COMPREHENSIVE FCPA GUIDE TO DUE DILIGENCE FOR THIRD PARTIES

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# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
<td>3</td>
</tr>
<tr>
<td>Assessing the Company’s Third Party FCPA Risks</td>
<td>3</td>
</tr>
<tr>
<td>Creating an FCPA Policy for Third Parties</td>
<td>3</td>
</tr>
<tr>
<td><strong>Components of the Due Diligence Process</strong></td>
<td>4</td>
</tr>
<tr>
<td>1. Business Justification</td>
<td>5</td>
</tr>
<tr>
<td>2. Due Diligence Checklist</td>
<td>5</td>
</tr>
<tr>
<td>3. Intermediary’s Due Diligence Questionnaire</td>
<td>6</td>
</tr>
<tr>
<td>4. Agent Interviews</td>
<td>7</td>
</tr>
<tr>
<td>5. and 6. Review of Due Diligence and Resolution of any Red Flags</td>
<td>7</td>
</tr>
<tr>
<td>7. Agent Contracts</td>
<td>9</td>
</tr>
<tr>
<td>Ongoing Monitoring &amp; Audit of Agent Relationships</td>
<td>9</td>
</tr>
</tbody>
</table>
Introduction
Under the FCPA, a company can be liable for the activities of its agents, consultants, advisers, joint venture partners, and other relevant third parties (“Agents”). As recent cases have demonstrated, Agents are one of the most common channels for illegal payments. Where an Agent acting on behalf of or as the representative of a company pays a bribe to a government official, the company may be held responsible. Therefore, it is important that a policy on selection, appointment, monitoring, and audit of Agents is included as part of an effective compliance program.

Assessing the Company’s Third Party FCPA Risks
Before drafting a policy for Agents the company should carry out a global risk assessment to understand the types of Agents that the company utilizes. The assessment should identify all the company’s existing agents (“Legacy Agents”) and each agent’s contract. Each of these contracts should be reviewed and a database compiled showing the key provisions of each contract, including commencement date, duration, notice and termination provisions, choice of law, and dispute resolution. In addition, a compliance officer should ensure that each of these contracts has a provision requiring the agent to comply with the FCPA. This exercise will be an important part of the risk assessment and will in addition be a valuable tool in obtaining compliance by Legacy Agents once the policy is in place.

The steps below should apply to all Legacy Agents, as well as all agents the company will use in future, who interact with government entities.

Any third parties that interact with foreign governments on the company’s behalf (as sales agents, by obtaining licenses, such as attorneys, filing taxes such as accountants, etc.) should:

- go through a comprehensive due diligence process, as described below, before the intermediary is retained
- sign a statement saying they understand the key provisions of the FCPA and will abide by them (which should be renewed annually)
- both the due diligence and acknowledgement should be updated periodically to remind third parties of their obligations.

Creating an FCPA Policy for Third Parties
As a company, you should consider

- which of your third party intermediaries will be covered by the policy
- who will implement and supervise the due diligence internally
- how extensive you want the due diligence to be (consider a “two-tier” policy – more extensive due diligence for “high risk” agents)
- what procedure you will use to bring Legacy Agents within the Policy

Below, we have set out some sample provisions for such a policy:
Sample Policy: General Provision

To avoid potential liability under the FCPA for the conduct of international representatives, consultants, agents, or other third parties who interact with foreign governments on [YOUR COMPANY]’s behalf (collectively “intermediaries”), it is [COMPANY NAME]’s policy to investigate the background and reputation of its prospective intermediaries to give it a factual basis for concluding that the intermediary is capable of performing the work in question and will do so in a manner that fully complies with the FCPA and [YOUR COMPANY]’s corporate ethics policy. This “due diligence” must take place before the intermediary is retained and must be updated when extending or renewing an intermediary’s contract.

Sample Policy: Definition of Intermediary

“An Intermediary is defined as any agent, representative, adviser, (including professional advisers), joint venture partner, or other third party that that will, or may at some time in the future, represent the company with government entities.”

Two Tier Policy

Some companies have recently begun to categorize intermediaries into two distinct categories based on an assessment of the risks involved in dealing with such third parties. A typical categorization would identify higher risk agents who will represent the company with government entities on a longer term basis (such as joint venture partners, commercial agents, distributors, and customs agents), and lower risk agents such as tax advisors, law firms, and suppliers.

You may want to consider a more extensive and more frequent due diligence process for higher risk agents.

Legacy Agents

Where a company already has a prior relationship with an agent, imposing new anti-corruption policies on them can be delicate. However, any comprehensive compliance program must require existing intermediaries to successfully pass the due diligence exercise, be instructed on company anti-corruption policies, and very likely need to agree to contract changes to bring these relationships into line with the policy.

Components of the Due Diligence Process

Due diligence involves assembling substantial information about intermediaries. This information should be gathered by talking to the intermediary and its personnel; checking references, who should be asked to comment on the intermediary’s integrity; and reviewing publicly available information sources.

As part of the due diligence process, the responsible [YOUR COMPANY] employee [the legal department should designate who this is; usually a senior person within the company who seeks to hire the intermediary or the country legal counsel or controller.] must:

1. Have a written business justification for hiring the agent,
2. Complete the Due Diligence Checklist, including gathering all independent information described below,
3. Have the prospective intermediary complete the Intermediary Questionnaire,
4. Conduct an interview with the prospective agent;
5. The company should designate someone at a senior level (country controller or member of the legal staff) to review the information developed through the checklist and questionnaire to identify any potential red flags suggesting that the prospective intermediary may engage in corrupt activities, and

6. Further investigate any Red Flags until all concerns are resolved. Where any Red Flags are not resolved or there remains any question, the party may not be retained without the written approval of [General Counsel].

7. Require the new agent to sign an anti-corruption certification and a contract containing specific FCPA provisions.

We describe each of these steps in detail below.

**Detailed records must document each step in the due diligence investigation.** All information obtained about the intermediary, and all efforts to obtain such information, should be recorded in a **due diligence binder**. If information is received orally, it should be written down in a memorandum or email as soon as possible.

The due diligence record should include discussion of how the intermediary came to the attention of [YOUR COMPANY], an evaluation of its qualifications and reputation, and the reasons why it was selected. If other candidates were considered and rejected, the due diligence file should reflect the reasons for their rejection.

The due diligence documentation file should be maintained for the duration of the relationship with the intermediary and for at least an additional five years thereafter, or in compliance with your regular document retention schedule. Of course, all records should be maintained if a legal hold is in place.

Key items to include in your due diligence are (keep in mind that these are considerations, you may want to check with your legal counsel to ensure they are appropriate for your organization):

1. **Business Justification**
   Before hiring an Agent, consideration must be given as to whether the Agent is necessary, desirable, or economic, and if so, what work or services the Agent would be required to provide. Accordingly, the company should prepare a business justification. The fact that the company has not operated in the territory previously is not a reason for engaging an Agent. There should be a methodical search for the most qualified person or company.

   Regardless of whether or not an Agent is engaged, company personnel should always familiarize themselves with the relevant laws and business environment in the territory prior to beginning the search for an Agent.

2. **Due Diligence Checklist**
   For each prospective international representative, consultant, agent, or other third party interacting with a foreign government, the responsible company employee must create a binder that includes the following tabs to document relevant information.

   Your company can either do this internally, or hire one of the many companies that now independently do these checks (such as your legal counsel, or other companies that now specialize in this service).

   **Tab A.** Due diligence questionnaire filled out by intermediary (see section 3, below)

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1 Please remember that the FCPA has a very broad definition of foreign government official, so any agent interacting with a company even part owned by a foreign government (such as a hospital, state owned bank etc) would also be covered.
Tab B. Documentation of an in-person interview with the prospective third party (see section 4, below)

Tab C. Three years of Financial Statements for Intermediary

Tab D. Independent Indicators of Financial Condition
Obtain Dun & Bradstreet Report or U.S. Commercial Service International Company Profile -
http://www.export.gov/salesandmarketing/ICP.asp which includes the U.S. (This is the US Embassy’s assessment of the viability, reliability, and reputation of the prospective intermediary)

Tab E. References
Two written references (preferably from U.S. companies) and references’ views on the intermediary’s integrity. References should answer the following questions
How long have you done business with the intermediary?
What services do they provide for you?
How do you view the intermediary’s business practices and integrity?
Have you ever heard of the intermediary paying bribes, taking kickbacks, or doing anything else that would lead you to question their integrity?

Tab F. Independent Checks
Other indicators of the prospective intermediary’s general reputation for ethical or dishonest conduct. You must complete google and/or other database checks on the following:

- Company name and trade names
- Names of all officers, directors and all shareholders owning more than 10% of the company.

Tab G. Copy of Transparency International Index and Ranking of Countries where Intermediary Will Do Business

3. Intermediary’s Due Diligence Questionnaire
Every prospective agent should fill out a questionnaire providing at least the following information:

General Business Profile of Prospective Intermediary

- Name and trade names
- Contact information (address and telephone number for company and company contact)
- Location of incorporation and principal place of business
- Nature of business
- Years in business
- Principal clients/customers
- Number of employees
- Nature of business or service that the prospective intermediary would provide for [YOUR COMPANY], including countries

Ownership/Management
• List all owners and shareholders who own more than 10% of the intermediary (or major shareholders if a public company)
• Principal officers, directors, and employees
• Are any owners, shareholders, or other key personnel (or any affiliated entity) government officials or have connections (family, business, or otherwise) with government officials

4. Agent Interviews
During the selection process, your company should conduct and in person interview with a key representative of each agent, and document in writing the agent’s specific answers to the following questions:

• Nature of business or service that the prospective intermediary would provide for [YOUR COMPANY], including countries (ask again to check written response)
• Owners and shareholders (ask again to verify accuracy of written response)
• Are any owners, shareholders, or other key personnel (or any affiliated entity) government officials or have connections (family, business, or otherwise) with government officials
• Adequacy of physical facilities (Is this a real company? Or a shell?)
• Relevant industry and technical experience
• Proposed compensation
• Is the proposed compensation fair, reasonable, and within the normal range for the same country and services
• Proposed payment method and place of payment
• Who recommended this person/company?
• Has the company or is owners/principal officers ever been sued for fraud? Arrested? Accused of bribery or other misconduct?

5. and 6. Review of Due Diligence and Resolution of any Red Flags
When the due diligence report is received, it should be reviewed by company legal or compliance counsel, any red flags or concerns identified, and further information obtained as necessary. A red flag is a fact or circumstance that serves as a warning signal that an intermediary may act corruptly.

If red flags or other concerns arise, it is critical that further investigation is undertaken until it has been agreed with company legal or compliance counsel either that the red flags are no longer a concern, or that the proposed Agent is unsuitable. Red flags do not necessarily end the possibility of a business relationship with an Agent, but require significant additional investigation and resolution.

Until the due diligence review is complete and final internal approvals are received, the Agent should be instructed not to undertake any work on behalf of the company.
Potential Red Flags include:

Reputation

- The country has a reputation for corruption (see the Transparency International Corruption Perceptions Index)
- The intermediary has a reputation for unethical conduct
- The intermediary has been terminated by other companies for improper conduct
- The intermediary has been subject to civil or criminal enforcement actions

Ties to Government

- The intermediary has family or business ties to government officials
- The intermediary makes large or frequent political contributions
- The intermediary was recommended by a government official, who is a potential customer

Capabilities

- The intermediary is not expected to perform substantial work
- The intermediary lacks the staff or facilities to perform the required work
- The intermediary lacks relevant industry/technical experience or has not been in business for very long
- The intermediary has poor financial stability or credit

Compensation

- The intermediary requests a commission or other payment significantly above the market rate or requests a substantial up-front payment
- The intermediary requests that payment be made in cash or in checks payable to cash or bearer
- The intermediary requests that payment be made through a third party or in a third country
- The intermediary requests an invoice to reflect a higher amount than the actual price of the goods supplied
- The intermediary refuses to properly document expenses

Questionable Circumstances

- The intermediary requests anonymity or that the relationship remain a secret
- The intermediary does not cooperate with the due diligence investigation or refuses to make representations and warranties
- The representation is illegal under local law
- The intermediary makes suspicious statements such as needing money to “get the business” or “make the necessary arrangements”
7. **Agent Contracts**

Following the completion of successful due diligence, the Agent must be required to agree to the company standard agent contract. For the purposes of an effective compliance program, it is essential that such contracts include certain provisions to both guide the Agent in his activities and to protect the company. The Agent contract should:

- Describe clearly the work or services to be performed;
- Require adherence to company code of conduct and policies, especially regarding bribery and facilitation payments;
- Allow for immediate termination without penalty if the Agent breaches those policies;
- Require Agent to provide compliance certifications and attend compliance training as and when required by company;
- Require compliance with all laws with specific reference to anti-bribery laws;
- Prohibit Agent from making illegal payments on behalf of company;
- Provide an indemnity for damages arising from breach of the agreement by the Agent;
- Prohibit the Agent from subcontracting or assigning its obligations to other third parties;
- Require that all payments must be made directly to the Agent, (that is, not to a third party nominee or other entity), by a check or bank transfer - no cash transfers;
- Require that all payments to the Agent will be made in the country of the Agent’s domicile or incorporation unless the Agent provides an opinion or other evidence to the satisfaction of company that payment elsewhere is in accordance with law;
- Oblige the Agent to maintain accurate and transparent records;
- Provide a right of audit provision.

The basic premise for an Agent policy is that the Agent, while acting for the company, should comply with the same rules as the company and its employees. Typically, Agents will be supplied with a copy of the company’s code of conduct document and asked to formally agree that they will comply with the same rules, (normally included in “warranty” language in the agreement). Agreements should include certain protections for the company, such as warranties in relation to making illegal payments and prohibitions on subcontracting or assigning obligations. The Agent may be required to notify the company if they become aware of any links to government officials or indeed if any of the answers they have provided as part of the due diligence process change over time.

**Ongoing Monitoring & Audit of Agent Relationships**

*Management of Agents*

Once an Agent has been appointed, it is important to ensure that someone senior within your company actively manages the activities of the Agent. This can include periodic reporting and meetings to ensure that the Agent is kept informed of company policy and to review the work or services undertaken.

Additionally, management should ensure it is aware of any changes to the Agent’s business, such as changes in ownership, which could give rise to compliance issues. If the Agent is paid on a commission basis, there is a real danger that small bribes or facilitation payments can be absorbed within commissions. Where the company prohibits such payments and where the territory is one in which such payments are common, it will be an ongoing task to remind the
Agent that the company does not tolerate such payments and to ensure they are not being made by the Agent on the company’s behalf.

Training of Agents

Agents should be trained in company compliance and other relevant policies both on appointment and periodically thereafter. (Depending on the risk each agent poses, your company should consider frequent training of the agents appropriate to your organization. For example, an agent selling directly to a foreign government on your behalf should probably receive training once a year.) The training should be effective and match such training given to senior management within the company in similar areas of operation.

Repeat Due Diligence

Due diligence on the Agent should be repeated periodically so that the company can be sure that it is aware of any significant changes in the Agent’s business which could give rise to compliance issues.

Record Keeping

Under the FCPA, it is necessary for the company to be able to demonstrate a credible selection, appointment, and monitoring process in relation to policy and compliance audits. Accordingly, documentation leading to the appointment of an Agent, (business justification, selection process, due diligence records, approvals, and contract), should be retained in company files and available for audit. Similarly the ongoing management of the relationship (training, certifications, payments, and periodic repeat due diligence) should also be documented and retained in the company files.

Audit

To ensure that the Agent policy is being adhered to it is necessary to engage either internal or external auditors to periodically audit the company’s compliance with Agent contracts and procedures. These audits should include examination of the procedures for selecting and appointing Agents, contracts, and payments to Agents, as well as the ongoing management, oversight, and training of Agents.