

Prevention of Corporate Liability Current Report

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Filing Note:

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Cooperation

Compliance Experts Welcome DOJ Comments About Extensive Cooperation in Siemens Case

A top Department of Justice official lauded the cooperation efforts of Siemens AG as news broke that a group of former executives of the German firm are facing criminal and civil charges under the Foreign Corrupt Practices Act.

In response, the head of the Ethics and Compliance Officer Association welcomed the government's feedback about corporate compliance efforts. The issue has been a point of contention between federal prosecutors and the ethics and compliance community, which has expressed frustration over a lack of information coming out of DOJ. Compliance professionals say getting insight about how government attorneys evaluate an organization's compliance program can strengthen those efforts.

"This is certainly a first and positive step."

KEITH T. DARCY
ETHICS AND COMPLIANCE OFFICER ASSOCIATION

DOJ and the Securities and Exchange Commission Dec. 13 announced parallel charges related to an alleged bribery scheme to retain a \$1 billion contract to produce national identity cards for Argentine citizens (*United States v. Sharef*, S.D.N.Y., No. 11-cr-01056-DLC-1, 12/12/11; *SEC v. Sharef*, S.D.N.Y., No. 11 Civ. 9073, 12/13/11).

In separate news releases, the agencies said the charges against the executives follow from a 2008 plea deal in which Siemens agreed to pay a record \$1.6 billion in fines and penalties, including \$800 million to U.S. authorities, to settle charges that it paid bribes in Argentina and several other countries over a nine-year period. (See 3/16/09 *Prev. Corp. Liability* 28.) That amount remains the largest FCPA settlement to date, federal authorities said.

Breuer: 'Cooperation Was Simply Outstanding'

Lanny Breuer, assistant attorney general of DOJ's Criminal Division, said at a press conference that the corporation's cooperation after the 2008 case was instrumental in the recent investigation of the individuals. "Siemens's cooperation was simply outstanding and extraordinary, and it obviously played a large role in how we approached this matter," Breuer said.

A Dec. 13 DOJ news release said Siemens made disclosures to the government "after initiating an internal FCPA investigation of unprecedented scope." The company shared the results of that probe and "cooperated extensively and authentically with the department in its ongoing investigation,"

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DOJ said. Siemens also “took remedial action, including the complete restructuring of Siemens AG and the implementation of a sophisticated compliance program and organization,” the news release said.

Keith T. Darcy, the chief executive officer of the Waltham, Mass.-based ECOA, explained that people who run corporate ethics and compliance programs believe a dearth of feedback from prosecutors leaves corporations wondering whether investment is worthwhile.

The U.S. Sentencing Guidelines provide incentives for organizations that have effective compliance and ethics programs, but most corporate corruption cases settle out of court, Darcy said. That leaves compliance officers with “very little or no information about what or if any consideration has been given to offending companies” about their compliance and ethics activities, he said.

DOJ’s communications about the actions Siemens took is “a step in the right direction,” Darcy said. “Obviously, if there’s slightly more detail, hopefully that might be a next step, but this is certainly a first and positive step.”

Jodi Avergun, a partner at Cadwalader, Wickersham & Taft LLP, Washington, D.C., said DOJ’s announcement shows that Siemens has likely continued to cooperate with and provide information to government lawyers since it entered the plea agreement in 2008.

“A company that cooperates and settles FCPA charges must be prepared to continue providing evidence to the DOJ and SEC long after the ink dries on the settlement agreement,” Avergun told BNA.

Darcy cited another reason that compliance and ethics professionals,

and the corporations they work for, should be encouraged by the Siemens case. The firm’s 2010 year-end earnings indicate that the company had a record year. That is “a very positive statement to the population of Siemens, the 400,000 employees, that if you do it the right way you can actually still succeed and be at the top of your game,” Darcy said.

Board Member Among Accused

According to DOJ and the SEC, the executives and their co-conspirators engaged in an elaborate scheme from 1996 to early 2007 that caused Siemens to pay nearly \$100 million in bribes to high-ranking Argentine officials, members of the opposition party, political candidates, and others. The officials included two former Argentine presidents and former cabinet members, SEC said.

DOJ’s indictment, unsealed Dec. 13, charged six former Siemens executives and two intermediaries and agents:

- Uriel Sharef, a former managing board member at Siemens from July 2000 to December 2007;

- Herbert Steffen, chief executive officer of Siemens Argentina from 1983 to 1989, and again in 1991, and group president of Siemens Transportation Systems from 1996 to 2003;

- Andres Truppel, chief financial officer of Siemens Argentina from 1996 to 2002;

- Ulrich Bock, Stephan Signer, and Eberhard Reichert, former senior executives at Siemens Business Services; and

- Carlos Sergi and Miguel Czysch, who served as Siemens intermediaries and agents in the alleged plot.

The indictment charged the defendants with wire fraud, money laundering conspiracy, and conspiracy to

violate the FCPA and the wire fraud statute.

Officials at the press conference said the case is noteworthy in that this is the first time a former board member of a Fortune Global 50 company has been charged with FCPA violations.

The SEC’s complaint also charged Sharef, Bock, Signer, Steffen, Truppel, and Sergi. In addition, the SEC charged Bernd Regdantz, the chief financial officer of Siemens Business Services from February 2002 to 2004.

Regdantz, without admitting or denying the allegations, settled the SEC’s charges by agreeing to the entry of a judgment that permanently bars him from future violations, the commission said in its release. He also agreed to pay an administrative fine of €30,000 (about \$40,000) ordered by German officials. He was not charged by DOJ.

Breuer told reporters that the indictment’s allegations “reflect a stunning level of deception and corruption.” The defendants, who are foreign nationals based in Argentina, Germany, and Switzerland, are not currently in U.S. custody, he said.

Robert Khuzami, director of the SEC’s Enforcement Division, similarly told reporters that “there were few lines these executives were not willing to cross to win and maintain” the Argentine contract.

Bribes Allegedly Piled Up

According to the SEC and DOJ, the defendants first paid bribes to secure the \$1 billion contract. After the contract was canceled due to a change in the Argentine administration, the defendants again allegedly bribed high-ranking government officials to get the contract reinstated. Subsequently, when Siemens sought to enforce the contract against the

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PREVENTION OF CORPORATE LIABILITY

BNA’s Prevention of Corporate Liability (ISSN 1067-6104) is published monthly in conjunction with the *BNA/ACCA Compliance Manual: Prevention of Corporate Liability* by The Bureau of National Affairs, Inc., 1801 S Bell St, Arlington, VA 22202-4501. Correspondence regarding editorial content should be directed to the managing editor.

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Republic of Argentina through an arbitration action in Washington, D.C., the executives allegedly paid more bribes to ensure Argentine officials did not testify that the contract had been secured through bribes and corruption, the agencies said.

Although much of the alleged misconduct occurred overseas, Breuer stressed that the United States has “ample” grounds on which to assert jurisdiction, including the \$25 million that was funneled through U.S. banks and the meetings that the defendants held in the United States as part of the conspiracy. Moreover, the arbitration proceeding that allegedly resulted in more bribery was held in the United States, he said.

Jurisdiction Issues May Arise

Breuer said it “remains to be seen” what complications can arise from DOJ’s bid to prosecute the foreign defendants. “It’s hard to predict,” he said. “We’ve had tremendous cooperation” with our overseas counterparts, and “we’ll just have to work together to see what happens.”

In this respect, Khuzami said Siemens’s cooperation becomes even more critical. The company’s “assistance in facilitating the collection of evidence and other matters will be of great benefit to the successful prosecution of the individuals,” he said.

Nicholas M. De Feis, of De Feis O’Connell & Rose PC, New York, told BNA that his client Regendantz “has acted honorably and in the best interests of Siemens at all points in this investigation.”

“He is pleased to resolve the SEC matter on the stated terms and we do not expect that he will be charged criminally,” De Feis said in an e-mail.

BY YIN WILCZEK
AND PEGGY AULINO

The SEC’s press release is at <http://www.sec.gov/news/press/2011/2011-263.htm>. DOJ’s press release is at <http://www.justice.gov/opa/pr/2011/December/11-atj-1626.html>

Social Media

Experts Urge Businesses To Address Online Comments

Employers have shifted from “being skeptical about social media to embracing social media,” but they may not be entirely aware of the legal issues surrounding employee usage

of the technology, and should adopt guidelines covering it, an attorney said during a Nov. 15 BNA webinar.

Christine E. Lyon, a partner with Morrison & Foerster, Palo Alto, Calif., and Miriam H. Wugmeister, a partner in the firm’s New York City office, co-hosted the webinar, titled *Managing the Social Workforce: Employee Privacy and Social Media*.

Employee social media use poses risks such as the disclosure of confidential or trade secret information and damage to the company’s reputation, Lyon said.

Technology, Labor Laws Apply

Even so, there are limits to monitoring employee social media use, the speakers said. For example, under the Stored Communications Act, an employer cannot access an employee’s social networking account without prior express authorization from the employee, Lyon said.

The National Labor Relations Act also can protect some social media postings, such as those that discuss conditions of employment. Even a comment that seems unprofessional or negative may be protected, Lyon said.

Wugmeister cautioned employers about using information concerning an employee’s off-duty conduct for an unlawful discriminatory purpose. On the other hand, employers may have an affirmative duty to act upon off-duty social media information if they learn of unlawful harassment or discrimination, she said. She called it an area where “technology is way ahead of the law.”

Consider These Rules

Lyon identified the following guidelines for employee social media use that companies should customize to their own needs:

- “Do not divulge nonpublic information; protect confidential information.”
- “Use privacy settings . . . but don’t assume they will shield your comments from becoming public.”
- “Be respectful of others; refrain from posting harassing or disparaging comments about the company, your colleagues, or competitors.”

Wugmeister further recommended that employee confidentiality agreements address social media use and cautioned companies against “roll[ing] out globally” their U.S. social media policies.

Lyon noted that the Federal Trade Commission’s “Guides Concerning the Use of Endorsements and Testimonials in Advertising” require employees to disclose “material connections” with their employer.

When an employee is endorsing the company or one of its products on a social networking website, he or she should at least disclose that connection in his or her website profile, Lyon said.

Employees can make clear they are speaking on their own behalf by writing in the first person and including a disclaimer that the views they express are their own, she said.

Laws Are Evolving

Lyon recommended that employer social media guidelines include instructions to employees to:

- “identify yourself as a company employee when posting about the company or its products or services”; and
- “make it clear you speak for yourself, not the company.”

Lyon said employers should have several sets of guidelines, one for the majority of employees, another for employees that post on the company’s behalf, and a separate set if a company has its own social media platform.

Employers should update these guidelines periodically because “the law is evolving over time and practices evolve,” Lyon said.

BY KATIE W. JOHNSON

Securities Enforcement

Khuzami Defends SEC’s Use Of Deals Without Admissions

In a strong defense of the Securities and Exchange Commission’s settlement policy, Enforcement Director Robert Khuzami Dec. 1 said it would not be in the public interest for the commission to hold out against otherwise favorable agreements in order to obtain admissions of wrongdoing.

“A settlement conserves our resources and allows us to redirect them in productive ways,” Khuzami said. “Given the chance to reach a favorable settlement with at least some of the parties, and the opportunity to focus the SEC staff on the next fraud where victims need our help, I would not necessarily assume the risk of a

lengthy trial simply to get an admission.”

Citigroup Case Stirs Debate

Khuzami made his remarks at a conference organized in Washington, D.C., by the Consumer Federation of America. He was responding to recent criticism by Judge Jed S. Rakoff of the U.S. District Court for the Southern District of New York. Rakoff refused to approve a proposed \$285 million settlement between the SEC and Citigroup Global Markets Inc. over allegations that the firm misrepresented its role for a collateralized debt obligation.

In a Nov. 28 decision, Rakoff stated that the commission’s long-time practice of allowing settling defendants to neither admit nor deny the allegations would require a court “to impose substantial injunctive relief, enforced by the Court’s own contempt power, on the basis of allegations unsupported by any proven or acknowledged facts whatsoever.”

Such consent judgments are “neither reasonable, nor fair, nor adequate, nor in the public interest,” Rakoff said.

Settlements Called Crucial

Settlements are a critical enforcement tool for the SEC, which settles the overwhelming majority—around 95 percent—of its actions, according to statistics previously provided to BNA by NERA Economic Consulting.

During his speech, Khuzami stressed that the SEC only agrees to settlements that reflect staff’s best judgment of what the commission can recover at trial, “with consideration given to the risk of loss or lesser sanctions.” The “practical reality” is that most companies would refuse to settle with the SEC if they are required to admit to misconduct, for fear of exposure to shareholder and derivative private litigation, he said.

To reject reasonable settlements because of an absence of an admission is, “in my view, often unwise policy,” Khuzami said.

At another conference, on Dec. 6, Khuzami asserted that the average person understands that a settlement carries a clear message that the law was broken.

“Frankly, in my view, there’s not a lot of confusion that when companies write the \$285 million check, and we set forth very specific allegations in a complaint about what occurred, and they agree to adopt the business re-

forms, and we charge the responsible individuals in a separate action, and a company issues a press statement saying they hope to do better in the future, I don’t think there’s a lot of ambiguity that a violation of law has occurred despite . . . not requiring an admission under the no admit, no deny policy,” Khuzami said at a conference of the American Institute of Certified Public Accountants.

Speaking to reporters after his Dec. 1 address, Khuzami declined to say how the commission will proceed with regard to the Citigroup deal. Rakoff set the matter for trial beginning July 16. Khuzami also declined to say whether the SEC intends any changes to its settlement practices, including the neither-admit-nor-deny language.

“I would not necessarily assume the risk of a lengthy trial simply to get an admission.”

ROBERT KHUZAMI
SECURITIES AND EXCHANGE
COMMISSION

The SEC filed a record 735 cases in fiscal year 2011, the vast majority of which were settlements and the overwhelming majority of which were approved by the court as submitted, Khuzami told reporters. However, he said, “We listen to all commentary and constantly reconsider and re-evaluate . . . our approaches to cases and will continue to do that in the future.”

Authority Is Limited

In his formal remarks, Khuzami also said that commentators have expressed frustration with what they see as the low penalties recovered by the SEC.

The reality is that the agency is “strictly limited by statute” as to how much it can seek in civil actions, he said. Among other limitations, the SEC does not have the authority to recover investor losses resulting from a violation.

Khuzami observed that SEC Chair Mary Schapiro has asked legislators to give the commission more authority to seek higher penalties and to act against recidivist securities law violators. (See related story.)

“We believe that increased penalty authority would help us deliver a

tougher message of deterrence in situations where there is a disconnect between the harm caused by a defendant and the amount of penalty we can obtain,” Khuzami said. “With this authority we would be able to return not just a portion of investors’ losses but, where appropriate and when they are recoverable, all investor losses.”

As to recidivists, Khuzami said that when an individual or firm breaches an injunction that bars it from violating the law, the SEC’s civil contempt authority only allows it to move for a court order to stop ongoing misconduct. However, in the vast majority of the commission’s cases, “there is no ongoing misconduct to ‘stop,’ and thus no basis for civil contempt,” he said.

Return on Investment Touted

“To make sure we have a broad range of tools to address each situation, Chairman Schapiro also has asked Congress to give the Commission the authority to seek enhanced penalties against a party who violates a prior court injunction, separate and apart from any penalty we may seek for the underlying violation,” Khuzami continued. “In this way, there is an added punishment for repeating an offense.”

In other comments, Khuzami said the SEC continues to be hampered by budget shortfalls. He told the audience that in the last two years, the agency has “more than earned its budget,” having obtained court orders totaling \$5.6 billion in penalties and disgorgements and returned \$3.6 billion to harmed investors. The SEC’s total appropriations for 2010 and 2011 were about \$2.3 billion.

“Very few companies can claim to deliver the return on investment that the SEC is delivering,” he said.

Khuzami said he spoke his own views and not necessarily for the commission or its staff.

Text of Khuzami’s speech is at <http://www.sec.gov/news/speech/2011/spch120111rk.htm>.

Codes of Conduct

Think Tank’s Database Offers Hundreds of Codes of Conduct

A Texas attorney has gathered 489 publicly available corporate codes of conduct, and they are now searchable through the website of the Ethi-

sphere Institute, a compliance and ethics think tank.

The attorney, Ryan McConnell, told BNA the database can be a good resource for companies that are updating compliance programs. McConnell is a partner at Haynes and Boone LLP, Houston, specializing in corporate compliance and white collar defense. He is a former federal prosecutor.

McConnell said he was inspired to compile the codes from his experience speaking to compliance and ethics professionals at conferences. He described how, as a prosecutor, he was often asked by attendees for feedback on specific items in their codes. They might want to know if their company had adequate limits in place on the value of gifts employees could accept from contractors or vendors, for instance. When McConnell responded that he was prohibited from giving an opinion, he was usually asked, "What are other companies doing?"

That's when this idea hit him, he said: "Wouldn't it be great for companies to have a database where they could go see . . . what their peer companies were doing with respect to certain areas?"

With the help of an associate and a law student, McConnell set out to gather codes of conduct from every Fortune 500 company. They came up with the list of 489 because 11 of the companies do not offer public access to their codes.

Ethisphere calls the free web page its "Code of Conduct Dataset." It allows users to search for codes by industry and by risk area, such as anti-trust, insider trading, and money laundering.

Help With New Laws

The U.S. Sentencing Guidelines for organizations spell out seven steps corporations should take to ensure that their compliance and ethics programs are effective. Compliance and ethics professionals often use those steps as a template for designing programs that will keep businesses out of trouble. One step calls for periodic assessment of the strength of the program. To that end, compliance and ethics professionals "are really interested in how their peer companies are addressing risk," McConnell said.

Many companies do those reassessments annually, and McConnell said this year has brought some new challenges. "We found . . . that a lot

of companies were in the process of trying to figure out how regulations and laws that have been passed this year . . . impacted their code of conduct and impacted their compliance program," he said, citing the Dodd-Frank Wall Street Reform and Consumer Protection Act and the U.K. Bribery Act. The database is "a good resource for them to see what companies were doing in view of these new regulations," McConnell said.

BY PEGGY AULINO

The Ethisphere Code of Conduct Dataset is at <http://ethisphere.com/code-dataset>.

Whistleblowers

Wrongdoing Is Now Riskier, Enforcement Chief Tells CPAs

Public companies and their officials that engage in misconduct face greater risks than in the past, in part because of the Securities and Exchange Commission's cooperation initiative and its whistleblower program, SEC enforcement chief Robert Khuzami told a conference of the American Institute of Certified Public Accountants Dec. 6.

Khuzami said the agency has received 25,000 to 30,000 items of information under the program.

"To be blunt, the risks of wrongdoing have increased."

ROBERT KHUZAMI
SECURITIES AND EXCHANGE
COMMISSION

Almost two years ago, the SEC began its cooperation initiative modeled on prosecutorial tools used to encourage defendants to provide regulators with useful information. In May, the commission adopted rules to implement a whistleblower bounty program under which informants in certain cases can receive from 10 percent to 30 percent of monetary penalties obtained by the SEC. (See 6/20/11 Prev. Corp. Liability 61.)

Audit Committees Must Be Vigilant

"To be blunt, the risks of wrongdoing have increased," he said.

Moreover, information received by the commission after the start of the

whistleblower bounty program is of higher quality than that provided previously, Khuzami said.

The prediction that the program would lead to a flood of submissions "in fact, really hasn't proved to be the case," Khuzami said. Such tips and submissions are "an important source of information," Khuzami stated.

In other comments, Khuzami reminded his audience that audit committee members have duties to watch for potential malfeasance that, if carried out, could attract the SEC's attention. He warned against audit committees displaying "willful blindness to red flags."

For example, Khuzami described actions brought against outside directors at a Florida military body-armor maker formerly known as DHB Industries. In November, three outside directors of the firm agreed to pay more than \$1.6 million in disgorgement and penalties to settle charges over their alleged roles in an accounting scheme at the company.

The three directors did so without admitting or denying wrongdoing.

BY STEVE BURKHOLDER

Internal Controls

EU Auditor Proposal Addresses Conflicts

Insistent that cozy relationships between auditors and companies contributed significantly to the financial crisis that erupted in 2008, the European Commission Nov. 30 proposed sweeping reforms for auditors that would dramatically reshape the industry if approved by European Union member states and the European Parliament.

While the EU executive body was forced to drop a plan to force joint audits by listed companies, the proposal—which includes both a regulation and a directive—does include a "conflict-of-interest" provision that would prohibit audit firms from offering both accounting and non-audit services to the same company. As for the Big Four, the proposal would oblige them to separate their audit activities from non-audit services to ensure no conflicts of interest.

In addition, the plan calls for a mandatory rotation of audit firms, mandatory tendering of contracts, and a European supervisor of the au-

dit sector. In addition, the plan would establish an EU-wide scheme that would allow auditors to work in all 27 EU member states and establish the use of international auditing standards in the EU.

“Investor confidence in audits has been shaken by the crisis and I believe changes in this sector are necessary,” said Internal Market Commissioner Michel Barnier. “We need to restore confidence in the financial statements of companies. Today’s proposals address the current weaknesses in the EU audit market by eliminating conflicts of interest, ensuring independence and robust supervision and by facilitating more diversity in what is an overly concentrated market, especially in the top end.”

The European Commission has made no secret of its desire to loosen the hold that the Big Four have in the EU when it comes to reviewing the financial statements of listed companies. (See 10/17/11 Prev. Corp. Liability 124.)

It planned to require joint audits where a company would need two different auditors as one way to stimulate more competition in the industry, but a fierce lobbying campaign from the Big Four and opposition from some member states forced that scheme to be dropped. The proposal now gives member states the option to require joint audits.

Despite the setback on the joint auditing provision, the EU executive body is hopeful that the conflict-of-interest provisions in the proposal will go a long way in reducing the 85 percent market share held by the Big Four in the EU. Based on the terms of the proposal, audit firms will be prohibited from providing non-audit services such as tax advice and others consultations to their audit clients.

Reactions Differ

The proposal has triggered intense criticism from both large and small audit firms.

The European Federation of European Accountants insisted that the commission proposals would “severely damage” the quality of audits and would lead to less competition. It said the mandatory six-year rotation required of companies would “severely restrict the auditor’s knowledge of the entity being audited and reduce the value of the audit, increasing risks and disruptions.”

Speaking on behalf of large audit firms in Belgium, including the Big Four, as well as smaller ones, Belgian Institute of Regulated Auditors said the conflict-of-interest provision in the European Commission would have the opposite effect than intended, as it would drive smaller audit firms out of the business.

“The fact is that many smaller audit firms have built their business model on providing both audit and non-audit services,” said David Szafaran, the secretary general of the Belgian IRA. “This proposal would force many of them to give up the auditing services and concentrate on non-audit activities, as that is where many of them make more revenue. Both the Big Four and medium-size audit firms working in Belgium are in agreement on this.”

“We need to restore confidence in the financial statements of companies.”

MICHEL BARNIER
EUROPEAN COMMISSION

The reaction from other mid-size companies offering audit services was different, as they expressed disappointment that the proposal had been “watered down.”

“It is extremely unfortunate that certain parts of the draft proposal relating to the reform of the market structure, including joint audit and other measures that would strengthen the independence of the auditor, have been removed or watered down,” said Martin van Roekel, chief executive of the medium-sized auditing firm BDO. “The dilution of these important proposals before they have been democratically and publicly debated simply serves to maintain the status quo and does not serve the public interest well.”

The lobbying over the proposal now moves to the European Council of Ministers and to the European Parliament, both of which must agree on the terms of the legislation before it will become law. The legislative process is expected to take at least a year.

BY JOE KIRWIN

Text of the European Commission proposal, which includes both a regulation and a directive, is at

http://ec.europa.eu/internal_market/auditing/docs/reform/COM_2011_779_en.pdf and http://ec.europa.eu/internal_market/auditing/docs/reform/COM_2011_778_en.pdf.

Sentencing Guidelines

Ethics Group Wants Feedback On Review of Guidelines at 20

The Ethics Resource Center is seeking feedback on a draft report that examines the “impact and relevance” of the U.S. Sentencing Guidelines for organizations and offers suggestions for improvement.

The guidelines, which took effect 20 years ago, take a carrot-and-stick approach aimed at converting companies “from passive bystanders who hoped employees would behave well, into active advocates of an ethical culture in the workplace—in short, to enlist companies themselves in the fight against corporate crime,” according to the report’s executive summary.

Chapter 8 of the guidelines, which addresses wrongdoing by organizations, identifies seven steps that businesses should take if they want their ethics and compliance programs to be considered “effective.” Having an effective program helps a corporate defendant achieve a lower sentencing guidelines score, which can lessen the punishment if the entity is convicted of a crime.

The report, which runs about 100 pages, credits the guidelines with leading to “vigorous efforts by many U.S. companies and other organizations to adopt comprehensive compliance/ethics programs.” It also identifies “four specific challenges” that could “erode the effectiveness” of the guidelines and cause some businesses “to reduce their commitment” to compliance and ethics. The challenges, and some of the corresponding recommendations, are listed below.

Issue 1: Feedback

The first challenge addresses the fact that cases against corporations seldom reach the sentencing stage. “Corporate offenders are not receiving credit for effective compliance/ethics programs at sentencing because cases are being steered out of the traditional criminal justice process,” the executive summary says.

Rather than risk a trial, corporations often enter into deferred-

prosecution or nonprosecution agreements with federal prosecutors. That eliminates the need for judges to calculate the sentencing guidelines range, which leaves the company in the dark as to whether its compliance and ethics program is considered effective in the eyes of the court.

Department of Justice attorneys are supposed to evaluate compliance programs while making charging and plea bargaining decisions. "But there is little hard evidence that organizations are receiving the promised consideration for their compliance programs and prosecutors rarely point to compliance/ethics programs when publicly discussing case resolutions," according to the ERC report.

The report offers five recommendations for DOJ. They include: adopting the sentencing guidelines standards as the basis for evaluating compliance and ethics programs; promoting "greater internal consistency" about how compliance and ethics efforts are treated; and communicating broadly how prosecutors assess such programs when evaluating cases.

Issue 2: Agency Inconsistency

Government agencies are taking inconsistent approaches toward ethics and compliance programs, the report says.

"More than 20 federal agencies play a role in enforcing laws that govern corporate conduct, but each agency—and even divisions within agencies—has its own approach to corporate compliance/ethics programs," the report says. "This lack of consistency is compounded by a lack of transparency."

The report recommends that the president direct all federal enforcement agencies to "establish and publish clear policies" regarding how they recognize compliance and ethics efforts.

Issue 3: Emphasis and Clarity

Some parts of the guidelines are "underemphasized or unclear," which makes some corporate programs "fall short of their potential," according to the report. The guidelines "would benefit from ongoing review and a greater use of 'plain English,'" the report says.

It recommends that the U.S. Sentencing Commission "do what the Guidelines ask of companies: continuously improve." To that end, it identifies three steps the commission

could take to improve the guidelines: "more strongly encourage" organizations to use ethical performance as a basis for employee evaluations and reviews; put new emphasis on language in the guidelines that requires managers "to promote an organizational culture of compliance and ethical performance"; and encourage companies to address cultural differences in their locations worldwide.

Issue 4: Lack of Passion

Business leaders who are "genuinely passionate about ethical performance . . . are the exception," the report says. "Too many companies are still content with meeting minimum standards and too many compliance/ethics professionals must constantly fight for the resources required to build strong compliance/ethics programs."

To address this concern, the report recommends that business leaders "demand compliance/ethics programs that go beyond mere compliance" and "focus on the broad goal of building a strong ethical culture."

The ERC, a nonprofit organization based in Arlington, Va., convened an advisory group to evaluate the guidelines. The group of about 20 experts includes judges, attorneys, compliance professionals, and college professors.

The ERC is accepting comments on the draft until Jan. 6 and plans to send the final report to Congress, the Sentencing Commission, DOJ, and other enforcement agencies.

The report, "The Federal Sentencing Guidelines for Organizations at Twenty Years: A Call to Action for More Effective Promotion and Recognition of Effective Compliance and Ethics Programs," is at <http://www.ethics.org/fsgo>.

Compliance

OECD Offers Russia List of Needed Reforms

Public corruption and other obstacles to real competition stand in the way of Russia's goal of joining the ranks of the most advanced market economies, the Organization for Economic Cooperation and Development reported Dec. 12, outlining a list of needed reforms.

The "OECD 2011 Economic Survey of the Russian Federation" notes

that Prime Minister Vladimir Putin has said the country wants to become one of the world's top five economies within a decade.

The 156-page report comes as Russia is poised to enter the World Trade Organization in early 2012, a key prerequisite to the more exclusive prize of OECD membership, which the country has said it also wants to achieve soon.

Goals Called 'Doable'

The Paris-based OECD, whose 34 member countries include the world's advanced economies, said Russia's goals are ambitious but doable, and it cited several recent steps the country has taken to try to modernize its economy.

However, OECD said that, despite these efforts, Russia's business climate remains clouded, among other things, by public graft and product market regulations that hinder competition. "This is holding Russia back from being the modern diversified economy that it aspires to be," it said.

The organization urged the country to use the OECD accession process to reform areas of its economy where it still significantly lags OECD standards.

The report said Russia is growing at a trend rate of about 4 percent, but the country has not fully tapped assets that include vast natural resources, a skilled workforce and relatively flexible labor rules, a large national market, and very low public debt.

Overreliance on oil revenues, low productivity, high inflation and high inequality, and poor environmental performance are among problems delaying full recovery from the severe 2008/9 recession, it said.

But the biggest problem is that Russia's business climate is a "glaring and persistent handicap" that weakens competition, slows financial development, and saps foreign investment and trade, OECD said.

For example, Russia has some of the world's most restrictive product market regulations, and state involvement in the economy is higher than in any OECD country. The report cites a 2010 World Bank finding that Russian managers spent 22 percent of their time dealing with government regulation, higher than all but one country in Eastern Europe and Central Asia.

OECD urged the country to enact reforms to eliminate legal barriers to

competition and to reduce administrative burdens for companies.

Corruption Addressed

OECD noted that Russia has recently implemented administrative measures to clamp down on public bribery and improve the investment climate. In November, Russia's parliament amended the country's anti-money laundering law and its anti-corruption laws to require financial disclosure, as part of its effort to join the WTO and OECD.

At OECD's ministerial council in May, Russia signed OECD's 1997 Anti-Bribery Convention, opening the way for it to join the organization's Working Group on Bribery. (See 6/20/11 Prev. Corp. Liability 72.) When Russia first announced new anti-corruption measures, the U.S. ambassador to the OECD, Karen Kornbluh, called them a "big step" for improving competition in the country.

But Kornbluh said OECD membership is likely to take significantly longer. Other observers cite continuing problems with corruption in Russia. The country ranked 152nd out of 178 countries on the recent Corruption Perceptions Index by Transparency International, which called Russia the most corrupt country in Europe.

The OECD survey said that "Now, as in Soviet times, the use of blat [bribes] arises in large part from defects in the system that make it necessary to break rules in order to do business without undue difficulty," it said.

BY RICK MITCHELL

The survey is available at: http://www.oecd.org/document/13/0,3746,en_2649_33733_49101325_1_1_1_1,00.html.

Corporate Governance

Proposal in Brazil Takes on Corruption

With Brazil's Congress discussing the country's first corporate compliance law, representatives of Brazilian and foreign companies released their suggestions in November for a measure that would hold companies responsible for acts of corruption.

The list of 14 proposals was drawn up by the Brazilian Institute of Busi-

ness Law, which is made up of lawyers who represent Brazilian and multinational firms. The institute's suggestions were prepared by a team of 20 attorneys, eight of them from foreign firms, and were sent to the lower house of the National Congress of Brazil as well as the government's controller general's office.

The main proposal was that the legislation include clear rules to provide benefits to companies that invest in compliance programs and that cooperate in corruption investigations. These benefits would involve the reduction or elimination of sanctions that might be applied to companies, according to the proposal.

"For the battle against corruption to be effective, there must be a change of mentality."

BRUNO MAEDA
TRENCH, ROSSI, AND WATANABE

The bill as it now stands would allow the government to apply fines of between 1 percent and 30 percent of a company's annual gross revenues should it be found to have been involved in an act of corruption. In addition, the government could intervene in a company, suspend its operations temporarily, or terminate them permanently.

The team of attorneys who drew up the proposals for the business community objected to the absence of incentives for companies to cooperate in corruption investigations or to create compliance programs. The text of the bill states only that the existence of a compliance program would be taken into consideration should a company be accused of corruption and face sanctions.

The attorneys representing the business community said this is insufficient and that the benefits should be spelled out clearly. That would motivate firms to establish effective compliance programs, they said.

"In reality, only if the benefits for the companies are clear will they be stimulated to create programs," said the text of the document prepared by the Institute of Business Law.

New Mindset Needed

"For the battle against corruption to be effective, there must be a change of mentality," said Bruno

Maeda of the law firm Trench, Rossi, and Watanabe, who was one of the 20 attorneys who prepared the proposals.

According to Maeda, the document also proposes leniency agreements in cases where companies cooperate with corruption investigations. At present, the bill states that a company's cooperation would be taken into consideration when determining sanctions but offers no option for bargaining. Maeda said that including this option would serve as an incentive for companies to approach authorities spontaneously, providing information that might not be available otherwise.

Special Agency Suggested

The business representatives also recommended that the government create a special agency to deal with acts of corruption. The agency would be part of the justice ministry and would have the authority to initiate investigations into alleged corruption. It would operate with special courts and prosecutors that would deal only with corruption cases, according to the proposal.

The corporate compliance bill is currently before a special lower house committee which has not set a date to vote on the proposal.

In its 2010 corruption perceptions index, Transparency International ranked Brazil 69th out of 178 countries. Brazil was ranked better than all of the South American countries with the exception of Chile and Uruguay.

TI said Brazil could do better but lacks a commitment to combat official corruption, especially at the state and regional levels where election fraud and influence peddling are common.

The ratings of countries are based on surveys among businessmen and analysts and measure the perception of corruption in politics and the public sector.

BY ED TAYLOR

Securities Enforcement

SEC Wants Higher Fines; Defense Bar Pans Proposal

Defense attorneys are up in arms against the Securities and Exchange Commission's recent request to Congress for the power to impose larger fines. The current penalty

structure is more than sufficient, they asserted.

They also said there is little likelihood that such legislation, if proposed, will pass in the current Congress.

SEC Chair Mary Schapiro Nov. 28 told Senate Banking Securities Subcommittee Chairman Jack Reed (D-R.I.) and ranking member Mike Crapo (R-Idaho) that the effectiveness of the SEC's enforcement program would be substantially enhanced if the agency could seek much higher fines.

Among other changes, Schapiro suggested that the per-violation cap for the most serious securities law breaches—tier three violations—be increased from \$150,000 per individual to \$1 million and from \$725,000 per entity to \$10 million.

Schapiro further recommended that the SEC be given the power to impose additional penalties for repeat offenders.

Penalties Already High, Critics Say

"Anyone who thinks that the SEC doesn't have enough penalty authority hasn't been on the wrong end of an enforcement action yet," said Mark Schonfeld, a partner in the New York office of Gibson, Dunn & Crutcher LLP.

Schonfeld, a former head of the SEC's New York Regional Office, observed that the commission, when it wants to, "has been successful at obtaining very large penalties against major financial institutions." He cited AIG's 2006 agreement to pay \$800 million to settle SEC accounting fraud allegations related to reinsurance transactions with General Reinsurance Corp.

The commission's penalty request "is a popular response to the criticism that the SEC lacks sufficient teeth," Schonfeld said.

Schapiro sent her letter to the lawmakers on the same day that Judge Jed S. Rakoff of the U.S. District Court for the Southern District of New York rejected as contrary to the public interest the proposed \$285 million settlement between Citigroup Global Markets Inc. and the SEC to settle misrepresentation allegations concerning a collateralized debt obligation.

Shareholders Are Real Victims

Larger fines would do little to prevent future fraud, said Thomas Gorman, a partner in the Washington, D.C., office of Dorsey & Whitney LLP. "The fact of the matter is that fines for large corporate players make good headlines and congressional testimony, but they do next to nothing to prevent a future violation," he said. "The only real parties hurt by those fines are the shareholders that the SEC is obligated to protect."

"Is the SEC going to now be in the business of bankrupting corporate America?"

MICHAEL LOWMAN
JENNER & BLOCK LLP

In practice, the statutory limits in SEC penalties do not restrain the agency in settlements, Gorman said. "Consider the size of the Goldman fine, for example. Likewise, those limitations had nothing to do with the relatively small fine sought in the Citigroup case," he said.

Among other criticisms, Rakoff faulted the SEC for proposing only a \$95 million fine for Citigroup, whereas it had imposed a \$535 million penalty against Goldman Sachs & Co. in a prior case, also involving a CDO.

It would be more beneficial for the enforcement program if the SEC were to focus on remedial measures tailored to the violations and to the business in question to safeguard against future misconduct, Gorman continued. "The SEC should revamp its entire approach to remedies to focus less on fines and headlines and more on future prevention—a point for which fines are ill-suited," he said.

Michael Lowman, a partner in Jenner & Block LLP, Washington, described the SEC's request for the authority to recover investor losses as "the most frightening." If granted, that would allow the agency to set penalties commensurate with the damages available in the class action context, which can run in the billions of dollars, he said.

"Is the SEC going to now be in the business of bankrupting corporate America?" Lowman asked. "Is it fair or logical to have a public company be subject to market impact damages in the class action context and then double up on that through an SEC penalty?"

Jeffrey Robertson, a partner in Schulte, Roth & Zabel LLP, Washington, also suggested that the request could be problematic. "The SEC's proposal to tie penalties to investor losses may prove unwieldy due to difficulties in measuring such losses," he said.

Congressional Approval Unlikely

In any event, the SEC's request for such a large jump in penalties probably will not be acceptable to lawmakers, the attorneys told BNA.

Schonfeld noted that every few years, Congress has passed legislation to increase the maximum penalties that the SEC can seek. Most recently, the Dodd-Frank Wall Street Reform and Consumer Protection Act's Section 929P increased the agency's per-violation cap for tier three penalties from \$100,000 to \$150,000 for individuals, and from \$500,000 to \$725,000 for entities, he said.

"The likelihood that Congress would adopt the dramatic increases in penalties that the SEC is now seeking would seem to be slim," he said.

Robertson said there are strong views by some in Congress that portions of the Dodd-Frank Act should be repealed. Against this backdrop, "legislative initiatives to increase the SEC's ability to impose larger penalties seem unlikely to succeed," he said.

The attorneys similarly questioned the necessity of the SEC's bid for additional authority against repeat offenders. Schonfeld described the request as a "red herring."

"In any highly regulated business, such as the securities industry, even the best institutions with top-shelf compliance programs will inevitably have run-ins with their regulator," Schonfeld told BNA. "This does not make them recidivists." The "true recidivists," i.e., repeat criminal offenders, will not be deterred by SEC financial penalties, he said.

BY YIN WILCZEK

(continued from page 152)

mean what you profess will quickly see through the charade of high-sounding words and shallow training initiatives.

There is no one formula for success and program strategy will vary depending on parent and subsidiary cultures, defined risks, risk territories, and the integrity of employees at all levels. Keep in mind that acquired subsidiaries may be financially integrated for revenue reporting purposes but not culturally aligned with the parent.

The initial inquiry is to determine exactly how serious senior management is about avoiding non-compliant activity. What does the code of conduct say and how has it been communicated to managers, employees and even stakeholders? What is the compliance officer's reporting relationship? That reporting structure provides insights into how serious a company is about compliance. To whom a compliance officer reports is dependent on many factors, such as the CO's seniority, management's confidence in the CO's judgment, and trust in the CO's uncompromising integrity. Nonetheless, if the position is several levels down from senior management, perhaps coupled with limited funding options, then the message "communicated" to company employees and managers is that the function and any resulting program are not a priority.

Strive for Direct Reporting

The first foundational element is a place at the table. When a chief executive officer has the compliance officer as a direct reporter, the non-written message to other key executives is, "The boss thinks our commitment to business integrity is important." It is a message worth sending. The reporting relationship now speaks volumes. When the CO designs and builds a compliance strategy, the activity is viewed as activity with the full support of the CEO.

Reporting relationships at other levels of the organization are less effective but not necessarily without impact, depending on the stated support for the CO's position and funding for its activities. A CO reporting directly to the organization's general counsel is acceptable but not as effective as reporting directly to the CEO. This is because it is the CEO's vision and leadership that is ultimately reflected in the communication of the

ethics and compliance program. The "tone at the top" is not filtered, and the communication plan is, in a true sense, "personal" to the CEO. Before you engage in a worldwide compliance effort, you need to have a well-defined mission statement, commitment from the top, and allocated resources to get the job done.

Access to key managers and board members enhances the program's effectiveness.

Once the reporting reality is embraced, the next foundational element is building relationships with management and the governing authority, the board of directors. Access to key managers and board members enhances the program's effectiveness. Understanding their personal vision of the company's integrity program will help shape the message. The CO can leverage the commitment and benefit from the guidance of experienced business executives who sit on the company's board or manage critical functions of the company. The nature and context of the program's message are impacted by these relationships.

The primary goal of the CO is to have the governing authority, in most cases the board of directors or a committee of the board, both knowledgeable and supportive of the CO's plans and activities as approved by the CEO. This relationship also meets a requirement expressed in the U.S. Sentencing Guidelines pertaining to business organizations.

At a minimum the CO will ensure the board is fully aware of:

- (1) the creation, review, approval, and funding of the compliance plan;
- (2) the development of compliance policies and procedures; and
- (3) the process for assessment, an annual review, and approval of the compliance plan.

The CO's relationship with the board is never intrusive. There is a reporting relationship, but it is through the authority of the CO's superior and does not get mired in unnecessary details taking unwarranted time from board members. However, it should be understood that the CO is to have unfiltered access to the board when

and if a situation develops that requires such access.

Engaging with key employees and managers throughout the world in frank and direct talks about their commitment to the program should be a consideration. An effective CO has to get into the field, meet key managers and employees, and listen to what they have to say about the compliance risks associated with their respective departments and organizations. The CO's open and receptive attitude to the concerns, suggestions, and needs of the organization's managers and key employees are valuable in building and communicating your program. The effort is one of active listening at all levels of the organization. An important message to all managers is that company business leaders must own the program with the CO providing appropriate tools, resources, and support.

The CO's partnering with the company's internal audit function will add efficiencies to the company's compliance program. The internal audit function is about compliance, and it is critical to proper oversight of the company's financial reporting integrity and control policies. The CO can bring new insights to the function and be instrumental when considering the scope and depth of planned audits. A CO should be aware of the schedule of internal audits, the proposed audit plan, and the personnel conducting the audits to maximize the effectiveness of the company compliance program. A team approach to compliance is appropriate and turf issues are counterproductive. Working together, the CO and head of internal audit can develop and provide forensic training to audit personnel, focusing on the red flags of commercial bribery and other non-compliant activity.

Study Applicable Laws

Once the fundamentals are in place, it is time to consider the communication challenges. First, inventory and read all company publications referencing compliance with laws, regulations, and company policies. Include the CEO's speeches in public forums referencing business integrity, ethics, and compliance. These publications communicate the compliance culture of the company. Much of this material may already be incorporated in the company's code of conduct.

The company code of conduct is a key document with its guiding prin-

principles and the “do’s and don’ts” of employee conduct. A common practice is to distribute the code to all managers and employees each year, evidenced by signed acknowledgments of receipt. Thoughtful use of electronic means of distribution of the code of conduct will save time and money.

Use Good Translators

Since the code of conduct is the baseline document for a compliance program, multinational companies need relevant translations of the code and other compliance documents for their non-English speaking employees. Many countries require that in order for employee policy communications to be enforceable, they must be written in the local language. Approval notifications to labor authorities and works councils as well as local regulations regarding disciplinary sanctions may require employee policy communications to be in the language of the country where the business is located.

It is imperative that the compliance officer is knowledgeable about the laws and regulations impacting business activities at all company locations, including those that impact supply-chain activity. Translation services may be required in order for the CO to study and fully understand the

regulatory environment in the countries where company businesses are situated. Teaming with managers in various countries to ensure a thorough understanding of relevant laws and regulations will enhance the quality of the translated documents. Company instruction on ethics and compliance can then be supplemented to embrace local concerns.

Next, every opportunity to promote the company’s CEO as the organization’s ethics leader should be implemented. In every CEO communication to employees, a suitable expression of his or her expectation for the ethical conduct of company managers and personnel in the discharge of their respective duties is pure “tone at the top” and should not be overlooked. The CEO leads by example. The CEO’s messages promoting business integrity may be incorporated in messages from other managers who profess their commitment to business integrity.

Encouraging managers to routinely demonstrate support of the company’s ethics and compliance guidelines at functional business gatherings and working with the compliance officer by scheduling compliance training within their business units are signs of a healthy compliance program. The CO is a guide and a resource to the business manager. Assisting the business manager

with monitoring and risk analysis in support of the manager’s business goals keeps both the CO involved and the business manager committed in ensuring an effective program.

Integrity Equals Success

The compliance officer, without wanting the designation, could be viewed as the moral conscience of the organization—seeking to promote managers and employees to do the right thing and what “ought” to be done to maintain the ethical standards of the company. The successful CO will work effectively with each staff and management function in promoting compliance in all business and staff activities.

It is an immense responsibility and cannot be done without support from all company managers and employees, and importantly, the CEO. The success of a compliance program is not measured in dollars and cents. It is measured by employee awareness of the integrity goals of the organization; the employee sense of personal responsibility to maintain those goals; and a continuous effort by the CO to avoid and eliminate risks to the organization’s reputational standing, product brands, and trust in the business leadership team. It is a demanding job, but a job worth doing and worth doing well.

Journal

Calendar

Ethics and Compliance: The Ethics & Compliance Officer Association presents its 2012 “Asia Symposium,” Jan. 17-18 in Shanghai. Information is at <http://www.theecoa.org>.

Compliance and Ethics: The Society of Corporate Compliance and Ethics presents its “Basic Compliance Academy,” Jan. 30-Feb. 2 in San Francisco. Information is at <http://www.corporatecompliance.org>.

Ethics and Compliance: The University of California, Berkeley, Haas School of Business, Center for Executive

Education presents “Leading With Ethics and Compliance,” Feb. 13-15. Information is at <http://executive.berkeley.edu/programs/leading-ethics-and-compliance>.

Bribery: Marcus Evans presents its “Canadian & Global Anti-Corruption Compliance Conference,” Feb. 27-29 in Toronto. Information is at <http://www.marcusevans.com>.

Focus

Compliance Programs

Communication Is Key to Successful Compliance Efforts

BY WILLIAM A. WISE

Accurate and timely warnings of severe weather can lessen the risks of harm to people and property. Communicating those warnings requires continuous diligence and use of appropriate media. Displaying elaborate charts, tracking a storm with news video, and providing other information are of limited value if trust in those communicating the risks is missing. The message is effective when there is trust in the messenger.

Ethical and compliance lapses in business organizations create storms of a different kind with varying degrees of damages to people and property. Such lapses may harm a stellar reputation, destroy a product brand, invite criminal and civil sanctions, and wash away trust in a business leadership team. Collateral damage to company stakeholders may be extensive.

Goal Is to Avoid Risk

The vigilance and focus associated with communicating the risks associated with approaching storms are also part of the effort in communicating a company's ethical and compliance message. The objective in one is to save lives and preserve property. The objective in the other is to avoid risks damaging a company's integrity and eroding trust in the company's business leaders. Communicating your compliance and ethics program requires continuous diligence, use of appropriate media, and trust in company messengers.

The focus of this article is to identify the foundational elements of an effective compliance program and

then to consider the communication challenges to "getting the word out" to all stakeholders. Success of a program depends on having in place solid fundamentals prior to communicating your program.

Before you engage in a worldwide compliance effort, you need to have a well-defined mission statement, commitment from the top, and allocated resources to get the job done.

The Wall Street Journal and other business media routinely provide news of government investigations of companies and their executives reportedly engaging in corrupt business activities. The United States is not alone in investigating business crimes. Recently enacted legislation in the United Kingdom provides extraterritorial reach of U.K. law to combat private (commercial) and public bribery by companies to obtain or retain business opportunities. Other nations are revising and adopting laws in their fight against corruption. In addition, the cooperation extended between enforcement authorities of different countries is increasing. An incident in the U.K. of commercial bribery may lead to a "coordinating" contact with an appropriate U.S. official, spurring fur-

ther inquiry about a company's sales practices in other parts of the world.

Recent U.S. investigations associated with the Foreign Corrupt Practices Act have produced fines in the hundreds of millions of dollars, which may motivate enforcement agencies to increase staff and investigative capabilities. Sophisticated enforcement techniques are emerging, as recently reported in the press.

The dramatic increase in enforcement activity, particularly with the FCPA, and the widespread implementation of compliance and ethics programs may suggest that companies are motivated and equipped to avoid risks associated with corrupt business activities. That's well and good, but many companies charged with corrupt activities have integrity programs and codes of conduct calling for compliance with law and ethical principles. What needs to change to make these programs effective?

No two people are identical, and no two companies, although similar in many respects, have identical cultures. The unique personalities, beliefs, and value systems embedded in a company's leadership are accounted when considering a company's success, or lack of success, in the market. Today most companies profess goals of compliance with laws and regulations pertinent to a company's business activity and mean it.

Consider Culture

Communicating your company's compliance program and ethics policy must be done with consideration of the company's culture. The goal of having an effective message resonating at all levels of the organization depends on the strength of a company's compliance culture. Having a program that appears broad and encompassing but lacks depth and management's belief in its purposes may be worse than not having a program at all. Government prosecutors who sense that you do not really

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William A. Wise is an attorney in Holland & Knight LLP's Boston office and the chief ethics officer of the Ethics and Compliance Officers Association. He wishes to acknowledge the support and insights of Keith Darcy, executive director of the ECOA, and Laurie Weberman Roussel, senior international counsel of Boston Scientific Corp., in their review of the final draft of this article.