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January 2013

# Financial Crime Update.

Allegations of corruption are not confined to countries in the bottom half of Transparency International's corruption perceptions index. If calls from governments of developed countries for other states to drive out corruption are to remain credible, those same governments must themselves be free from claims of bribery and fraud. As we report this month, the imprisoning of a former MEP for bribery, allegations of corruption amongst Europe's political elite and critical reports from the OECD suggest that there is still a long way to go.

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## Global news

**IMF issues guidance on the influence of AML and CFT on financial stability**

The International Monetary Fund (IMF) has issued a framework document providing guidance on the consideration that should be given to anti-money laundering (AML) and countering the financing of terrorism (CTF) issues when assessing a country's financial stability.

In some cases, the IMF warns, instances of crime and corruption may be so serious as to undermine a country's domestic financial system and macroeconomic performance and may even "spill over" to effect global stability. This is because national governments and regulators may prohibit their domestic banks from dealing with institutions from countries with weak AML frameworks or subject their transactions to tougher controls. In addition, where governments fail to deal effectively with these problems, allowing criminals to amass wealth, power, and influence, the rule of law may be compromised, destabilising society and the economic system as a whole.

Whether AML issues should be taken into account when assessing a country's financial stability will depend on an overall assessment of the country's circumstances. For example, the level of actual or potential abuse of financial institutions, estimated proceeds of crime generated in the country and number of transactions in specific illegal markets relative to the country's GDP would be relevant. The extent to which criminal elements own or control interests in the financial sector or key financial institutions and the effectiveness of the regulatory and judicial systems to supervise the domestic financial system should also be taken into account.

Where a country's AML/CFT programme is assessed to be damaging its financial stability, IMF staff may work with domestic authorities to design and implement appropriate policies and strategies for improvement.

## Policy and practice

**OECD criticise failure of the Netherlands, Spain and Austria to prosecute foreign bribery**

The OECD Working Group on Bribery has published three Phase Three reports evaluating the implementation of the Convention on Combating Bribery of Foreign Public Officials (the Convention) by the Netherlands, Spain and Austria. While noting that all three countries have taken positive steps to fight foreign bribery including, variously, raising awareness of bribery offences, increasing penalties and strengthening law enforcement agencies, all were also criticised for failing successfully to prosecute any cases of foreign bribery since signing the Convention over a decade ago. Of 22 allegations of foreign bribery made in the Netherlands, two are proceeding to trial (scheduled for later this year) and a further four are under investigation. However, 14 were closed without investigation. In Austria, the first case to be tried is currently proceeding through the courts, two more are likely to lead to charges this year and a further four are under investigation. However, all seven investigations opened in Spain were closed without further action.

In each case the Working Group considered that the country was failing to demonstrate a sufficiently rigorous and robust strategy for tackling bribery and corruption. Specific weaknesses in their individual systems were identified and recommendations for improvement given. In the Netherlands, a more proactive investigation of bribery allegations concerning Dutch individuals or companies and increased resources are needed to enable Dutch law enforcement authorities to carry out investigations and prosecutions. So-called "mailbox companies" – companies incorporated in the Netherlands but which pursue their activities entirely from abroad - were highlighted as being a particular concern (12 of the 22 allegations related to this type of company).

The situation in Austria was found to be more encouraging but amendments to its Penal Code, enacted to address recommendations made in OECD's Phase 2 report, have still to take effect and could not be evaluated. Access to bank information was singled out as a barrier to foreign bribery investigations and insufficient use of tax information found to hamper the detection and reporting of suspicions of bribery. The disparity between the maximum penalties for individuals convicted of bribery (€1.8 million) and that for companies (€1.3 million) was also criticised.

However, it was the situation in Spain that gave the Working Group most cause for concern. 13 years after the entry into force of relevant legislation in

Spain, no individual or company has been prosecuted or sanctioned for foreign bribery. The Working Group was particularly critical of a new foreign bribery offence which came into force in 2010 and includes a separate offence for the bribery of European officials, retaining previous deficiencies relating to the scope of the offence, level of sanctions and limitation period. In addition, although the 2010 law introduced Spain's first regime for holding companies criminally liable for bribery, state-owned enterprises are excluded from the regime.

As with other Working Group reports, the three countries will provide a self-assessment within 12 months reporting on the steps it has taken to implement the recommendations made. This will be followed by written reports on progress made submitted to the Working Group within two years, which will be publicly available.

**Spain: Public pressure leads to more transparent government**

In the midst of a crisis like the one Spain is currently going through, public and investor confidence in the country's economic and political institutions is key to recovery. Spaniards are becoming increasingly aware of this necessity and concern is growing, leading to ever louder calls for an end to political corruption and fraud. For the average man or woman on the street, this should be one of the nation's main goals in the next five years.

Public awareness of the need for transparency in the country's governance and finances is such that no political party or public office is free from in-depth scrutiny. In fact, politicians from all parties and at all levels of government (local, regional and national) are now under legal investigation over alleged improprieties. A number of officials have resigned for this reason in recent months and not even the Royal Family and General Council of the Judiciary (*Consejo General del Poder Judicial*) are immune from investigation.

The pressure for greater transparency came to a head in the recent case of alleged corruption amongst the ranks of the country's ruling party. Certain information became public that pointed toward a possible case of illegal financing and the party's former treasurer is accused of having made off-the-books payments to various public officials. In response to these allegations, the President of the Government announced this week in the Spanish parliament that his party's accounts would be opened up for independent audit; an unusual step for Spanish political parties. In addition to thorough examination of its books, the governing party has also announced that an internal committee will be set up to investigate irregularities and clear out all those responsible. The committee could be headed up by the former chairman of Endesa, although this has not yet been confirmed.

**U.S.: SEC settlements reach five-year high in 2012**

According to a report issued on 14 January 2013, the U.S. Securities and Exchange Commission (SEC) struck 714 settlements in 2012, more than in any year since 2007 and representing an increase of 6.6 percent over 2011. The increase in SEC settlements can be traced to the agency's increased focus on insider-trading cases, which reached a record 118, nearly doubling its 2011 output, and included a $92.8 million civil penalty against Galleon hedge fund leader Raj Rajaratnam. Several enforcement areas saw a slight downturn in SEC settlements, however, such as FCPA settlements, which were two fewer than 2011.

In addition to the high volume of settlements, the median SEC settlement amount - $221,000 for individuals – was the highest since 2003. Over the nearly four-year tenure of SEC chairman Mary Schapiro, who stepped down as SEC chairman in December 2011, the median settlement with individuals increased by nearly 40 percent. Overall, the report, prepared by NERA Economic Consulting, recognizes that it may be too early to identify "signature trends" during the Schapiro era, though it does appear that the SEC is focused on cases involving insider trading, Ponzi schemes and foreign bribery, while settling fewer cases that deal with misstatements by public companies.

The report is available here.

## Investigations and decisions

### EU: "Cash for laws" MEP jailed

The former Austrian Interior Minister and MEP, Ernst Strasser, has been sentenced by a court in Vienna to four years in prison for bribery after being caught in a "sting" operation on camera. Two journalists from the UK's Sunday Times posing as lobbyists approached dozens of European Parliament members. They met with 14 and offered them money in return for proposing amendments to European legislation. Strasser, who was an MEP from 2009 to 2011, offered to propose amendments to legislation on handling electronic scrap and on regulating investments in exchange for €100,000 a year.

Strasser was one of four MEPs caught up in the so-called "cash-for-laws" scandal. While Slovenia's Zoran Thaler resigned, the two others - Romania's Adrian Severin and Spain's Pablo Zalba Bidegain - still sit in the European Parliament. Strasser plans to appeal against the verdict.

The European Parliament has been forced to develop a new code of conduct for MEPS, including new rules on party funding, lobbying and politicians' finances to counter the risk of corruption. The new code, adopted in December 2011, bans MEPs from acting as lobbyists and requires them to disclose their financial interests. However, critics have argued that the code, which was developed in the wake of the cash-for-laws scandal, does not go far enough.

**UK: Businessmen sentenced to imprisonment for bank loan frauds**

In two separate cases, three UK businessmen have been convicted of defrauding high street banks of millions of pounds. In both cases the victim banks were criticised for failing to carry out adequate checks on the borrowers, where evidence existed that could have raised suspicion from the outset.

In London, Achilleas Kallakis and Alexander Williams were convicted on 16 January 2013 of defrauding a number of banks including Allied Irish Banks (AIB) and Bank of Scotland (BoS) of millions of pounds and euros and sentenced to seven and five years' imprisonment respectively. Confiscation proceedings are to follow. The defendants used forged or false documents including fabricated guarantees from a well-respected and legitimate property company, to borrow substantial funds from AIB in particular to purchase commercial property. By the time the frauds were discovered, Kallakis had amassed a property portfolio totalling £740 million. The banks were persuaded to lend more than the properties were worth, with the fraudsters spending the difference living a "champagne lifestyle".

Meanwhile, on the same day in Manchester, Waheed Luqman was found guilty of fraud and false accounting and sentenced to seven and a half years' imprisonment in his absence, having fled the UK before his trial began. With his brother and other family members (who were not tried, having left the country before they could be charged), he had borrowed extensively from various banks, including Barclays, purportedly to fund a bridging loan business. The business collapsed in 2006 with debts of over £100 million. Luqman was disqualified from being a director for 15 years and ordered to pay costs to the SFO of £250,000.

In both cases it was commented that the victim banks could have done more to protect themselves. Kallakis and Williams both had previous convictions for deception and/or forgery and were operating under false names. Trial judge Judge Andrew Goymer commented that AIB and BoS should bear some degree of responsibility for the fraud as "corners [were] cut" and "checks [were] superficial and cursory". Likewise, the SFO commented in the Luqman case that although Barclays had carried out checks on the loans to the company "there was a great deal of trust involved" which turned out to be misplaced.

It is possible that the Financial Services Authority (FSA) will bring its own proceedings against the banks involved. Following thematic reviews into anti-money laundering procedures and previous cases where banks' systems and controls have failed to prevent fraud occurring, the FSA is increasingly taking action against institutions that have taken insufficient steps to prevent themselves becoming conduits for financial crime.

**UK: Rolls Royce appoints senior litigator to review procedures**

Following allegations of corruption by overseas subsidiaries, Rolls Royce has announced the appointment of a high profile and senior UK litigator, Lord Gold, to conduct a review of its compliance procedures. Lord Gold will report to the Ethics Committee of Rolls' board.

We reported on claims that internal investigations by Rolls had revealed potential corrupt payments by its intermediaries in Indonesia in our December issue of Financial Crime Update. Additional allegations posted on a US political chat site by an anonymous blogger claim that Rolls bribed a Chinese airline executive, later arrested, to secure deals worth $2 billion contracts with Air China in 2005 and China Eastern Airlines in 2010.

The SFO has not yet commenced an official investigation of its own but is awaiting the outcome of Rolls' internal review.

**U.S.: UBS to pay $1.5 billion to settle allegations of Libor manipulation**

On 19 December 2012, UBS AG, the Swiss global bank, agreed to pay $1.5 billion to regulators in the U.S., U.K. and Switzerland to settle allegations that it was one of a number of banks that manipulated Libor and other benchmark interest rates. UBS acknowledged the regulators' charges, and a unit in Japan, where much of the wrongdoing occurred, pled guilty to criminal fraud. U.S. prosecutors separately filed criminal charges the ringleader, Thomas Haynes, and a former UBS trader named Roger Darin. According to legal filings, UBS staff rewarded brokers with payments to participate in the manipulation and offered financial rewards to employees at other institutions to join in their rigging efforts.

The size of the fine not only represents one of the largest ever imposed on a bank, it could also signal large settlements at other banks who are still under investigation. In June 2012, Barclays agreed to pay $453 million to settle allegations it had manipulated Libor rates. The largest ever fine imposed on a bank remains the $1.9 billion paid by HSBC relating to the laundering of drug cartel money.

The U.S. Department of Justice's (DOJ) press release announcing that UBS's subsidiary agreed to pay a $100 million penalty is available here, and the non-prosecution agreement with the DOJ requiring UBS to pay an additional $400 million penalty is available here.

## Legislation

**Hong Kong: China issues guidance on self-reporting bribery cases**

On 26 December 2012, the Supreme People's Court of the People's Republic of China and the Supreme People's Procuratorate issued an Interpretation relating to the handling of criminal bribery cases (the Interpretation of the Supreme People's Court and the Supreme People's Procuratorate of Several

Issues Concerning the Specific Application of the Law in the Handling of Criminal Bribery Cases). The Interpretation, which has the force of law, clarifies the sentencing guidelines relating to bribe payers under Article 390 of the Criminal Law, addresses self-reporting issues, the confiscation of property and receipt of other improper benefits.

The self-reporting provisions will be of particular interest to companies. Article 7 of the Interpretation addresses self reporting prior to a prosecution taking place. It provides that an entity which has paid a bribe may have the penalty against it and any responsible persons mitigated or waived if it voluntarily confesses to the act of bribery prior to prosecution. It also incentivises whistle-blowers by according similar treatment to any person directly responsible for bribery by an entity, or an individual bribe payer, who reports such conduct by the company or themselves as the case may be. Articles 8 and 9 also encourage bribe payers to cooperate with the Chinese authorities by incentivising confessions in some circumstances where a prosecution has commenced and the reporting of other criminal acts by the recipient a bribe.

The Interpretation came into force as of 1 January 2013. It is not yet known how these potential penalty reductions or waivers will be applied in practice. Self-reporting issues will continue to require careful consideration in any given case.

**U.S.: Recent Updates to Iran Sanctions Legislation**

On 2 January 2013, President Obama signed the National Defense Authorization Act for Fiscal year 2013 (NDAA 2013) which contains new Iranian sanctions that are aimed at preventing Iran from circumventing prior sanctions that targeted its petroleum industry. Subtitle D, §§ 1241-1255 of the NDAA 2013, the "Iran Freedom and Counter-Proliferation Act of 2012," bars all transactions with Iran's energy, shipping and shipbuilding sectors and its ports, and designates them as entities of "proliferation concern." Importantly, the law instructs the President, on or after 1 July 2013, to block and prohibit any transactions in property of any person – including a financial institution – that provides "significant" financial support to anyone: (i) in the energy, shipping, or shipbuilding sectors of Iran, (ii) who operates a port in Iran, or (iii) who is an Iranian on the list of specially designated nationals and blocked persons maintained by U.S. Treasury Department's Office of Foreign Asset Control (OFAC). Thus, financial institutions engaged in transactions with anyone in the Iranian energy sector or any designated Iranian national faces significant risks.

The NDAA 2013 also includes restrictions on trade in precious metals and materials relevant to Iran's shipping sectors, such as graphite, aluminum, and steel. Pursuant to the new law, foreign financial institutions face sanctions if, on or after July 1, 2013, they facilitate a significant financial transaction for goods or services used in connection with the energy, shipping, or shipbuilding sectors of Iran, or of precious metals and certain commodities, or of natural gas to or from Iran. Companies operating in affected sectors should evaluate the potential impact of these measures on their global activities, assess their compliance policies, and implement any necessary enhancements to assure conformity with the new sanctions.

Separately, on 26 December 2012, OFAC issued a general license giving foreign subsidiaries of U.S. companies through 8 March 2013 to wind down any transactions or dealings with Iran that would otherwise subject them to sanctions. Section 218 of the Threat Reduction Act, as implemented by Executive Order 13628, extended the restrictions imposed by U.S. sanctions against Iran to include any foreign entity owned or controlled by a U.S. parent. Under the deadline originally imposed, U.S.-parent companies whose foreign subsidiary engaged in Iran-related transactions had until 6 February 2013 to either divest their interest in the subsidiary or obtain a specific license.

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## Further news and publications

**France: Linklaters' Paris office contributes to the first issue of the Anti-Bribery and Anti-Corruption Review**

The Anti-Bribery and Anti-Corruption Review is a new annual guide to domestic and foreign anti-corruption laws in the most significant jurisdictions worldwide, designed to help legal counsel and private practitioners navigate the complexities of foreign and transnational business. The book will feature at the Annual IBA Anti-Corruption Conference in Paris on 12-13 June 2013, as well as at other relevant conferences and events over the course of the year. Kiril Bougartchev, Emmanuel Moyne and Sebastien Muratyan from Linklaters' Paris office authored the French chapter of the Review.

The French Chapter focuses on the legal framework of both domestic and international bribery, as well as how it is enforced in France. It confirms that French law is not, in fact, insufficiently punitive and that it is continually being strengthened in the field of anti-corruption law. It also deals with several related offences, such as misuse of corporate assets, money laundering or the receiving of the proceeds of crime, and evokes various other laws which affect the response to corruption in France.

The Anti-Bribery and Anti-Corruption Review is published by Law Business Research as part of its Law Review series.

Author: Jane Larner



## Contacts

For further information please contact:

**Satindar Dogra**
Partner, London

(+44) 20 7456 4316

satindar.dogra@linklaters.com

**Joseph P. Armao**
Partner, New York

(+1) 212 903 9200

joseph.armao@linklaters.com

**Melvin Sng**
Partner, Hong Kong

(+852) 2901 5234

melvin.sng@linklaters.com

One Silk Street
London EC2Y 8HQ

Telephone (+44) 20 7456 2000
Facsimile (+44) 20 7456 2222

Linklaters.com



A16104394/0.1/23 Jan 2013