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Third-party assessments of ethics: A proactive tool to demonstrate due diligence

- » It is difficult for companies or compliance professionals to assess their own program.
- » An assessment of an established E&C program by an independent entity can avoid bias or erroneous conclusions based on employee feedback.
- » The goal of a program assessment is to gain insight into the strengths of a company's corporate culture as benchmarked against those of similar companies.
- » A company's investment in a third-party assessment can become a significant asset and end up being its best defense.
- » Proactive evaluations help forward-thinking companies identify potential weaknesses or risks.

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An increasing number of federal and state regulatory enforcement actions against companies are requiring ethics and integrity reforms, along with fines and penalties, as part of the settlement or resolution. Such actions—which include deferred prosecution agreements (DPAs), non-prosecution agreements (NPAs), administrative agreements, consent decrees, and court-ordered settlements—all presuppose that the cited misconduct occurred due to an absence of effective controls, discipline, or corporate compliance. More importantly, many government actions specifically cite the absence of an effective ethics and compliance (E&C) program and controls, or weak corporate ethical culture, as the leading causal factors contributing to the

company's misconduct. Conversely, companies that can demonstrate a corporate commitment to ethics and compliance and present a strong defense that their misconduct is truly due to one or more "bad actors" (rather than a tainted culture) fare better in the enforcement actions. "Better" often means lower fines and penalties, as well as avoidance of the costs and inconvenience of hiring an independent monitor, if required by the government agreement or ordered by a court.

Much to their benefit and credit, many national and international corporations recognize that ethics and compliance is much more than a written set of rules and policies. Companies use E&C programs to communicate company mission statements, goals, and expectations; to encourage staff to share the same set of corporate values; and to drive their behaviour in day-to-day business activities. However, if a company is truly committed to an effective E&C program, establishing a written set of policies and controls is simply not enough to withstand scrutiny. Moreover, those companies that have established strong comprehensive E&C



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programs know that they are not static and can get stale without appropriate regular care and attention. E&C programs evolve as companies change, employees turn over, new laws and regulations are enacted, and compliance priorities evolve, depending on government agency enforcement objectives and the public discourse on ethics and integrity matters.

Third-party assessments has advantages

With so many factors to consider, how can a board of directors or senior corporate leadership ensure that the ethical culture they want to build is working and effectively driving employee behaviour? How can legal counsel help better prepare companies to be able to demonstrate their due diligence to government regulators or law enforcement if (or more likely, when) employee misconduct puts the company in the crosshairs of enforcement actions? To gain a better understanding of the effectiveness of corporate E&C efforts and to identify any gaps in one company's approach compared with the best practices of other companies, some legal counsels recommend that their clients engage specialized, third-party consultants to conduct an independent assessment of their ethical culture and E&C programs *before* a crisis occurs.

An independent third-party assessment of a corporate E&C program is a specialized evaluation of a business entity conducted by a team of experienced E&C professionals. Its purpose is to provide an unbiased evaluation of a company's corporate culture, assess its ethics and compliance policies and anti-corruption controls, determine whether employee training is having its intended effect, and assess whether the company is consistently and fairly enforcing its rules on ethics and integrity. An independent evaluation can help a forward-thinking

company to identify potential problem areas before violations occur, improve its ability to manage the risk of compliance or ethical violations, and demonstrate its due diligence to governmental regulatory authorities and stakeholders, if the inevitable violation occurs.

The question could be asked, why would legal counsel recommend that a company bring in an outsider to evaluate its E&C program? The answer is quite simple: It is very difficult for a compliance officer or committee to effectively self-evaluate their own program. There is a lack of objectivity in such an assessment (both real and as perceived by outside stakeholders and regulators), and often, corporate compliance officers lack a deep understanding of the best practices in the field or the ability to benchmark their program against those of other companies. Most importantly, if an enforcement action were to take place, the government is unlikely to attach much credibility to a compliance program or corporate culture evaluation conducted by the company itself.

Remove biases to increase honesty

An objective third-party assessment addresses such concerns. The outside perspective removes the biases and subjectivity that we all bring to our own work and office environment. We have found that when companies conduct self-assessments, their findings are often inaccurate or incomplete, because the information and feedback about their program on which they are relying comes from staff, through surveys and interviews, which can be less than forthright. We have found that staff are frequently uncomfortable about questioning the policies and practices of their employer.

Because the heart of E&C programs is the people they are intended to reach, even the very best programs should occasionally be checked to see if they are effectively

achieving their objectives. When such an assessment is undertaken, the company should be prepared for some degree of healthy, but sometimes negative, feedback. In addition, the company must be prepared to listen and take appropriate action to remediate any deficiencies that might surface from the assessment. A company's ability to demonstrate that it invested the time and effort to engage a third-party assessment, and that it implemented substantive changes as a result, could end up being its best defense if a future investigation and/or enforcement action targets the company.

It is human nature to look at the world with an optimistic bias. Business leaders often unconsciously assume that not knowing bad facts within their organization means that these facts do not exist. Leaders sometimes make the mistake of believing they cannot be held responsible for bad actions they never knew about; but *not* knowing is viewed as an offense in and of itself by many regulators.

Obtaining internally unbiased and useful information about the effectiveness of a company's compliance program and the strength of a corporate ethical culture can be challenging. Internal or external audits do not usually attempt a comprehensive review of a company's overall compliance infrastructure or ethical culture, because they are better suited to address specific programs, internal controls, or processes. Furthermore, the question remains as to how effective it is to ask the managers responsible for implementing the program to evaluate their own effectiveness or success. Finally, even if such a self-evaluation mechanism is established, getting honest answers from recalcitrant employees (who may have a deep-seated fear of retaliation in responding to questions about ethics and compliance) is difficult and can lead to skewed results.

Begin with an analysis

The scope of an independent assessment of a company's ethics and compliance posture will vary depending on multiple factors, including the type of industry and the nature of the regulatory environment; the size and geographic dispersion of the employee population; the risks associated with countries in which the company might be operating; and the organizational structure, authorities, and resources currently provided to the E&C program and its leaders. Any effective assessment typically begins with an analysis of the existing E&C program and the internal control process established to operationalize the program throughout the company. This high-level review evaluates the program for completeness in ensuring compliance with government regulations, in effectively training and communicating corporate policies, and in investigating and remediating reported instances of non-compliance or other misconduct within the organization. Other aspects of this type of review include:

- ▶ Assessing the effectiveness of the organizational structure and reporting lines for the Compliance function, including whether the E&C function has been provided the authority, independence, and adequate resources to succeed;
- ▶ Reviewing the adequacy and completeness of the company Code of Ethics and Business Conduct in setting the parameters for employee behaviour in the organization;
- ▶ Determining whether the company has established credible reporting mechanisms for employees to raise concerns and ask questions;
- ▶ Evaluating how well the company responds to allegations of suspicious or questionable activities within its

- ranks, including the adequacy and professionalism of internal investigations;
- ▶ Reviewing whether the company's ethics and compliance objectives are sufficiently aligned with the performance management systems that incentivize promotions, bonuses, and assignments; and
- ▶ Benchmarking all aspects of the company's program with those of similarly sized companies in like industries.

As the evaluation goes deeper, input is usually sought from senior leadership, mid-level managers, and working level staff. This part of the review will evaluate whether the program is actually effective by identifying and analyzing, from the staff's perspective, what impact the program is having on the organization and its employees. For example, do the employees understand the company's Code of Ethics and Business Conduct and related policies? Is the E&C training effective, or merely a "check the box" exercise? Are employees convinced of the important role they play in compliance? Do the company and their immediate managers place a high value on integrity, or do employees receive mixed messages from their managers and leaders? Have employees invested themselves in the success of the program and, if so, how? Do employees feel that the E&C program is fairly implemented throughout the company, regardless of rank or level of contribution?

This assessment approach allows the independent evaluator to learn about the effectiveness of the company training programs and the staff's awareness of any communication or whistleblower hotline channels available to them. The independent evaluator can assess staff-level comfort in raising issues and questions and whether staff input is taken seriously. In addition to a greater understanding of the ethical culture,

a third-party independent assessment can contribute to a more in-depth understanding of risk areas that staff on the ground might be observing throughout the company and attempting to manage, thereby contributing to a more robust enterprise risk management assessment, where perspectives may be limited in the top and middle management layers of the organization.

Collaboration is key

One of the most effective practices to insist upon when engaging a third-party assessment is a collaborative process between the evaluation team and the company at every stage, from developing a practical work plan to selecting staff for interviews and focus groups, and in soliciting input for the draft report. This approach ensures that the assessment is targeting those areas where the company has the greatest concerns, ethical risks, or just wants to learn more about the effectiveness of its E&C efforts. The assessment approach must also consider cultural differences that can develop in various business units and geographic locations of a single company, particularly in satellite field offices that are located a distance away from the corporate headquarters. Experience has demonstrated that attention to the internal differences in culture is fundamental to assessing the overall corporate commitment to ethics and compliance and understanding the impediments that might be preventing individual supervisors, managers, and business units from ensuring compliance in their day-to-day operations.

When companies conduct a self-assessment of their programs, they often rely on quantitative data gained from the frequency of whistleblower hotline calls, the number of staff trained, or the absence of a major compliance or ethics failure as an objective measure of success. Although

this data can contribute some necessary information, such measures can be misleading and incomplete. For example, is the fact that the company is not receiving a large number of whistleblower complaints evidence that the program is working, or might the staff be hesitant to report issues due to a fear of retaliation? Is the deployment of a computer-based ethics and compliance training module with 100% participation evidence that the training effectively familiarized the staff with their responsibilities, or might they be “pushing the button” with little comprehension to get the training completed in the shortest period of time possible? Without further insight, such data does not offer an understanding of the effectiveness of an E&C program and its impact on the workforce. An independent assessment offers a deeper, more realistic, and thorough view on whether the E&C program is helping the company manage its risk in the manner intended.

Once an E&C assessment is complete, the company is typically provided with detailed findings and conclusions drawn from the data collected. The assessment will also make recommendations to address any gaps that may exist in the program and strengthen the ethical culture. Some of the recommendations may be drawn from best practices observed during similar evaluations in other companies. In effect, the company is provided with a detailed road map for improvement.

Conclusion

Independent third-party assessments provide more than the assurance that the investment that the company has made in their E&C program has added value. The assessment itself, which involves staff at all

levels of the company, also functions as its own independent role in educating staff of the key elements of compliance and ethics that the company has established. In fact, just the process of conducting the assessment can send a strong message to the workforce on the company’s commitment to providing more than just words when it comes to ensuring that ethics and integrity are incorporated into the day-to-day business of the organization. This message can also resonate with outside stakeholders, government regulators, and enforcement agencies if a “bad actor” shines the spotlight on a company’s E&C commitments.

With an increasing government focus on the prosecution of corruption, fraud, and other improprieties, including the scrutiny placed on existing E&C programs, companies and their legal counsel are recognizing that it is better to invest in a program that can help manage the risks of E&C problems occurring and proactively discover matters that could be self-reported to government regulators. In this way, corporate budgets are targeted on areas that add value to the company, rather than hoping that the established program is sufficient and subsequently funding the increasingly high cost of litigation, fines, and penalties when it turns out to be less than robust and real.

The use of third-party independent assessments can be a valuable resource for companies. Effective use of this risk management tool is the next step in the evolution of the field of corporate ethics and compliance for forward-leaning companies committed to ensuring that their organizations act with integrity, follow pertinent laws and regulations, and maintain a commitment to excellence. *