Third Party Management: Best Practices

IIA Annual Fraud Symposium
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90% Rough Share of FCPA Cases Involving Liability from Third-Party Relationships

Why do you think you experienced compliance issues with a third party after due diligence had been conducted?

- 45% Issue did not exist at onboarding
- 29% Issue concealed
Main Compliance Concerns

40% Third Party Misconduct

- Regulatory Complexity
- Employee Misconduct
- Resources
- JVs
- Other
Key Relationships Of Concern

• HCPs
• Customs/customs brokers
• Tender facilitators
• Distributors and their third parties
• Product regulation specialists
• Business “Facilitators”
Managing Third Parties

- Risk-Based and Integrated Processes – How has the company’s third-party management process corresponded to the nature and level of the enterprise risk identified by the company? How has this process been integrated into the relevant procurement and vendor management processes?

- Appropriate Controls – What mechanisms have existed to ensure that the contract terms specifically described the services to be performed, that the payment terms are appropriate, that the described contractual work is performed, and that compensation is commensurate with the services rendered?

- Management of Relationships – How has the company considered and analyzed the third party’s incentive model against compliance risks? How has the company trained the relationship managers about what the compliance question? How has the company monitored the third party’s risks are and how to manage them? How has the company incentivized compliance and ethical behavior by third parties?
Considerations For Engagement

- What work will the third party do and how will it be paid for?
- Is the third party fee higher than normal?
- What is the ownership structure of the third party?
- Background check done?
- Does third party have appropriate qualifications?
- Recommended by a government official?
- Previous corruption allegations?
Continuous Improvement

RESOURCES GUIDE TO THE FCPA

Continuous Improvement:
Periodic Testing and Review

Finally, a good compliance program should constantly evolve. A company’s business changes over time, as do the environments in which it operates, the nature of its customers, the laws that govern its actions, and the standards of its industry. In addition, compliance programs that do not just exist on paper but are followed in practice will inevitably uncover compliance weaknesses and require enhancements. Consequently, DOJ and SEC evaluate whether companies regularly review and improve their compliance programs and not allow them to become stale. According to one survey, 64% of general counsel whose companies are subject to the FCPA say there is room for improvement in their FCPA training and compliance programs. An organization should take the time to review and test its controls, and it should think critically about its potential weaknesses and risk areas. For example, some companies have undertaken surveys.

Attachment C
Corporate Compliance Program

15. Orthofix will conduct periodic review and testing of its anti-corruption compliance code, standards, and procedures designed to evaluate and improve their effectiveness in preventing and detecting violations of anti-corruption laws and Orthofix’s anti-corruption code, standards and procedures, taking into account relevant developments in the field and evolving international and industry standards.

U.S. Department of Justice Criminal Division Fraud Section
Evaluation of Corporate Compliance Programs

9. Continuous Improvement, Periodic Testing and Review

Evolving Updates – How often has the company updated its risk assessments and reviewed its compliance policies, procedures, and practices? What steps has the company taken to determine whether policies/procedures/practices make sense for particular business segments/subsidiaries?
Distributor Controls

**Teva (Mexico)**

Teva Mexico conducted no due diligence on Company, did not have a written distribution agreement, did not require Company to certify compliance with Teva’s anti-corruption policies, and knew there was no legitimate purpose for an increased margin received on sales to Mexican government customers.
Distributor Management

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**Third Party Management**

**Appropriate Controls** – What was the business rationale for the use of the third parties in question? What mechanisms have existed to ensure that the contract terms specifically described the services to be performed, that the payment terms are appropriate, and that the described contractual work is performed?
Room for Compliance

Teva (Mexico)
In 2011, at a meeting of the Company’s compliance team for Teva Mexico, the Regional Compliance Officer said that the compliance program “was not relevant for the Latin America region and was to be ignored.”
Compliance as Business Partner

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Autonomy and Resources

Stature – How has the compliance function compared with other strategic functions in the company in terms of stature? What role has compliance played in the company’s strategic and operational decisions?
D. Orthofix Made Improper Payments Through Distributors

- Orthofix Brazil provided a high discount ranging in certain instances of up to 70% to the distributors, who then used part of the profit generated by that discount to make improper payments to certain doctors. The high discounts were purportedly meant to allow distributors to make a sufficient profit while also covering their overhead costs. In reality, part of the discount was often used to make the improper payments to certain doctors at public hospitals.

F. Orthofix Lacked Adequate Internal Accounting Controls

- The internal accounting controls were deficient with respect to the setting, approval, and payment of commissions and discounts. Orthofix had no policies or processes in place to standardize or centrally approve and monitor the commissions and discounts that Orthofix Brazil was providing to third parties, which allowed Orthofix Brazil to push through high commissions and discounts that ultimately were used to facilitate improper payments.
Operational Integration
Approval/Certification – How have those with approval authority or certification responsibility in the processes relevant to the misconduct known what to look for, and when and how to escalate concerns? What steps have been taken to remedy any failures identified in this process?
Traditional Risks Revisited

Sale of Unregistered and Mislabeled Products into Mexico

To address these importation issues, with the knowledge of the head of 3i Mexico, Mexican Customs Broker divided shipment items based on whether they had valid registrations and proper labeling. Mexican Customs Broker imported the registered products through the Mexico City airport, while hiring sub-agents to smuggle the unregistered and mislabeled product through Laredo by paying bribes to Mexican customs officials at the border. Once the divided items entered Mexico, Mexican Customs Broker would recombine them and deliver the complete shipment to 3i Mexico.
Traditional Risks Revisited

Third Party Management

Management of Relationship – How has the company considered and analyzed the third party’s incentive model against compliance risks? How has the company monitored the third parties in question? How has the company trained the relationship managers about the compliance risks and how to manage them?
Traditional Risks Revisited

**Improper Conduct at AstraZeneca PLC China**

7. In numerous instances, AZ China sales staff submitted, and managerial employees knowingly approved *fake fa piao* (fake receipts) for fraudulent reimbursements to generate cash that was used to make improper payments to HCPs.

8. Other methods were also used, such as engaging a collusive travel vendor who submitted *fake or inflated invoices* to generate cash that could be used to funnel money to HCPs.

10. Similarly, AZ China paid speaker fees to HCPs despite AZ China service contracts that were incomplete, containing no meeting date, venue, subject or fees associated with the particular speaker event. In some instances, the related speaker engagement was totally fabricated and never occurred.
Traditional Risks Revisited

Operational Integration
Payment Systems – How was the misconduct in question funded (e.g., purchase orders, employee reimbursements, discounts, petty cash)? What process could have prevented or detected improper access to these funds? Have those processes been improved?

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Key Takeaways

- Understand the role played by the third party
- Understand and monitor compensation
- Review and revise engagement terms
- Understand risks in the relationship
- Build controls to contain the risk
- Cultivate culture where concerns are elevated
- Update agreements to reflect expectations
- Resolve “red flags” in responsible ways
- Impose appropriate sanctions where warranted
- Continuous improvements!