



Government Support for Ethics & Compliance

Eric Morehead

May 18, 2011

Government Standards

- Federal Agency Standards (such as the Federal Acquisition Regulations)
- Criminal & Regulatory Settlements (such as DPA/NPA and CIA Agreements)
- Foreign Measures (such as The UK Bribery Act, OECD Guidance, UN Convention)

Common denominator :
Organizational Sentencing Guidelines

Background on U.S. Sentencing Commission

- Established in 1984 by the Sentencing Reform Act
- First Guidelines for individuals effective in 1987
Organizational Guidelines first effective in 1991
- Independent body made up of seven, bi-partisan Commissioners appointed by President
- Commission promulgates sentencing guidelines and collects and analyzes sentencing data

U.S. Sentencing Commission Amendment Process

- Sentencing priorities are established mid-summer
- Policy teams are established and conduct empirical study, informal outreach, and other forms of research through the fall
- Proposed amendments are published in the federal register
- Public comment period extends into spring
- Public hearing in March
- Submission to Congress May 1st
- Effective date November 1st

General Principles of the Organizational Guidelines

- Organizations should remedy harm caused by offense
- Organizations with criminal purpose should be divested of assets
- “Carrot and Stick Approach” for penalties -- fine ranges are determined by seriousness of offense and culpability
- Probation to implement sanctions and reduce recidivism

Goal: provide “structural foundation from which an organization may self-police its own conduct through an effective compliance and ethics program.”

Significance of Organizational Guidelines

For Enforcement Agencies

- The Organizational GL's are the benchmark for government agencies to evaluate the appropriate disposition of investigations of organizations
- Basis for sentencing convicted organizations

For Organizations

- The seven minimal requirements in § 8B2.1 provide organizations with a framework for effective ethics and compliance programs
- If an organization becomes subject to investigation, the Organizational GL's provide roadmap to mitigate potential penalties

Measuring Organizational Culpability

Six Factors used to either increase or decrease “culpability score” under the guidelines:

- ↑Tolerance of criminal activity
- ↑Prior history
- ↑Violation of prior agreement or order
- ↑Obstruction of justice
- ↓Effective compliance and ethics program
- ↓Self-reporting, cooperation, acceptance of responsibility

Minimum Requirements

1. **Clear and effective articulation of policies:** “standards of conduct and internal control systems that are reasonably capable of reducing the likelihood of violations of law”
2. **Accountability:** resides with the board itself, which must select a “high-level” individual to oversee the compliance program and assign compliance responsibility to managers throughout the organization
3. **Due diligence in the selection of high-level officers:** must not assign compliance responsibilities to someone who has a propensity to engage in illegal activities or conduct inconsistent with ethics program
4. **Training and communication:** steps must be taken to communicate standards and train employees, including at upper levels of the organization

Minimum Requirements

- 5. Auditing effectiveness:** a compliance program must include monitoring and auditing programs designed to detect criminal conduct, periodic reevaluations of the effectiveness of the program, and mechanisms for anonymous reporting by employees
- 6. Enforcement through incentive and discipline:** appropriate discipline against those who fail to monitor compliance vigorously, and incentives for compliance performance
- 7. Prevention & remediation:** the organization must be responsive and comprehensive in responding to a violation and in modifying the program to prevent future violations and should periodically assess risks

Ethics and Compliance Program Expectations

- No longer enough to just have a compliance program -- no “paper programs” -- the program must be “effective” (i.e. meet at least the 7 minimal standards)
- High level responsibility for compliance program including a greater role for audit committees and Board
- Focus on corporate culture – “tone at the top”
- Programs must be individualized and include risk assessments
- Expectation of self-policing and self-disclosure

Program Must Be Clear and Effective

- DOJ Guidance (US Atty's Manual) – two “fundamental” questions, is the program well designed, and does the program work?
- SEC (*Seaboard* Decision) -- What compliance procedures were in place to prevent misconduct and why did procedures fail?
- UK Bribery Act (2010) – procedures need to adequately reflect risks faced by the organization and be communicated effectively

Leadership Responsibility

- DOJ guidance asks if the directors are provided with information sufficient to enable the exercise of independent judgment, and are internal audit functions conducted at a level sufficient to ensure independence and accuracy?
- SEC guidance asks if the Audit Committee was fully informed?
- Sentencing Guidelines state the Board must be knowledgeable about program and exercise reasonable oversight
- The UK asks for “top-level commitment” to foster an appropriate corporate culture

Corporate Culture

- DOJ McNulty Memo: “Management is responsible for a corporate culture in which criminal conduct is either discouraged or tacitly encouraged.”
- DOJ ex-AAG (ABA Speech): “The question we are going to be looking at fundamentally is, is this a corporation whose culture and structure in some way facilitated or allowed this to happen?”

New Amendments to The Organizational Sentencing Guidelines

November 2010

Commission Outreach and Public Comment

- Guidance on the “reasonable steps” an organization should take when criminal conduct is detected
- Credit for “effective compliance and ethics program” has only been applied five times since 1991
- Compliance personnel’s access to highest level of the organization remains a challenge
- Guidance on particularized assessment of risk and responsibilities of high-level officers
- Consolidation and expansion of probation terms to reflect best practices

Final Promulgated Amendments

- Application note that clarifies the type of “reasonable steps” that an organization should take to respond to criminal conduct and prevent further criminal conduct
- Extension of mitigation credit to organizations with effective compliance and ethics programs even when high-level or substantial authority personnel are involved in criminal conduct
- Consolidation and simplification of organizational probation terms

The Seventh Minimal Requirement under § 8B2.1(b)(7)

After criminal conduct has been detected, the organization shall take reasonable steps to respond appropriately to the criminal conduct and to prevent further similar criminal conduct, including making any necessary modifications to the organization's compliance and ethics program.

What should an effective compliance and ethics program include to respond to criminal conduct?

New Application Note 6 under § 8B2.1

Application of Subsection (b)(7).—Subsection (b)(7) has two aspects.

*First, the organization should respond appropriately to the criminal conduct. The organization should take **reasonable steps, as warranted under the circumstances**, to remedy the harm resulting from the criminal conduct. These steps **may include, where appropriate**, providing **restitution** to identifiable victims, as well as other forms of **remediation**. Other reasonable steps to respond appropriately to the criminal conduct **may include self-reporting and cooperation with authorities**.*

New Application Note 6 under § 8B2.1

Second, the organization should act appropriately to prevent further similar criminal conduct, including assessing the compliance and ethics program and making modifications necessary to ensure the program is effective. The steps taken should be consistent with subsections (b)(5) and (c) and may include the use of an outside professional advisor to ensure adequate assessment and implementation of any modifications.

Current “Blocker” for Credit for An Effective Compliance and Ethics Program in § 8C2.5

- (3)(A) Except as provided in subdivision (B) subsection (f)(1) shall not apply if an individual within high-level personnel of the organization, a person within high-level personnel of the unit of the organization within which the offense was committed where the unit had 200 or more employees, or an individual described in §8B2.1(b)(2)(B) or (C), participated in, condoned, or was willfully ignorant of the offense.
- (B) There is a rebuttable presumption, for purposes of subsection (f)(1), that the organization did not have an effective compliance and ethics program if an individual—(i) within high-level personnel of a small organization; or (ii) within substantial authority personnel, but not within high-level personnel, of any organization, participated in, condoned, or was willfully ignorant of, the offense.

Bottom line: only 5 Organizations in 20 years have qualified

New Subdivision Under § 8C2.5 Credit for Effective Compliance and Ethics Program

(C) Subparagraphs (A) and (B) shall not apply if—

- (i) the individual or individuals with operational responsibility for the compliance and ethics program (see § 8B2.1(b)(2)(C)) have *direct reporting obligations* to the governing authority or an appropriate subgroup thereof (e.g., an audit committee of the board of directors);**

Application Note 11, § 8C2.5: "Direct Reporting Obligations"

*For purposes of subsection (f)(3)(C)(i), an individual has "direct reporting obligations" to the governing authority or an appropriate subgroup thereof if the individual has **express authority to communicate personally** to the governing authority or appropriate subgroup thereof*

(A) promptly on any matter involving criminal conduct or potential criminal conduct, and

(B) no less than annually on the implementation and effectiveness of the compliance and ethics program.

New Subdivision Under § 8C2.5 Credit for Effective Compliance and Ethics Program

(ii) the compliance and ethics program detected the offense before discovery outside the organization or before such discovery was reasonably likely;

(iii) the organization promptly reported the offense to appropriate governmental authorities; and

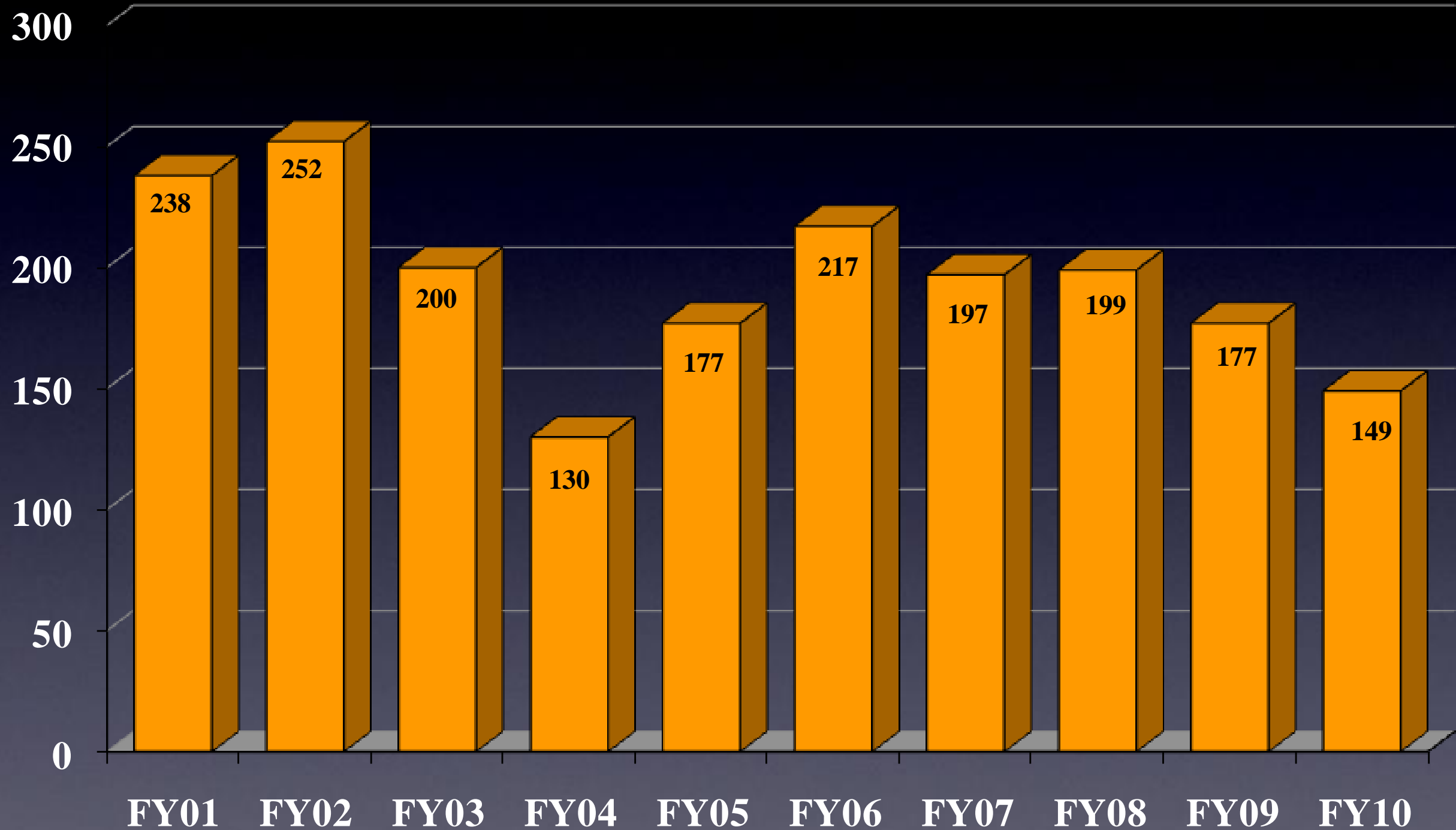
(iv) no individual with operational responsibility for the compliance and ethics program participated in, condoned, or was willfully ignorant of the offense.

Operation of § 8C2.5(f)(3)(C)(ii) &(iii)

- Whistle blower report will not necessarily cause the organization to lose credit for an effective compliance and ethics program.
- Application Note 10: no reporting is required if the organization “reasonably concluded, based on the information available, that no offense had been committed.”

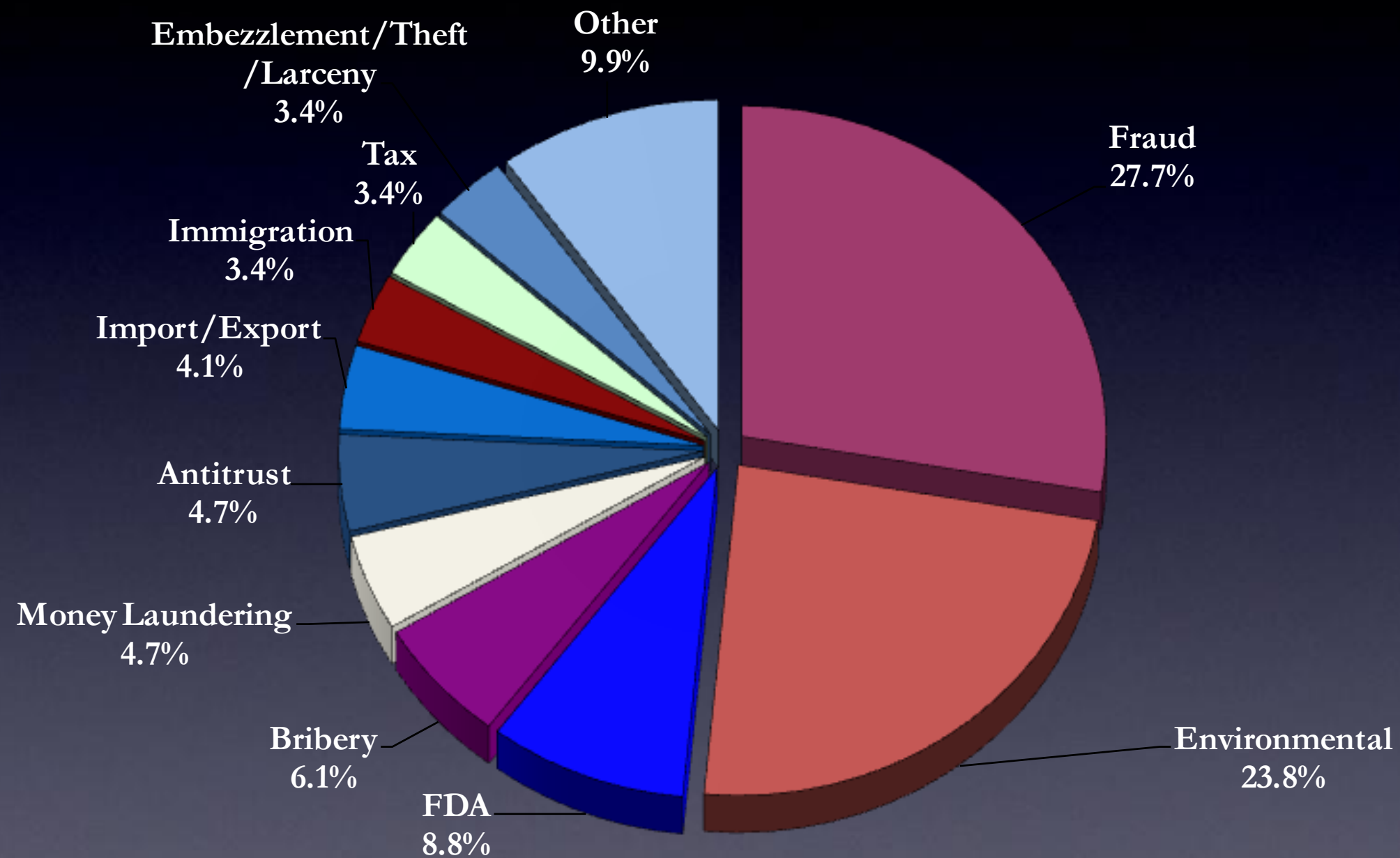
Recent Organizational Sentencing Data

Number of Organizational Cases FY01-FY10



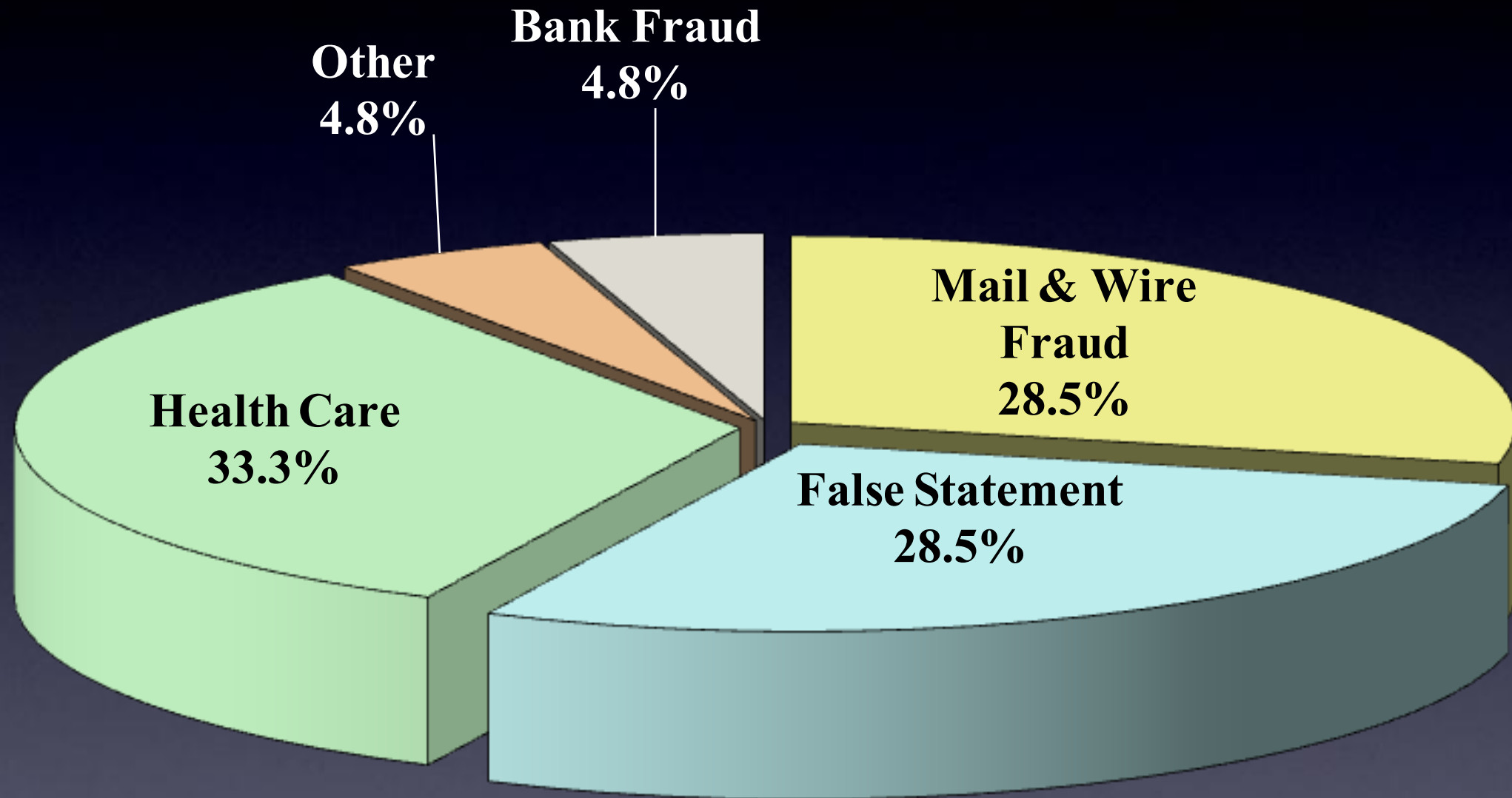
SOURCE: United States Sentencing Commission, 2001-2010 Sourcebook of Federal Sentencing Statistics.

Primary Offenses of Organizational Cases FY10

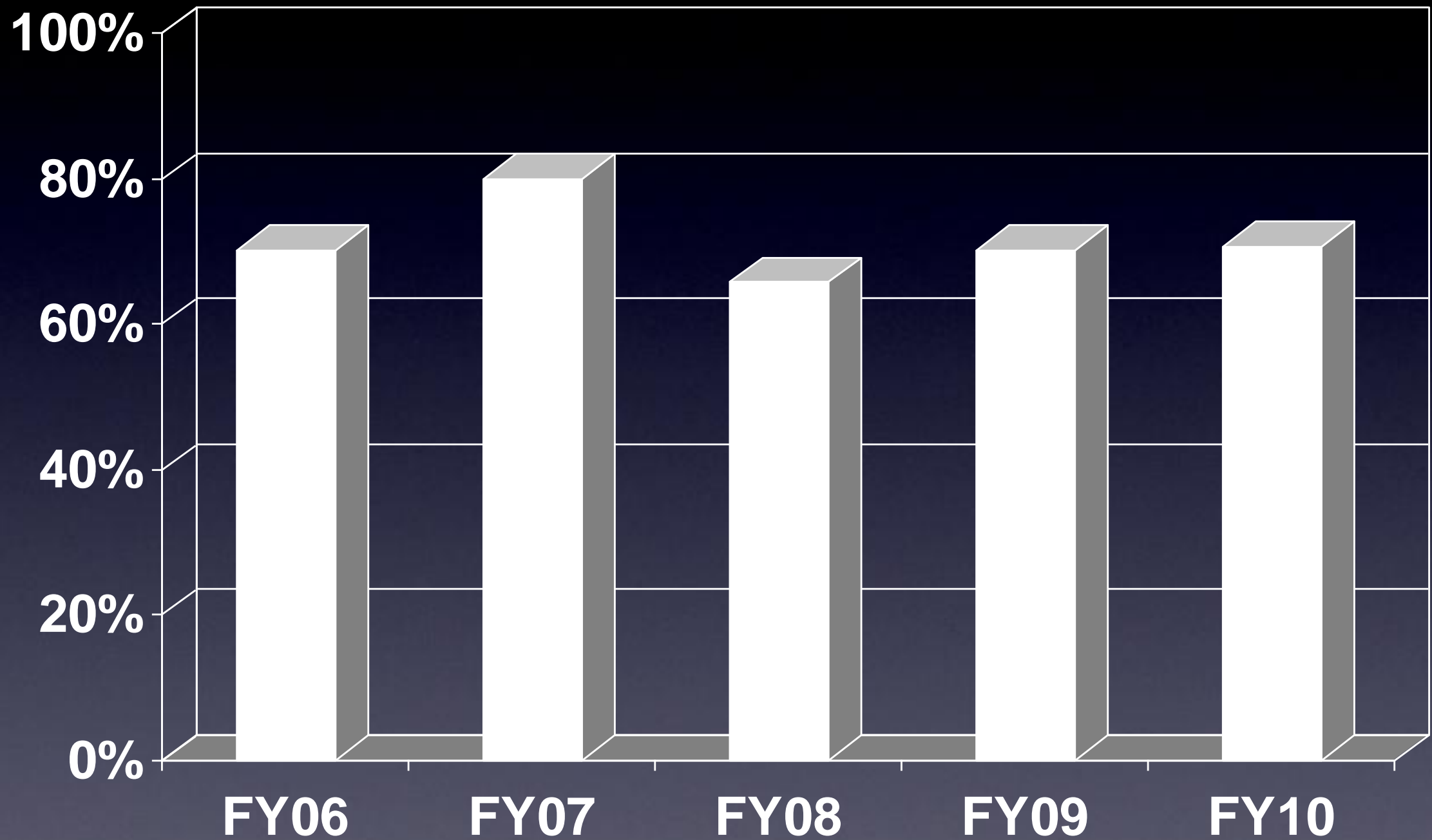


SOURCE: United States Sentencing Commission, *2010 Sourcebook of Federal Sentencing Statistics*. The Environmental category includes the following offense types: Environmental-Water Pollution, Environmental-Air Pollution, Environmental-Hazardous/Toxic Pollutants, and Environmental-Wildlife.

Fraud Offenses in Organizational Cases FY10

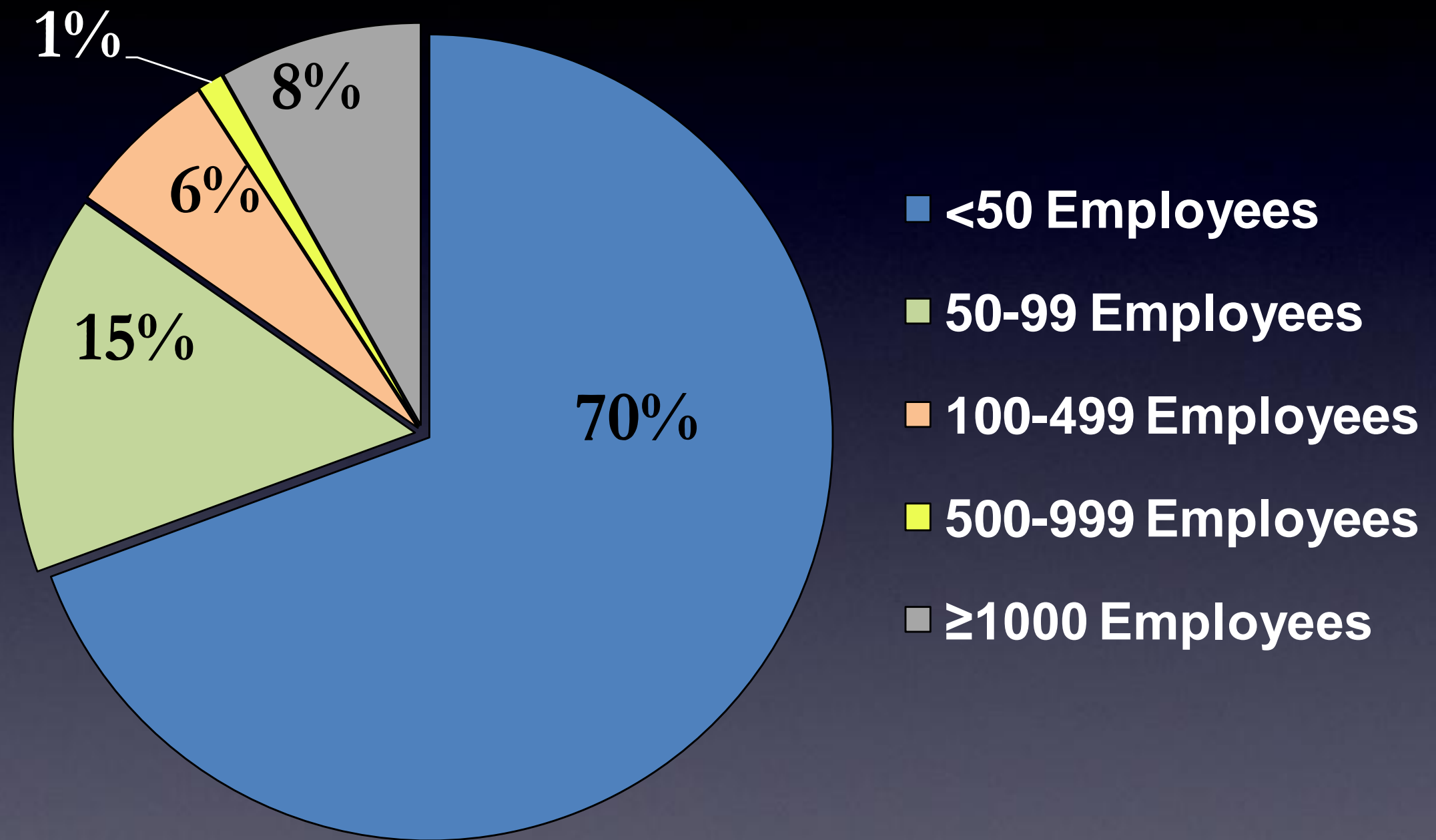


Percentage of Organizational Cases Receiving Probation Fiscal Year 2006-2010

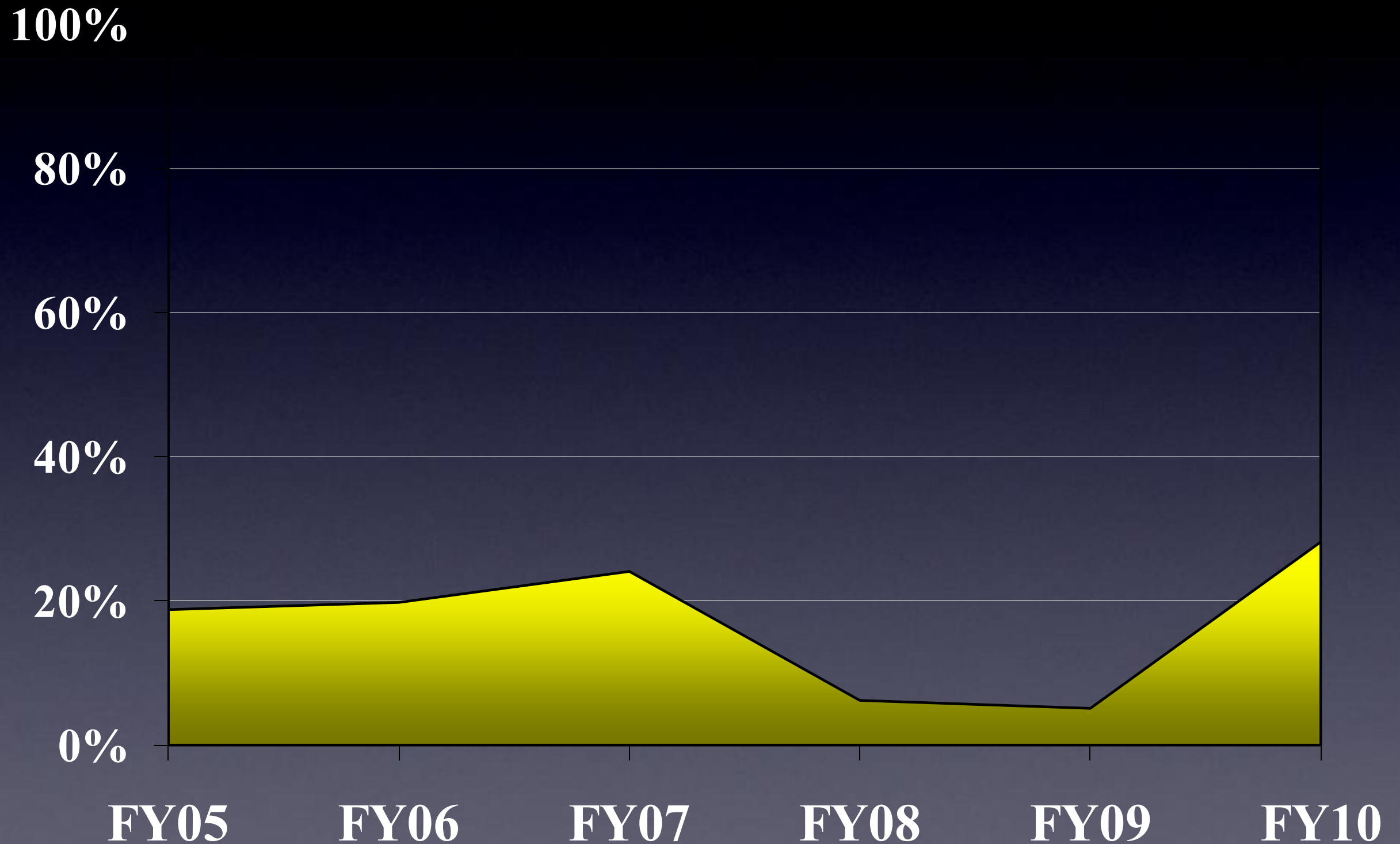


SOURCE: United States Sentencing Commission, 2006-2010 Sourcebook of Federal Sentencing Statistics.

Size of Organizations Sentenced By Number of Employees in Fiscal Year 2010

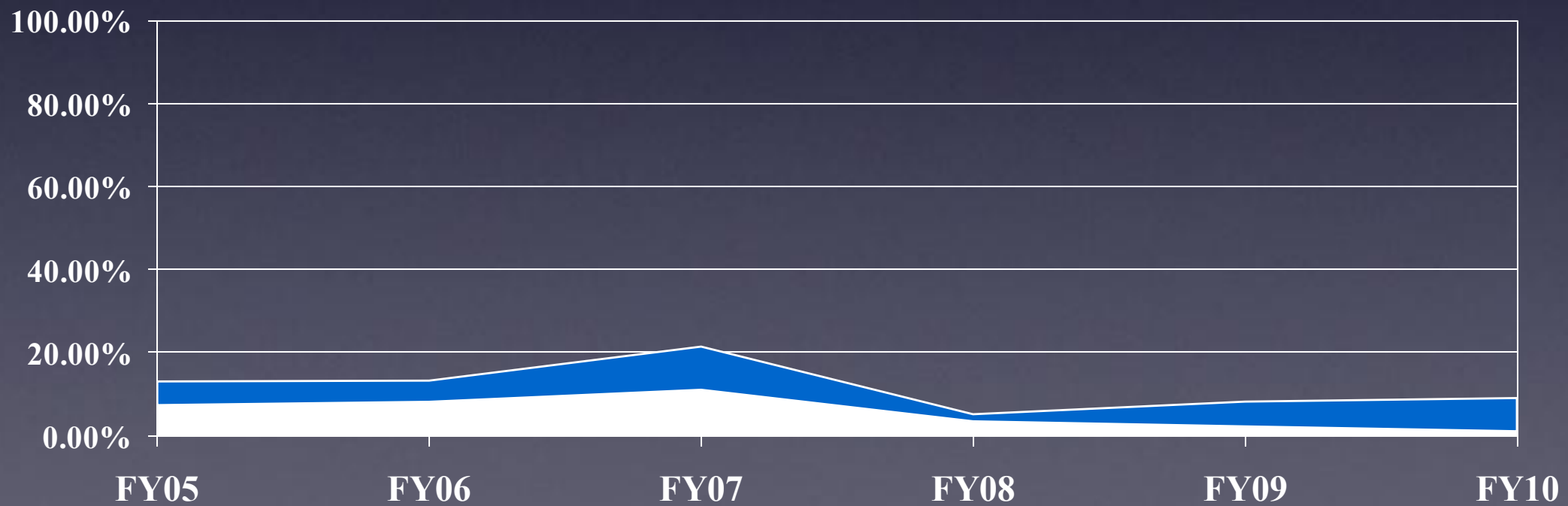
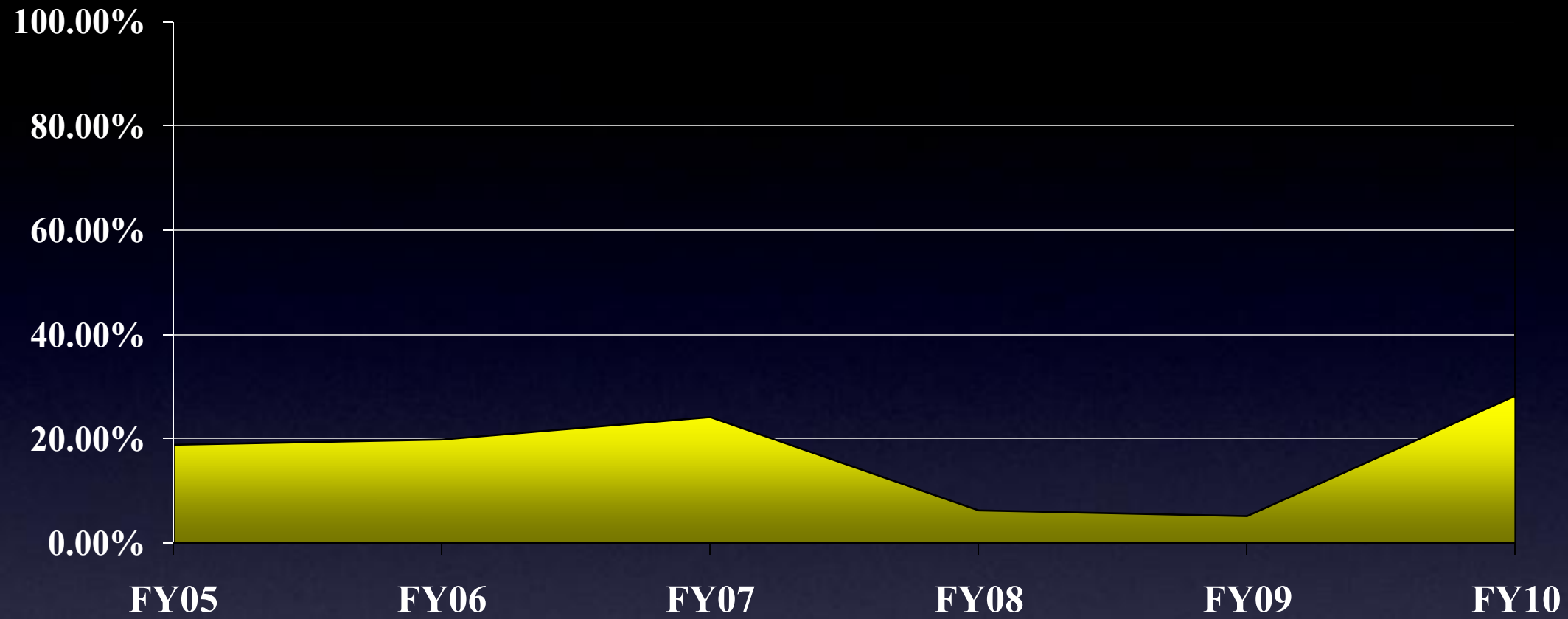


Percentage of Organizational Cases With Court Ordered Compliance / Ethics as Component of Sentence Fiscal Year 2006 - 2010

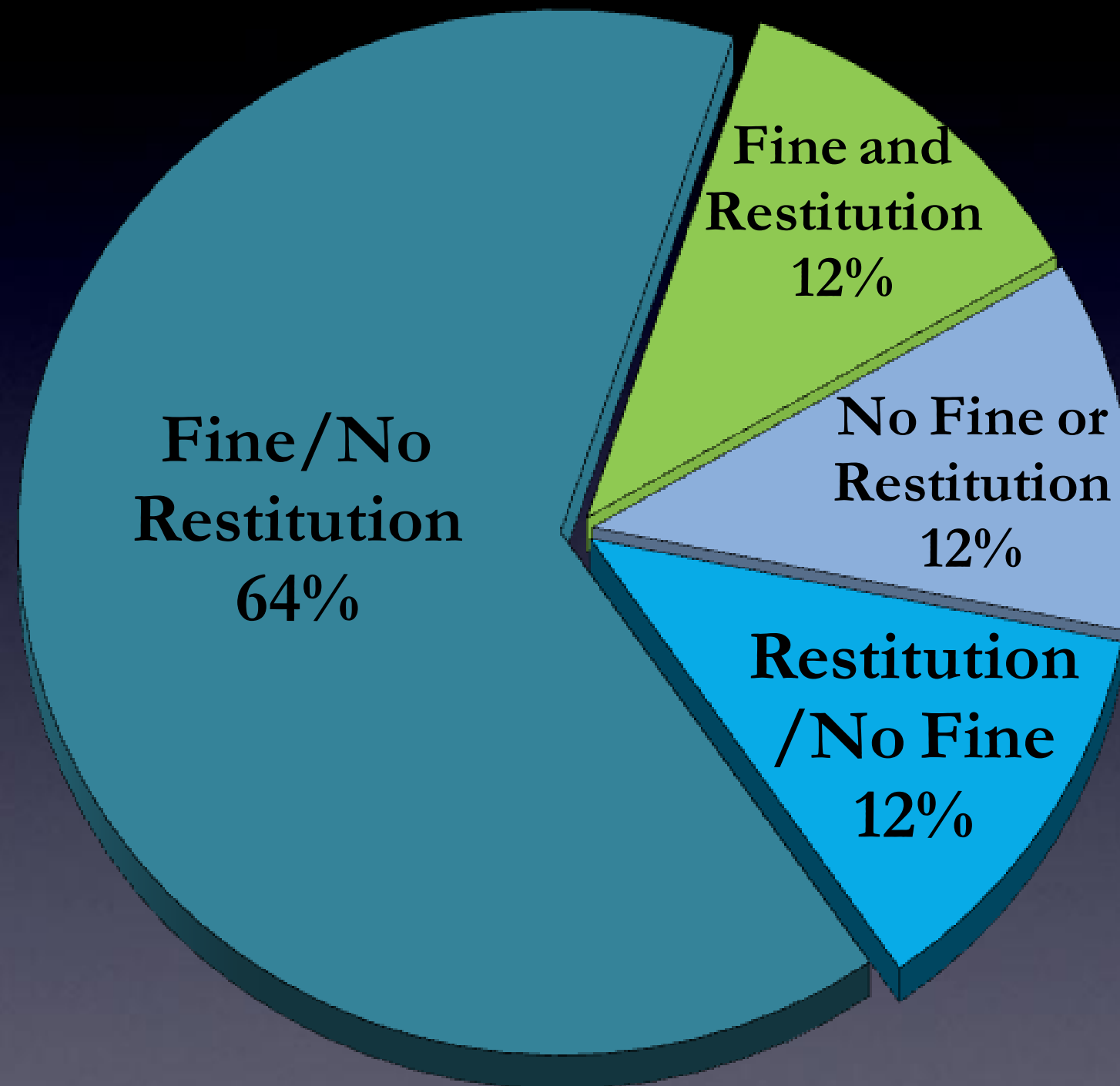


SOURCE: United States Sentencing Commission, 2006-2010 Sourcebook of Federal Sentencing Statistics.

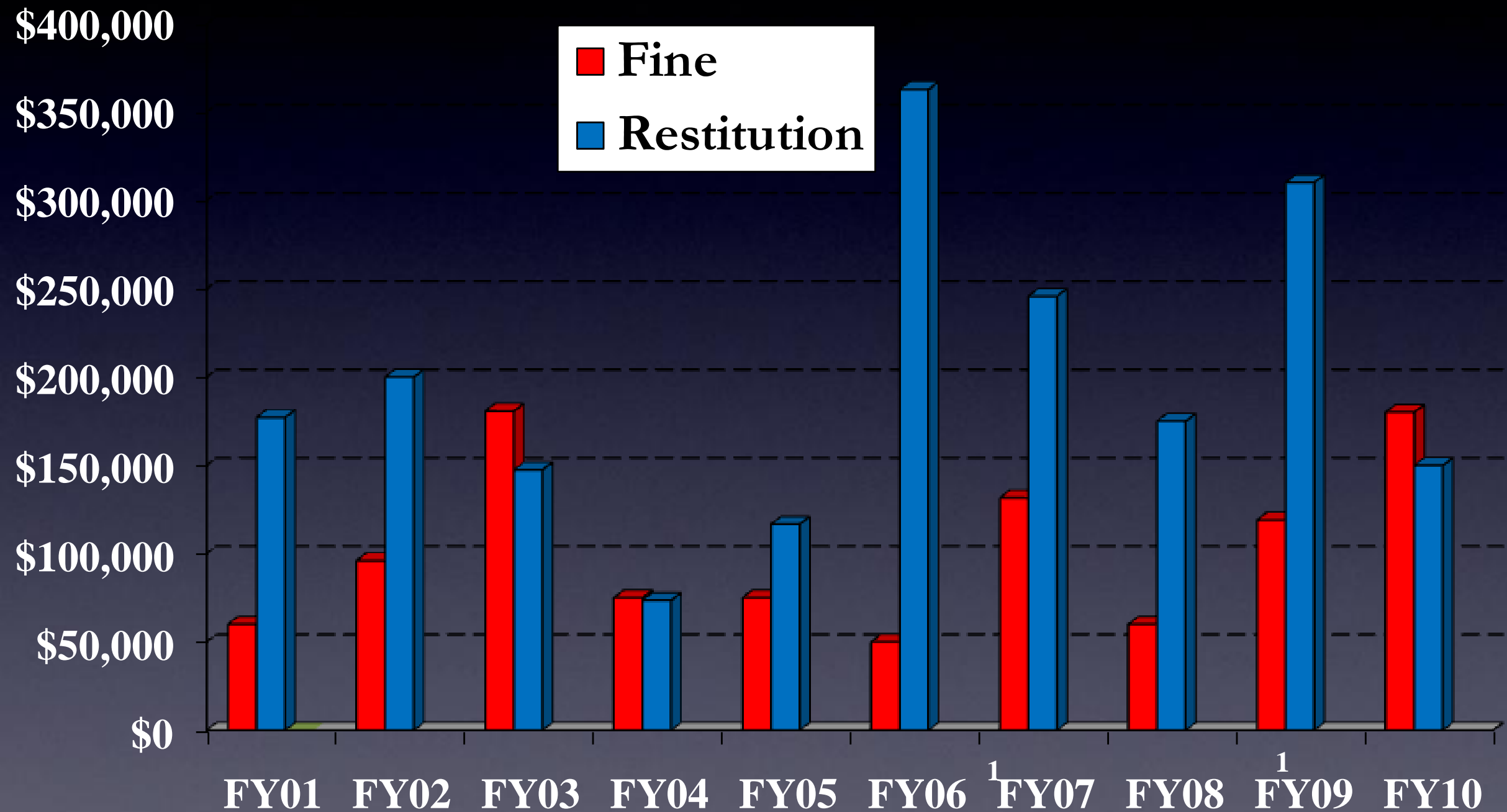
Percentage of Organizational Cases With Court Ordered Compliance/ Ethics as Component of Sentence and Percentage of Larger Organizations Sentenced Fiscal Year 2005 -2010



Types of Monetary Sentences FY10



Median Fine and Restitution for Organizations FY01-FY10



¹FY04 data consists of only pre-*Blakely* data from October 1, 2003 through June 24, 2004. FY05 data consists of only post-*Booker* data from January 12, 2005 through September 30, 2005.
SOURCE: United States Sentencing Commission, 2001-2010 Sourcebook of Federal Sentencing Statistics.

Top Ten Organizational Fines and Restitution Orders by Offense Type (Millions of Dollars) - Fiscal Year 2010

Fines

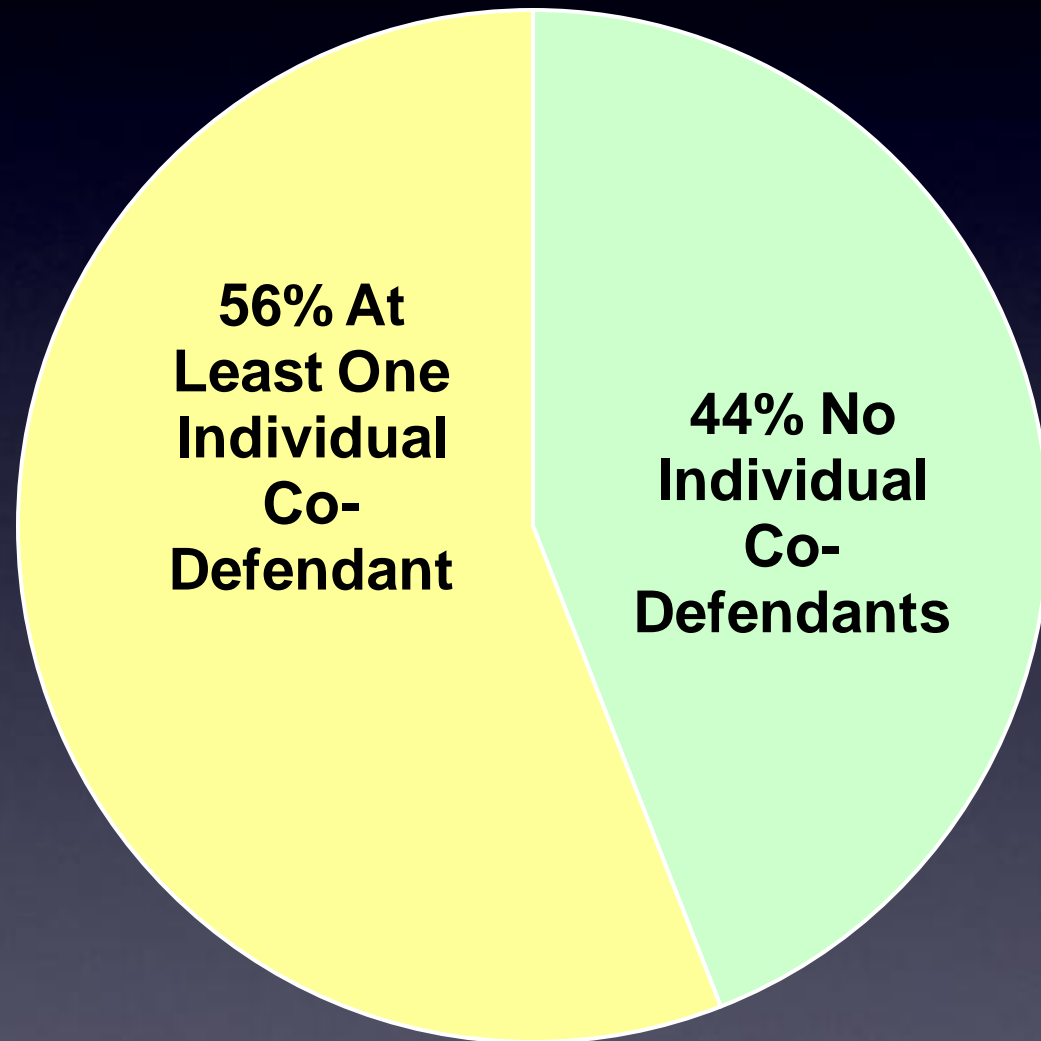
Food & Drug	\$1,195.0
Bribery	\$400.0
Antitrust	\$38.0
Antitrust	\$30.0
Bribery	\$29.1
Racketeering	\$28.2
Bribery	\$27.4
Bribery	\$17.1
Bribery	\$14.1
Antitrust	\$9.0

Restitution

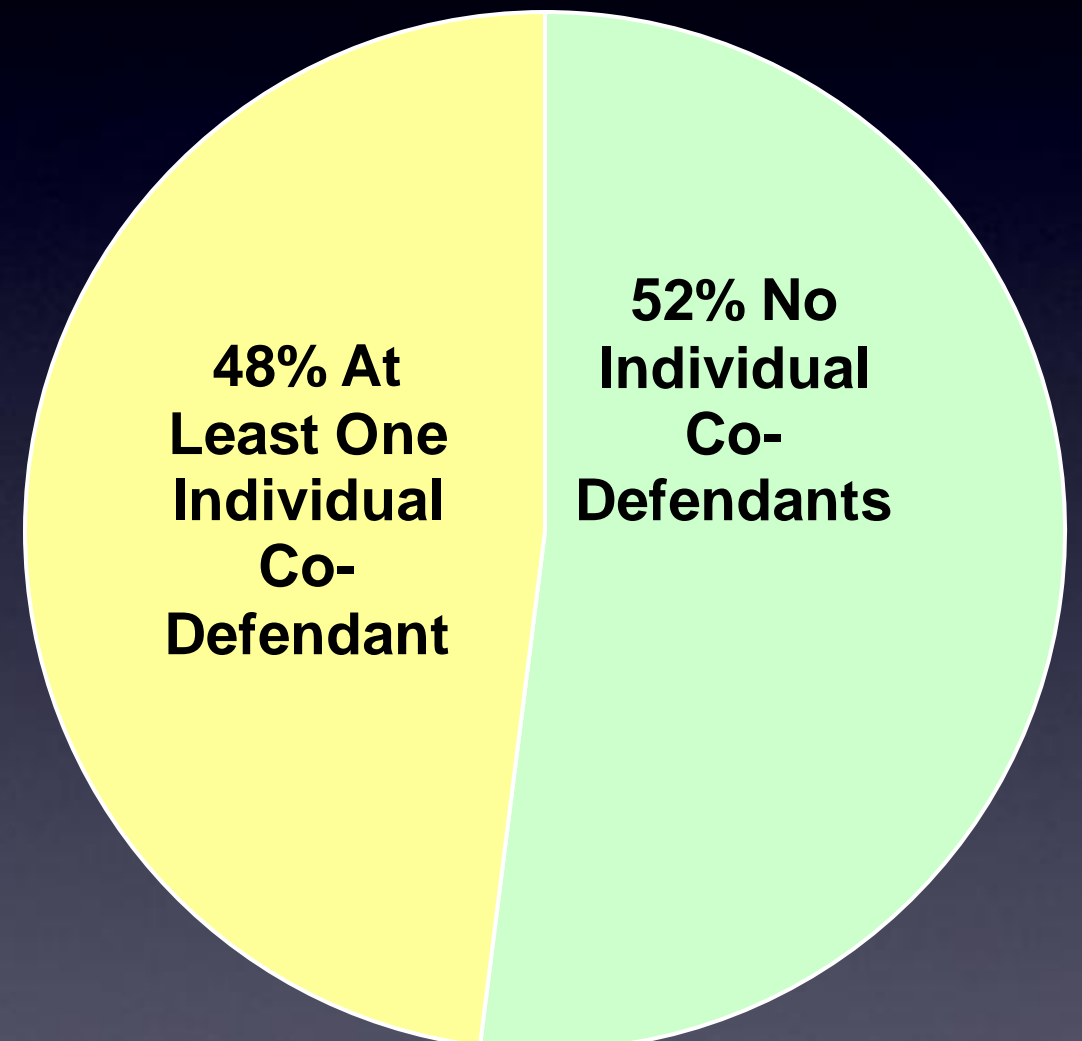
Fraud	\$200.0
Fraud	\$200.0
Fraud	\$200.0
Fraud	\$16.2
Money Laundering	\$1.5
Bribery	\$.8
Fraud	\$.8
Fraud	\$.7
Fraud	\$.7
Fraud	\$.6

Relationship of Individual Offender Cases to Organizational Cases in Fiscal Year 2009 & 2010

FY09



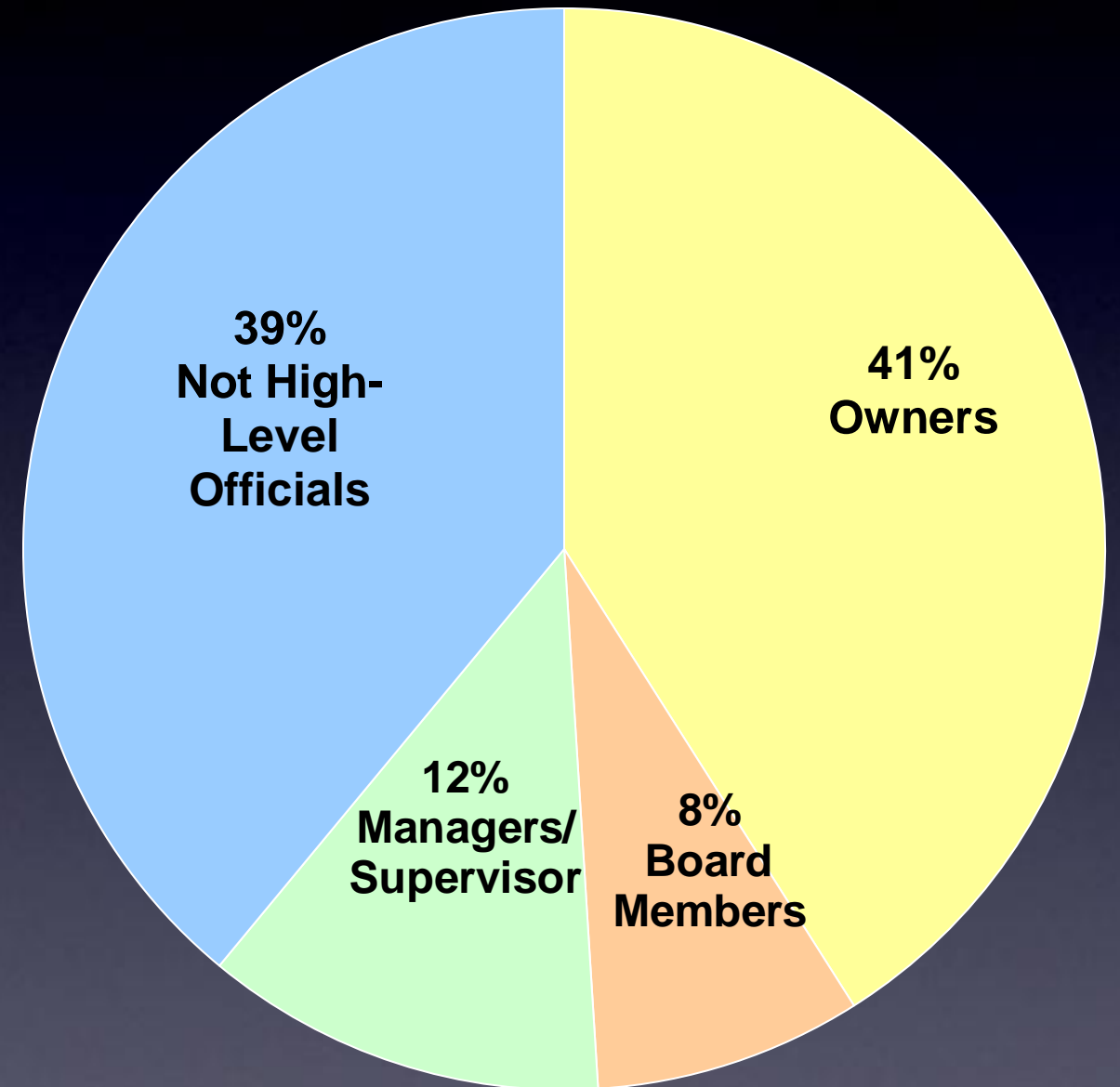
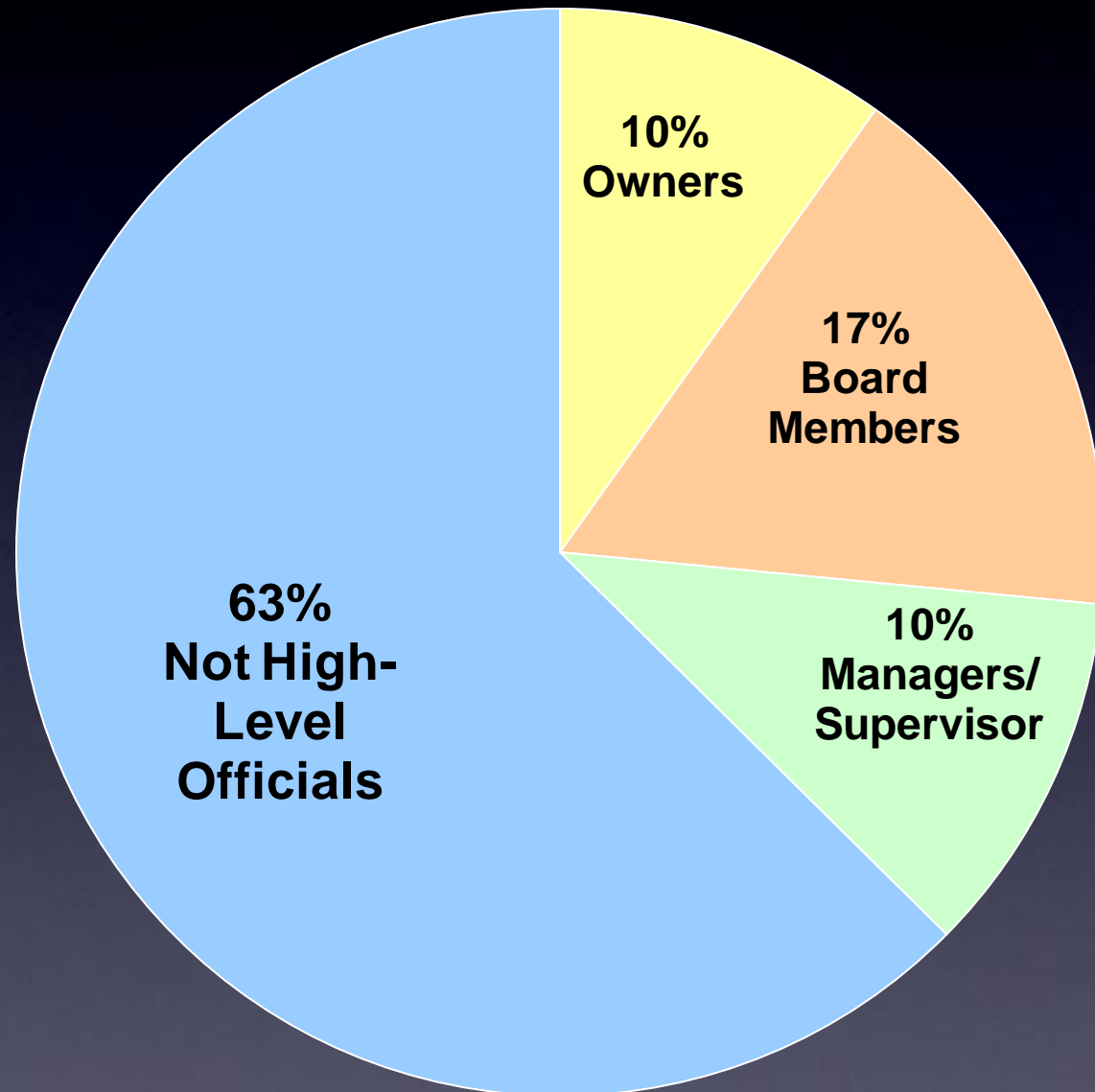
FY10



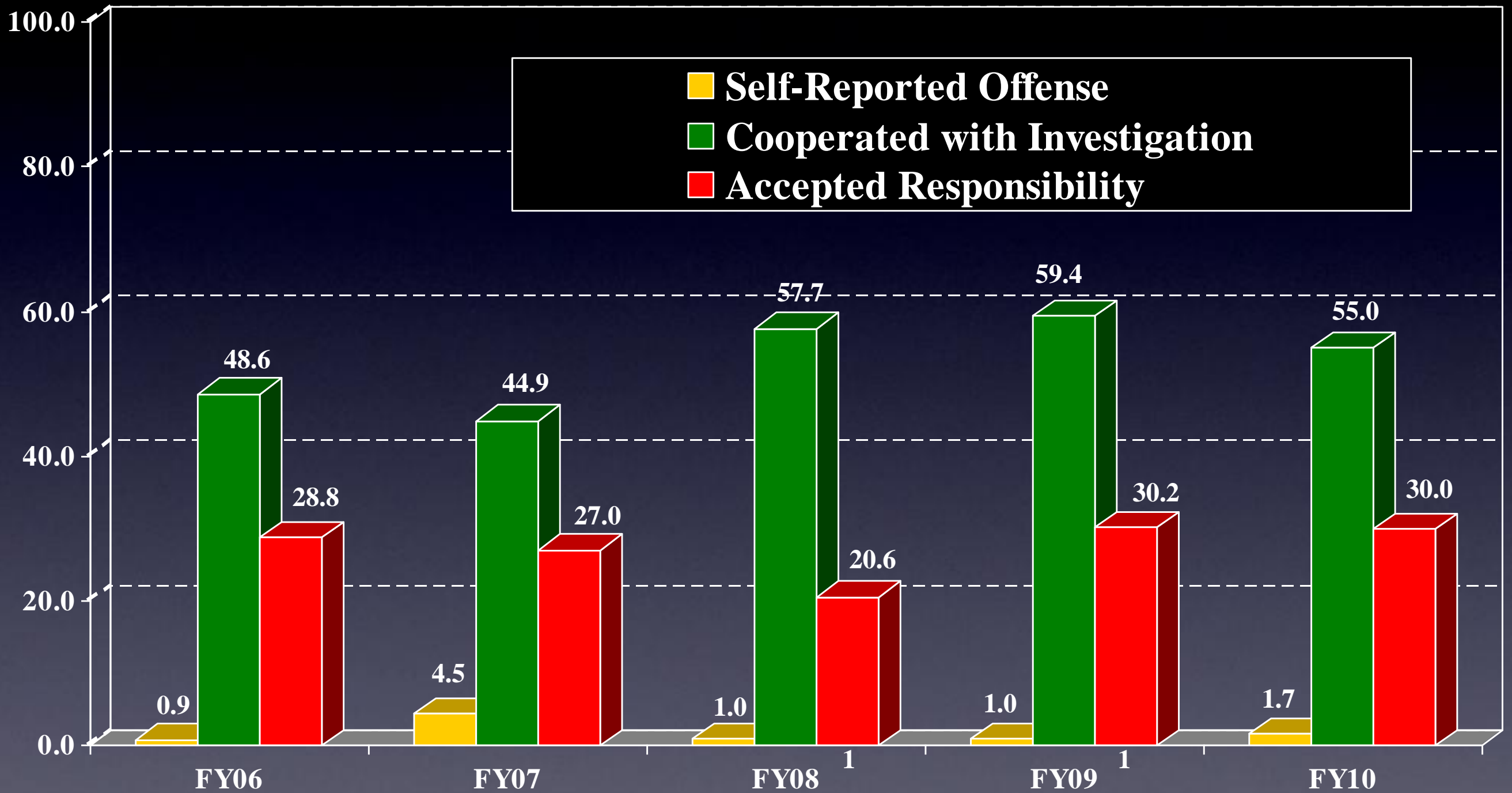
Percentage of Individual Offenders Who Were “High-Level” Officials of Co-Defendant Organizations Fiscal Year 2009 & 2010

FY09

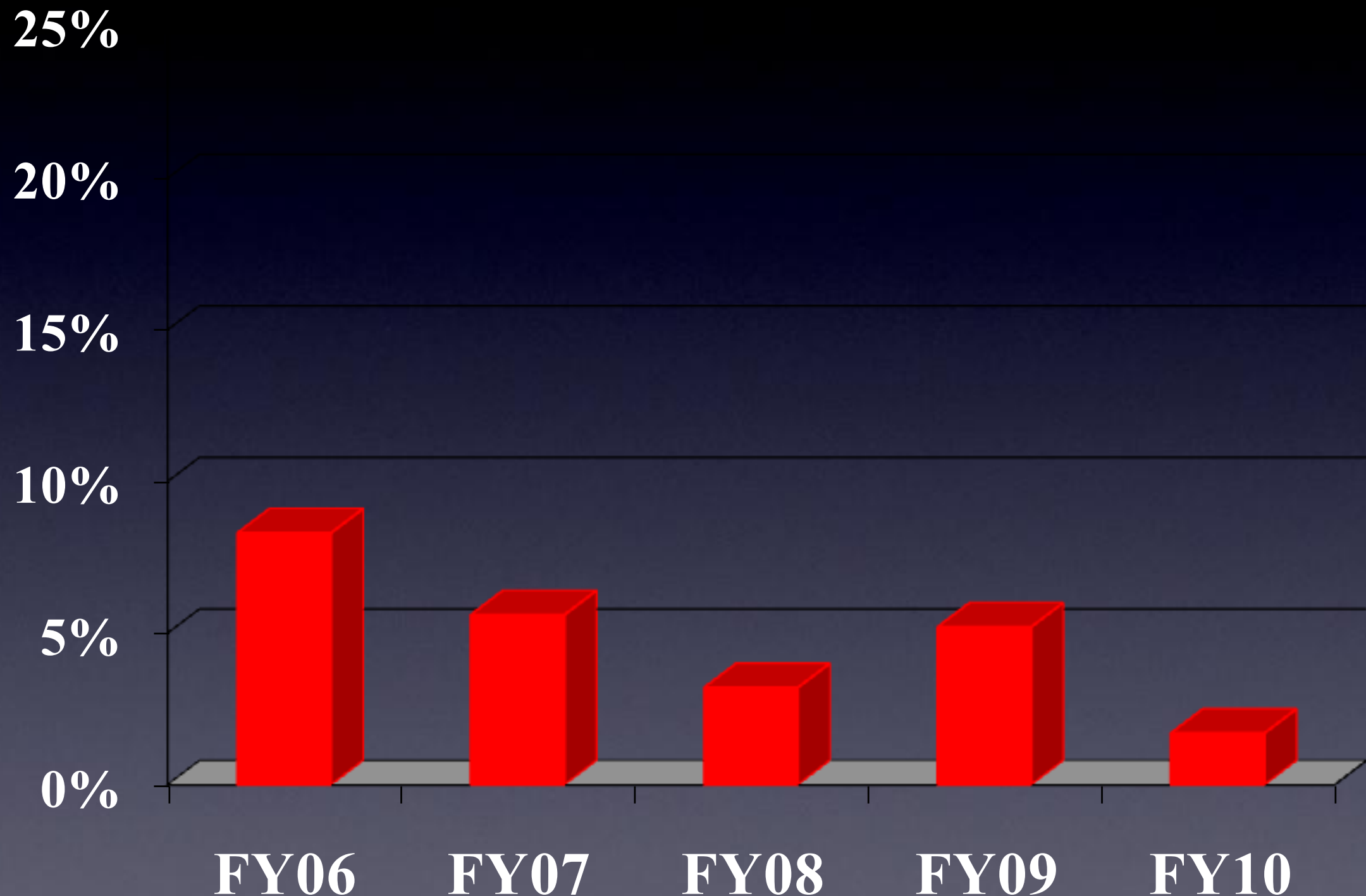
FY10



Percentage of Organizational Cases Receiving Reduction in Culpability Score Under § 8C2.5(g) Fiscal Year 2006 - 2010

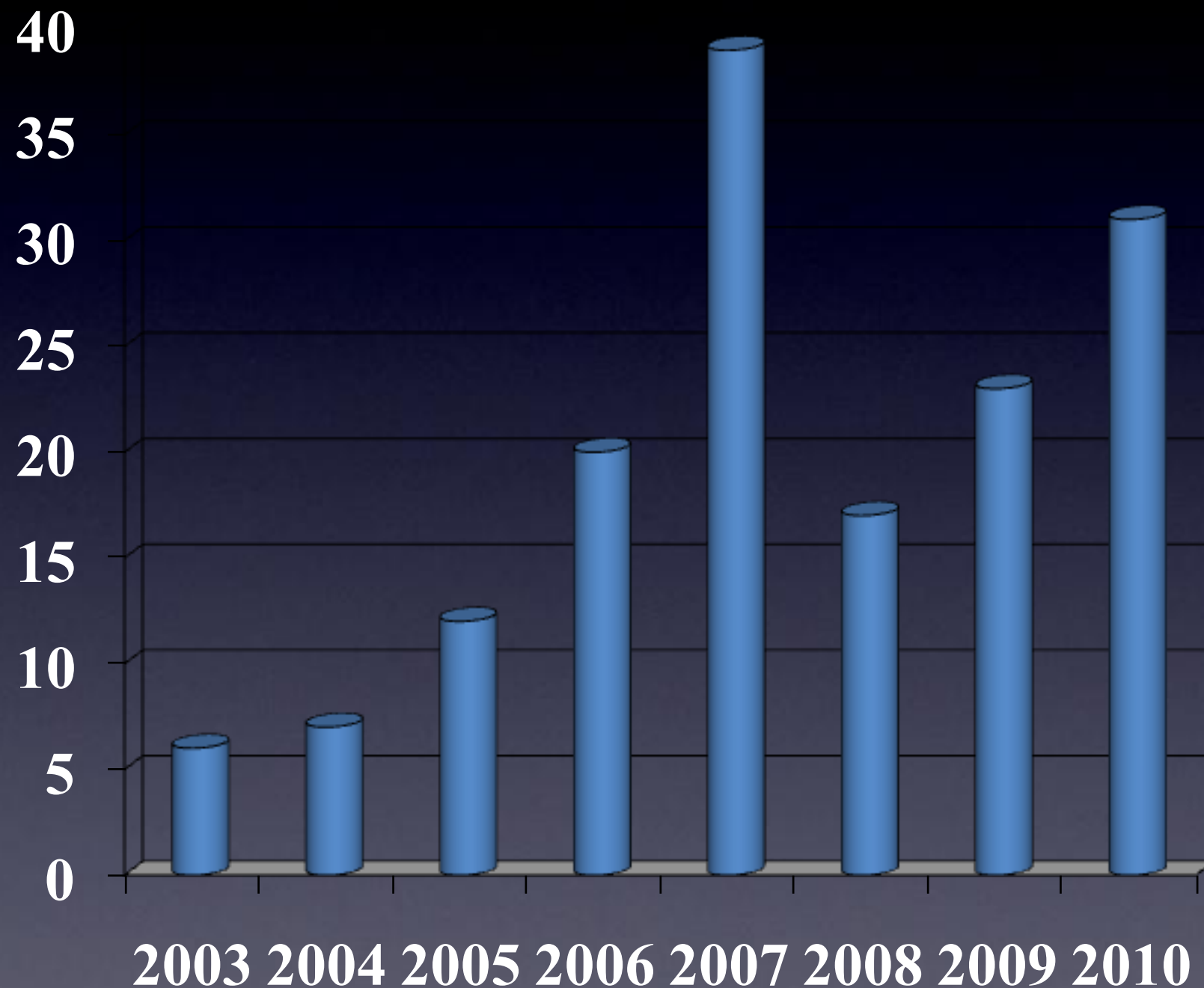


Percentage of Organizations Sentenced that Obstructed Justice (§ 8C2.5(e)) Fiscal Year 2006 - 2010



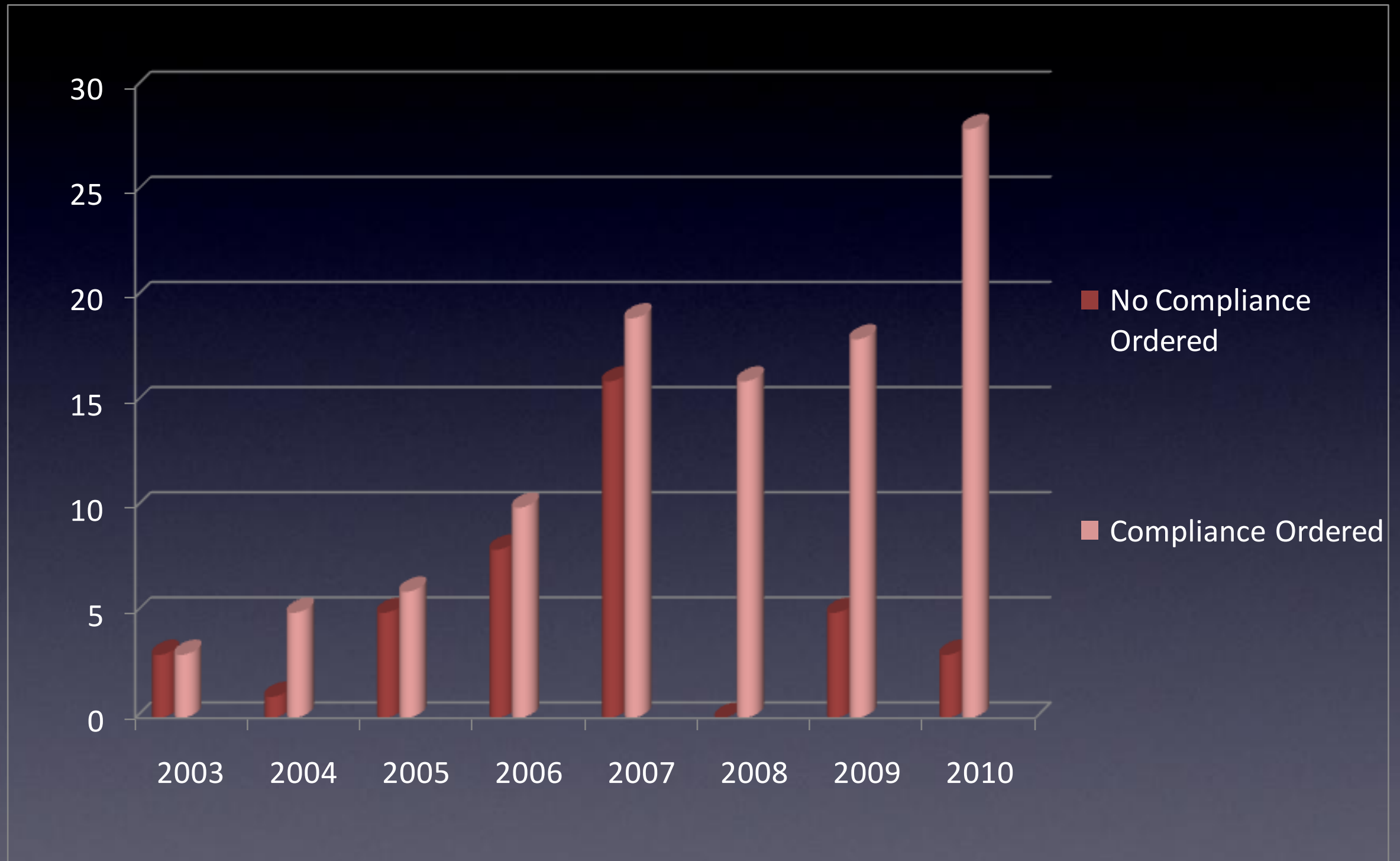
Deferred Prosecution and Non-Prosecution Agreements

Deferred Prosecution and Non-Prosecution Agreements for Organizations FY03- FY10



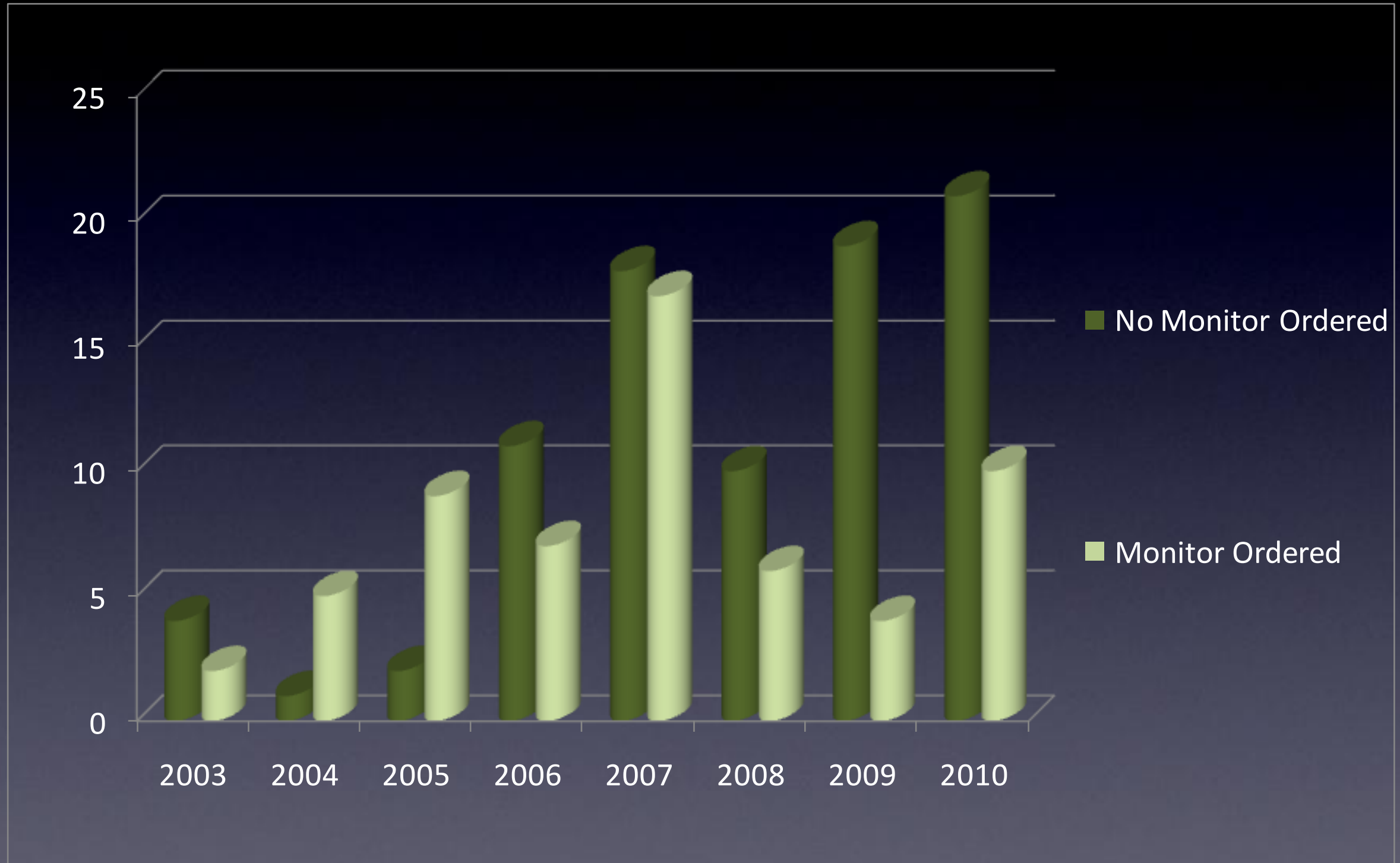
Source: Submission and Letter from Principal Deputy Assistant Attorney General Brian Benczkowski to Chairman John Conyers, Committee on the Judiciary, U.S. House of Representatives, May 15, 2007; Lawrence D. Finder and Ryan D. McConnell, Annual Corporate Pre-Trial Agreement Update 2007 (2008); Lawrence D. Finder, Ryan D. McConnell, and Scott L. Mitchell, Betting the Corporation, Compliance Programs in the Context of Deferred and Non-Prosecution Agreements (2009); Jay Martin, Ryan D. McConnell & Charlotte A. Simon, Plan Now or Pay Later: The Role of Compliance in Criminal Cases (Spring 2011).

Deferred Prosecution and Non-Prosecution Agreements for Organizations FY03- FY10



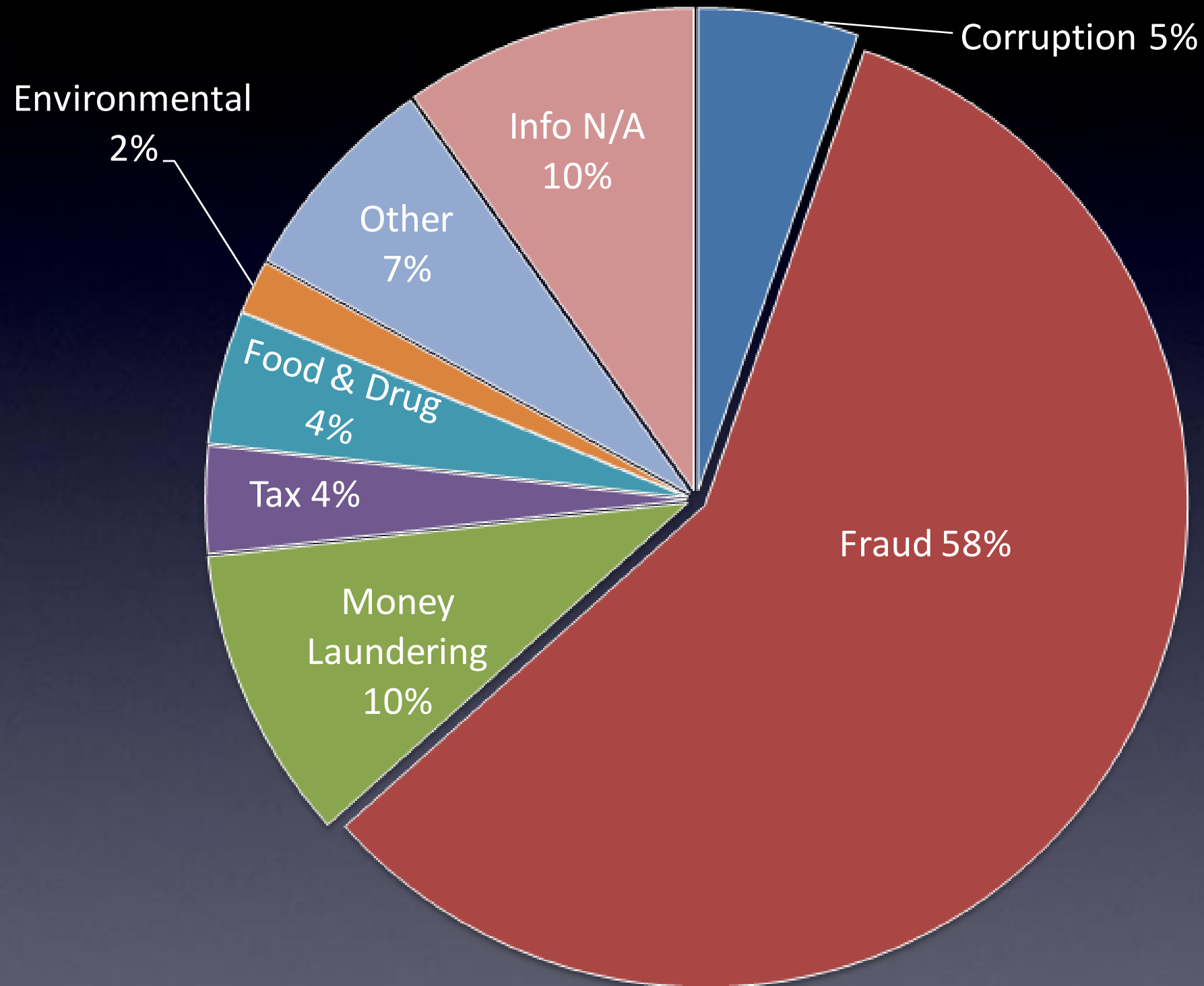
Source: Submission and Letter from Principal Deputy Assistant Attorney General Brian Benczkowski to Chairman John Conyers, Committee on the Judiciary, U.S. House of Representatives, May 15, 2007; Lawrence D. Finder and Ryan D. McConnell, Annual Corporate Pre-Trial Agreement Update 2007 (2008); Jay Martin, Ryan D. McConnell & Charlotte A. Simon, Plan Now or Pay Later: The Role of Compliance in Criminal Cases (Spring 2011).

Deferred Prosecution and Non-Prosecution Agreements for Organizations FY03- FY10



Source: Submission and Letter from Principal Deputy Assistant Attorney General Brian Benczkowski to Chairman John Conyers, Committee on the Judiciary, U.S. House of Representatives, May 15, 2007; Lawrence D. Finder and Ryan D. McConnell, Annual Corporate Pre-Trial Agreement Update 2007 (2008); Jay Martin, Ryan D. McConnell & Charlotte A. Simon, Plan Now or Pay Later: The Role of Compliance in Criminal Cases (Spring 2011).

Deferred Prosecution and Non-Prosecution Agreements for Organizations FY93- FY08



Source: Submission and Letter from Principal Deputy Assistant Attorney General Brian Benczkowski to Chairman John Conyers, Committee on the Judiciary, U.S. House of Representatives, May 15, 2007; Lawrence D. Finder and Ryan D. McConnell, Annual Corporate Pre-Trial Agreement Update 2007 (2008); and other public sources.

Eric Morehead
Senior Compliance Counsel
Corpedia Corporation

512-961-3890

emorehead@corpedia.com

www.corpedia.com

www.ethisphere.com