

Cutting-Edge Third Party Risk Management

SCCE
*Utilities & Energy Compliance & Ethics
Conference*

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Third Parties – What Are They?



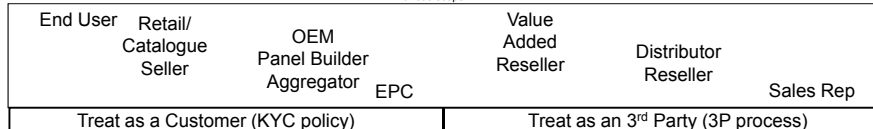
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The Spectrum

Customer to Third Party Representative/Agent

Attributes

- Ultimate purchaser of product or service
- Does not resell
- Buys products from multiple manufacturers
- Passively sells company products
- Buys company product to make into separately branded product
- Enhances own product and sells as branded product
- Prime bidder on project, subcontracts various scope
- Enhances product and sells as solution
- Authorized VAR
- Buys product/service
- Resells at markup
- Licensed Company Rep
- Receives no direct compensation from Company
- Facilitates sale of company product/service
- Gets commission on sale



Risk Consideration

- | | | | | |
|--|---|--|---|---|
| <ul style="list-style-type: none"> • Money Laundering • Prohibited Countries | + | <ul style="list-style-type: none"> • Intellectual Property • Int'l Trade Controls • Conflicts of Interest • Kickbacks • Conflicts of Interest | + | <ul style="list-style-type: none"> • Improper Payments • Bribery • FCPA • Working With Gov't • Competition Laws • Bid-Rigging • Price Fixing |
|--|---|--|---|---|



3rd Party Characteristics

- ✓ Authorized by Company
- ✓ Holds itself out in the market as having a formal relationship with Company

Distributor/Reseller

- ✓ business entity
- ✓ **takes title** to company product
- ✓ **receives no direct compensation** from company, but derives income from discount
- ✓ has **discretion with respect to prices**, T&Cs for resale of purchased product
- ✓ distributor holds stock/reseller does not

Value Added Reseller

- ✓ **takes title** to company product
- ✓ **adds some features** to the product or enhanced package
- ✓ **receives no direct compensation** from company
- ✓ **derives income from adding features** to company products or services and reselling to customer as an **integrated product or enhanced package**
- ✓ has **discretion as to prices**, T&Cs for resale of the purchased products

Sales Representative

- ✓ reimbursed on a **commission** basis
- ✓ **provides assistance** in the expectation of making a profit from any transaction involving the sale of goods or services
- ✓ promotes sale of specific products and services **to assigned customers or within a specific territory**
- ✓ normally, **Company contracts with end-user** customer



3rd Party Characteristics

✓ Working on
behalf of the
company

Sales Marketing Consultant (SMC)

does not take title to GE products
compensated on a **fixed fee** basis
is **not** paid contingent upon an order or other event
provides services and assistance to facilitate the
sales and marketing of GE products/ and/or
services.

to assigned customers or within a specific territory

Not directly responsible for soliciting individual
orders from end-user customer

GE contracts with end-user customer

Administrative Service Provider (ASP)

Acts on companies behalf seeking official
administrative action



5

*Third Party Challenges:
Why do we Care?*



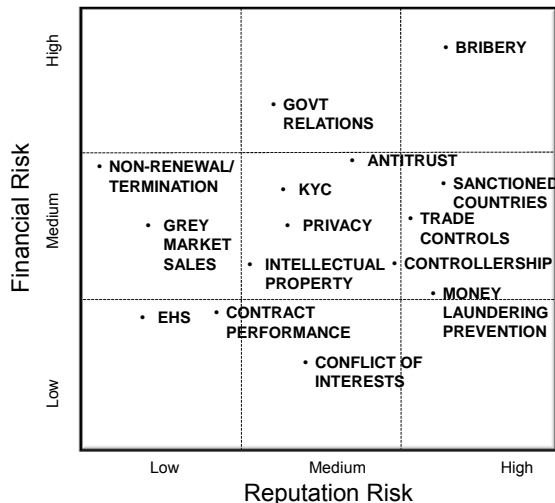
What makes TPs special? Why do we care?

Companies can be held liable for the actions of its independent third parties and intermediaries!

- TP must have actual or apparent authority to facilitate a sale of the companies products or services or must be authorized to act on the company's behalf in seeking official administrative action for the companies benefit
- Transacting business on the companies' behalf or for the companies' benefit poses significant risks
- Risks include:
 - Reputational
 - Financial (fines, penalties)
 - Legal (choice of law, venue, jurisdiction)



What are the risks?



- Reputational vs. Financial
- Other Risks:
 - Security & Crisis Mgmt
 - Human Rights
 - Data protection
 - Country risks
 - Contract Risks
 - Expired agreements
 - Evergreen

Similar risks faced by direct sales



What are the Challenges?

- Headlines!
- Bribery, corruption, and fraud remain widespread
- Rapid investment and growth in new global markets
- “Lumpy” economic environments
- Expectations and increased focus of enforcement agencies



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Headlines!

The screenshot shows a news website interface with several headlines highlighted in boxes:

- Top Right Box:** Risk & Compliance Journal. THE WALL STREET JOURNAL. August 15, 2013, 10:18 AM ET. Wal-Mart to Spend at Least \$150M More on 2013 FCPA
- Middle Left Box:** Vast Mexico Bribery Case Hushed Up by Wal-Mart After Top-Level Struggle
- Middle Right Box:** Lilly Settles With S.E.C. for \$29.4 Million. By THE ASSOCIATED PRESS. Published: December 20, 2012. INDIANAPOLIS (AP) — The drug maker Eli Lilly & Company said Thursday that it had agreed to pay \$29.4 million to resolve federal allegations of possible corrupt business practices by the company's
- Bottom Left Box:** THE WALL STREET JOURNAL. WSJ.com. BUSINESS | Updated August 21, 2013, 8:12 p.m. ET. Microsoft Bribe Probe Reaches Into Pakistan, Russia Deals. Justice Department Reviewing Allegations Involving Deals in Five Countries

At the bottom left of the screenshot is the GE logo with the tagline "imagination at work". At the bottom right is the number "43".

Regulations and Regulators

- Dodd-Frank Whistleblowers
- UK Bribery Act
- Proposed legislation
 - India
 - Brazil
 - China
 - Russia?



44

Components of a TP Risk Management Process



McKinsey & Company Report

“Invest in partners for mutual profit. Companies can no longer afford to treat third-party partners as a second-class channel. In many cases, a partner is the best or only way to reach the fastest-growing markets.”

(Sales Growth Insights from Leading Sales Executives, McKinsey & Company 2011)



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Go To Market Strategy

- What is Your “Go to Market Strategy?”
- Will TPs and Intermediaries help you carry out that strategy?
- Factors may include:
 - Coverage strategy
 - Product segmentation
 - Price & margin expectation
 - Capabilities – technology, solution, price/value, resources, type of partner, product fit
 - Local legal requirements/termination/agency



Why Use TPs?

- **Coverage:** Can partnering extend the Company’s reach into existing and new markets with addition of distribution locations, proximity to customers or access to decision makers.
- **Competitiveness:** Can partnering help the Company serve its customers better by enhancing its offerings, adding complimentary value to customers, and bring efficiency to order fulfillment.
- **Customer:** In cases where partnering is required by customers, and the customer has a preference on who can best address their buying process, will working with third parties enhance the customer experience.



49

Hiring TPs: Factors to Consider

- **Business Model:** Do we need third parties to reach our customers or can we build the organization ourselves?
- **In-house Capabilities:** Do we already have the organization in place to handle these capabilities?
- **Overlap:** Do we already have a TP in the region/country that can handle our needs?
- **Volume of Business:** How much business will this TP bring?
- **Compliance Risk:** Where is the TP located? Will they interact with government officials? Do they have same commitment to compliance?
- **Regulatory Environment:** Simple or Strict? Chances of regulatory violations?
- **Reputation:** What is the TP's Reputation in the market?



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Onboarding

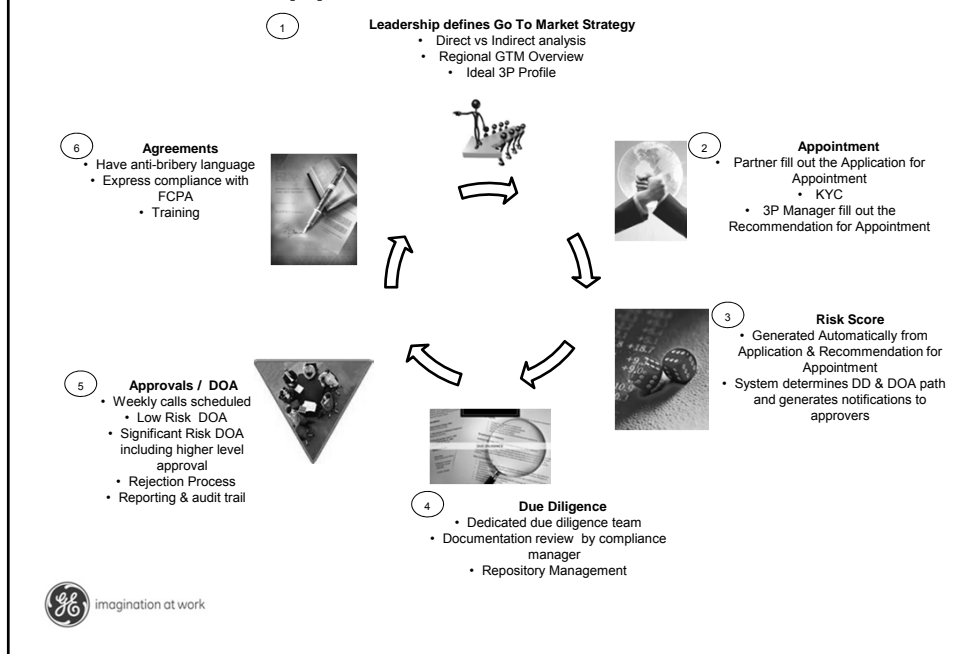
- Must have a rigorous onboarding process including:
 - Business need analysis
 - Financial analysis
 - Verified partner information (from all parties)
 - Thorough due diligence/screening
 - Balanced risk analysis

“Businesses may reduce the FCPA risks associated with third-party agents by implementing an effective compliance program, which includes due diligence of any prospective foreign agent”

- FCPA Guidelines pg. 23



Appointment Process



Compact Model Requirements?

- Rank by risk – low, medium, high
- Internet search
- Watch List Screening
- Reference Checks
- Interview TPs
- Agreement to abide by bribery, and anti-corruption laws
- Contract terms

Luxury Model

- Prioritize by risk level
- Require business sponsor and accountability
- Obtain written detailed application
- Electronic search
- Independent screening
- Reference checks
- Site visit and interviews
- Require written acknowledgement of Code of Conduct
- Ethics training
- Internal business, legal, compliance review of high risk partners
- Contract terms
- Internal and external audits
- Annual updates
- Quarterly re-screening



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21

Approaches Adopted in Managing TP Relationships *E&Y 2012 Survey*

Approved supplier database	59%
Background checking system	56%
Check on ownership of the third party	50%
Audit rights/regular audits of the third party	45%
Use external provider to run checks	34%
Use software – technology based check of third party	30%



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22

Risk Analysis - Process

- Low Risks – limited review and analysis
- High Risks – escalated review and analysis
 - Compliance Leader/Officer analysis
 - Legal review
 - Business Leadership review
 - Finance review/input
- High Level Internal Review Approval Process



23

Risk Score Drivers

- Country channel is located in or sells into
- Experience with channel
- Type of TP
- Commission rate – standard v. non-standard
- Sub-dealers
- Sell to government entity or instrumentality
- Principal, Officer or Agent work for government, entity or political party
- Mandated by customer/end user
- Contract duration
- More than one project
- Historical compliance issues
- Percent sales with products or services
- Annual revenue



24

Risk Analysis - Red Flags

- Excessive commissions to TPs
- Unreasonable discounts
- Vaguely described services
- TP in a different line of business than that for which it has been hired
- Close association with a foreign official
- TP required to be used by foreign official
- TP is a shell company incorporated offshore
- TP has an offshore bank account



25

Risk Scoring - Quantifying Risk



2010 CPI Examples

- Sweden	9.2
- Germany	7.9
- Japan	7.8
- UK	7.6
- US	7.1
- UAE	6.2
- S. Africa	4.7
- Saudi Arabia	4.5
- S. Africa	4.5
- Brazil	3.7
- China	3.5
- Nigeria	2.4
- Russia	2.1
- Iraq	1.5

The Corruption Perception Index (CPI) measures the perceived level of Public Sector Corruption in 178 countries around the world



Example Scoring factors considered in evaluating risk in 3P relationships

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Low Risk Risk Score ≤ xx	Significant Risk Risk Score > xx		

Compliance

- TPs must agree to:
 - Commit to compliance standards of company
 - Stay current and obey all applicable legal and regulatory provisions
 - Comply with all contractual provisions
 - Grant audit rights (define scope of rights)
 - Agree to report violations
 - Certify compliance on a regular basis
 - Site visits
 - Complete compliance training



Relationship Management

- Assign relationship manager/TP Manager
- Establish ongoing communications
- Provide ongoing training
 - Face to face training and online
 - Product/compliance/sales/services/EHS
- Provide platform for business improvement

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User Login

Username:

Password:

> Register New User
> Forgot Password?
> Contact Support

for SSO ID users

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Monitoring/Improving/Refining

- Processes in place to
 - Refresh due diligence
 - Review and Renew Agreements
 - Conduct and document regular site visits
 - Conduct periodic audits
 - Rationalization of TPs



When is Enough Enough?

- When you can show the government agency asking that you have taken appropriate steps to design, implement, and enforce a compliance program that is generally effective in preventing and detecting criminal conduct.

§8B2.1 U.S. Federal Sentencing Guidelines



30

Thank you.



31