Third Party Ethics & Compliance Programs: Good for Business

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Topics for Discussion

- Introductions
- Third Party Risk
- Liability, FCPA, UK Bribery Act...
- Business Benefits
- Practical Application

Discussion and Comments
Speakers

• Marjorie Doyle, JD, CCEP, CCEP-F, Principal, Marjorie Doyle LLC, a Global Ethics and Compliance Consultancy, providing expert advice and professional services in ethics, compliance and risk. Marjorie has deep corporate experience including serving as EVP & CECO Vetco International, and earlier, as CECO DuPont.

• Diana Lutz, JD, Managing Director and CECO, STEELE, a global advisory and risk management company providing investigative due diligence, risk assessments, and compliance program development. Prior in-house experience includes VP at Vetco International (Houston), Director E&C at Qwest Communications.

Third Parties – Level Setting

• Global companies routinely work with third party intermediaries all over the world.
  – For efficiency, expertise, scalability, etc.
• Commonly used third parties include:
  – Contract employees, agents, lobbyists, distributors, resellers, consultants, companies who service your products, freight forwarders, suppliers, joint venture partners...

DISCUSSION AND COMMENTS:
How else are companies using third parties?
What other third party types are companies encountering?
Third Parties – Level Setting Continued

• Technology crosses the distance but doesn’t close the gap.
  – Doing business by cell phone, e-mail, internet and video conferencing.
  – We are doing business with people we don’t really know.
• Businesses are competing to enter remote markets; to work with the best suppliers (*and sometimes only*), distributors and experts to gain advantages and win choice contracts.
  – In the field, speed and results can be everything, compliance can be an afterthought or unwelcome burden.

Third Parties - What’s the risk?

• From a practical perspective, the risk comes from:
  • Your company doing business with people your employees don’t know.
  • Your company is working with third parties who are geographically remote from your company management or in location(s) with little oversight or true accountability.
  • The third party companies and individuals may work in a different culture with varying rules and expectations.
  • Unless you tell them, third parties don’t know your company rules and don’t have to comply with them.
  • Third parties are under pressure to perform quickly and win deals for you.
  • There is pressure from the business to “do business.”
We’ve All Heard the News

• Third Party corruption risk and attendant enforcement actions no longer come as a surprise to us, thanks to:

DISCUSSION AND COMMENTS:

Any comments or predictions about enforcement?
Any illuminating, current third party war stories or successes?

DOJ / SEC / Others Globally

• What are we seeing and hearing about how new corruption and bribery cases are being identified?
• In addition to strongly encouraging self reporting, agencies are:
  • Actively out looking for violations.
  • Creating new, specialized enforcement units and dedicating resources.
  • Increasing cooperation between authorities, sharing info. (Siemens).
  • Watching global news items for new leads.
  • Setting up “stings” (Vegas).
  • Soliciting tips on violators.
  • Following the threads of one case, from one third party to other customers of those third parties.
  • Targeting industries at high risk.
Third Party Compliance Programs: Good for Business

- As Ethics and Compliance professionals, lawyers, auditors, managers... how can we support risk mitigation, ethics and compliance program responsibilities and support our business?
- Work with your business; before designing and implementing programs, take the time to know your business and objectives, consider seasonal demands, current challenges, plans for growth, resources, and existing processes.
- Be ready and willing to explain, discuss and support your projects and concerns. Build credibility. Make the business case, not because you have to, but because you can.
- Extending your ethics and compliance program to third parties is good for your business, good for your third parties (ultimately, fighting corruption is good for the global economy).
Raising Awareness Internally

• Third party risk may be on your radar, if in compliance, international legal dept., audit, or supply chain. To raise broad awareness internally:
  • Incorporate third party risk to overall compliance risk assessment process.
  • Update policies and train staff to spot red flags and adhere to policy.
  • Communicate risk to senior management and the Board.
  • Provide formal, specific, subject matter training.
  • Analyze how due diligence can be incorporated into current processes.
  • Work with sales, supply chain, etc. to identify ROI for the business.
  • Identify ROI (go beyond avoidance of fines, penalties, reputational harm).
  • Assess and address adequate resources: staff, expertise, professional services, advice, due diligence investigations, technology, program audit.

DISCUSSION AND COMMENTS:
Any success to share on engaging the SR team or Board on this topic? Highlight the concern, recommend / conduct assessment then follow up with a plan and updates.

Third Party Corruption – Who’s Liable?

• Liability for corrupt acts by third parties can be a complex question...
  • You have to consider civil or criminal implications, corporate liability or individual liability, books and records or anti-bribery provisions, direct fines and penalties, investigative and legal costs or reputational and company financial consequences.
  • Also consider the heightened risk of the current enforcement environment and apparently expanding scope of enforcement.
  • At the end of the day, do we really want to rest the future success of our business on a defense of... “we didn’t pay the bribe, we didn’t know, we couldn’t control them?”
  • The head in the sand defense will not prevail.
Liability for Third Party Corruption

- Companies must ensure that improper payments are not made indirectly through others.
- The FCPA prohibits indirect corrupt payments and offers, imposing liability for “knowing” that the third party will make a corrupt payment.
- “Knowledge” means either being aware of such conduct or substantially certain that such conduct will occur, or consciously disregarding a “high probability” that a corrupt payment or offer will be made.

- While the implementation has been delayed to Spring 2011, the UK Bribery Act specifically addresses a company’s liability for the wrongful actions of a third party.
- To avoid UK criminal liability under the corporate offense in the Bribery Act, companies will need to put in place and to maintain clear and effective anti-bribery “adequate procedures.”

Bottom Line on Liability

- Liability exists. Criminal, civil, individuals and companies, US, UK and globally, coupled with increasing shareholder suits.
- Avoid putting yourself in a defensive position over liability for third parties and whether you had knowledge.
- Proactively follow the guidance that exists from recent cases, DOJ Opinion Procedure Releases, DPAs, benchmarks and enforcement authorities public statements, UK Bribery Act (forthcoming), others...
- Continuously test, monitor and update to ensure prevention and maintain effectiveness.
- Complete program for third party compliance will include elements mirrored to your own internal anti-corruption, anti-bribery compliance program.
Mitigating Risk - Let’s Just Run Them All Through a Check

• Why not just run all your third parties through the same type of due diligence and be done with it?
• From a risk perspective, not all third parties are the same nor do they require the same level of scrutiny.
  • Each category of third party exposes their partners to varying types and levels of compliance risks.
• Obtaining detailed due diligence on an overly broad group will consume more resources than you likely have, and can cause delay or failure of your program.
• Doing point in time checks or relying on minimal, publically available information means some risky third parties are not getting the level of scrutiny that is justified by the risk.

Conduct a Focused Risk Assessment to Define Risk

• How do we get beyond check the box, shotgun approach to due diligence and get something more tailored, and risk specific?
• Know which areas of your business (geography, business units, relationship types) present the greatest exposure for your company.
• Be strategic with your resources when defining training, due diligence, and audit requirements.
• Plan a narrowly focused risk assessment to inventory and classify your third parties.
• Be alert to some of the challenges we often see in practice:
  • No centralized tracking of third parties.
  • Different systems for payment, contract approvals.
  • If there is centralization of third party info. it may be limited to suppliers / materials.
  • Little info. collected on principals, revenue, number of employees.
Tailor the Level of Diligence to the Risk

- Classify third parties by categories.
- Use data on services, revenue, contract, location, gov’t contacts, etc.) to create risk scores.
- Assign a risk profile to each category.
- Assign an initial level of due diligence to each category.
- Beneficial approach to getting started on third party diligence.
- Consistent and systematic approach, well documented.
- Especially helpful where your backlog or unchecked third parties may be in the hundreds or even thousands of entities.
- Individual third parties can be afforded increased scrutiny as circumstances dictate and when red flags occur.

DISCUSSION AND COMMENTS:
Any experience in conducting creating risk profiles for third parties?
How many categories? How were risks scored?
How many resulting risk classifications?

Create a Written Due Diligence Program

PROGRAM COMPONENTS
- Program Objective & Scope
- Roles and Responsibilities
- Definitions, Exceptions
- Risk Based Due Diligence

PROCESS
- For Conducting Due Diligence
- When a Red Flag Is Discovered
- For New and Existing Third-Parties
- Repetition of Due Diligence Process
- Process at Renewal orModification of Legal Agreement
- Filing and Retention of Documents Created under this Program
- Payment of Cost for Due Diligence Services

ROLES, RESPONSIBILITIES AND TRAINING
Business Benefits from Implementing the Due Diligence Process

• Centralized tracking of third parties
  – Allows for easier identification and removal of duplicate and inactive (more than 2 years) third party accounts.
  – Rationalization of third parties often leads to reduction of number of third parties, reducing administrative burden.
  – Need to allow lead time for due diligence can lead to better advance planning for supply chain, avoidance of some “emergencies” that could lead to use of inferior suppliers.

Overview of Third Party Compliance Program

• Identify third parties that present the highest risk.
• Consider corruption index of location for business to be conducted, interaction with government, contract size, compensation model when assigning risk ratings to third parties.
• Use due diligence process to mitigate risk and eliminate those third parties who present unmanageable levels of risk.
• Ensure third parties are educated and agree to company ethics & compliance program standards.
• Ensure own company staff is well trained and able to spot red flags and address them.
• Include terms in third party contracts that require compliance and audit rights and provide for contract termination if noncompliance arises.
• Ensure ongoing monitoring and requalification of third parties.
• Continuous oversight of third party activities and payments.
• Train your team to recognize and stay alert for red flags.
A Few Specific Red Flags

• Representative referred by a government official.
• Lack of experience or qualifications to perform the services.
• History of corruption in the region, country or industry (CPI).
• Refusal to certify to compliance program or FCPA.
• Unusually high commissions or odd compensation model.
• Lack of detail on work to be done.
• Unusual payments or financial arrangements.
• Lack of transparency in expenses and accounting records.
• Dealing with the government official rather than the agency.
• Unexplained additional 3rd parties brought into transaction.

Sample Contract Topics

• Inclusion of an anti-corruption clause
• Identify all relevant laws related to their service
• Right to terminate for compliance violations
• Right to audit/investigate their operations for compliance with contract
• Require proper record keeping
• Require adoption of your Code of Conduct or review theirs
• Identify how questions or violations are to be addressed, i.e. hot lines
• Require reporting on change in status, ownership, legal violations, etc.
• Require your approval before they engage sub-agents for your business
• Make training and education requirements clear
Ongoing Requirement of Third Party Oversight

- Third parties must be actively managed by someone in the company.
- This person maintains and updates documentation on third party.
- Degree of supervision depends on degree of risk with the third party, their tasks, financial dealings and their geography.
- Audit schedule needs to be created and implemented.
- Conduct evaluations of third party adherence to the contract.
- Stay current on changes of third party ownership, business, legal concerns, etc.
- Evaluate your managers on their performance of third party oversight.
- Third party’s failure or success is an added responsibility of the company’s manager for that entity.

TOOLS OF THE TRADE

Wrap Up

- Third parties are a necessity in today’s business world.
- Business leaders must understand that they are not necessarily a cheaper alternative.
- The same rigor in ensuring an effective ethics and compliance program for the company, applies to its third parties.
- Third parties who have effective ethics and compliance programs have a competitive advantage with their customers - engenders trust.
- Risk assessments, due diligence processes, programs addressing and mitigating particular risks, strong contracts, and ongoing internal management and monitoring are essential.