scenarios against the back drop of COVID-19. To set the scene, the COVID-19 pandemic has led to businesses across many industries and sectors facing challenging times as economic conditions have worsened both in the UK and overseas. Now, although countries across the globe including the UK, have already started to ease the measures and restrictions imposed to help manage COVID-19 related risks, it is likely that we will see some companies emerge with uncertain futures whilst others emerge with cash that they plan to use to target more struggling entities. This in turn may lead to increased distressed M&A activity in the market. As with any M&A activity, it is important to consider potential bribery and corruption risks as well as other criminal offence risks when assessing a target's business and progressing the transaction. And in the UK, these risks are heightened, in particular, by the broad jurisdictional reach of the UK Bribery Act and particularly the possibility of corporate criminal liability under section 7 of that Act. But depending on the jurisdictions in which the businesses are based or operate, parties to a transaction may also need to think about other equivalent or similar risks that may arise overseas and I'm thinking here about acts such as the US Foreign Corrupt Practice Act. Now during today's podcast, we are going to touch on the key risks area or, often called red flags that may arise from a UK Bribery Act perspective and how a potential acquirer can seek to mitigate them during the acquisition process. So to kick things off, Ella, David, perhaps you could take us through why it is important to have these risks on your radar during an M&A transaction.

Ella Williams	I think the first thing to talk about is the concept of successor liability, so this concept refers to the possibility that an acquiring company might incur liability for a target company's past misdeeds and potentially face enforcement action once the deal completes. It's a very well developed concept in other jurisdictions, such as in the United States. Here in the UK, generally, parent companies are not criminally liable for the past acts of acquired companies but there are still ways in which a purchaser can be liable for an entity that is purchased. So they will inherit any ongoing bad practices and there are money laundering implications under the Proceeds of Crime Act 2002, if the target holds tainted cash or the profits of investments from improperly obtained contracts or assets and there have been some high profile examples of this in recent years including when David was a director of the Serious Fraud Office.
David Green	Yeah focusing on the enforcement perspective by way of example, in the ICBC Standard Bank plc, a 3 day deferred prosecution agreement with the SFO, in November of 2015, and in doing so it was accepting responsibility for the failure to prevent bribery contrary to the section 7 of the Bribery Act that the conduct which formed that offence occurred prior to the acquisition of Standard Bank plc by ICBC. So why did they decide to accept that responsibility – my best guess is that they wanted finality, in other words commercial certainty and also they wanted to better their image and maintain it as a lender amongst various African countries. Finally, in the absence of a DPA, a company which is found guilty of a section 7 Bribery Act offence is liable of course to pay an unlimited fine and possibly compensation orders and most dangerous to a company of all, it may find itself debarred from competing for public procurement contacts in Europe and also in the US.
Tim Blanchard	So David, if I asked you to gaze into your SFO crystal ball, how much appetite do you think the SFO will have to investigate potentially criminal conduct that took place during the COVID-19 pandemic in the future and do you in the meantime see any change in an approach likely to happen as to how the SFO is dealing with current active cases?
David Green	Dealing with current active cases, that dealing continues as we can see in last week's charging of GPT, a subsidiary of Airbus, after an 8 year investigation. So it's business as usual. My gut feeling is that there will be no specific action focused around whatever happened during the COVID crisis because I think the overbearing priority of the government indeed of most organisations involved will be to get the economy moving again. So I would see DPAs continuing, I think we Rio Tinto is a possibility for a future DPA and I've got a feeling as well, my gut feeling is, that most misbehaviour, economic or financial misbehaviour, directly linked to COVID will not really be of the type of offending in which the SFO is traditionally interested.
Ella Williams	Having said all that David, I mean while we anticipate that the immediate focus, and even a medium term focus, will be to get the economy back on track, it's worth noting that there's no statute limitations in the UK so if there is anything

	that's going on during this pandemic that the SFO might be interested in then that could become a focus in the future.
David Green	Yes certainly I agree with that.
Tim Blanchard	That's an interesting point, Ella, and I think you know if we are saying that risk might not arise now, it might not arise in the short term, but it might still be out there in the medium to long term. Filippo, from a practical perspective, what should purchasers be thinking about to help mitigate that risk arising?
Filippo de Falco	Well, you know the straightforward answer is, they really need to put assessment of that risk high up on their agenda early on in an acquisition process. And make sure that they be thoroughly diligent before they actually commit to buy a target company so that they know where they stand and at a high level the two key questions they'll ask themselves at the start is, does the target operate in a jurisdiction or in an industry that prevent the heightened risk of bribery incidents and once it has accessed that there is a typical laundry list of questions that it will ask of any seller and target from enquiring around the use of agents, around facilitation payments, around whether the business has ongoing and regular interruptions with government officials as well as enquiring around any historic allegations of bribery and investigations and looking what policies the target has in place.
Tim Blanchard	So just pausing for a moment to reflect further on what exactly may be on that laundry list of red flags, now Filippo as you've said, if the target's business involves the use of engagement of agents to operate on the company's behalf or assist them with their business operations, then those relationships, of course, should be a focus of the due diligence exercise and that in practice can be somewhat challenging particularly if you are faced with circumstances where the target itself may not even have full transparency over its agent's day to day activities. Also you should be looking at whether the target operates in jurisdictions where so called facilitation payments are customary or whether those types of payments are regularly being made by employees or agents. Other points to consider include the target's gifts and hospitality policies and procedures, and how those are being applied in practice, and also you'll want to be thinking about whether the target business has made any significant sponsorships of local entities or charitable donations and whether it has any existing policies and procedures in place that govern those practices. Finally, in the current environment, you'll also want to be thinking about what actions the target may have taken in response to the COVID-19 pandemic. And here I'm thinking about things such as new contracts that have been entered into or perhaps new third party relationships that have been established.
David Green	From a potential enforcement risk perspective, a company in this situation will also want to look very carefully obviously and see whether there are any ongoing or threatened or leaked investigations or information requests from

	law enforcement agencies. Secondly, they will want to check carefully that anti-bribery and corruption policies and procedures are efficacious and in that company and readily understandable and backed up by training and so forth. And also lastly, obviously it will be important to look at whether there any open ongoing whistleblower complaints still under investigation.
Tim Blanchard	And Filippo, so let's say we get through the due diligence process and no red flags or risk areas have been identified, of course that's not necessarily to say that they aren't out there and they just haven't been picked up during the process. What can be done to mitigate that risk?
Filippo de Falco	Yes, look, I think solution probably fall within 3 buckets. The first is a comprehensive set of warranties so that you really focus a seller's mind on these issues and illicit disclosures of anything that might not have come up and been uncovered in your due diligence. The second is potentially looking at financial remedies whether indemnities or price adjustments and those will help you if you have identified something that may result, for example, into a regulatory fine on the target and will address your ability to recover that. And the third is a broad bucket, if you like, of structural remedies and those could range from increased access during the period between signing and closing so that you can do a more in depth investigation and looking at policies on how you might start enhancing them with effect from closing to a much more radical solution of potentially leaving a part or a subsidiary of the target business behind, if you had been able to identify that any heightened bribery risk really sits in that particular area of business.
Ella Williams	And to add to all that, you may need to consider your reporting requirements if you do spot a problem in a pre-acquisition stage. So the ones I am thinking about, is that there may be reporting requirements under the Proceeds of Crime Act 2002, to report suspicions of money laundering to the National Crime Agency. For example, the buyer might need to report if it has a suspicion that it's about to receive criminal property because otherwise receipt of that property could be a further money laundering offence and also the buyers professional advisers might need to report although there is an exception for information that has been received in privileged circumstances certified lawyers are unlikely to have an obligation to report but for other professional advisers, this is a statutory duty that overrides any confidentiality or non-disclosure agreements with the target. In doing that report, it's also important not to tip off the target and by that I mean to disclose either inadvertently or expressly to the target that a suspicious activity report has been made because doing that is a further offence under POCA. And then obviously, listed companies have market disclosure obligations and Filippo you will know all about that.
Filippo de Falco	Yes that's right, of course once a deal closes the listed company will have to update the market in relation to material events affecting the target in the normal way. So if the buyer was not thinking about those possible announcements beforehand, and whether relevant circumstances that it has

	uncovered, for example evidence of historic corruption or any perceived risk of regulatory actions or fines coming down the road, require disclosure because the passed the inside information test or indeed whether there are any safe harbours that allow them to delay disclosure for example, while negotiations with the regulator continue. And if that disclosure is required then a buyer will really be focused on that and look at it very carefully because it will be very unpalatable to make a disclosure of this type whilst also announcing what, no doubt, the buyer will want to present to the market as a very positive deal.
Ella Williams	In a worst case scenario, doing that analysis before acquisition and alighting on the fact that such an disclosure would need to be made on the acquisition occurring, could lead to a situation where the acquisition doesn't proceed at all, potentially.
Filippo de Falco	Absolutely.
Tim Blanchard	And I think that takes us nicely on to our final topic which is around post-completion. So let's assume that things go well, no issues identified during the due diligence stage and the person decides to proceed with the transaction and it completes. That's unfortunately not the end of the story, is it Ella? Because there are other issues and considerations that the company needs to look at and I'm thinking here in particular around compliance programmes.
Ella Williams	Yeah that's right. So I mean I think the first thing that I'd mention is that, Filippo said earlier that you might be able to negotiate a period of time to do a deeper dive pre-acquisition. If that's something you've not been able to do then that is certainly something that you want to do immediately post-acquisition and by that I mean taking a closer look at any high risk areas that have been identified as part of the due diligence exercise. That might involve a thorough audit of the acquired company and its practices, what are they doing and how are they doing it. And then as you mention, you'll also need to look at the compliance programme. I mean when a target company is bought, there is obviously a process it's gone through to integrate that target company into the parent company group and part of that should be ensuring that the compliance process and procedures are aligned and that if the target company's processes and procedures are not as gold standard as the parent companies then bringing them up so that the target company is brought into the compliance culture of the parent. That can involve redrafting compliance procedures, it can involve rolling out training programmes for employees of the target. A whole host of things that you can think about doing in that regard.
David Green	Post-acquisition, there are two, I think, areas of potential interaction with the enforcement authorities. The first is a target company might have been subject to information requests from, for instance, the SFO, that could be either before an investigation is launched in the case of a bribery investigation, or during the course of an investigation. Secondly, the second area, is that if misconduct, historic misconduct, is discovered soon after acquisition then the board has to

	make a decision as to whether or not self-report to the SFO. That, of course, depends very much on the board's appetite for risk and that of course is based on the likelihood or not of the information coming to light and being made public. The important thing is for the board to stay ahead of the game and it's worth bearing in mind that the SFO, would, I think, always be sympathetic to a new corporate regime taking over, discovering historic problems and acting properly in relation to them.
Tim Blanchard	Well that does give us plenty of food for thought then for the post-acquisition steps and thinking as well. So that brings us to the end of today's podcast. Thank you all for listening. If you would like any more information about anything that we've discussed today, please do feel free to reach out to us or to your usual Slaughter and May contact.

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