

Business integrity certification: Overall concept appraisal for ETHIC Intelligence¹

Basel Institute of Governance², September 2006

1. Increasing legal and reputational risk of economic crime

The fight against financial and economic crime is constantly growing in importance, and regulators throughout the world nowadays increasingly state this as being one of their prime goals. Rapidly evolving regulations on corporate governance, fraud and money laundering in the wake of such scandals as Enron, Parmalat etc. are the direct consequences of this development. Notably most forms of corruption are by now illegal in virtually every country, liability of legal persons for bribery has been introduced in a growing number of jurisdictions, and the enforcement of anti-corruption legislation – so far relatively poor – is becoming more efficient and strict. Finally, the behaviour of corporations comes increasingly under scrutiny by stakeholders and the wider public. Ethical business practices and good corporate governance are considered a crucial factor towards protecting stakeholder interest, not the least because being seen as a good corporate citizen generates business.

In light of this enhanced legal and reputational risk, and the related financial costs of crime, companies are well advised to implement strict policies and behavioural rules on corruption, bribery, money laundering and other forms of economic crime.

Experience from the financial services industry, which was faced with similar developments in the area of money laundering prevention a few years back, can provide useful guidance on how other industries should react, and whether certification may prove to be an adequate solution. Consequently, the Basel Institute on Governance in this appraisal of the concept of business integrity certification systematically reflects on this experience.

2. Current trends and lessons from the financial industry

A proper control environment to avoid a bank's involvement in money laundering (AML), corruption payments or terrorist finance (CTF) is not only a legal and regulatory requirement but for most banks has become part of their corporate governance and culture. The potential involvement in criminal activities is seen as one of the highest risks to a firm's reputation which can have serious consequences for the firm's senior management and its share price.

¹ The Basel Institute on Governance has been mandated by ETHIC Intelligence International to conduct a multi-layered appraisal of the concept of "business integrity certification". The present document briefly considers background and objective of business integrity certification and evaluates the advantages and potential risks for the private sector in engaging in such endeavour. The Basel Institute on Governance authorizes ETHIC Intelligence to make this statement publicly available and to use it in its contacts with clients and partners. Any excerpt that is made from this text has to be authorized by the Basel Institute on Governance prior to publication.

² The Basel Institute on Governance is an independent non-profit organisation specialised in policy development, research and consulting in the areas of corporate, public and global governance.

Several layers of complexity have further been added over the past few years, such as the expansion of AML legislation to all serious crimes with financial gains as predicate offences, the fact that proceeds of crime no longer only take the form of money, and the inclusion of a wide range of non-bank financial institutions (brokers, insurance companies, asset managers, lawyers, diamond traders, etc.).

A trend that is of particular importance to the non-financial industries relates to the fact that before long, trade and service companies will, like banks, be held accountable for what they deal in and whom they trade with – as suppliers as well as buyers. The wider concept of AML starts to generate risks that go beyond the financial sector, and adequate reactions to these developments are required.

3. Certification as a form of self-regulation: ETHIC Intelligence

As indicated above, the financial sector is strongly regulated and supervised and as a consequence subject to regulatory sanctions. A central element of supervision is the recurring inspection by regulators, external auditor, internal auditors or special control departments such as legal and compliance. This helps with the enforcement and adherence to respective rules and regulations.

Supervision by regulators and external auditors is a process that comes close to constant certification because the public, the shareholders and the clients can assume that where supervision is exercised properly, the regulators have convinced themselves that adequate policies and procedures against an organisation's possible involvement in financial crime are in place.

This is not the case for other sectors of the economy because without exception, they are not subject to similar independent scrutiny. However, in view of the growing risks outlined above, companies in trade and industry may be well advised to submit themselves on a voluntary basis to such a process. The degree thereof is a matter of a firm's assessment of this risk, senior management's view on and commitment to the fight against crime and last but not least a reflection of an industry's or trade's business risk as a result of its line of business or geographical reach. Voluntary submission to a certification process can add substantially to a firm's reputation and is a logical step beyond the mere public commitment to an industry or international code of conduct.

The proposal of ETHIC Intelligence to set up a certification agency on a private and voluntary basis is not only very timely but one wonders why such an initiative has not been started before. It is in the utmost interest of trade and industry that companies can submit themselves voluntarily to such an independent review and control in a self regulatory manner.

Self regulation in many ways is less bureaucratic and more flexible than public supervision. In addition it is difficult to imagine that any kind of public regulator would take up the topics addressed by ETHIC Intelligence and even trade organisations might be reluctant to play an advisory or even supervisory role on their members in such a sensitive area. As a trade organisation they might be confronted with a lack of credibility due to an obvious conflict of interest. Therefore, the idea to create an independent organisation owned and run by experienced and well known experts is very appealing. The curricula of those in charge should ascertain professionalism, independence and integrity.

The program of course is still at an early stage and certain aspects of it will need to be worked out in more detail. "Certification" creates high expectations as to the quality of the certification

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process itself, and the challenge that ETHIC Intelligence is taking up therefore should not be underestimated. In view of the sensitivity and complexity of the matter, the limited resources usually available to a company during the start up phase, and in the interest of speedy implementation, it is recommended to keep the processes as simple and transparent as possible.

The initiators and founders of ETHIC Intelligence should be lauded for their initiative. The Basel Institute on Governance fully supports their endeavour and is available to continue to cooperate with ETHIC Intelligence International and its licensed partners in assessing processes and ensuring quality of implementation.

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