



# **Corruption risks in private sector**

Tallinn September 8<sup>th</sup> 2010

## **Corporate risk management**

by

**Arvid Halvorsen**

Member of the board

Transparency International Norway

# **AGENDA**

- 1. Corruption risks and damages**
- 2. Anti-corruption programme as a risk management tool**
- 3. Programme content: Corruption forms**
- 4. Programme content: Business relations**
- 5. Programme implementation**
- 6. Dilemmas**

# **Corruption risks and damages**

# Increasing risk of discovery

- Converging legislation
- Increasing enforcement
- Fewer places to hide
- Pressure group activities

# Corruption damages to companies

- **Reputation:**
  - Undesirable business partner
  - Unattractive employer
- **Value:**
  - Share price drop
  - Lost business
- **Financing:**
  - Unattractive to investors
  - Unattractive to lenders
- **Legal:**
  - Criminal liability
  - Civil liability
- **Cost:**
  - Fines
  - Disgorgement
  - Compensation
  - Lawyer fees

# **Corruption – consequences for involved employees**

- Demotion
- Termination of employment
- Bad references for new job
- Criminal prosecution
- Fines
- Imprisonment

**Anti-corruption programme as a  
risk management tool**

# Why is a programme useful? (1)

- Decreases risk of corrupt acts
- Protects company against corrupt acts committed:
  - deliberately
  - reluctantly
  - erroneously
  - accidentally
- Creates a platform for legal and ethical decisions in the company
- Builds company culture, pride, loyalty and work motivation

## Why is a programme useful? (2)

- Increases investor trust and company market value
- Limits business disruption and distraction of management focus
- Protects and improves the company's reputation
- Minimises risk of litigation
- Prevents prosecution of company and employees
- Increases ability to attract and retain talented employees
- Reduces expenses and losses

# Transparency International tools / guidelines / research

- Business Principles for Countering Bribery (BPCB)
- BPCB – SME Edition
- BPCB Guidance Document
- ABC – Anti-bribery checklist
- Six step implementation process
- Self-evaluation tool
- Corruption Perceptions Index (CPI)
- Global Corruption Barometer (GCB)
- Bribe Payers Index (BPI)
- Integrity Pact
- Global Corruption Report 2009 (Corruption and the private sector)

# **The Business Principles for Countering Bribery**

- The enterprise shall prohibit bribery in any form whether direct or indirect
- The enterprise shall commit to implementing a Programme to counter bribery

# **Developing an anti-corruption programme - what is a programme?**

The Programme is the whole of an enterprise's anti-bribery efforts including values, code of conduct, detailed policies and procedures, risk management, internal and external communication, training and guidance, internal controls, oversight, monitoring and assurance.

(The Business Principles for Countering Bribery)

# **Risk assessment - a basis for an anti-corruption programme**

## **Review:**

- Applicable legislation
- Countries of operation
- Type of business

## **Mapping practices and risks:**

- Assess practices and corruption risks in the organisation, with its business relations and in relevant countries and markets
- Assess the most exposed units, e.g. procurement, business development, foreign subsidiaries

May use interviews or questionnaire

# Developing an anti-corruption programme - programme elements

- Values
- Code of conduct / Code of ethics
- Written rules and guidelines
- Training
- Information and reporting
- Whistle-blowing
- Controls and auditing

**Programme content:**

**Corruption forms**

# Bribery

## **Bribery:**

**The offering, promising, giving, accepting or soliciting of an advantage as an inducement for an action which is illegal or a breach of trust.**

- The Business Principles for Countering Bribery

- Stringent ban
- Knowing the risk
- Consistent practice

# Examples of bribes

- Cash
- Cash equivalents
- Expensive gifts
- Gifts with conditions
- Lavish hospitality
- Expense coverage
- Facilitation payments
- Promise of business
- Free use of equipment and facilities
- Kick-backs
- Free or discounted services
- Free or discounted goods
- "Loans"

# The nature of Facilitation Payments (FPs)

- FPs are bribery and illegal in most countries
- Mostly demanded by public officials
- Thrives in complex and non-transparent bureaucracies
- The FP demander usually has low salary and a lot of power
- FPs are made to secure a routine action
- The payer has legal rights to the service without paying
- The receiver has no legal right to payment
- Small amounts compared with consequence of not paying
- FP demands may come from personal opportunity and initiative, or is institutionalised
- The distinction between FP and extortion is not always clear
- Paying FPs will encourage escalation

# Facilitation payments (FPs) – how to deal with it?

- Policy that forbids FPs, or a plan to avoid/eliminate
- FPs should never be volunteered, but resisted
- A "way out" is needed in case of physical threat or other severe consequences
- Risk analysis: Where and how does it occur?
- Consultation with superior on how to handle a demand
- Processing incidents in organisation to learn and decide actions
- Reporting incidents to police
- Working with peers
- Correct book-keeping of any FPs made

# Political contributions – how to reduce risk?

- An option is not to allow political contributions
- Be aware of possible conflicts of interests and no private gain
- Can the donation be seen as an attempt to influence a decision?
- Contributions made to an organisation, not to a person
- Decision process to pay to involve more than one person
- Motivation, evaluation and decision to be documented
- Contribution to be covered by written agreement and receipt
- Employees to be informed of any political contributions
- Political contributions to be communicated externally

# Charitable contributions – how to reduce risk?

As for political contributions +

...ensure that:

- charities are not fronts for decision makers
- key personnel of the charity not holding positions with authorities or in business that have other connections with the company

# Sponsorships – how to reduce risk?

As for political and charitable contributions +

...ensure that:

- nobody receives return favours, except if:
  - small values (such as event tickets)
  - to several people
  - transparent

# Gifts / Hospitality / Expenses – how to reduce risk?

- Modest in value and frequency
- Appropriate circumstances
- Transparency
- No obligations or expectations created
- Same principles for giving and receiving
- Same principles in all countries ( be aware of local value)
- Gifts and hospitality of value: Proper recording in the accounts

At last, but not the least:

- Extreme care during contract bidding, evaluation and award (and afterwards)

# Conflict of interest – how to reduce risk?

- **Conflict of interest mostly occur with:**
  - Purchasing
  - Contracting
  - Sales
  - Business development
  - Recruitment
- **Precautions:**
  - Dealing with potential situations up-front
  - Transparency
  - Decisions to be taken by others than the person involved
  - Exit from the affected activities within the company
  - Exit from the conflicting outside interest
  - Documented handling of cases

**Programme content:**

**Business relations**

# **Business relationships -- What are the risks?**

- Legal complicity
- Value loss
- Reputation loss

# Business relationships -- How to reduce risk?

- Ask for your programme to apply to the business associate
- Demand an anti-corruption programme of minimum standard
- Anti-corruption commitments in the contract
- Termination clause in contract (in case of corrupt behaviour)
- **INTEGRITY DUE DILIGENCE**
  - In cooperation with IDD object, or without his knowledge
  - Open sources search
  - In-depth investigation by a consultant

# **Business relationships -- Examples of "red flags"**

- A history of bribe paying suspicions or convictions
- Poor corporate governance, lack of anti-corruption system
- A public official owns a significant part of the company
- A company manager owns a significant part of a competitor
- Unwillingness to disclose identity of owners
- The company is black-listed
- Close association with politicians, competitors or criminals
- Suspect contract conditions, use of tax havens

# **Business relationships -- Dealing with "red flags"**

- Terminate the relationship
- Continue investigation and evaluation in more depth
- Confront the business associate with the findings
- Give the business associate opportunity to explain
- Help the business associate to fix the problem
- Continue relationship, but implement risk mitigation plan

# Subsidiaries and part-ownerships – How to reduce risk?

## **Subsidiary:**

A legal entity fully owned and controlled by a parent company

## **Partly-owned company:**

A legal entity jointly owned by several

## **Joint venture:**

An unincorporated cooperation, where rights and obligations of the partner companies are regulated by contract

- Parent company anti-corruption programme to apply when it has full- or majority-ownership, voting control, or operating control
- A minority owner should influence partners to implement anti-corruption programme for the jointly owned company/venture
- A minority owner should exit if the programme or performance are inadequate and cannot be sufficiently influenced

# Agents – What is their role and what is the risk?

- Entities or persons who are contracted by a company to act on its behalf to assist with sales, business development, or government relations
- Agents are often used for legitimate reasons
- Agents represent companies, but may be unfamiliar with the company's anti-corruption standards and with anti-corruption legislation
- In some cases, companies have used agents to bribe on their behalf
- In many cases, agents have bribed without the company's knowledge
- Companies are prosecuted for bribes paid by agents

# Agents – How to reduce risk?

- Integrity due diligence before engaging
- Always written contract
- Concrete description of tasks and objectives
- Reasonable compensation for work and achievements
- Anti-corruption and termination clauses in contract
- Sign-on to company's anti-corruption programme
- Anti-corruption training
- Audit rights
- Close monitoring

## **Agents – examples of "red flags"**

- Agent has little experience with the company's line of business
- Agent has little experience with the type of work he is contracted for
- Agent resides in a different country
- The country of the agent or the project scores low on TI's CPI
- Agent is associated with persons that represent a problem
- The customer requests that a specific agent is used
- Compensation requested is dis-proportionate to the amount of work
- High success fee requested for obtaining results
- Agent asks for payment in advance, to another person, or country
- Agent asks for additional payments to "close the deal"

# Contractors and suppliers – how to reduce risk?

- **Robust procurement procedures, with focus on:**
  - Security and confidentiality
  - Conflict of interest avoidance
  - Competitive bidding
  - Clear responsibilities
  - Checks and balances
  - Anti-corruption requirements
- Integrity due diligence
- Anti-corruption criteria in pre-qualification and tender evaluation
- Anti-corruption requirements in contract
- Supplier declaration covering anti-corruption
- Supplier anti-corruption requirements towards sub-suppliers
- Visits, inspections and audits

# **Programme implementation**

# Programme implementation

## – **Commitment from the top**

- The Board of Directors should commit to an anti-corruption policy
- The top management shall leave no doubt about the seriousness and priority of the programme
- Demonstrate at all times that doing the right thing is not a choice, but a necessity – strong ethical leadership

# Programme implementation

- **Organisation involvement**

- Consultation with employees, trade unions and other bodies – to ensure necessary depth of ownership and commitment
- Person/group to administer the programme – independent of business line organisation

- **Training programmes**

- Include the entire organisation, but considering relevant challenges and risks
- Discussion of cases and dilemmas (group work, plenary discussions)
- Dilemma training creates engagement and common understanding – contributing to a good company culture

# Programme implementation

- **Accountability and consequences**
  - All employees have a responsibility to make sure that the programme is followed and works
  - Sanctions if breach of requirements
- **Internal controls and auditing**
  - A robust financial control system fundamental for preventing and detecting corruption
- **Investigation of incidents**
  - Interviews, review of contracts and payments, analysis of financial data, review of e-mails and files
  - Illegal acts to be reported to police

# Programme implementation

- **Whistle-blowing**

- Supplements top-down commitment and actions
- Must not provoke retaliation
- Whistle-blowing to be encouraged
- Managed by independent staff unit reporting to CEO or Board
- Opportunity to report anonymously
- Open to employees, business relations, and general public
- Confidentiality, adequate protection and fair handling of individuals
- All cases to be brought to conclusion:
  - Reporting to police if suspected breach of law
  - Reprimand or disciplinary action of employees if appropriate
  - No action if no breach of law or company policy
- Debriefing of individuals involved
- Filing of cases and improvement actions

# Programme implementation

- **Information and communication**
  - Effective internal and external communication of the programme
  - Annual reporting
  - Reporting on practices
  - Managers' reporting:
    - Implementation progress
    - Self-assessment of risks and practices
    - Compliance statement
- **Programme review and adjustment**
  - Review suitability, adequacy and effectiveness
  - Independent assessment/external review
  - Implement improvements

# Dilemmas

# Dilemma - sales agent

- Your company has a regional sales agent. The agent's sales are vital for your company's factory, and the agent has been credited for securing the work places for employees there.
- As the new marketing manager, you meet the agent and ask to learn about his business. He is evasive and says the company supplies the products and then he takes over. As you investigate, you become sure that he has used bribery to succeed. However, you have strong suspicions and "gut feeling" rather than hard facts .
- To bring the matter up will create a lot of problems. The partner will be furious and may terminate his contract. No-one can replace him in this market and sales may stop.

QUESTION:                      What will you do?





# Dilemma – gifts and hospitality

- You are the administration manager of a company and responsible for the contract with the travel agent.
- Every year, the travel agent invites all his corporate customers to a Christmas party.
- This year, the travel agent introduces a free lottery for all participants. You are lucky and win a week-end trip to a Mediterranean resort, with travel and accommodation paid for.

QUESTIONS: 1. Should you accept invitations to such parties?  
2. Should you accept the lottery prize?

# Dilemma – family favouritism

- Your company has introduced an education program to increase the qualifications of employees and build competence in the local community. There is a screening procedure and criteria to select the best candidates.
- A top official in a ministry that has a strong influence on the company's business has made it clear that his son must be included in the program. His son is qualified, but the number of more qualified candidates is larger than what can be included in the program.

QUESTIONS:

1. What are the risks?
2. How could this be solved?