

TEID Ethics Summit 2015

**Third Party Due Diligence and
Compliance: What is Required of
Multinational Companies and
their Global Business Partners**

Severin Ian Wirz

Director, Advisory Services

17 June 2015



Third Parties – A Perennial Risk

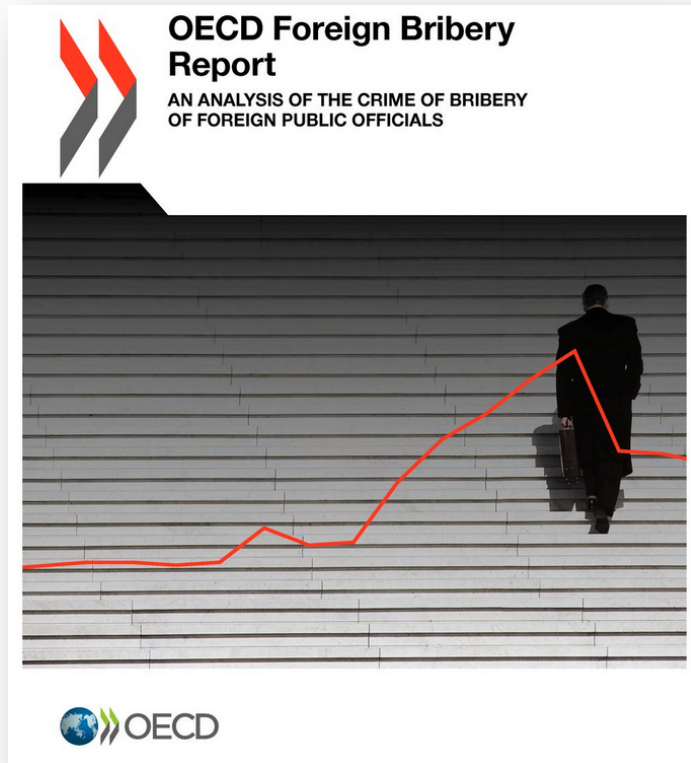
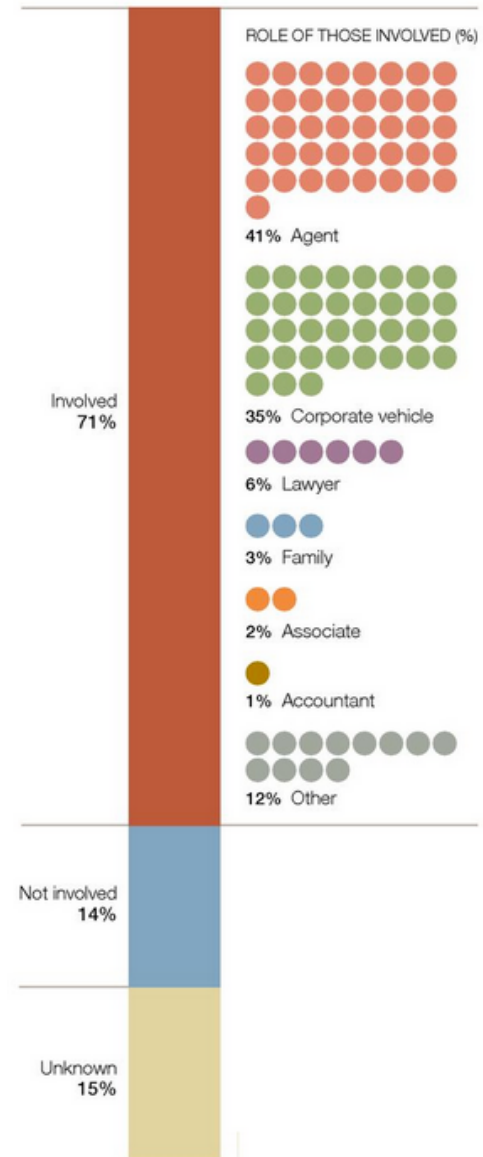
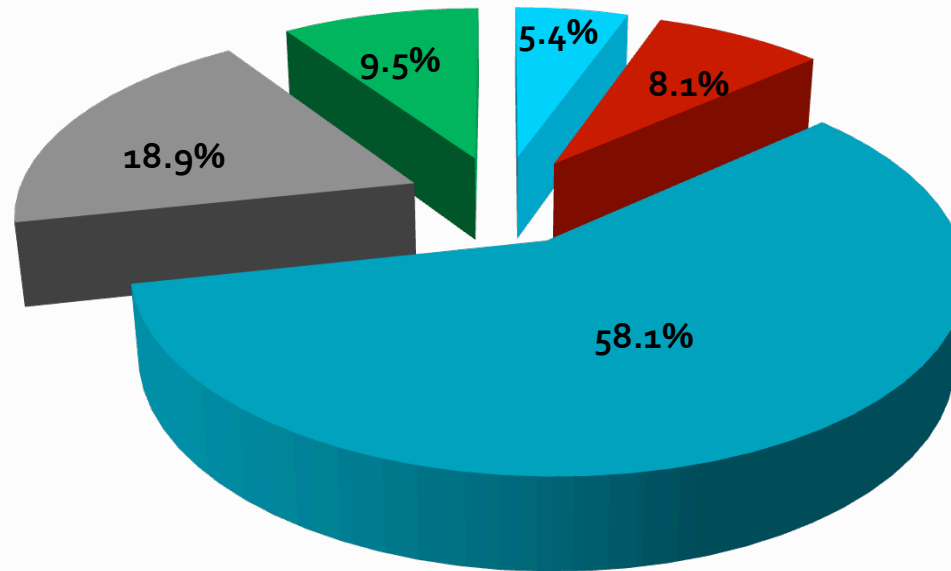


Figure 16. The involvement and role of intermediaries in foreign bribery cases



Source: OECD analysis of foreign bribery cases concluded between 15/02/1999 and 01/06/2014. Based on the 304 cases in which intermediaries were used.

What do you view as your company's most significant anti-bribery compliance challenge?



- Understanding government expectations when evaluating adequacy of compliance programs
- Gifts, hospitality and entertainment
- Third party due diligence ← 58.1%
- Supply and marketing chain compliance
- Dealing with state-owned enterprises

What is a “Third Party”?

- A third party is an intermediary who is put in contact with or in between two or more trading parties.
- A third party is usually understood to be a conduit for goods or services offered by a supplier to a consumer.
- A third party can act as a conduit for legitimate economic activities, illegitimate bribery payments, or a combination of both.
- Business inherently rely upon third parties to achieve a wide range of business objectives.

Third parties include:

- suppliers
- freight forwarders
- agents, traders
- consultants
- resellers
- distributors
- channel partners
- system integrators
- subcontractors
- customs brokers
- JV partners, etc.

Legal Framework: Agents and “Knowledge”

- Under many countries’ foreign bribery laws, the company is responsible for any improper payments made by third parties where a company employee has “knowledge” that the bribe will be paid.
- Knowledge includes:
 - Actual knowledge
 - Constructive knowledge
- Under the law, a person “knows” a bribe will occur if they are aware of circumstances that indicate a payment is a high probability

Third Party Liability

Third Party	Company	Allegations
Distributors	Biomet, Inc.	Distributors paid bribes on Biomet's behalf to doctors in China and Brazil.
Sub-contractors	IBM Argentina	Subcontractor made payments to Argentinian bank owned by Argentine government on behalf of IBM.
Resellers	Veraz Networks	Singapore reseller paid bribes to state-controlled Vietnamese company on behalf of company.
Sales Agents	InVision Technologies Inc.	Sales agents paid exorbitant commissions with knowledge that money would be used to pay officials in China and the Philippines.
Charitable organizations	Eli Lilly	Small charitable foundation used as intermediary for payments to Polish health official.
Suppliers	Siemens	Investigation included improper payments to supplier related to oil and gas business in Central Asia.
Customs agents/brokers	Diageo Plc	Kickbacks to a third-party customs broker used to pay \$86,339 in bribes to a Korean customs service official.
Legal service providers (e.g. notaries)	Alcatel	Notary entered into several sham agreements on behalf of Alcatel to obtain telecommunications contracts in Costa Rica.
Freight forwarders	Panalpina World Transport (Holding) Ltd.	Freight-forwarding company paid bribes on behalf of several oil and gas companies in order to circumvent local import rules and regulations.
Marketing/advertising advisors	BAE Systems PLC	BAE was held liable for failing to maintain proper accounting records for payments made to marketing advisors in Tanzania and other jurisdictions.
Real estate agents/brokers	Montedison S.p.A.	Real estate developer paid bribes to Italian politicians on company's behalf in connection with a dispute over control of a joint venture.
Joint venture partners	Rae Systems	Chinese joint venture partner used to pay bribes to Chinese public officials on behalf of US company.
Lawyers	TSKJ	British lawyer Jeffrey Tesler was hired to pay bribes to Nigerian officials on behalf of oil and gas consortium.
Accountants	Baker Hughes	Indonesian accountant paid \$75,000 in bribes to local Indonesian tax official on behalf of Baker Hughes.
Lobbyists	Tatra A.S.	Indian lobbyist offered bribe to army general to purchase defective Tatra equipment.

Managing Third Party Risks

1. Background “due diligence” prior to partner on-boarding or retention
 - Can be renewed on annual or biennial basis
2. Contractual assurances and commitments
3. Anti-corruption training and communications
4. Transactional “due diligence” to examine unusual circumstances and auditing of invoices/outlays

NOTE: Third Party Risk is Not Just About the Third Party

- Third parties can be a vehicle for corrupt payments, but in ALL cases there is **collusion** between employee(s) of the company and the third party (e.g. falsification or of invoices).
- Third party due diligence is necessary, but to eliminate all third party risk you also need **a range of controls** to train and monitor your employees.
- An effective compliance program integrates risk-mitigation controls across a variety of areas of the business.

1. Background Due Diligence on Third Parties

- U.S. DOJ and SEC considers the **level** and **thoroughness** of Third Party Due Diligence when they decide whether to prosecute under the FCPA.
- “Due diligence of specific prospective **third party intermediaries** could significantly mitigate these risks.” *UK Bribery Act 2010 Guidance*, p. 28 (UK Serious Fraud Office)

Due Diligence#1: Business Justification

Legitimate

- Intermediary provides necessary service that business cannot accomplish on its own
- Government mandates use of intermediaries

Illegitimate

- An official's family, friends and other third persons act as intermediaries
- Intermediaries who do not provide any identifiable service
- Intermediaries who provide a combination of legitimate and illegitimate goods and services

Business Justification

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA
10-20907-CR-MOORE/SIMONTON
CASE NO.

15 U.S.C. § 78m(b)(2)(B)
15 U.S.C. § 78m(b)(2)(A)
15 U.S.C. § 78m(b)(5)
15 U.S.C. § 78ff(a)
18 U.S.C. § 2

UNITED STATES OF AMERICA

vs.

ALCATEL-LUCENT, S.A.,
f/k/a "Alcatel, S.A.,"

Defendant.



government official, in exchange for favorable treatment of ALCATEL, Alcatel CIT, and Alcatel Mexico.

55. In or around 2002, at the request of the brother of Senior Government Official 2 in Honduras, Alcatel Standard retained a new consultant in Honduras, Honduran Consultant 1, to perform vaguely described marketing and advisory services such as "maintaining liaisons with appropriate government officials." Honduran Consultant 1, however, was, in fact, an exclusive distributor of "brand name perfumes," and had no contacts in, or prior experience with, the telecommunications industry in Honduras or anywhere else. Rather, Honduran Consultant 1 was selected by Senior Government Official 2's brother, who instructed Sapsizian and an ACR employee to use Honduran Consultant 1 as an agent. Sapsizian and other ACR employees believed that all or some of the money paid to Honduran Consultant 1 would be paid to Senior

Common Red Flags for Third Parties

- The Third Party refuses to certify compliance with anti-bribery laws
- The Third Party wants to work without a contract or with a vague contract
- The Third Party requests payments that are to be
 - made to a party other than the party named in the contract
 - directed to a country other than where the counterparty is located or the service is rendered
- The Third Party has family or business ties to Government Officials
- The Third Party is owned, in whole or in part, by a Government Official
- The Third Party uses a shell company, holding company, blind trust or other structure in order to obscure ownership or the identity of its principals

Due Diligence#2: Collecting Information on Qualifications and Background

- Corporate information, e.g. business registration documents, names of owners, partners, principal officers, shareholders, affiliated companies, etc.
- Financial references and data
- Qualifications and experiences of the intermediary, its officers and personnel
- Relationship between the intermediary's owner or employees and any government official;
- Description of organizations and people who will work on behalf of the company;
- Reputational checks (denied parties watchlists, media, internet, etc.)
- Litigation and bankruptcy history
- World Bank Debarment Lists

Due Diligence #3: Assessment of Risk

- Third Party Qualifications/Business Rationale
- Payment Terms
- Possible conflicts of interest
- Level of interaction with government officials
- Geographic risks
- Existing Compliance Program

Sales and Distribution Risk Matrix

1. TERRITORY RISK	Territory Risk Level 1 (LOW RISK)			Territory Risk Level 2 (MEDIUM RISK)			Territory Risk Level 3 (HIGH RISK)			Exceptional Territories (HIGH RISK)
	1.1 (< 30%)	1.2 (30% or above & < 65%)	1.3 (65% or above)	2.1 (< 30%)	2.2 (30% or above & < 65%)	2.3 (65% or above)	3.1 (< 30%)	3.2 (30% or above & < 65%)	3.3 (65% or above)	All Deals
Due Diligence	Steele Open Source Investigation (OSI)	Steele OSI	Steele OSI	Steele OSI	Steele OSI	Steele Enhanced Due Diligence (EDD)	Steele OSI	Steele EDD	Steele EDD	Legal Entities: Steele or Alpha Search + Site Verification
				Dunn & Bradstreet (D&B)	D&B		D&B			Indiv: Steele or Alpha (Only Ukraine, Belorussia, Kazakhstan) EDD elsewhere
	⊖	⊖	⊖	⊖	⊖	⊖+ Reference Check	⊖	⊖+ Reference Check	⊖+ Reference Check	⊖+ Reference Check
Training	⊖	⊖	⊖	⊖	⊖	⊖ Training on Anti Corruption policy & other relevant policies for all Intermediary employees working on NBCU a/c & NBCU employees working with them. Confirm familiarity with local bribery laws (Webex/phone). Obtain Acknowledgement	⊖	⊖ Training on Anti Corruption policy & other relevant policies for all Intermediary employees working on NBCU a/c & NBCU employees working with them. Confirm familiarity with local bribery laws (In person/vid conf). Obtain Acknowledgement	⊖ Training on Anti Corruption policy & other relevant policies for all Intermediary employees working on NBCU a/c & NBCU employees working with them. Confirm familiarity with local bribery laws (In person/vid conf). Obtain Acknowledgement	⊖ Training on Anti Corruption policy & other relevant policies for all Intermediary employees working on NBCU a/c & NBCU employees working with them. Confirm familiarity with local bribery laws (In person). Obtain Acknowledgement
	⊖	⊖	⊖	⊖	⊖	⊖ Right to conduct Audit without cause	⊖	⊖ Right to conduct Audit without cause	⊖ Right to conduct Audit without cause	⊖ Right to conduct Audit without cause
Written Contractual Safeguards	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖
Monitoring & Auditing	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖
Approval	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖	⊖ IRB Approval (1 year app term)	⊖ IRB Approval (1 year app term)

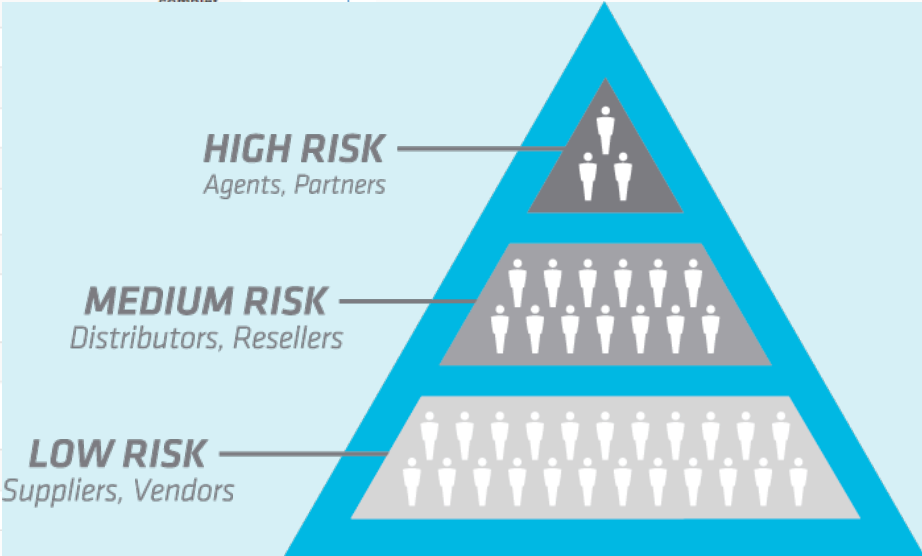


Software Tools

Completed DDCs

Company: TRACE International | Review Period: 03/04/2014- No End Date | Internal Sponsor: All

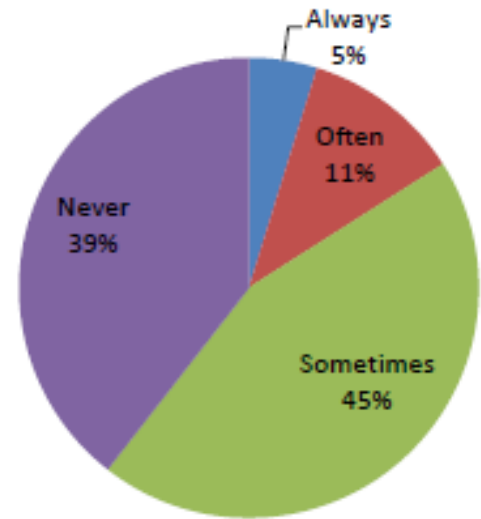
Tracking#	Company Name	Internal Sponsor	Original Score Range	Adjusted Score Range	Submitted Date	Due Diligence
12-234-45	Test Company A	TRACECustomerAdmin	Low Risk	Medium Risk	11/19/2014	No red flag
23-345-56	Test Company B	TRACECustomerAdmin	Medium Risk	Low Risk	11/12/2014	Reviewed r 3...
	Test Company C	TRACECustomerAdmin	Low Risk	Low Risk	11/12/2014	This comp...
	Test Company D	TRACEUser3	Low Risk	Low Risk		
	Test Company E	TRACEUser4	High Risk	High Risk		
	Test Company F	TRACEUser5	Medium Risk	Medium Risk		
	Test Company G	TRACECustomerAdmin	High Risk	Medium Risk		
	Test Company J	TRACECustomerAdmin	High Risk	High Risk		
123456M	Test Company M	TRACECustomerAdmin	Low Risk	Medium Risk		
	Test Company V	TRACECustomerAdmin	High Risk	Medium Risk		
	Test Company T	TRACECustomerAdmin	High Risk	Medium Risk		
	Test Company Y	TRACECustomerAdmin	Medium Risk	Low Risk		
124569	Test Company U	TRACECustomerAdmin	Low Risk	Low Risk		
	Test Company N	TRACECustomerAdmin	Medium Risk	Low Risk		



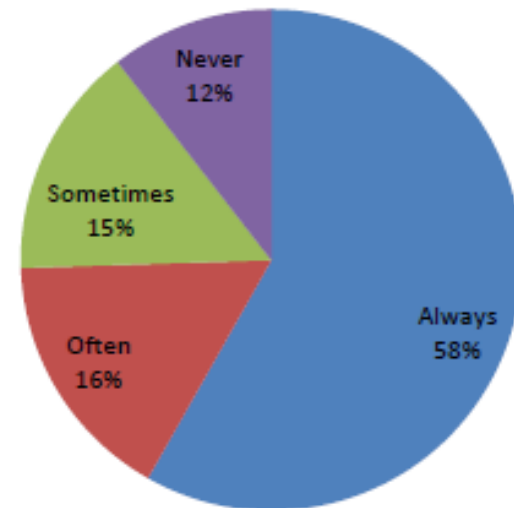
2. Contractual Assurances

- Anti-bribery representations and warranties;
- Vendor re-certification of compliance with applicable anti-bribery laws and regulations;
- The right to audit expenses paid on behalf of the Company upon a reasonable suspicion of wrongdoing;
- Delegation of work (sub-contracting);
- Termination rights for improper conduct

How often does anti-bribery compliance arise as an issue in your contract negotiations?



How often do you include provisions on anti-bribery compliance in your contracts?



How important is this, really?



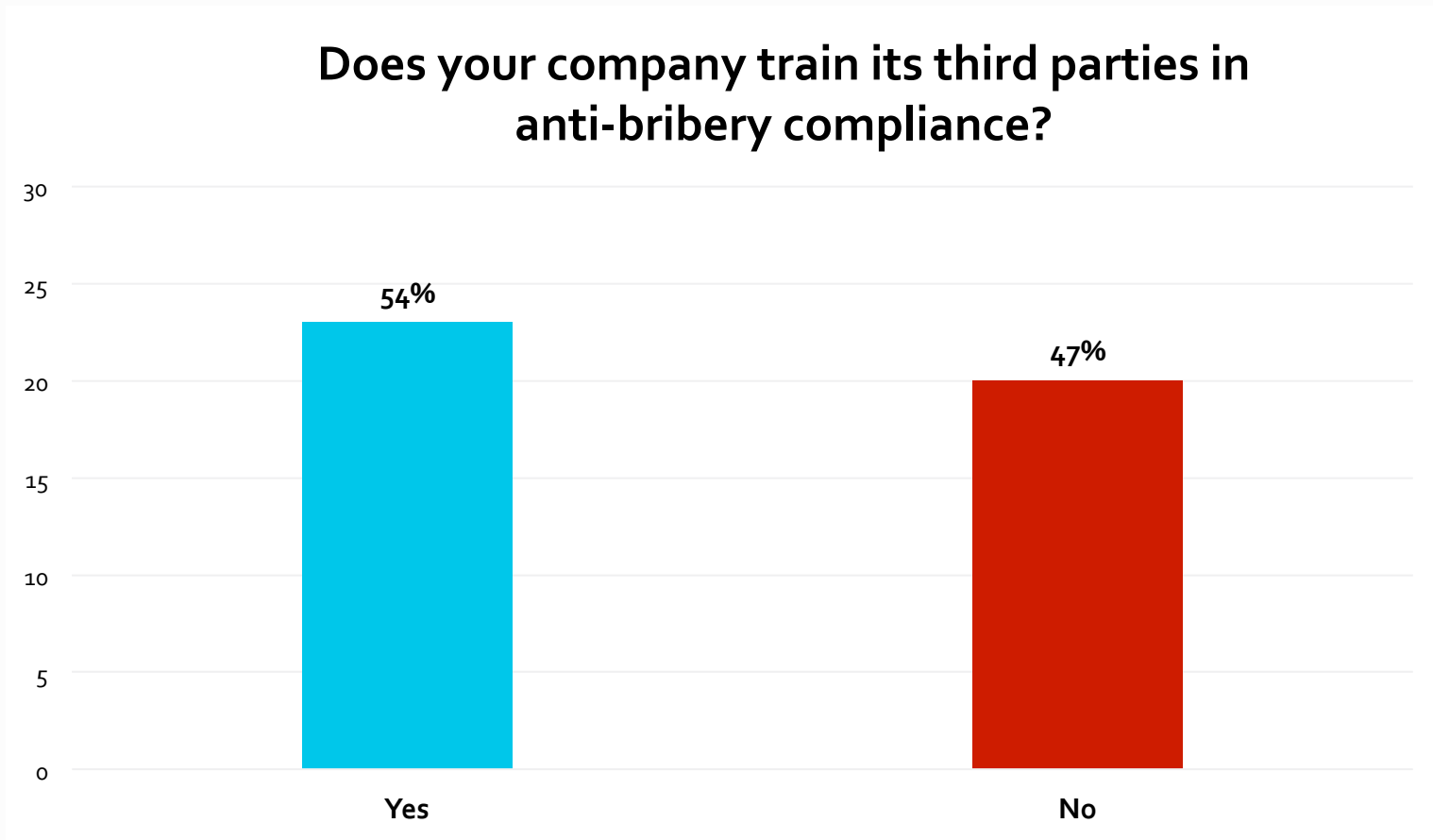
UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

U.S. SECURITIES AND EXCHANGE COMMISSION,)	
)	
Plaintiff,)	4:13-cv-3500
)	
v.)	
)	
WEATHERFORD INTERNATIONAL LTD.)	
)	
Defendant.)	

COMPLAINT

14. WSL entered into a consultancy agreement with the Swiss Agent. The original draft of the consultancy agreement used by Weatherford’s legal department included an FCPA clause prohibiting the Swiss Agent from giving anything of value, directly or indirectly, to an official or employee of any government. **The Swiss Agent rejected the clause in an email stating that “in view of the nature of the business I cannot accept the original wording.”** Despite this red flag, no steps were taken to ensure that the agent was not paying bribes to foreign officials. Instead, Weatherford’s legal department in Houston permitted WSL to enter into the consulting agreement without the FCPA clause, and with an alternate clause simply requiring the agent to “comply with all applicable laws, rules and regulations issued by any governmental entity in the countries of business...”

3. Anti-corruption training and communications



4. Ongoing Monitoring of Third Party

- Renewal of due diligence/business justification
- Auditing of invoices/unusual payments
- Due diligence of subcontractors
- Live training sessions

Hypothetical: Outlays and invoices

- As part of an internal audit of a subsidiary, you come across the following invoice from a 3rd party customs and immigration broker:

OUTLAYS	
1 - SHORT TERM VISA X 10	850.00 ✓
2 - EMERGENCY VISA	2,400.00 ✓
3 - IMIGRATION FINE	250- 1,110.00
4 - CASH ADVANCE	1,911.00 ✓
<hr/>	
SUBTOTAL ON OUTLAYS	USD 6,271.00

What suspicions does this provoke? How should you respond?

What is Portable Due Diligence?



- “Portable” reporting represents an **evolution** in due diligence.
- Third parties complete due diligence process – to a high standard – **one time per year** at the entity’s expense.
- Portable due diligence ***helps companies realistically manage risk*** across **thousands** or **tens of thousands** of suppliers.

Questions?



Visit us online at

www.TRACEinternational.org

 facebook.com/TRACEinternational

 twitter.com/TRACE_inc

 youtube.com/TRACEinternational

 [linkedin.com/company/
TRACE-international-inc.](https://linkedin.com/company/TRACE-international-inc.)

