The FCPA Compliance Audit: A Market Approach to Moving the Bar Forward

The issue of audit rights in compliance terms and conditions is one that leads to debates both pro and con. My ***This Week in FCPA*** colleague Howard Sklar and I have sparred on this issue. Usually the debates centers around the threshold question of if you have the rights must you audit the contractual counter-party which has agreed to allow itself to be audited. I argue that if you have audit rights that you must, at least selectively use them. However, if you do not ever use these audit rights, it may put you in a worse position than if you did not have the rights. The next argument is usually along the lines that the counter-party will never allow your company to audit them. The third argument is that auditing takes too much time and is too costly.

In my discussions with Howard I usually respond that it is always better to have audit rights. The concept of the compliance audit of counter-parties is in the US Sentencing Guidelines for organizations accused of violating the Foreign Corrupt Practices Act (FCPA); the Department of Justice's (DOJ) *best practices* for effective compliance programs which have been released with each Deferred Prosecution Agreement (DPA) over the past year; the UK Bribery Act's Six Principles of *Adequate Procedures*; and the OECD Good Practices. The reason all of these guidelines incorporate it into their respective practices is that it is one of the key tools to utilize in managing any business relationship from the compliance perspective going forward.

In response to the second argument, I think the answer is more straight-forward. Under any reputable commercial contract, the party paying the money ALWAYS has the right to audit the company which receives the money. While this audit is typically limited to auditing invoices, backup documentation and other evidence of services provided or product delivered, it is nevertheless a standard clause that almost every company has seen in a contract. I believe that good communication with a counter-party, to explain the genesis of the compliance audit and why it has become a *best practice*, is an important part of the ongoing dialogue between the parties, both before, during and after contract negotiations.

I believe that the response to the third objection is also straight-forward. I previously wrote about the Apple 2011 Supplier Responsibility Report. Apple looked at a variety of issues that affect its business relationships with its suppliers, these areas included training, protecting of workers, use of underage labor and social responsibility. One of the areas that Apple audited and reported about was compliance. I believe the Apple example shows that companies can successfully audit their suppliers, channel ops partners and any others in their sales or distribution chains. I understand that people will respond that this is Apple, one of the biggest and most visible US companies around. However, my point is that Apple is a concrete example of a successful and transparent compliance audit.

While not in the compliance area, I recently read about two US companies, Proctor & Gamble and Kaiser Permanente, who grade their suppliers on their environmental practices. In an article in the November 2010 issue of FastCompany, author Damian Joseph quotes Dean Edwards, VP and chief procurement officer at Kaiser Permanente, "We're sending a message to vendors loud and clear…Green up your act today, lest you lose a huge client tomorrow." Author Joseph posed the question to Jeff Erikson, an expert in supply chain management as "How do you control distant suppliers and enforce new standards?" Erikson answered, "There are no easy answers but asking the question is a positive change in behavior."

I think that the final two quotes encapsulate the strongest reasons for the compliance audit. Nothing changes company or business behavior like market based factors. The (FCPA can and does change behavior to move companies and countries toward the rule of law. That is certainly an advantage of the Act and something that should be considered when amendments to the FCPA are bandied about under the claim that the FCPA costs US company's jobs.

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