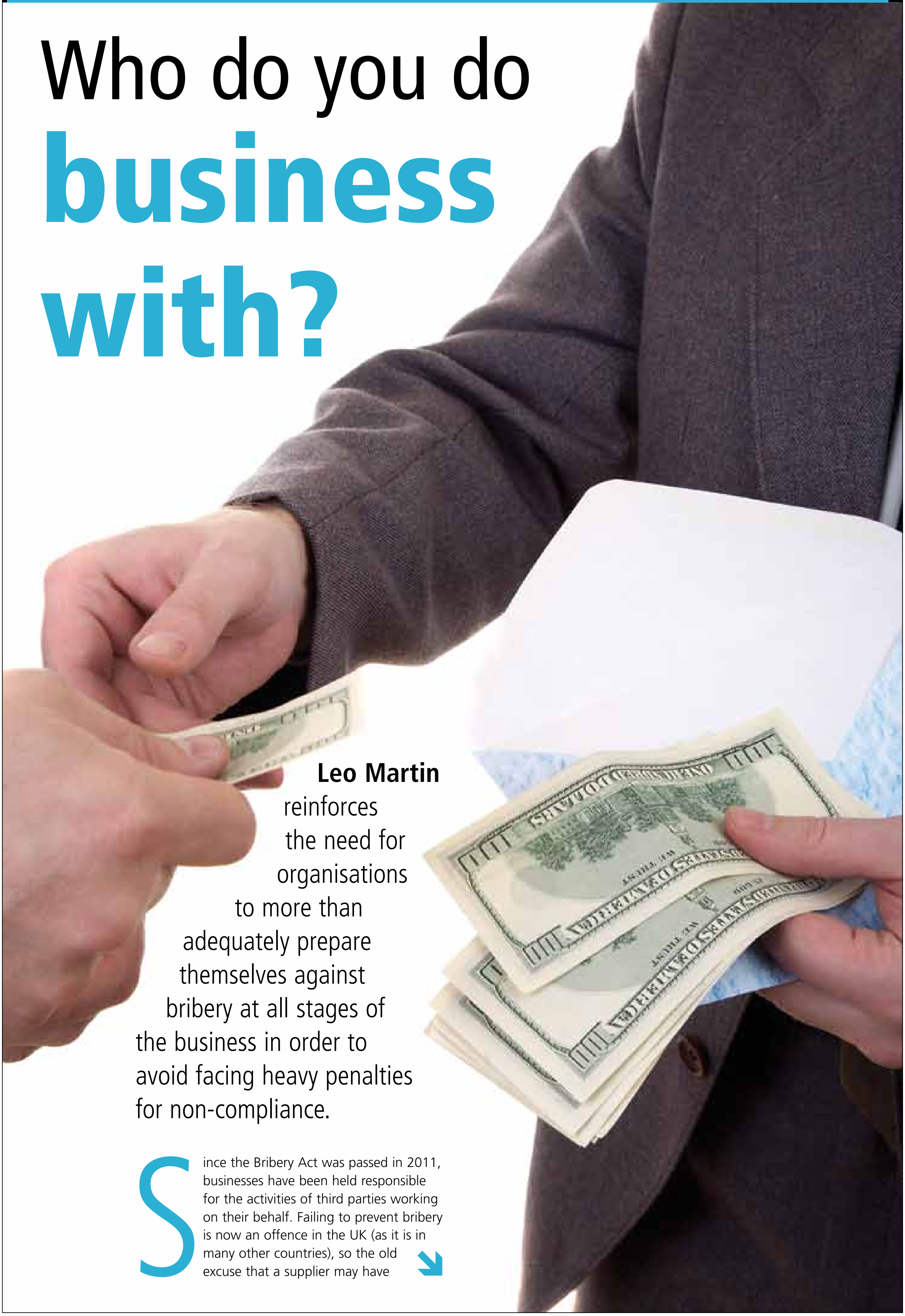
Who do you do **business with?**



Leo Martin reinforces the need for organisations to more than adequately prepare themselves against bribery at all stages of the business in order to avoid facing heavy penalties for non-compliance.

Since the Bribery Act was passed in 2011, businesses have been held responsible for the activities of third parties working on their behalf. Failing to prevent bribery is now an offence in the UK (as it is in many other countries), so the old excuse that a supplier may have

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'exceeded their remit' will no longer wash.

With unlimited fines and a ten-year jail sentence being the possible penalties, businesses have been understandably concerned about how best to manage the activities in their supply chain. With some organisations working with tens of thousands of suppliers, this is no small feat, so where should companies start and what constitutes best practice?

Business ethics advisors GoodCorporation, have been working with organisations for over ten years to help measure and manage responsible business practices. Increasingly this has focused on testing anti-bribery and corruption programmes, often with an emphasis on robust third party due diligence. Leo Martin, a Director of GoodCorporation, outlines the company's recommended best practice.

Developing effective anti-corruption due diligence is proving to be one of the most challenging aspects of ensuring a company fulfills the adequate procedures remit outlined in the Bribery Act. Even the most well prepared companies are struggling with this area of Bribery Act compliance, often doing too much or too little.

This presents a real danger to businesses, despite the lack of prosecutions from the Serious Fraud Office (SFO). The behaviour of third parties has been a key aspect of Department of Justice prosecutions for some time and the Rolls-Royce case suggests that it will also be a major issue under the UK Bribery Act.

Part of the problem is structural; those responsible for compliance are often physically remote from the sales and procurement teams that are actually appointing and using third parties on the ground. This has led to many companies falling into one of two traps – either using databases to undertake a large process of ineffectual checks, or doing more rigorous checks on too few third parties. Not only that, but it has also raised the issue of checking existing suppliers as well as new ones. This is a challenge for many companies, but particularly those that have inherited large numbers of suppliers through mergers and acquisitions; often these suppliers can be hard to track down, let alone check.

Developing a process to get this challenging area of anti-corruption due diligence right is clearly vital. Carefully designed decision trees can be invaluable, but few companies are using them effectively. Decision trees help businesses to identify 'the animals in the park', to gauge the level of due diligence that is proportionate and reasonable.

Key third parties to check are:

- sales agents and intermediaries;
- joint venture partners;
- permit/commercial agents;
- new employees and contractors; and
- recruiters of suppliers.

So, what constitutes best practice – how does a company manage these 'animals in the park'? Some simple desk research can be useful. Look for an anti-corruption policy on the intermediary's website, or for a statement on facilitation payments. If these can't be found, alarm bells should start ringing. However, although online checks can be a useful start, effective due diligence needs to be more rigorous and scientific.

Know all third parties

It is a time consuming exercise, but it is vital to have a list of all suppliers, particularly the key third parties from the list above that pose the most risk, including sub-agents and non-standard sales agents.

Screening

Once the full list of suppliers has been drawn up, they should be screened to determine if due diligence is needed. There are five key elements to the work they do on your behalf that indicate whether or not due diligence should be conducted.

- Do they sell a product with a service element?
- Do they deal with customers on your behalf?
- Do they interface with government or public officials?
- Do they select or manage other suppliers?
- Are they joint venture partners?

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If the answer to any of these is yes, further due diligence is required.

Risk assessment

The next step is to categorise these suppliers according to risk and identify the appropriate due diligence to carry out. Again, a simple decision process should be employed.

- Do they operate in a high-risk market?
- Are they associated with government and/or public officials?
- Is there any hint of improper business practices?
- Have they requested any non-standard fees or payments?
- Do they have opaque ownership or weak anti-corruption controls?

If the answer to all these questions is 'no', place them in the low risk category. One 'yes' should place the supplier in a medium risk category, and more than one 'yes' is high risk.

Risk-based due diligence

Low Risk suppliers should be asked to

complete a due diligence questionnaire, the results of which should be scrutinised to identify any possible risks.

Medium Risk suppliers should be asked to provide independent verification of their answers to the due diligence questionnaire and these references should be followed up with telephone calls.

High Risk suppliers should undergo background, database and policy checks, receive on-site visits and where possible, certification and training, in addition to a questionnaire and client reference checks.

Any red flags, such as negative references, incomplete or contradictory feedback or a lack of transparency need to be highlighted and steps taken to mitigate that risk, if a contract is to be awarded or the relationship continued.

This can be the hardest part of due diligence. In some markets or sectors, red flags are bound to exist and despite knowing what ought to be done, successfully mitigating those risks is far from easy. It is a process that requires effective and persuasive communication and training.

Although it should be thorough, companies need to understand that this is just the start of the process. Not only might remedial action be required to reduce risks, but ongoing monitoring is also advisable, particularly in high risk sectors or locations. Some businesses may choose to walk away if they feel the risk outweighs the potential reward; there are many examples of this happening. Other companies may choose to stay in these challenging locations, preferring to work hard to bring about change. There is no right or wrong answer here, but ensuring that steps are clearly being taken to prevent bribery will be vital to those companies that choose to stay.

The bigger picture

In addition, the best companies will also stand back and ask broader questions: where is the corruption risk with this activity? What is the potential for kickbacks? Does the contract structure create risks? Can commission-only structures be avoided?

We are also seeing an increasing number of companies asking if they really need to use a third party at all. Many are consciously reducing the number of sales agents they use, bringing these activities in house in order to manage them more effectively and reduce the associated risk.

Senior commitment and global reach

A robust anti-corruption due diligence programme will be most effective if it is driven from the chief executive and the board. It should be one part of a wider anti-bribery policy that clearly specifies the company's expectations of behaviour and best practice. In some parts of the world, these expectations will require significant change to take place in the third party. This should be factored into a due diligence programme that is being applied in parts of the world where the cultural challenges are significant.

Experience demonstrates that we know that this is a difficult problem to solve. Due diligence of third parties often throws up results that require careful ongoing monitoring and management. In some ways, due diligence is just the start of the process.

GoodCorporation's growing database of assessments identifies due diligence as one of the weakest anti-corruption practices for UK corporates. Even top quartile companies are generally still 'inadequate' in terms of due diligence.

Getting due diligence right is a problem that businesses must solve, as the risk is great and the penalty for failure high. The risk of wasting significant management time by adopting an unfocused approach should help to make this a priority. However, it is not all doom and gloom. Some companies perceive a commercial advantage to be gained by establishing a reputation as a company that only does business with trusted companies. This works for the organisation and its suppliers in equal measure and should be seen as a positive step for business. Furthermore, by carefully planning their approach to due diligence, many companies find that they can easily eliminate many third parties from any due diligence and the project becomes much more manageable.

We are still in the early stages of the development of anti-corruption compliance, but robust due diligence programmes look set to become the norm, supported by on-going checks and monitoring to effectively minimise the risk of third party corruption.

» About the author

Leo Martin is a Founder and Director of GoodCorporation.