



VENABLE



# Top Ten Risks Facing Nonprofits Operating Internationally

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Venable LLP, Washington, DC

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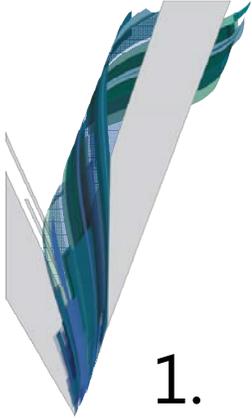
- **January 12, 2017: [Top Ten Hot-Button Insurance Issues Facing Nonprofits](#)**
- **February 2, 2017: Top Ten Cybersecurity Tips for Nonprofits: Managing Your Technical and Legal Risks** *(details and registration available soon)*



# Introducing Venable's New Government Grants Resource Library

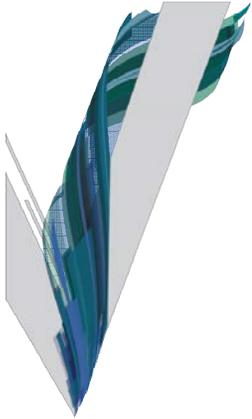


To view Venable's Government Grants Resource Library, visit [www.grantslibrary.com](http://www.grantslibrary.com).



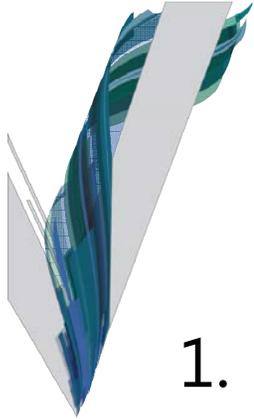
# Top Ten Risks Facing Nonprofits Operating Internationally

1. In-country without authority
2. Poor partner and contractor selection
3. Inadequate controls for corruption
4. Rogue employment approaches
5. Limited financial controls
6. Failing to meet funding partner expectations
7. Losing control of your intellectual property
8. Entering weak contracts
9. Ignoring the tax bill
10. Inadequate insurance



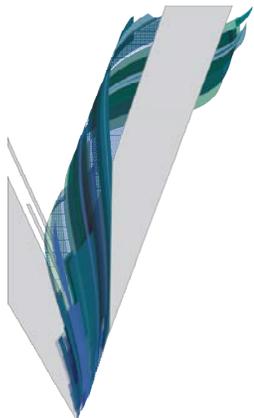
# Risks Need Solutions





# Top Ten *Solutions* for Nonprofits Operating Internationally

1. Legal presence
2. Procedures for vetting partners and contractors
3. Anti-corruption and sanctions compliance controls
4. Employ wisely
5. Financial controls including purchasing
6. Compliance with funding requirements
7. Control of intellectual property
8. Contract terms and conditions for the jurisdiction
9. Pay the tax man
10. Insurance

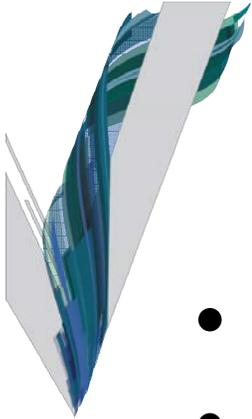


# Solution #1

## Legal Presence

**YOU ARE HERE**





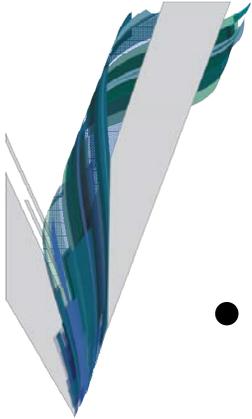
## Legal Presence: Analysis

- Scope the activities (now and the future)
- Determine short- and long-term activities
- Identify human resource needs
- Clarify the revenue sources
- Determine the expenses
- Identify the experts needed to analyze conditions (legal, accounting, tax, security, insurance, government, and other organizations)



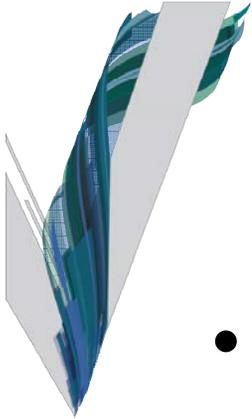
## Legal Presence: Key Questions

- When are you “doing business” in the country?
- What are the permitted legal forms in the country?
- Can your nonprofit control a local entity?
- What are the legal controls on money?
- What are the legal requirements for employees?
- What is required if you engage a contractor?
- Is there an opportunity for a phased approach?
- What does it take in money, time, and form to remain legally present?



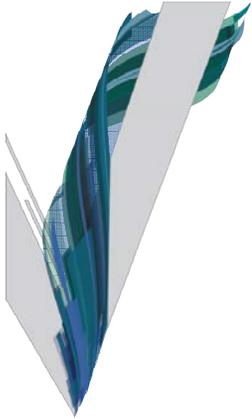
## Legal Presence: Select a Model

- Consider phased approaches
  - Grant making to a nonprofit
  - Short-term events
  - Working through another nonprofit
  - Association management company
  - Contractor to perform
  - Joint ventures
  - Temporary activity under a federal government agreement
  - Establishing a branch
  - Forming an entity (nonprofit or for-profit)



# Legal Presence: Keep Good Counsel

- Retain U.S. counsel with experience in international operations and risks
- Retain local (in-country) counsel with experience in your activities
- Opening memo of rationale and scope
- Establish a process of legal compliance
- Maintain a strong relationship with counsel
- Annually review operations for mission change
- Annually review changes in law
- Adjust for changes



## Solution #2

# Procedures for Vetting Partners and Contractors





# Vetting Partners and Contractors

## The Basics: Due Diligence

- Who?
  - Legal form, ownership, and controlling individuals
  - Screening of U.S. (and related foreign) “lists to check”
- Reputation?
  - References including reputable entities, other known local nonprofits, industry leaders, NGOs, multilaterals, and federal government officials
  - Public records on corruption
- What?
  - What is their expertise?
  - What is their experience doing the type and size of activities you seek?
- How?
  - How does the partner operate currently?
  - Book and records; professional advisors (such as accountants)
  - Programmatic capacity
  - Subcontractor selection and controls

Practice Tip: Ask for and retain *written* records.

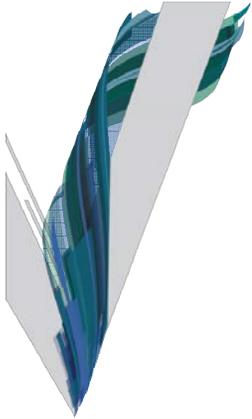


# Vetting Partners and Contractors

## Financial Due Diligence:

- Financial records
  - How far back? Audited?
  - Cash policy and controls
  - Tax management
  - Financial viability
- Accounting system
  - Automated? Manual?
- Labor tracking and reporting
- Experience with third-party compliance
  - Uniform Guidance, World Bank, etc.

Practice Tip: Kick the tires!  
If your potential partner is not willing to provide the info, this is a red flag.

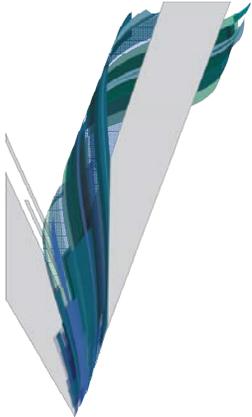


# Vetting Partners and Contractors

## Example

*Small mother and child clinic in Angola  
or  
Regional hospital in Lusaka, Zambia*

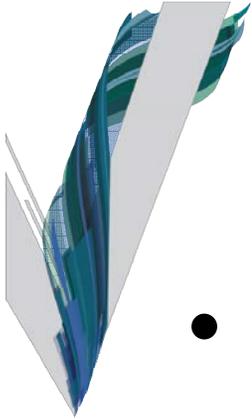
- They have varying levels of risk, in different areas, and the MC clinic may be easier in some ways to “deal” with
- This work begins to overlap with the Uniform Guidance requirements for federal grants



## **Solution #3**

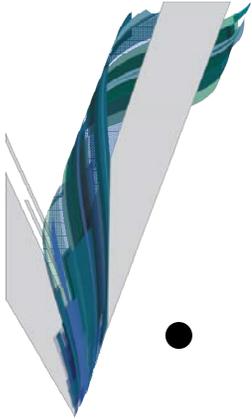
# **Anti-Corruption and Sanctions Compliance Controls**





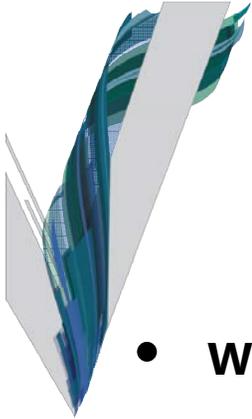
# Anti-Corruption Controls

- **U.S. Foreign Corrupt Practices Act (FCPA):** U.S. law enacted by Congress in 1977 to halt rampant bribery of foreign government officials.
- **Anti-Bribery Provisions:**
  - Prohibits paying of, offering, promising to pay (authorizing to pay or offering) money or “anything of value,”
  - With corrupt intent, directly or indirectly,
  - To a “foreign government official” or political party official,
  - For the purpose of (i) influencing an official act or decision; (ii) causing the official to fail to perform his lawful duty; or (iii) obtaining or retaining business or to secure any improper advantage.
- Certain *limited* exceptions and affirmative defenses exist.



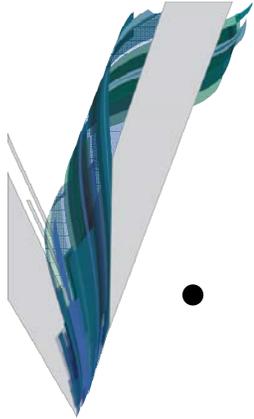
# Anti-Corruption Controls

- **Applicability of the FCPA:**
  - Current “red flag” countries
  - Nonprofits *not* exempt
  - Who is a “foreign official”?
  - “Agency” relationship with partners abroad → U.S.-based nonprofit or association can be held liable for the acts of partners abroad under FCPA
  - Provision of “samples” or other incentives
- **Other National and International Anti-Bribery Laws:**
  - Local (foreign) laws
  - U.K. Bribery Act
  - OECD



# U.S. Economic Sanctions Compliance Controls

- **Why do I care?**
  - U.S. export controls and economic sanctions apply to “**U.S. persons**,” which includes:
    - Any corporation, business association, partnership, society, trust, or any other entity, *organization, or group that is incorporated to do business in the United States*
    - U.S. Citizens, lawful permanent residents, refugees, or asylees
    - All persons *in* the United States (even foreign nationals)
    - Any U.S. *government entity* – federal, state, or local – operating anywhere in world
  - Nonprofit entities are *not* exempt!
- **U.S. Export Controls (U.S. Department of Commerce)**
  - Controls on “exports” (or releases) of U.S.-origin goods, technology, and services to certain destinations, entities, and end users
  - Are you exporting computers, technology, or other goods in support of your overseas venture? (Materials for a trade show, hand-carry items can be subject to controls.)
  - What is the country of ultimate destination? Who is your end user? Even if the item is not controlled, the end user might be (e.g., in Russia or Sudan).



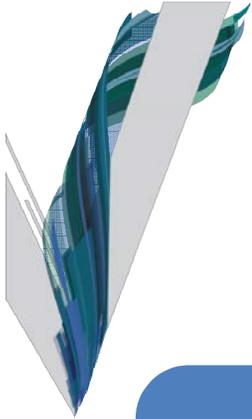
# U.S. Economic Sanctions Compliance Controls

- **U.S. Economic Sanctions:**

- U.S. economic sanctions bar and/or substantially restrict exports to, or the participation by, **“U.S. persons”** in commercial activities involving designated countries, individuals, and/or entities
- Comprehensive sanctions prohibit *most* transactions with entities, persons, or government entities in those countries (“informational materials” exemption)
- Office of Foreign Assets Control (OFAC) of the U.S. Department of Treasury: Primary role in administering and enforcing U.S. sanctions programs

- **A Few Important Principles:**

- Each sanctions regime is UNIQUE
- Sanctions are NOT static – can change daily
- There may be overlap with other (UN, EU) sanctions; U.S. laws can vary significantly
- U.S. persons and entities subject to jurisdiction prohibited from dealing – directly or indirectly – with restricted countries, persons, and entities
- Expansive concepts of prohibited transactions: “export of services” and “facilitation”
- Broad anti-evasion provisions



# OFAC Economic Sanctions: Country-Based Restrictions

## Comprehensive embargoes

- Cuba
- Iran
- Sudan (not South Sudan)
- Syria
- Crimea Region of Ukraine

## Targeted Restrictions on *persons* and *entities*

- Balkans
- Belarus
- Burundi
- Iraq
- Libya
- Lebanon
- Somalia
- Russia-related sanctions
- North Korea
- Venezuela
- Yemen
- Zimbabwe

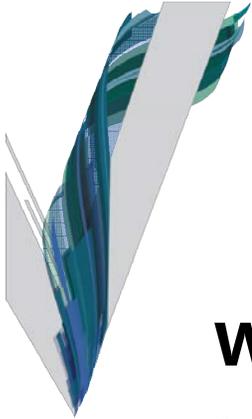


# OFAC Risk Matrix: Sanctions and AML Considerations

- Grantees: U.S. Treasury Department's "voluntary" [Anti-Terrorist Financing Guidelines](#) and [Risk Matrix](#)
- Acknowledgment by OFAC that "**charitable sector**" has been exploited by terrorists to raise and move funds, and to provide logistical support and cover, and operational assistance
  - Nonprofits have been "put on notice" and are thus expected to have knowledge and compliance protocols in place to combat threat, including *SCREENING*.

## Risk Factors for Charities Disbursing Funds or Resources to Grantees<sup>5</sup>

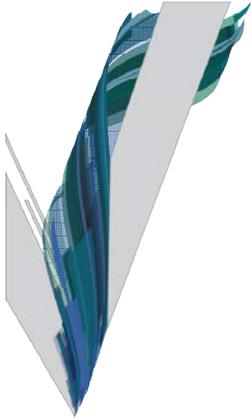
Low Risk	Medium Risk	High Risk
The grantee has explicit charitable purposes and discloses how funds are used with specificity.	The grantee has general charitable purposes and discloses how funds are used with specificity.	The grantee has general charitable purposes and does not disclose how funds are used.
The charity and the grantee have a written grant agreement that contains effective safeguards. For example, provisions addressing proper use of funds by the grantee, delineation of appropriate	The charity and the grantee have a written grant agreement with limited safeguards.	The charity and the grantee do not have a written grant agreement.



# Effective Compliance and Controls

## What are “effective controls”?

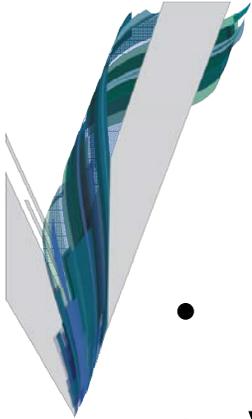
- Senior management environment of compliance
  - A senior manager with independent decision-making authority should have direct responsibility over overseas programs
  - Specific compliance manager within the organization
- Develop policies/procedures based on risks, organizational risk tolerance, and common practices in your sector
- Employ a due diligence “checklist”
- Regular training...and re-training
- Obtain certifications from grantees or contractors
- Recordkeeping (five years)
- Auditing (internal and your partners, subcontractors)



## Solution #4

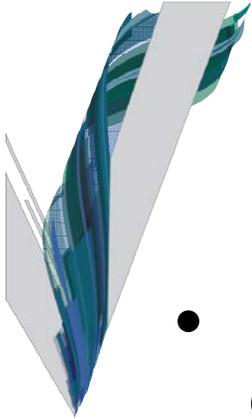
### Employ Wisely





# Employ Wisely

- Day 1: Employee policies controlling for bribery, corruption, and money laundering
- Visas and travel security controls
- Worker registration/permits
- Insurance coverage
- Local nationals, expats, and third-country nationals
- Employees v. independent contractors
- Employment rights and policies
- Customs and culture
- Background and due diligence
- Data security
- Payroll and benefits
- Taxes
- Exit strategy



## Employ Wisely: Taxes

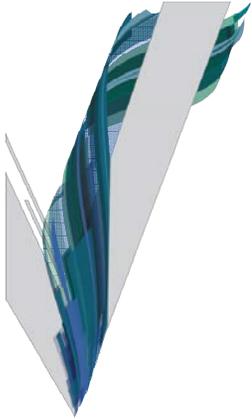
- Liability to local government, U.S., and/or employee's home country
- Employer location: Local, U.S., or third country
- Employee is U.S. national resident or third-party national
- Independent contractor
- Assignment length (contract in place or a long-term "visit")
- Social taxes



# Treaties and Bilateral Agreements

60+ tax treaties or protocols with U.S.

The triggers for classifying an individual as an “employee” for tax purposes vary widely and create obligations on employee, employer, and in multiple jurisdictions.



# Solution #5

## Financial Controls





# Financial Controls

- The organization provides the employees opportunities to commit fraud by having ineffective (or no) internal controls.
- The organization's employee creates the pressure/rationalization to commit fraud.
- Regardless of the size of the local office, DO NOT think that your employees would never commit fraud against the organization.
- Regardless of the size of the organization, a segregation of financial duties can exist, to some level.
- Regardless of the size of the organization, fraud can occur. Trust, but verify.
- Don't tolerate an opportunity to commit fraud against the organization.



# Financial Controls

It begins and ends with cash...

- Ability to pay vendors/procurement
- Ability to pay personnel salaries
- Ability to provide subgrantees funding



# Financial Controls

It begins and ends with cash...

- Ability to pay vendors/procurement:
  - Validate vendors (not just one time!)
  - Strong procurement policy/vendor selection/“too good to be true” concept
  - Validate pricing of good for the region where you purchased
  - Are the procured goods of the quality you bid on?
  - Is one vendor selected repeatedly? Why?
  - Did the activity happen? Hotel stays, transport, trainings, etc.



# Financial Controls

It begins and ends with cash...

- Ability to pay personnel salaries:
  - Simple question: does the employee exist?
  - Time records, accurate, timely, and reviewed/approved?
  - Involvement of senior executives in HR process?
  - Salary change approvals?



# Financial Controls

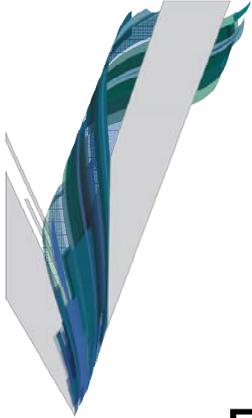
It begins and ends with cash...

- Ability to provide subgrantees funding:
  - How did you, as the prime recipient, validate the subgrantee financial report?
  - Did the personnel really work on the project? What verifiable evidence have you reviewed?
  - Did the trainings/events/outreach really occur? How did you validate?
  - Were the number of patients processed real?



# Financial Controls

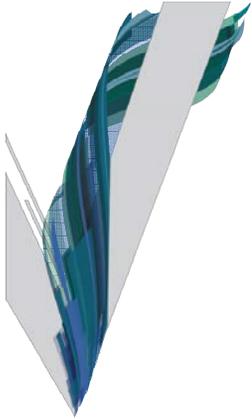
- Low-hanging fruit for any organization anywhere in the world:
  - Performance of bank reconciliations timely and accurately by persons not involved in the cash disbursement process.
  - IT controls work if you let them work. Password changes often...
  - Perform vendor checks on a regular basis.
  - Organization's name on a bank account instead of member of staff.
  - How do you keep data records (backup and recovery)? Do they leave an audit trail?
  - Altered documents should be challenged.
  - Photoshop is incredible; consider validating invoices through other means rather than just the piece of paper.
  - Challenge your whistleblower policy.



# Financial Controls

## U.S. Treasury Interests

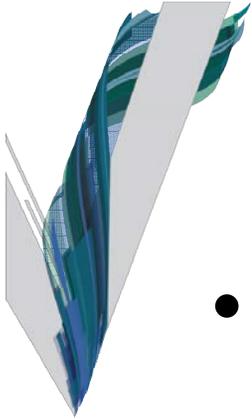
- Financial Crimes Enforcement Network (FinCEN) Form 114: Report on Foreign Bank and Financial Accounts
- IRS Form 8938: Statement of Specified Foreign Financial Assets
- IRS Form 926: Return by a U.S. Transferor of Property to a Foreign Corporation



## **Solution #6**

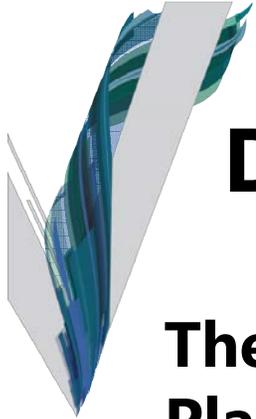
### **Compliance with Funder Requirements**





# Compliance with Funder Requirements

- Funding sources vary:
  - Institutional and government
  - Personal in-country donors
  - Membership
  - Events
  - Sales of products, such as publications
  - Sale of services, such as certifications



# Donor Activities

The Donor Oversight World Is a Changing Place...



Department  
for International  
Development



Investing in our future

**The Global Fund**

To Fight AIDS, Tuberculosis and Malaria



VENABLE





# Donor Activities

Donors are demanding more...

- Transparency
- Access to books and records
- Focus on “their” dollar, euro, krona, West African franc, pound, etc.
- Focus on “their” piece of the program
- Responsiveness by receiving organization



## Donor Activities

Significant increase in the past four years related to:

- Performing audits of specific grant activity at grant materiality level
- Performing “agreed-upon procedures” on activity specific to their grant
- More increased scrutiny surrounding matters noted and attempts to claw back funds in question
- Focus on international accounting standards (not just U.S. GAAP)



# Donor Activities

Significant increase in the past four years related to:

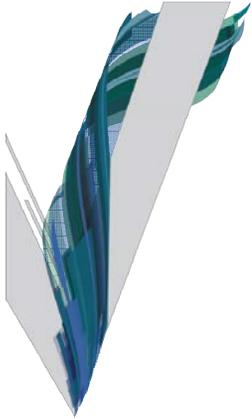
- “Letter of the law”
- Far more focus on negotiating terms of reference
- Focus on subgrant monitoring and oversight of subgrants:
  - Monitoring of use of funds
  - Performance criteria



# Donor Activities

## Things to consider:

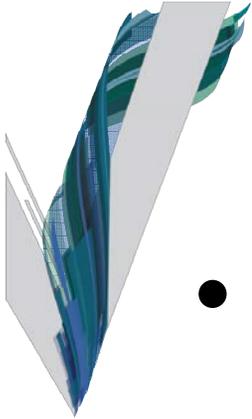
- Upfront negotiation
- Understand the cost (negotiate who pays the costs incurred)
- Far more focus on negotiating terms of reference
- Negotiate terms of the audit/AUP or timing
  - Does it need to be done annually?
  - Only once?
  - AUP *or* Audit?
  - Local or international firms?
- Some money is not good money



# **Solution #7**

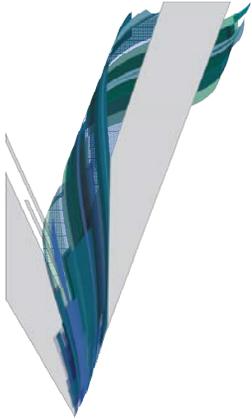
## **Control Intellectual Property and Data**





# Control Intellectual Property

- Protecting your Intellectual Property (IP):
  - Registered IP: Logos, trademarks, certification marks, and patents
  - Copyrighted material, such as standards
  - Depending on target country, IP rights and protection may be a high-risk issue
  - Is target country signatory to any international IP conventions?
- Is your IP registered and recorded in the U.S.?
  - Consider registration of IP (or “international” version of IP) under local laws in target country
  - Differentiating between IP and “confidential information,” i.e., business proprietary info (also requires contractual protections)



## Solution #8

### Contract Terms and Conditions





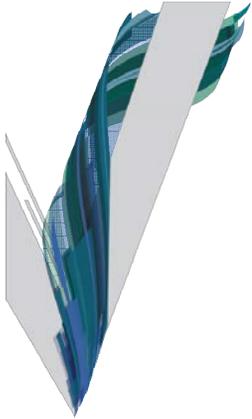
# Contract Terms and Conditions

Essential provisions for protecting your interests:

- Careful review of any agreement or contract between your U.S.-based nonprofit and a foreign entity is *key*.

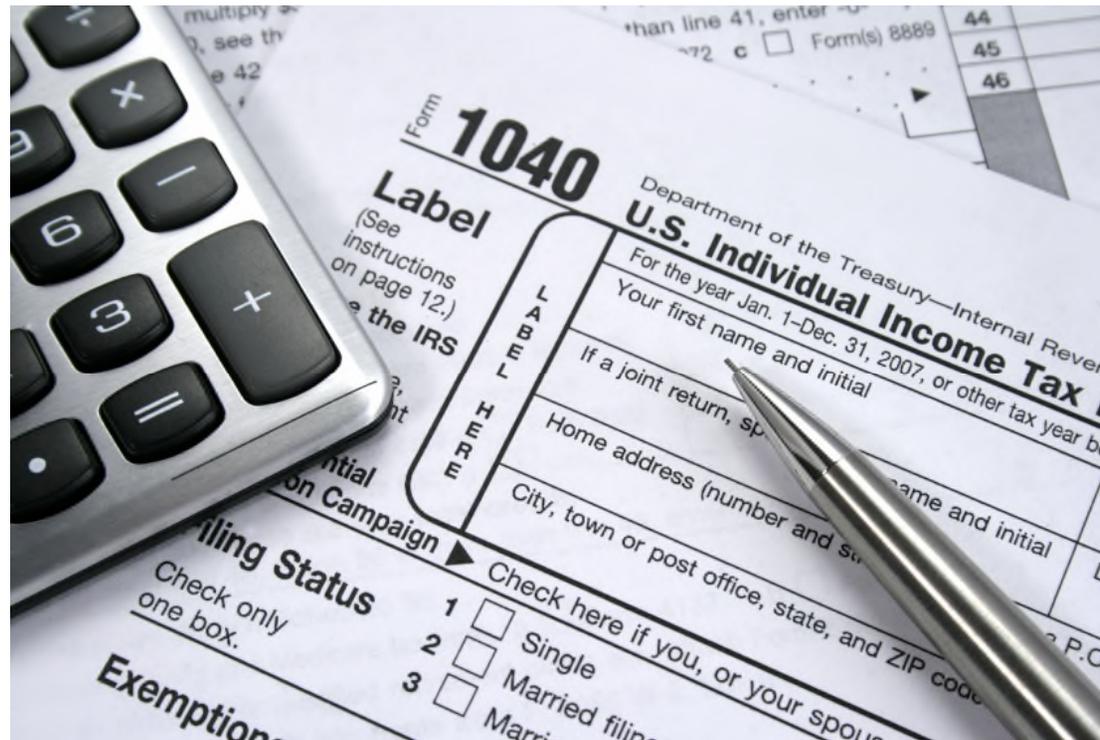
A few “sticky” provisions:

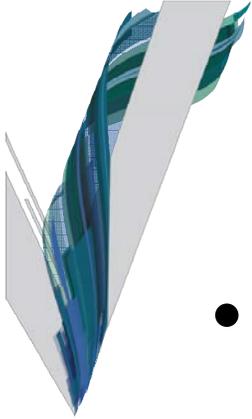
- ✓ Dispute resolution: Forum, place, and type (e.g., mediation, arbitration, and litigation)
- ✓ Governing law: *Excluding a “conflicts of law provision”*
- ✓ Language
- ✓ Agency v. “independent contractor”
- ✓ IP: Firm IP and copyright language
- ✓ Performance-based measurable outcomes
- ✓ Flow-down provisions from funders
- ✓ Termination provisions (always *in writing*)
- ***Always a country- and fact-specific analysis.***



## Solution #9

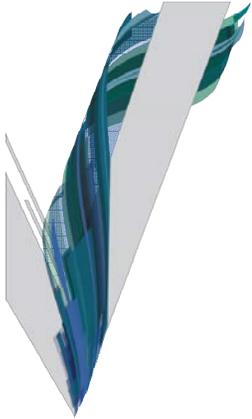
### Pay the Tax Man





# Pay the Tax Man

- All country and local taxes:
  - Income
  - VAT and other sales taxes
  - Social taxes
  - Property taxes
- U.S. Reporting Requirements:
  - IRS Form 5471 for nonprofit's foreign corporation
  - IRS Form 8858 for disregarded entity
  - IRS Form 8865 for partnership entity



# Solution #10

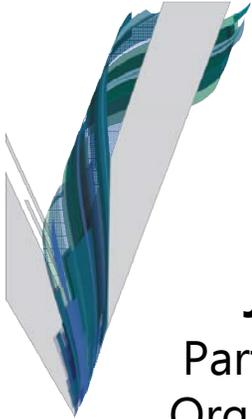
## Insurance





# Insurance

- Determine if your existing policy covers international operations.
- Get legal advice on mandatory or advisability of in-country policies.
- Evaluate the risks associated with the activities.
- *Regularly* consult with authorities and experts for political, cultural, financial, and physical security risks in countries.
- Consider persons exposed to the risk (employees, volunteers, contractors, etc.).
- Determine what protocols and policies reduce risk and increase chance of coverage.



# Questions?

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