Tool 4: Due Diligence Investigation of WSI Participants

Due diligence refers to the care a reasonable and prudent party should take before entering into an agreement or transaction with another party — whether they are NGOs, government, or private companies. It involves a systematic collection and analysis of information on how a particular organization is managed or conducts its business.[1] A due diligence investigation reveals whether a potential participant in a WSI commits to professional and ethical business practices, and uncovers the risks and opportunities that come along with involving this participant. A due diligence assessment will be useful for the **WSI initiators** while scoping prospective participants in order to assess whether that organization is fit to assume a specific role in the WSI.

Level of Effort:

Simple investigation: Applied to all potential participants

In-depth investigation:

- To be used following the outcome of a simple due diligence that highlights potential areas of conflict

- To be used if a WSI is intended to address sensitive areas (such as regulations)

- To be used if a potential participant will play a key role (e.g., WSI facilitator).

Tool	An example "Know your **WSI participants**" checklist and other sources of information relating to due diligence investigations.
Related Key Activity	Analyze **WSI participant** records and incentives.
Questions Addressed	How can the WSI understand the track record of its potential participants to ensure the integrity of the initiative?
Purpose	A proper due diligence process will help **WSI participants** identify potential past unethical behavior by any participant, in order to determine proper next steps and avoid conflicts: ✓ Develop greater understanding of **WSI participants** at the outset. ✓ Mitigate risk of integrity issues related to past participant behavior and track record.
Possible Users	**WSI initiator**, might be a single organization or a small group of organizations that are providing financial support to a WSI or are involved in its development, including donor agencies planning to support a WSI.
Level of Effort	From simple checklist to comprehensive background research by an independent party.
WSI Phase	1: Incubation and Initial Analysis, completed in 2: Formalization.

There is intentional damage and neglect of the water infrastructure by the municipality staff. [Donor/ESA]

XXX is distancing themselves from the partnership when it's not bringing immediate benefit. [Civil Society]

(From Field Testimony)

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[1] Pinow, "Due Diligence Investigations" (no date), http://www.pinow.com/investigations/due-diligence.

A due diligence process usually includes an analysis of the relevant organizations'

- Image

- Social responsibility

- Environmental accountability

- Financial soundness

- Policy compatibility

- Capability to engage

- Interest and incentives.

Table 7 lays out additional issues for consideration. In this regard, it is important to vet whether the interests and water use of a potential participant can be aligned with the principles of **sustainable water management**.

Information gathered in the due diligence can also be used when developing the WSI's [finance and audit protocols](#) (Tool 8).

Potential data sources for due diligence

- Publicly available information on the potential participant (depending on size of company or organization: website, local and/or international newspapers, information provided upon request).

- Information from the anti-corruption and procurement agencies or from local or provincial governments (black- or whitelists for public procurement), competition agency (cases of collusion), environmental protection agencies, watchdog NGOs.

- Cross-checking with local corporate registries, telephone, business, professional, and Chamber of Commerce directories, and NGO networks; in some countries CSO performance reports exist and may be a useful information source.

- Announced visit to the company, organization, or government agency.

- Interviews or informal consultations with trusted individuals who have a track record of working in the area, on related topics, or with the WSI participants.

- Follow-up on local references provided by the participants regarding their suitability as partners.

By conducting due diligence investigations, WSIs can reduce the chance of future conflicts of interest or unpleasant surprises linked to the behavior or the track record of participants, which may affect the credibility of the initiative and the reputation of other participants. For example, it could harm the other participants or the WSI as a whole if one participant is engaged in illegal practices or simply has no capacity to live up to expectations. However, in reality many WSIs must include participants with an

imperfect track record; indeed many WSIs exist because of historical legal action or because stakeholders lack capacity. Due diligence for WSIs is therefore more about having important information upfront and knowing your **WSI participants** than preventing participation. Besides the immediate results, conducting due diligence can also help to establish a common understanding of expected standards of professional conduct among participants. Moreover, it can initiate capacity development by responding to shortfalls (e.g., participants implementing new policies and processes).

Interpreting and acting on due diligence investigations

A proportional approach to diligence has to reflect the nature and context of the WSI and respond to the concerns of **WSI participants** and **affected stakeholders**. For example, local organizations should not be excluded from a WSI simply on the basis of low capacity or lack of financial sustainability. Rather, their status should be understood so that the WSI can plan additional support wherever necessary. Similarly, a company that has been convicted for serious breaches of environmental law in the past does not necessarily have to be excluded from taking part in the WSI.

What is important is the disclosure of critical issues, and open discussion and agreement on whether the risks posed to the WSI are acceptable and manageable by the participants. Ultimately it will be for the **WSI participants** themselves to interpret and respond to information generated by due diligence checks. To enhance transparency and provide the opportunity for meaningful communication, it is recommended that the WSI document the interpretation and decisions resulting from due diligence investigations. Critical results of the investigation such as conflicts of interest (e.g., potential for commercial or financial benefit) should be addressed explicitly (e.g., in a Code of Conduct, Tool 10b), and WSI participants should structure the WSI governance and management of roles and responsibilities (Tool 9) accordingly.

Step 1: Define Methodology and Data Sources

- To streamline data collection processes, the due diligence investigation can be linked to the stakeholder mapping exercise and context and political economy analyses that should be carried out at the outset of a WSI.
- Investigation should include different sources of information (see box on potential data sources).
- If methodology for participants consists of a reduced/simplifed checklist, thresholds should be defined for deeper investigation.

Step 2: Conduct Initial Investigation

- WSI initiators select who will conduct the investigation based upon the goals, objectives, and potential-make-up of the WSI. Question to ask include, "Who is best positioned to carry out the due diligence? Would an external party be helpful to work through potential conflicts of interest?
- Options for how to conduct such an investigation includes a local consultant; external independent organization or individual according to terms of reference (TOR, see Tool 5, Step 1); key members of the WSI who utilize a simple checklist of verified information.
- Table 8 provides guidance on questions that should be explored during the investigation.
- Where a WSI might be operating in a high-risk context, WSI initiators might consider conducting further background checks with local experts to verify outcomes.

Step 3: Reach and Document Conclusions

- Discuss initial findings among WSI initiators resulting in a joint decision about who to invite to participate in the WSI.
- Where the investigation finds critical issues, WSI initiators may choose to hold a bilateral meeting with the individual/organization to assess whether and how the identified problems or sensitive issues might be addressed.
- Exclusion of potential participants should be based on an in-depth investigation.
- In circumstances where a number of sensitive or controversial issues might arise, an efficient and constructive way to collate and weigh due diligence information gathered in Step 2 is likely a meeting or worskhop setting.
- In the workshop, potential WSI participants introduce their organizations, and findings of the intial investigation are presented.
- The workshop format allows the group to discuss and come to consensus about any controversial issues.
- Intelligent workshop design and facilitation will be necessary to handle sensitive issues.

Step 4: Follow Up

- Continued due diligence reporting and monitoring should be carried out to adapt to new issues as they emerge.
- In particular, a conflict of interest register should be kept up to date and should be acted upon. The results of due diligence can also be made public to increase the credibility and legitimacy of the WSI.

Table 1: Know Your WSI Participants — Key Issues to Consider

Background information	Find out more about participant status, purpose, and governance. Consider checking: - Governance documents (articles of incorporation, bylaws, NGO registration) - Annual reports, brochures, etc. - Ownership structure (who is behind the institution?) - Curriculum vitae of trustees or directors and senior staff - Board of Trustees/Directors meeting minutes - Political affiliations - Previous or pending legal cases, fraud, or accusations of improper conduct or corrupt practice What is the legal status of the organization? What is its core purpose? To whom is it accountable, who is it of use to, and who does it actually represent?
Public image and reputation	What is the public perception of the organization? - Do the public and stakeholders know about the organization? What do they associate the organization with? - Are there any particularly negative or positive perceptions? If so, what are they?
Social responsibility	How socially responsible is the organization? - What is the corporate social responsibility (CSR) portfolio? Does it reflect good practices in social responsibility? - Is practice in line with public policy? How is this demonstrated? - Does the organization pay appropriate tax, or is it engaged in tax avoidance?
Environmental performance	What are the environmental credentials of the organization? - Does the organization have an environmental policy and register of environmental issues? - Is the organization compliant with environmental law in the country of operation? Internationally? - Have there been major environmental issues in the past? What has been the organization's response? - Does the organization disclose environmental performance?
Policy compatibility	Does the organization have policies relating to the following areas? Are they adequate, and are they followed? How is this demonstrated? - Protection of children and vulnerable people - Anti-corruption, including whistle-blowing safeguards - Health, safety, and Environment - Equal opportunities - Conflicts of Interest - Ethics - HIV and AIDS in the workplace

	- IT security
Financial position	Consider checking the sustainability and financial viability of the participant: - Most recent annual reports, financial statements, and regulatory reports (audited, if available) - Budget for upcoming financial year and current and projected income forecasts - Finance manual and expenditure procedures
Capability and conduct	Will the organization be able to deliver on agreements and roles set out in the WSI? Consider checking: - Organizational structure chart - Curriculum vitae of key staff and reporting/accountability lines - Human resources policy - Staff performance management policy - Internal performance processes (KPI framework, etc.) - Existing partnership agreements and performance against these (MoUs, etc.)
Intent and incentives	Why is the organization relevant to the WSI? What is its rationale for engagement? - What are the benefits sought by the organization through its involvement with the WSI? Are they in line or can be aligned with **sustainable water management**? - How will those benefits be measured and tracked? - Are there any other potential benefits or stakes at risk that motivate the organization's involvement? - Are there any conflicts of interest (such as positioning for contracts, access to decision makers), and how will they be managed?

Further reading:

- Partnering Against Corruption Initiative (PACI). 2013. "Good Practice Guidelines on Conducting Third-Party Due Diligence." (Geneva: World Economic Forum). http://www3.weforum.org/docs/WEF_PACI_ConductingThirdPartyDueDiligence_Guidelines_2013.pdf. *N.B.:* Contains sample questionnaires for due diligence assessments that can be adapted.
- Guide to Combating Corruption and Fraud in Development Projects. 2014. http://guide.iacrc.org/local-and-on-site-due-diligence-checks/.
- For information on filing requirements, see World Bank Group (2014), "Starting a Business," http://www.doingbusiness.org/data/exploretopics/starting-a-business.
- Matteson Ellis. February 4, 2014. "The Master List of Third Party Corruption Red Flags," FCPAméricas Blog, http://fcpamericas.com/english/anti-corruption-compliance/master-list-party-corruption-red-flags/#.
- PInow. (no date). "Due Diligence Investigations." http://www.pinow.com/investigations/due-diligence.