

## FCPA Compliance: Addressing Third-Party Risks

Every U.S. company conducting or seeking business abroad is subject to the Foreign Corrupt Practices Act (FCPA). The FCPA's anti-bribery provisions generally prohibit U.S. citizens or firms, as well as their officers, directors, employees, agents, or controlling shareholders from offering, paying, promising, or authorizing the payment of money or "anything of value" to a "foreign official" in order to "obtain or retain business" or to secure an improper advantage.

The FCPA's anti-bribery provisions prohibit not only direct corrupt payments to a foreign official to obtain or retain business, but also indirect payments made through third parties. The FCPA bars payments made to "any person, while knowing that all or a portion of such money or thing of value will be offered, given, or promised, directly or indirectly to any foreign official."

Set forth below are our suggested "best practices" for minimizing this key FCPA risk – conducting business abroad indirectly through third-party representatives, consultants, agents, or distributors.

The U.S. Department of Justice and Securities and Exchange Commission's Resource Guide to the U.S. Foreign Corrupt Practices Act (Guide) suggests that a U.S. company that conducts business abroad through third parties should perform a risk-based evaluation of these parties based on the specifics of the proposed relationship. For example, a U.S. company that considers hiring a consultant to procure a contract with a foreign government agency should perform a "heightened FCPA-related due diligence" on the proposed consultant, including careful vetting of the consultant and his role in the transaction and evaluation of the consultant's relationship with the government officials. The Guide also suggests that the contract with the proposed consultant spell out what services the consultant will be providing. The Guide also recommends that the company train the consultant on the FCPA and other anti-corruption laws, require the consultant to represent that he will abide by the FCPA and other anti-corruption laws, include audit rights in the contract, exercise those rights, and ensure that payments to the consultant are properly supported and approved.

Policing such a tangled web of risks requires care and discipline on the part of the company. The following offers a number of practical steps a company can take to minimize its FCPA third-party risks:

### **PRE-ENGAGEMENT DUE DILIGENCE OF THIRD PARTIES**

FCPA-specific due diligence will overlap with basic commercial due diligence. A company can leverage its normal, commercial due diligence as a means of also satisfying its FCPA due diligence needs. As part of both inquiries, a company that is concerned about mitigating the anti-corruption risks it faces should ask

why the third party's engagement makes sense from a business perspective, whether the particular third party selected is competent and experienced, and whether the proposed compensation is reasonable, customary, and appropriate.

### **FOR MORE INFORMATION**

In today's ever-evolving regulatory environment, can your company really afford not to have the right internal controls in place? Foley is here to help. Contact Foley Partner **David Simon** at 414.297.5519 or [dsimon@foley.com](mailto:dsimon@foley.com) today.

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In addition, prior to engaging a third party, a company should:

- Understand the FCPA risks posed in the jurisdiction where the third party will operate and assess risk based on the nature of the proposed relationship and the services the third party will perform on behalf of the company
- Conduct due diligence using publicly available databases to determine if there are known worrisome facts regarding the third party
- Require the third party to complete a detailed FCPA questionnaire
- Have the third party execute an FCPA acknowledgment letter
- Use these materials, and other information, to assemble a complete and thorough due diligence file on the third party

## FCPA QUESTIONNAIRE

The FCPA questionnaire should be designed to identify any FCPA “red flags.” At a minimum, the third party should provide:

- Contact information of its owners/principals and board of directors, including percentage of ownership by each, and other businesses in which each might have an interest (with a particular focus on ties to the government)
- Information on related companies
- Business, banking, and credit references
- Information on relationships with current or former government officials or political parties, including relationships of close family members within the government

All of this information must be examined and any red flags addressed and resolved before agreeing to enter into a formal business relationship.

## FCPA ACKNOWLEDGMENT LETTER

A company should secure the third party’s pledge to abide by the company’s FCPA policies and procedures. The company should send prospects an acknowledgment letter that generally explains the FCPA’s requirements and the company’s commitment to FCPA compliance. At a minimum, the third party should acknowledge, in writing, that it:

- Has been made aware of, understands, and agrees to comply with the FCPA and company policies
- Understands that the company is subject to the FCPA and that its actions can subject the company to FCPA scrutiny
- Acknowledges that the third party will be required to provide proof of the disposition of funds received under the arrangement, and will be required to open its books and records if there is any reasonable suspicion of violation of the FCPA
- Acknowledges that any violation of the FCPA will constitute grounds for immediate termination of the relationship, with full return to the company of fees paid under the arrangement

## FCPA DUE DILIGENCE FILE

In the event that a third party makes some sort of improper payment on behalf of the company and the company did not participate in or know of the payment – if there was participation or knowledge, FCPA liability will inevitably attach – the company’s liability will turn on a “willful blindness” inquiry. The first question U.S. regulators will likely ask in such an enforcement action is: What due diligence did the company conduct prior to engaging the third party? While due diligence is not a legal defense to an FCPA violation, the amount of due diligence conducted has a close bearing on whether the U.S. company will be assumed to have “knowledge” of a violation, and also the level of fines/sanctions

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that the U.S. government will consider imposing. A company will be in the best possible position to answer this question if it has created a complete pre-engagement due diligence file.

In addition to the completed FCPA questionnaire and an executed FCPA acknowledgement letter, a complete FCPA due diligence file should include a report summarizing the company's due diligence efforts, the resolution of any red flags raised during the due diligence process, and a list of company personnel or counsel who performed specific due diligence activities. At a minimum, the due diligence report should discuss:

- Why third-party services are necessary and whether its fees are reasonable and customary
- The third party's business experience and qualifications
- A summary of the third party's business, banking, and credit references
- The identification and resolution of any FCPA red flags

The FCPA Guide identifies the following common FCPA red flags when dealing with third parties:

- The third party wants payment through convoluted or suspicious means, often through an offshore bank account
- The third party requests payments of excessive commissions
- The third party gives unreasonably large discounts to third-party distributors
- The third party wants to enter into a "consulting agreement" that includes only vaguely described services
- The third party is in a different line of business than that for which it has been engaged

- The third party is related to or closely associated with the foreign official
- The third party became part of the transaction at the express request or insistence of the foreign official
- The third party is merely a shell entity incorporated in an offshore jurisdiction

Additional red flags may include the following:

- The third party places reliance on political/government contacts as opposed to knowledgeable staff and investment of time to promote company interests
- The third party is unwilling to agree in writing to abide by the FCPA and other relevant laws and company policies
- The third party is unwilling to agree in writing to subject its books and records to audit by the company
- The third party wants to keep the representation secret

If any of these red flags are identified in the due diligence process, they must be adequately and satisfactorily addressed and resolved before proceeding with the engagement. In some instances, it will be possible to do so and to proceed with the relationship. In others, the red flags will be of a nature that will simply preclude proceeding. Experienced counsel should be consulted in making this important decision.

## **FORMAL ENGAGEMENT OF A THIRD PARTY**

All high-risk relationships with an international third party should be memorialized in a written agreement. Nonetheless, willful blindness or conscious disregard of facts that suggest a third party might make an improper payment cannot be remedied by mere contractual language prohibiting such payments. Even so, a company should include in its written

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agreement with the third party certain contractual provisions, including the following:

- Third party representations and warranties that it is not owned or controlled by a foreign government, that no foreign official holds an ownership interest in it, and that it will abide by the company's FCPA compliance policies and procedures
- The right of the company to audit, at its discretion or at least based on reasonable suspicion of a violation, the third party's books and records and other business records<sup>1</sup>
- The right of the company to terminate the agreement if it has a good-faith belief that the third party has made improper payments, and to have all funds previously paid under the arrangement be returned
- The right of the company to disclose the third party's conduct to U.S. regulators
- The right of the company to require annual certifications of prior and future compliance with the FCPA to be signed by all significant members of the third party (sales people, people with regular contact with the government, and so forth)
- The right to indemnification if the third party's actions cause the company to sustain losses

## POST-ENGAGEMENT MONITORING OF THE RELATIONSHIP

Vigilance over a third party's activities does not end when the third party is engaged. Rather, it continues during the period the third party is engaged by the company. Recent enforcement actions show that the DOJ and the SEC will not tolerate a "check the box" mentality with respect to third-party due diligence and subsequent monitoring. The FCPA Guide similarly recommends that a U.S. company should exercise its audit rights over a third party and verify compliance

with the FCPA. At a minimum, and as warranted by the circumstances of the third party's engagement (for instance, is the third party dealing with foreign government officials or operating in a notoriously corrupt country?), a company should have its third-party business partners certify, on an annual basis, that they are in compliance, and will continue to comply, with the company's FCPA policies and procedures. The arrangement should continue to be monitored to ensure that the amount of the payment is commensurate with the value of known, legal work that the third party is conducting. In addition, regular audits of the books and records of the third party should be considered, even if no suspicious circumstances present themselves. Any red flags raised by the third party's activities should be fully investigated and the relationship re-evaluated based on the results. If the company becomes aware of possible FCPA violations through a third party, the company should immediately curtail the use of that third party and assess the appropriate response.

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<sup>1</sup> While the enforcement agencies have long suggested that audit rights should be included in third-party contracts, they have nevertheless recognized that there may be "non-red flag" business reasons for why such provisions may not be practicable.