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Anti-Corruption Compliance: Avoiding Liability for the Actions of Third Parties

KEITH M. KORENCHUK, SAMUEL M. WITTEN, AND DAWN Y. YAMANE HEWETT

This article outlines the key legal considerations and practical steps companies can take to protect themselves from undue risks in working with third parties.

Nearly every company in today's global economy does business by using a combination of its own employees and third parties to help it perform essential tasks, such as dealing with government officials to obtain permits to do business and perform services, complying with local law and regulation, and moving personnel and goods across borders. In today's environment of heightened enforcement of anti-corruption laws, however, every company should be aware that the actions of third parties on its behalf can lead to exposure to major liabilities if those third parties act corruptly in violation of applicable law.

Under the US Foreign Corrupt Practices Act[1] ("FCPA"), the UK Bribery Act,[2] and many other laws, a company can be held liable not only for the corrupt actions of its employees, but also a third party's actions when

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Keith M. Korenchuk, a partner in the Washington, D.C., office of Arnold & Porter LLP, counsels and advises global companies on regulatory and compliance matters worldwide. Samuel M. Witten is counsel, and Dawn Y. Yamane Hewett is an associate, in the firm's office in Washington. The authors can be reached at Keith.Korenchuk@aporter.com, Samuel.Witten@aporter.com, and Dawn.Yamane.Hewett@aporter.com, respectively.

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that third party acts on its behalf. The FCPA, for example, contemplates enforcement actions when a bribe or offer of something of value is made to a foreign government official "for the purpose of obtaining or retaining business for or with, or directing business to, any person," including where the bribe or offer is made indirectly through a third party.[3]

Companies should therefore be vigilant in selecting and monitoring third parties that act on their behalf. For most companies, this means developing and implementing a rigorous third party due diligence program to properly identify, mitigate, and respond to the specific risks associated with the use of their third parties. This article outlines the key legal considerations and practical steps companies can take to protect themselves from undue risks in working with third parties.

OVERVIEW OF LEGAL FRAMEWORK

There are many types of third party actions that regularly implicate anti-corruption laws such as the FCPA. For example, regulatory third parties (such as vehicle licensing agents and visa processors), shipping third parties (such as customs brokers and freight forwarders), and professional services third parties (such as lawyers, accountants, regulatory consultants, travel agencies securing visas, and lobbyists) regularly deal with host government authorities. In a large number of settled cases, the conduct of third parties has led to liability for companies when operating on their behalf. For example, in the U.S., the Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC") charged Alcatel-Lucent with using third party consultants to bribe foreign government officials in Costa Rica, Honduras, Malaysia, and Taiwan, fining the company over $137 million (U.S.) in civil and criminal penalties.[4] The corrupt payments included agreements with consultants to pay bribes in exchange for contracts and nonpublic information regarding tenders, as well as payments to consultants who never performed work for the company. U.S. regulators have vigorously pursued cases involving third parties[5] and the DOJ has made clear in its recent series of deferred prosecution agreements under the FCPA that companies must develop and implement robust internal anti-corruption compliance regimes to guard against corrupt payments by third parties.

Importantly, companies can be liable for the wrongful actions of their third parties not only if they instruct them to undertake corrupt acts, but also if they show willful blindness toward, deliberately ignore, or consciously disregard suspicious actions or circumstances. In this respect, third party liability under the FCPA and other anti-corruption laws[6] is of particular concern, because third parties conducting business in other countries often operate under different cultural norms and expectations, and some third parties may view illicit actions as consistent with, and even necessary in, local markets. Indeed, some studies have shown that most of the major anti-corruption cases in recent years have involved third parties. In 2010, the vast majority of the settled cases have included third parties.

With this backdrop of heightened enforcement and the high risks inherent in using third parties, it is critical for companies to establish and maintain a third party due diligence review process for making critical inquiries about third parties. The following steps provide a roadmap, based on our experience, to assist companies worldwide in designing, implementing, and operating compliance programs, combined with our analysis of language on third party compliance programs in recent FCPA deferred prosecution agreements.

IMPLEMENTING AN APPROPRIATE THIRD PARTY DUE DILIGENCE PROGRAM

As detailed below, a properly organized and implemented third party anti-corruption due diligence program will have a number of essential elements, all of which should be in place and in continuous use for the program to work effectively.

➤ The framework should be based upon a risk assessment of the business and how, when, and why it uses third parties.

➤ The compliance program should be formalized in written policies and procedures, and they need to be accompanied by a clear top-down instruction about the importance of following those procedures (the "tone at the top" must be clear).

➤ The company must determine which third parties are "in scope" for the third party due diligence review, typically focusing on those third parties that are likely to be interacting with government officials or are in high-risk locations for corruption.

➤ The actual due diligence should consist of a more than careful review of third party selection and conduct by appropriate company officials, the exact structure of which will depend on the risks related to the activities of the third party.

➤ The company should employ mechanisms to minimize and mitigate risks brought on by the use of third parties, including oversight options discussed below.

➤ The company should monitor and audit the company's payment of third parties, including, in many cases, the payments made by the third parties, to ensure that the third party's actions comply with the company's policies and relevant anti-corruption laws. The company must also have mechanisms in place to take quick and decisive action in the event corruption is discovered at any stage in the review or the ongoing relationship.

➤ Finally, the company should consider who should actually conduct and oversee the entire due diligence review process, as every company should organize its compliance framework to meet its particular needs.

1. RISK ASSESSMENT

The first step to implementing any due diligence program is a well-considered cost/benefit analysis and risk assessment of the hiring, retention, and oversight of third parties.[7] Every company will have a different assessment process depending on a number of factors, such as the type of business in which the company is engaged, the markets in which it operates, the contemplated interactions with foreign government officials, the types of third parties typically used for such interactions, the way the company is structured, and the company's anticipated growth and business plan. It is clear, however, that a risk assessment must identify key types of interactions creating risk, the types and locations of third parties who perform work on behalf of the company, and the frequency of those interactions. A comprehensive risk assessment will act as the cornerstone of the design and operation of the third party due diligence program, as it guides key program design questions as to the scope, intensity, resources, and organization of the program.

One key threshold question is whether the use of any particular third party is fundamentally necessary to achieve the company's business objectives or whether the actions contemplated can be handled "in house," which frequently brings with it better oversight, more accountability, and potentially significant cost-savings. Indeed, because a company generally has less control over third parties than it would over its own internal operations, a company should consider whether the potential liability engendered by the use of third parties is appropriate and worth the risk.

2. CLEARLY ARTICULATED WRITTEN POLICIES AND PROCEDURES

Once a company conducts its assessment and confirms the necessity of using third parties for particular tasks, the next step is to develop and implement clear anti-corruption policies and procedures detailing the third party review. These policies and procedures must be known to all company directors, officers, and employees, as well as to actual and potential third parties.[8] These written materials should have a number of underlying objectives, including: providing a framework for identifying, reporting, and resolving warning signs of corruption arising out of the third party review; minimizing actual corruption risks; and ensuring the company is partnering with appropriately qualified third parties for proper business purposes. The risk assessment and the written policies and procedures the company creates will drive the questions asked in the actual review process outlined below.

Most importantly, the written policies and procedures cannot be simply announced on paper — they must be accompanied by clear and unambiguous instructions from the top of the company that the compliance framework is essential and non-discretionary, and there must be substantial consequences for failing to follow the policy.

3. WHICH THIRD PARTIES ARE "IN SCOPE"?

The first level of review is to determine which third parties are "in scope" and thus should be subjected to a heightened due diligence review. In this respect, all third parties that deal with foreign government officials on behalf of a company present corruption risks and should therefore be presumptively "in scope." In this connection, because each company will need to develop its risk analysis based on its own circumstances, it may decide that certain third parties are automatically "in scope" if they hold contracts with the company over a certain monetary threshold. Companies may also want to consider the type of government interactions likely to be pursued by third parties and also the country or countries in which the third party operates. For example, because of endemic corruption risks in a particular country, a company may decide that *all* third parties operating in that country are "in scope," even if their primary responsibilities do not include government interactions on behalf of the company. If the third party is not "in scope" (e.g., it is not expected to have dealings with foreign governmental authorities on behalf of the company or is otherwise not subject to additional scrutiny), then companies may choose to limit or adapt the due diligence described below or may decide it is ultimately unnecessary.[9]

4. HEIGHTENED REVIEW FOR THIRD PARTIES "IN SCOPE"

For those third parties "in scope," some kind of a multi-tier system of review should follow, both in vetting them for possible relationships and in overseeing their work for the company. The type and structure of such a review will be a highly individualized decision for each company, based on important issues of timing, manner, and the depth of review of existing third parties and new third parties. However, there are some common elements that should be present in any effective program:

- After the initial determination of which third parties are "in scope," the company should ask those parties some preliminary questions on a variety of relevant issues, including, but not limited to, their qualifications, staffing, level of experience, references, and history. These responses are typically provided by a third party in a written questionnaire.

- The company should also conduct reference checks with other parties with whom a third party conducts business, but should not include any references who may receive compensation from the third party under review. The results of these inquiries should be thoroughly documented.
- A background search for news concerning a third party's prior conduct, as well as the conduct of the third party's owners, officers, directors, senior management, and those executives who are principally involved in the relationship with the company, is also an essential part of the review. These searches will also assist in identifying any connections or relationships with government officials. Options for conducting these types of searches include commercial databases, the Internet, local news sources, and the local U.S. or other relevant embassy.
- The company at each point in its due diligence process should look for the classic warning signs of corruption, such as excessive requests for compensation, substantial amounts sought in advance, payments going to third parties' subcontractors, payment only upon "success," or involvement of government officials in the company or its operations. If there are still questions, the company should always leave open the option of a further review with additional follow up questions and due diligence review relating to actual or possible problems, which could involve further questions, a background search, or a site visit. The situation may also require the hiring of an outside expert to conduct a more detailed diligence review.
- In the course of conducting the due diligence review, if warning signs cannot be resolved, the company may decline to begin a relationship with a new third party or terminate its relationship with an existing third party. Companies may seek to address potential warning signs — if possible and prudent — through enhanced reporting, more training, a more robust compliance program, anti-corruption contract clauses, more auditing, ongoing monitoring, or other risk-mitigation strategies.
- In addition to an initial review, the company should have a policy on how often a third party should be reviewed again. Most companies

will elect to review each third party relationship at set periods, for example, every two to three years.

5. TOOLS A COMPANY MAY USE TO MITIGATE CORRUPTION RISKS WITH THIRD PARTIES

Companies should have available a number of tools to mitigate corruption risks associated with the use of third parties. For example, the company should require annual compliance certifications (and, as set forth above, conduct periodic in-depth reviews). The finance function at the company should conduct a careful and independent review of any expenses and reimbursement requests sought by the third party prior to authorization of payment. This might include checking claims for payment carefully against the obligations under the contract and generally watching for warning signs of corruption. Finally, companies should include standard anti-corruption provisions in third party contracts. Depending on the circumstances, and as noted very clearly by the DOJ in recent deferred prosecution agreements, these contractual clauses might include:

> (a) anti-corruption representations and undertakings relating to compliance with the anti-corruption laws; (b) rights to conduct audits of the books and records of the agent or business partner [third party] to ensure compliance with the foregoing; and (c) rights to terminate an agent or business partner as a result of any breach of anti-corruption laws, and regulations or representations and undertakings related to such matters.[10]

Companies may also want to seek a written contractual commitment from their agents and business partners that they will comply with the company's policies and procedures and anti-corruption laws.[11]

6. MONITORING AND AUDITING

An important aspect of implementing a third party due diligence process is including a systematic and reliable way to monitor, audit, and review its third party relationships. Companies must have clear and defensible audit plans that provide oversight of their relationships with their third parties. The company may elect to impose an audit plan with respect to a selected portion of its third parties. The determination of which third parties to audit should be based on the initial risk assessment conducted by the company and a supportable rationale for the sample size selected and audit plan methodology to be utilized. In addition, if the company requires an annual certification demonstrating the third party's compliance with any terms that mitigate risks, the monitoring plan may include an inquiry into whether a third party actually has demonstrated compliance.

The auditing function should already be built into a company's internal controls through its finance function (i.e., a careful comparison of expenses and reimbursement claims against contractually required documentation and actual expenditures). In addition to the finance check, another control that many companies use is to designate a person within the company as the lead point of contact to manage the relationship between the company and the third party. This lead point of contact should have actual and ongoing knowledge of all relevant activities of the third party on behalf of the company. No matter the type and extent of the monitoring and auditing, the company should be sure to document its oversight so that the monitoring and auditing process itself can be reviewed periodically to ensure its effective operation.

7. WHO OVERSEES AND ADMINISTERS THE DUE DILIGENCE PROGRAM

A successful third party due diligence program needs support from top leadership as well as adequate staff and resources to administer such a program. Each company should consider a number of factors in deciding who actually administers the overall program, and each organization will have its own approach to who should conduct the due diligence review. Relevant considerations might include:

- The type of business involved and how it operates, with considerations including size, complexity, lines of business, and decision makers;

- The extent to which a company is decentralized or centralized and the roles to be undertaken by headquarters versus regional and local operations;
- The role of the legal department at various phases of the development and oversight of third party relationships; and
- Whether the due diligence relating to third parties should be conducted internally or externally, and if externally, at what point the external reviewers should become involved in the process.

The company personnel that actually conducts the due diligence review must understand the level of risk of relevant third parties, be specifically trained to address this risk, and understand how to raise concerns within the company when third party issues arise. It is also clear that to be effective, a review program must have built-in mechanisms to ensure consistency of review across the company, a mechanism to create and maintain a complete review "file" to document the work undertaken and the resolution of any warning signs, and appropriate oversight of program operation by senior management, regardless of how decentralized the implementation of the review. Accountability of those conducting the review for the company is also essential for program success.

CONCLUSION

Companies that carefully develop and implement a third party anti-corruption due diligence program will minimize the risks that arise when working with third parties. While the principles stated above provide some appropriate guideposts and checklists, risk assessments and mitigation programs must be individually tailored to particular company needs, capabilities, and markets. In this era of heightened enforcement of anti-corruption laws, inaction or a failure to properly oversee the actions of one's third parties is simply not an option.

NOTES

[1] The FCPA prohibits a broad range of persons and businesses, including

U.S. and foreign issuers of securities registered in the United States, from making a corrupt payment to a foreign official for the purpose of obtaining or retaining business for or with, or directing business to, any person. These provisions also apply to foreign persons and companies that take any act in furtherance of such a corrupt payment while in the United States.
The FCPA also requires companies with securities listed in the United States to meet its provisions on recordkeeping and internal accounting controls. These accounting provisions were designed to operate in tandem with the anti-bribery provisions of the FCPA, and require companies covered by the law to make and keep books and records that accurately and fairly reflect the transactions of the company and to devise and maintain an adequate system of internal accounting controls.

[2] 2010 UK Bribery Act, *available at*: http://www.legislation.gov.uk/ukpga/2010/23/pdfs/ukpga_20100023_en.pdf.

[3] 15 U.S.C. §§ 78dd-1, et seq. (1977).

[4] Deferred Prosecution Agreement, *United States* v. *Alcatel-Lucent, S.A.,* No. 10-20907 (S.D. Fla. Dec. 27, 2010) (Alcatel-Lucent DPA); SEC Files Settled Foreign Corrupt Practices Act Charges Against Alcatel-Lucent, S.A. with Total Disgorgement and Criminal Fines of Over $137 Million, SEC Litigation Release No. 21795 (Dec. 27, 2010), *available at*: http://www.sec.gov/litigation/litreleases/2010/lr21795.htm.

[5] *See, e.g.*, Alcatel-Lucent DPA; *see also*: *United States* v. *Siemens Aktiengesellschaft*, No. 1:08-cr-00367-RJL (D.D.C. Dec. 12, 2008). The enforcement action against Siemens resulted in the largest FCPA fines paid in history, totaling $800 million (U.S.) in civil and criminal penalties.

[6] The UK Bribery Act is likely to be interpreted even more widely in scope than the FCPA, prohibiting bribes not just to foreign officials but to commercial parties as well. Unlike the FCPA, the Bribery Act does not require that the government prove the *mens rea* (i.e., that that the bribe be paid or offered corruptly). The principles in this article related to an effective compliance structure regarding third parties are consistent with the Guidance issued by the British Government in connection with the Bribery Act. The Bribery Act was enacted on April 8, 2010, and comes into force on July 1, 2011.

[7] Alcatel-Lucent DPA, C-5; Deferred Prosecution Agreement Attachment C, *United States* v. *Panalpina World Transp. (Holding) Ltd.,* No. 10-00765 (S.D. Tex. Nov. 4, 2010) (Panalpina DPA), C-6 ("To the extent that the use of agents and business partners [third parties] is permitted at all by [the company], it will

institute appropriate due diligence and compliance requirements pertaining to the retention and oversight of all agents and business partners, including…. Properly documented risk-based due diligence pertaining to the hiring and appropriate and regular oversight of all agents and business partners.”).

[8] The DOJ has required that companies inform all third parties of the company's “commitment to abiding by laws on the prohibitions against foreign bribery, and of [the company's] ethics and compliance standards and procedures and other measures for preventing and detecting such bribery.” Alcatel-Lucent DPA, C-5; Panalpina DPA, C-6 & C-7.

[9] Of course, simply because a third party is not “in scope” for the heightened due diligence review, the company should not ignore the possibility of corruption issues and may want to take additional steps to ensure compliance with these or other laws, including appropriate reviews and certifications. It may also be wise for the company to insert standard provisions in all third parties' contracts, regardless of whether the third party is “in scope” or not.

[10] Deferred Prosecution Agreement Attachment C, *United States* v. *Tyson Foods, Inc.,* No. 1:11-CR-00037 (D.D.C. Feb. 10, 2011), p. 23; Alcatel-Lucent DPA, C-6; Panalpina DPA, C-7.

[11] To mitigate corruption risks, some companies may want to consider asking third parties to train their employees or in appropriate cases even offer to train the employees themselves.