Auditing Third-Party Business Partners for Fraud and Corruption Across the Globe

Hassan Gomaa, CPA, CIA, CFE, CCEP, DipIFR, CertIA
Global Compliance Auditor
Bio-Rad Laboratories

TOPIC OVERVIEW

* Objective of a Monitoring and Audit Program
* Well-Structured Contracts
* Basic Consideration for an Audit Program
* Elements of the Risk Profile
* Risk Score Point System
* Performing Third-Party Risk Assessment
* Scope of the Audit

* Three Types of Audits
* Information Gathering
* Audit Program Overview
* Common Pitfalls and Red Flags
* Using Data Analytics to Tell the True Story
* Creating an Effective Compliance Training Program
* When to Involve Legal
* Keys to Maintaining a Successful Ongoing Relationship

2

OBJECTIVE OF A MONITORING AND AUDIT PROGRAM

* Auditing is not just about the books and records but also evaluating what is being done to drive compliance from the company to the third-party business partners to mitigate corruption risks.
* A monitoring and auditing program should be based on the contract and obligations we have as a company.
* We should also understand all the requirements we are asking of our business partners so that we can better measure them against it.
* Guidance we give to the business partners must be clear, defined, and measureable.

3

MAJOR COMPONENTS OF A THIRD-PARTY MANAGEMENT PROGRAM
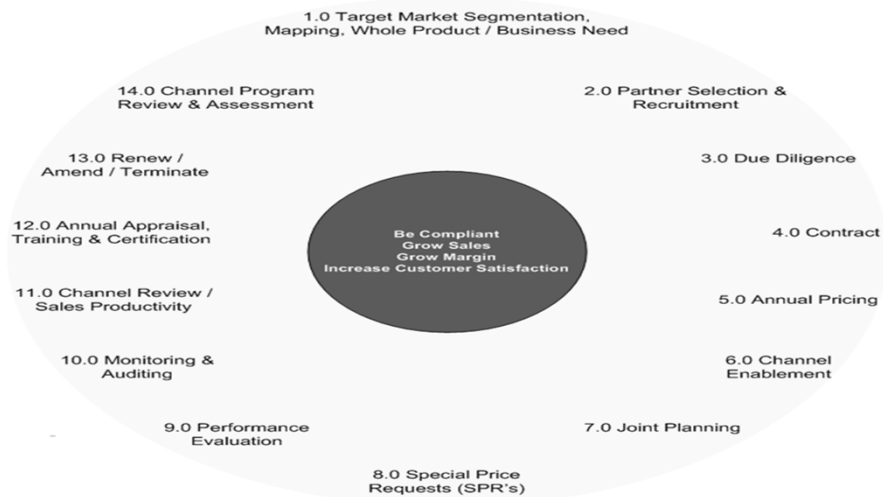
4

WELL-STRUCTURED CONTRACTS

* A clear definition of the services provided
* Clear pricing terms
* Agreement to allow reviews and audits to be conducted
* Required reporting
* Compliance requirements

Having these components provides valuable benefit to an effective auditing and monitoring program and ensures the company can meet its compliance and regulatory obligations and requirements

5

BASIC CONSIDERATIONS FOR AN AUDIT PROGRAM

* Contractual obligations
* Pricing to end users
* Business structure analysis
* Business relationships
* Fraud risk
* Regulatory needs
* Internal controls
* Expenditures

6

ELEMENTS OF THE RISK PROFILE

In order to determine which level of audit to undertake, we create a risk profile. These factors are assigned points that are later tallied to give the ultimate risk score.

* Who are they?
* Who are their customers?
* Do they sell to government-owned enterprises?
* Where are they located and doing business?
* What services are they providing?
* Do they have a compliance program in place?
* Are there any historical compliance issues?
* How much do they generate in sales?
* What are our obligations?

Part of Due Diligence Process

7

RISK SCORE POINT SYSTEM

Example of risk score point system:

Sales range = .5 to 3 pts.

Responses to DD questions = .5 to 1 pt. per question

Country Corruption Perception Index Score = 2 to 8 pts.

Raw Risk Score Scale:

Low Risk = Total Score < 8

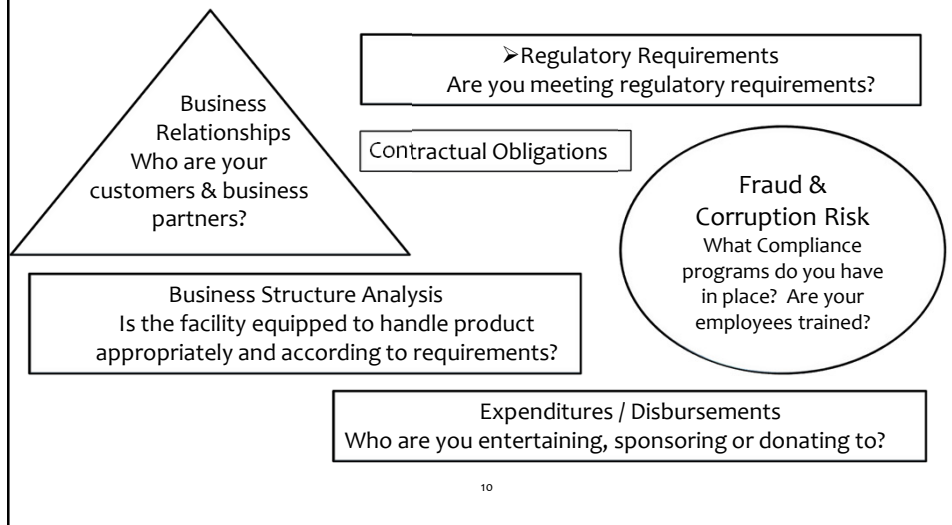Moderate Risk = Total Score > = 8 and < 11

High Risk = Total Score > = 11

8

PERFORMING THIRD-PARTY RISK ASSESSMENT

Step 1 • Export CP Data from System into Excel

Step 2 • Custom Sort List by YTD Sales & Current Risk Score

Step 3 • Calculate % of Total YTD CP Sales & Cumulative % of YTD Total CP Sales and Apply to CP

Step 4 • Calculate Coverage (Total YTD CP Sales x 50%)

Step 5 • Identify Audit Scope Based on Coverage up to 50%

Step 6 • Assign Audit Level Based on Risk
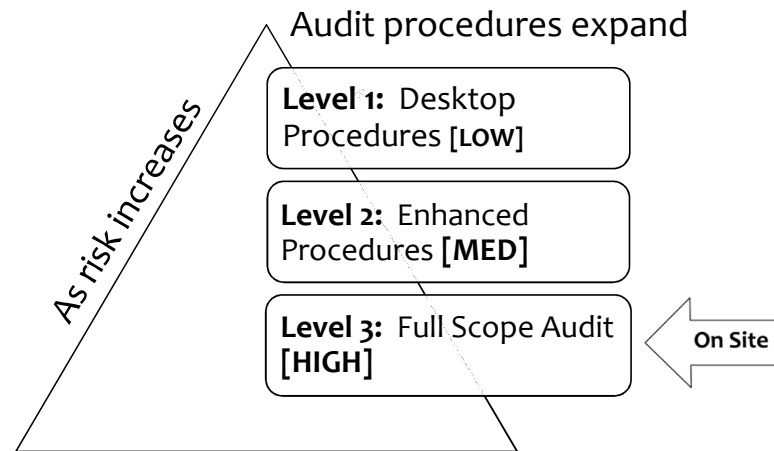
Step 7 • Communicate Scope to CP Mgmt.

9

Scope of the Audit

Business Relationships
Who are your customers & business partners?

➤Regulatory Requirements
Are you meeting regulatory requirements?

Contractual Obligations

Fraud & Corruption Risk
What Compliance programs do you have in place? Are your employees trained?

Business Structure Analysis
Is the facility equipped to handle product appropriately and according to requirements?

Expenditures / Disbursements
Who are you entertaining, sponsoring or donating to?

10

3 Types of Audits Performed

Audit procedures expand

As risk increases

Level 1: Desktop Procedures [**LOW**]

Level 2: Enhanced Procedures [**MED**]

Level 3: Full Scope Audit [**HIGH**]

On Site

11

BASIS OF A THIRD-PARTY AUDIT PROGRAM

* Planning and management
* Information gathering
* Fieldwork – analysis and test of data/transactions
* Reporting of results

12

THREE TYPES OF AUDIT – LEVEL 1 (LOW)

Level 1: Desktop Procedures

* Can be performed mostly remotely.

* Evaluate from a desktop procedure standpoint where they send documents/support that shows what they are doing.

* Use interviews to determine which records/documents to request based on the results of the interviews.

13

THREE TYPES OF AUDIT - LEVEL 2 (MED)

Level 2: Enhanced Procedures

* May be conducted remotely and partially onsite.

* Enhanced procedures also include conducting interviews and having documents sent to us for analysis, etc.

* Take a deeper dive into the business operations and may use data analytics to get the full story.

14

THREE TYPES OF AUDIT – LEVEL 3 (HIGH)

Level 3: Full Scope Audit

* Performed onsite.
* Conduct a full scope audit to fully understand what the organization really looks and feels like.
* Audit your company's transactions with the third party. (Contract may not include right to audit all their transactions).
* Broader scope to audit other significant transactions where documents or evidence of red flags may be present, such as T&E, cash, entertainment, and other commonly abused accounts (where permissible)
  * Auditors interview control owners to gain an understanding of the internal controls around an entire business process and identify control gaps that could be potential red flags. This includes an understanding of how transactions are:
* Initiated - Authorized - Recorded - Processed - Reported
* Heavy use of data analytics (where warranted)

15

INFORMATION GATHERING

* Once we have determined the risk level and the level of audit to be performed, we start the information gathering process.

* Begins with research and conducting targeted interviews to determine:
  * Contractual obligations
  * Operating metrics of the third party
  * Customer base (public vs. private)
  * Financial metrics of the third party
  * Qualitative information
  * Historical performance

* Once we have good information, a formal audit plan and tests of controls can be created and executed.

16

AUDIT PROGRAM OVERVIEW

Pre-Audit Steps:

| Step 1 | • Identify data needs. |

| Step 2 | • Create list of documents to be requested from the
• business partner. |

| Step 3 | • Create audit test plan. |

| Step 4 | • Schedule audits. |

17

AUDIT PROGRAM OVERVIEW

| Step 5 | • Send audit notification to business partners describing scope and timing of the audit. |

| Step 6 | •Execute audit:
•Audit kickoff meeting to explain the audit process.
•Perform interviews and test of controls.
•Identify findings.
•Conduct audit closed meeting to discuss findings, estimated remediation time frame, and obtain business partner response. |

POST AUDIT STEPS:

1: Issue audit report to management and business partner.

2: Follow up on remediation efforts.

18

COMMON PITFALLS AND RED FLAGS FROM GLOBAL AUDITS

* Policies exist but haven't been implemented.
* Procedures have been defined but haven't been observed.
* Standards of conduct have been developed but haven't been consistently communicated to employees who have interactions with government officials.
* Improper payments, gifts, or donations.
* Unsupported transactions.
* Undeveloped Compliance Program and/or Business Ethics and Code of Conduct Policy.

19

OFTEN ABUSED ACCOUNTS

* Consulting fees
* Cash
* Gifts
* Entertainment
* Commissions
* Free goods
* Customs
* Licenses and permits
* Public tender activity
* Sponsorships and training

The key is for us to understand where the weaknesses are and include them in the audit procedures.

20

CREATING AN EFFECTIVE COMPLIANCE TRAINING PROGRAM

* One key to preparing the business partner for audit is to incorporate a compliance training program.
* Elements of an effective compliance training program:
  ➢ Comprehensive
  ➢ Scalable
  ➢ Repeatable
  ➢ Provides the most current information
  ➢ Easily understood (may need to be translated into various languages)
  ➢ Interactive

21

CREATING A CONTINUOUS MONITORING PROGRAM

* Updating due diligence periodically
* Exercising audit rights (limited or full-scope depending on risk)
* Providing periodic compliance training
* Requesting an annual compliance certification by the third party.
* Automated daily / ongoing monitoring

22

WHEN TO INVOLVED LEGAL

* Non-disclosure agreement requested (NDA)
* Breach in contract/agreement
* Audit rights issue
* Evidence of fraud or corruption
* Decision to terminate

23

KEYS TO MAINTAINING A SUCCESSFUL, ONGOING, COMPLIANT PARTNERSHIP

* Incorporating an auditing and compliance program
* Instituting ongoing, continuous monitoring
* Performing regular due diligence
* Working together with compliance, commercial, and legal
* Having the flexibility to modify the program as business needs change and changes in the environment occur
* Embedding the third-party auditing and monitoring program into the larger business partner cycle across the organization

24

Thank you

Hassan Gomaa
Email: Hassan_Gomaa@Bio-Rad.com

25