

## Client Alert.

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# 2011 Ends With Over \$100 Million in Penalties and Disgorgements for FCPA Violations at Insurance Company and Telecom Company

By **D. Anthony Rodriguez**

Last year ended with a bang on the FCPA front, with the announcement of two large settlements. The settlements took the U.S. government's collection for FCPA penalties and disgorgement in 2011 over the half-billion dollar mark for the fourth year in a row. The settlements provide cautionary tales for business conduct and accounting. With the government on a sustained FCPA enforcement push, we expect to see more of the same in 2012.

### THE SETTLEMENTS

On December 20, the SEC announced a \$14 million settlement with Aon Corporation for failing to keep accurate books and records regarding payments to and for the benefit of foreign officials, and failing to devise and maintain adequate internal controls. Aon had to disgorge \$11.4 million in what the SEC called "ill-gotten gains" (presumably the premiums on policies that Aon obtained or retained because of its payments) and prejudgment interest (of more than \$3 million).<sup>1</sup> The same day, the DOJ announced that Aon would pay a \$1.76 million penalty to resolve FCPA violations stemming from payments in Costa Rica that also were a subject of the SEC action.<sup>2</sup>

On December 29, the SEC and DOJ announced settlements with Deutsche Telekom ("DT") and with Magyar Telekom, a Hungarian company that DT reported on its consolidated financials, based on Magyar Telekom's offering or making of improper payments and its failure to keep accurate books and records, and DT's failure to keep accurate books and records.<sup>3</sup> To resolve the DOJ matter, DT paid a \$4.36 million penalty and agreed to a two-year non-prosecution agreement, and Magyar Telekom paid a \$59.6 million penalty, and agreed to a two-year deferred prosecution agreement. To resolve the SEC matter, Magyar Telekom paid \$31.2 million in disgorgement and prejudgment interest.<sup>4</sup>

### THE AON CASE

#### ***Failing to Accurately Record Payments for Personal and other Non-Business Travel***

Aon's FCPA problems arose in part from training and travel payments. They provide a useful case study for companies that do business with foreign government-owned entities, and should be kept in mind when doing diligence before acquiring such a company.

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<sup>1</sup> Aon's UK subsidiary previously had paid a £5.25 million penalty to the UK's Financial Services Authority.

<sup>2</sup> DOJ Release No. 11-1678, "Aon Corporation Agrees to Pay a \$1.76 Million Criminal Penalty to Resolve Violations of the Foreign Corrupt Practices Act" (December 20, 2011), available at <http://www.justice.gov/opa/pr/2011/December/11-crm-1678.html>.

<sup>3</sup> DOJ Release No. 11-1714, "Magyar Telekom and Deutsche Telekom Resolve Foreign Corrupt Practices Act Investigation and Agree to Pay Nearly \$64 Million in Combined Criminal Penalties" (December 29, 2011), available at <http://www.justice.gov/opa/pr/2011/December/11-crm-1714.html>.

<sup>4</sup> DT and Magyar Telekom each also agreed to pay a several-million-dollar penalty to the SEC, but their agreements with the SEC, in effect, allowed them to offset those amounts entirely against the penalties that they each paid to the DOJ.

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Aon's UK subsidiary engaged in reinsurance with a Costa Rican government-owned reinsurance company, known as INS, that had to approve all insurance agreements in Costa Rica. Aon acquired a UK reinsurer in 1997. After that acquisition, Aon's UK subsidiary oversaw a "brokerage fund" that the UK reinsurer and other reinsurers had created, and contributed a portion of the commission on the INS account to the brokerage fund each year. INS also directed Aon Limited to create a second fund, using 3% of the premiums that INS paid to reinsurers.

The two funds ostensibly were for education and training for INS employees. INS directed Aon Limited when to disburse funds in accordance with invoices that INS would provide. The SEC alleged that INS required Aon Limited to administer the funds in order to continue in business in Costa Rica. Aon Limited disbursed more than \$800,000 from the two funds to pay for third-party services on behalf of INS officials.

The majority of the payments from the two funds were to a tourism company in Costa Rica where the head of insurance placement at INS served on the board of directors. The tourism company's records reflected commission payments to that official that coincided with times when Aon Limited made payments to the tourism company from the two funds. The INS official had \$44,000 in expenses for 14 trips over five years, including expenses for his wife on five of those trips. At times, Aon Limited reimbursed the official directly, in cash, for claimed expenses.

The SEC noted that a "substantial number" of the "purported educational conferences" were in "attractive tourist destinations," such as London, Paris, Monte Carlo, Zurich, Munich, Cologne, and Cairo, and "had no discernible purpose" or had no apparent connection to the insurance industry. The expenses included literary conferences, holiday expenses, pure entertainment or extensive leisure activities, and family-related travel. Aon Limited's records typically had generic descriptions for payments to the tourism agency, such as "various airfares and hotel," and often did not identify the leisure and non-business activities that were reimbursed.

The SEC also identified an Aon relationship with an Egyptian government-owned company. In 1996, Aon acquired the insurance broker that had the Egyptian company as a client, and an Aon subsidiary serviced the account through 2009. The Aon subsidiary's contract with the Egyptian company provided that the Aon subsidiary would pay for an annual 10-day trip by two Egyptian officers. Before 2004, the Aon subsidiary paid for these trips by making a cash payment to the Egyptian company and to the Aon subsidiary's Egyptian agent. After 2004, the Aon subsidiary organized and paid the expenses itself. Aon's subsidiary paid \$100,000 between 1998 and 2007 for these trips. Following an internal compliance review, the Aon subsidiary stopped paying for the trips. The SEC alleged that the Egyptians' trips had some business component, but that "they also included a disproportionate amount of leisure activities and lasted longer than the business component would justify." The SEC did not allege details.

### ***Payments to Facilitators***

Aon subsidiaries made payments to third parties that were retained to assist in obtaining insurance accounts from state-owned entities (such as airline and oil-and-gas entities) in several countries (Vietnam, Indonesia, the United Arab Emirates, Myanmar, and Bangladesh). The payments to the Indonesian "introducer" totaled \$3.5 million. In Vietnam, Myanmar, and Bangladesh, the payments to former employees who had become facilitators or to others ranged up to \$1 million. In the U.A.E., Aon acquired a broker that had made payments to the general manager of a private company for 14 years. After acquiring the broker, Aon made payments to an account in the Middle East, from which the funds were funneled to the general manager.

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The SEC alleged that the Aon subsidiaries made some payments without taking steps to ensure that they would not be passed on to government officials. The subsidiaries also made payments under circumstances in which the third parties did not appear to have performed any legitimate service, suggesting that the third parties only were conduits for payments to government officials in order to obtain or retain business for Aon.<sup>5</sup>

## THE DEUTSCHE TELEKOM & MAGYAR TELEKOM CASE

### *Paying Off Foreign Officials and the Resulting Books and Records Inaccuracies*

Magyar Telekom is a Hungarian company. DT owns a majority of its shares and is its parent, and DT's consolidated financial statements include Magyar Telekom. Magyar Telekom's alleged FCPA violations occurred in Macedonia and Montenegro. Magyar Telekom and Deutsche Telekom each filed Forms 20-F with the SEC during the relevant time period, and, until different points in 2010, had traded through American Depositary Receipts on the New York Stock Exchange.

In Macedonia, Magyar Telekom took steps to prevent adverse regulatory changes to the Macedonian telecommunications market. Magyar Telekom entered into a secret agreement with Macedonian officials, in which those officials agreed to delay a third licensed competitor's entry into the market, and to take other regulatory steps that assisted Magyar Telekom's Macedonian subsidiary. Now-former Magyar Telekom executives kept the company's copies of the agreement outside of the company's records. The executives used consultants, intermediaries, and other third parties, including in sham consulting and marketing work, to pay nearly €5 million, through an intermediary, that they knew (or were aware of a high probability that it would happen) would end up with Macedonian officials. Only the Magyar Telekom executives and a small number of what the SEC called "participants" knew of the scheme, and the SEC alleged that the executives had structured the contracts to circumvent internal controls and to avoid detection.

Magyar Telekom also made improper payments, totaling almost €7.5 million, that Magyar Telekom executives knew (or were aware of a high probability) would reach Montenegrin officials in exchange for having facilitated Magyar Telekom's acquisition of a state-owned telecommunications company. The payments were included in contracts that were backdated, had false counterparties, or were otherwise deceptive, and no legitimate services were performed. Two of the contracts purportedly were for consulting services in connection with purchasing shares of minority owners in the state-owned company, and were with shell companies in Mauritius and the Seychelles that had never before provided services to Magyar Telekom or to DT. Another "consulting" contract was used to funnel more than €500,000 to the sister of a Montenegrin official.

The SEC alleged that the Macedonian and Montenegrin contracts were not subjected to "meaningful review," and that substantially all of the amounts were paid without question. The Macedonian and Montenegrin sham consulting and other contracts were recorded as legitimate contracts, reflected in Magyar Telekom's financials, and ultimately in DT's consolidated financial statements.<sup>6</sup>

<sup>5</sup> Although the SEC alleged Aon's internal controls were inadequate, Aon's compliance department still appears to have saved Aon from a harsher penalty. The SEC's complaint has several references to Aon terminating payment arrangements or resigning from accounts after its compliance department discovered the arrangements.

<sup>6</sup> Three former Magyar Telekom executives did not settle with the SEC, and a complaint against them is pending.

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## TAKEAWAY POINTS

The settlements present classic FCPA violations that have been the subject of numerous enforcement actions. The Aon settlements, like many prior cases, confirm the pitfalls of paying training and travel expenses for employees of foreign government-owned entities unless controlled by strict approval policies and procedures, and of paying facilitators or introducers. The DT and Magyar Telekom settlements illustrate how alleged bribery schemes are implemented, and how accounting trouble can follow. These cases illustrate the importance of rigorous compliance monitoring, and, in the case of Aon, of due diligence when acquiring a company that does business in developing countries. The settlements also reflect that the government is looking for “extraordinary” (as the DOJ termed Aon’s) and “thorough” (as the DOJ called DT’s) cooperation as grounds for mitigating penalties.

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