



AUDITING COMPLIANCE & MEASURING EFFECTIVENESS

Joe Murphy, CCEP

JEMurphy@voicenet.com

**AUTHOR, 501 IDEAS FOR YOUR
COMPLIANCE AND ETHICS PROGRAM (SCCE;
2008)**

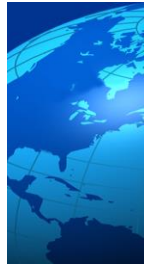
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Auditing under the USSGs

(5) The organization shall take reasonable steps—

(A) to ensure that the organization's compliance and ethics program is followed, including monitoring and auditing *to detect criminal conduct*;



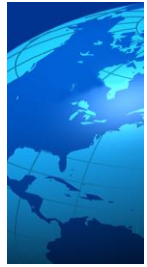
Compliance Audits

***WHAT'S GOING ON
OUT THERE?***



Factors to consider in compliance auditing

- **Conduct both “process” & “substantive” audits**
- **Utilize risk assessment to prioritize the substantive risks**
- **Review governmental, regulatory requirements/recommendations**
- **Determine audit frequency**



Factors to consider in compliance auditing

- **Determine methodology for each audit**
- **Does organization wish to attempt to protect the audit as privileged?**
- **Who should conduct the audit?**
- **Be sure management understands: this can be intrusive**



Who Does the Audit?

Lawyers?

Inside or outside?

Counselor or cop?

Others?

**C&E, internal audit, subject-matter
experts, HR**

Mixed teams?

Independence



Selecting Locations/targets

- **Risk factors**
- **What about the executives?**
- **Locations away from HQ**
- **Auditors' independent judgment in selecting**



Surprise! Guess who's here?

**Should you do unannounced
audits?**

What is meant by “auditing *to detect criminal conduct*”



At the Location

- **Explain purpose & scope to senior on-site manager**
- **Select employees to be reviewed**
- **Select files/computer records**
- **Walk the site**
- **Review docs, conduct interviews in secure site**



Types of Documents to Review – Antitrust Example

- **Expense vouchers, calendars, logs, meeting & trip reports, and status reports**
- **Files on competitors, suppliers who may also be competitors**
- **Trade associations/industry meeting files including handwritten notes**
- **“Top right hand desk drawer”**
- **E-mail and computer records**
- **Business plans**



Employee Interviews

- **Explain purpose**
- **Provide Upjohn or similar letter**
- **Don't be adversarial**
- **No notes by interviewee**



Scope of Employee Interviews

All levels, no exemptions

Some open-ended questions

Questions from documents

**Understanding of substantive rules &
compliance program**

What are supervisors' views

Closing questions



What Can You Expect to Find?

“I’ve been waiting for you to call”

- They won’t call, but they won’t lie either

It’s amazing what people write

- See DOJ’s lysine conspiracy video for examples
- Even conspiracies depend on records

People will talk - ask any reporter

- Learn at least as much as a WSJ reporter

Expect to be surprised



What Can You Expect to Find?

- **“LET’S BE PREDATORY ABOUT IT”**
- **“COMPETE – BUT NOT ON PRICE”**
- **ONE INTERNATIONAL CONSPIRACY HAD A PAID CONSPIRACY COORDINATOR!**



Enlist Internal Audit's Support

- **Auditors have a control orientation**
- **Include in internal audit's charter**
- **Train auditors on risk areas**
 - **Red Flags list**
- **Bring into the team at the beginning**
- **But get them not to practice law!**



Measuring Effectiveness

WHY MEASURE?

WHAT TO MEASURE?

HOW TO MEASURE?



Sentencing Guidelines item 5

(5) The organization shall take reasonable steps—

...

(B) to evaluate periodically the effectiveness of the organization's compliance and ethics program;



Why Evaluate the Program

EXTERNAL EXPECTATIONS

- THE GOVERNMENT EXPECTS IT
- PART OF PROGRAM STANDARDS

INTERNAL EXPECTATIONS

- MANAGEMENT EXPECTS RESULTS
- MEASUREMENT IS PART OF ANY MANAGEMENT PROGRAM



The Guidelines Question

**DOES THE COMPLIANCE &
ETHICS PROGRAM ACTUALLY
WORK?**



What to Measure

- **DESIGN**
- **IMPLEMENTATION**
- **IMPACT**



What to Measure

- **DESIGN**

**IF YOU DID EVERYTHING IN YOUR
PLAN, WOULD IT MEET THE
STANDARDS?**

REVIEW BY DESK AUDIT



Measuring Design

WHAT STANDARDS APPLY TO THE DESIGN?

USSGs 7+ ELEMENTS

U.S. ATTORNEYS' MANUAL

STOCK EXCHANGE REQUIREMENTS

GOVERNMENT MANDATES

“INDUSTRY PRACTICE”

BY RISK AREA

REGULATORY/ENFORCEMENT AGENCY

CASE LAW

BY JURISDICTION

U.S. STATES

OTHER COUNTRIES



What to Measure

- **IMPLEMENTATION**

**HAVE YOU ACTUALLY DONE
WHAT YOU SAID YOU WOULD DO?**

COUNTING WHAT IS THERE



What to Measure

- **IMPACT**

IS IT ACTUALLY WORKING

IN-DEPTH REVIEW, IN THE FIELD



The Kaplan Matrix

Measure:

- **EVERY RISK, in**
 - **EVERY BUSINESS UNIT, for**
 - **EVERY GUIDELINES ELEMENT**
-
- Kaplan, “Thinking Inside the Box: Risk Analysis in Three Dimensions” (ethikos, Sept./Oct. 2000);



The Kaplan Matrix – Every Risk

SOME EXAMPLES:

- **ANTITRUST**
- **GOVERNMENT CONTRACTS**
- **EEO/HARASSMENT**
- **PRODUCT SAFETY**
- **ENVIRONMENTAL**
- **BRIBERY/CORRUPTION**
- **CONFLICTS/GIFTS**
- **CONSUMER PROTECTION**
- **PRIVACY**
- **WAGE & HOUR**
- **SECURITIES FRAUD**



The Kaplan Matrix – Everywhere

- **Subsidiaries**
- **Sales offices**
- **Manufacturing plants**
- **Departments**
- **Joint ventures**
- **Partnerships**
- **Third parties**
 - Agents
 - Suppliers



Kaplan Matrix – Every USSGs Element

1. STANDARDS & PROCEDURES

2. GOVERNING AUTHORITY

**OVERSIGHT, MANAGEMENT ROLE &
PROGRAM RESPONSIBILITY/CHIEF
ETHICS & COMPLIANCE OFFICER
("CECO")**

3. SCREENING & PROPER DELEGATION

**4. TRAINING & DISSEMINATING
INFORMATION**



Kaplan Matrix – Every USSGs Element

5. AUDITING/MONITORING, REPORTING SYSTEMS & EVALUATING THE PROGRAM

6. DISCIPLINE & INCENTIVES

7. APPROPRIATE RESPONSE & PREVENTING RECURRENCE

C. RISK ASSESSMENT

COMMENTARY – PROGRAM FOLLOWS GOVERNMENT REGS/INDUSTRY PRACTICE



How to Measure – Some Tools

- **DESK AUDITS**
- **COUNTING INPUTS & OUTPUTS**
- **FOCUS GROUPS**
- **INDIVIDUAL INTERVIEWS**
- **AUDITS**
- **TESTS**



How to Measure – Some Tools

- **STATISTICAL ANALYSIS**
- **EXIT INTERVIEWS**
- **DEEP DIVES**
- **SELF ASSESSMENTS**
- **DRY RUNS**
- **SURVEYS**



Surveys – An Incomplete Answer

- **THEY MEASURE WHAT EMPLOYEES WANT TO TELL YOU**
- **EMPLOYEES GAME THE SYSTEM**
- **HOW YOU ASK AFFECTS WHAT YOU GET**
- **PERCEPTIONS ARE NOT ALWAYS REALITY**
- **COMPLIANCE IS NOT BY MAJORITY VOTE**



Measuring Impact – By Risk Area

HOW WOULD YOU MEASURE WHETHER THE PROGRAM WORKS IN EACH OF THESE RISK AREAS?

- **ENVIRONMENTAL – MANUFACTURE**
- **CONSUMER PROTECTION – RETAIL**
- **ANTITRUST – SALES & BIDDING**
- **OFF-LABEL SELLING – PHARMACEUTICAL SALES**
- **ACCOUNTING FRAUD – SEC REPORTS**



Could You Convince the Government?

- **THEY FOCUS BY RISK AREA**
- **THEY FOCUS WHERE THE VIOLATION OCCURRED**
- **THEY TALK WITH EMPLOYEES**
- **THEY LOOK AT WHAT YOU HAVE IN WRITING**
- **THEY EXPECT YOU TO HAVE DONE THE SAME**



Measuring Impact – What About Culture?

WHAT THE GUIDELINES SAY ABOUT CULTURE:

“(b) Due diligence and the *promotion of an organizational culture* that encourages ethical conduct and a commitment to compliance with the law within the meaning of subsection (a) *minimally require the following:*

[Steps 1-7]”

HOW TO MEASURE CULTURE?

THE JIM SHEEHAN TEST – TALK TO SOME EMPLOYEES!



Who Does the Assessment

RANGE OF OPTIONS

FROM

**LEAST INDEPENDENT, KNOWS THE MOST ABOUT
YOUR COMPANY**

- MANAGER'S SELF ASSESSMENT**

TO

**MOST INDEPENDENT, KNOWS THE LEAST ABOUT
YOUR COMPANY**

- OUTSIDE EXPERT, NO OTHER DEALINGS WITH FIRM**



Who Does the Assessment - Options

- **OUTSIDE INDEPENDENT COMPLIANCE EXPERTS**
 - DOES THIS ONE REVIEW ONLY
 - LAWYERS, ACCOUNTANTS, C&E FIRMS
- **OUTSIDE COMPLIANCE EXPERTS**
 - PROVIDE OTHER SERVICES FOR THE COMPANY.
- **OUTSIDE, RISK AREA SUBJECT MATTER EXPERTS**



Who Does the Assessment - Options

- **PEER REVIEWS FROM OTHER COMPANIES**
- **MIXED TEAMS – INSIDE & OUTSIDE, INTERESTED & DISINTERESTED**
- **IN-HOUSE MANAGERS/ PROFESSIONALS NOT INVOLVED IN THE C&E PROGRAM**
- **COMPANY C&E OFFICE.**
- **LINE MANAGEMENT (SELF-ASSESSMENTS)**



Who Does the Assessment – Consider:

- **INDEPENDENCE**
 - NOT ASSESS THEIR OWN WORK
 - NOT AFRAID TO ANGER CECO OR CEO
- **COMPETENCE**
 - RESOURCES
 - SUBJECT-MATTER EXPERTISE
 - COMPLIANCE & ETHICS EXPERTISE
- **CREDIBILITY**
- **COST**



Who Gets the Report

- **ROLE OF THE CECO**
 - **INPUT FOR THE REVIEW**
 - **BUT, CONTROL OF THE REPORT?**
- **ROLE OF SENIOR MANAGEMENT**
- **REPORTING TO THE AUDIT COMMITTEE**
 - **WILL THEY KNOW ENOUGH TO UNDERSTAND & ANALYZE IT?**



Who Gets the Report

- **RISK IN LITIGATION**
 - PRIVATE PLAINTIFFS
 - THE GOVERNMENT

PRIVILEGE PROTECTIONS

- CAN STRUCTURE TO MAXIMIZE PROTECTION, BUT . . .
- WRITE AS IF IT WILL BE PUBLIC
- FIX WHAT YOU FIND



Assessments from Afar

- **ACADEMICS & NGOs TRY TO ASSESS COMPANIES' PROGRAMS**
 - **RELIANCE ON CODES - BECAUSE THEY'RE EASY TO FIND**
- **IF YOU HAD TO PICK ONE C&E ELEMENT, WHICH WOULD YOU MEASURE?**



Assessments from Afar

- **CECO AS A LEADING INDICATOR**
- **IS CECO INDEPENDENT, CONNECTED, EMPOWERED & PROFESSIONAL?**
- **SOME INDICATORS:**
 - **LISTED IN ANNUAL REPORT**
 - **BACKGROUND, EXPERTISE, CCEP**
 - **REPORTS TO BOARD**
 - **CAN BE TERMINATED ONLY BY BOARD**
 - **NOT IN LEGAL DEPARTMENT**
 - **NO CARVE-OUTS FROM PROGRAM**



Follow-up

- **ONLY DO AN EVALUATION IF YOU ARE PREPARED TO ACT ON IT**
- **NEVER BELIEVE ANY EVALUATION THAT SAYS EVERYTHING IS PERFECT**
- **NO MATTER HOW GOOD THE REPORT, DON'T GET COMPLACENT**



Follow-up

- **ASSIGN FOLLOW-UP RESPONSIBILITY**
 - **ASSIGN RESPONSIBILITY TO SPECIFIC MANAGERS**
 - **MAKE IT PART OF THEIR OBJECTIVES & EVALUATIONS**
 - **COVER ALL KEY FINDINGS**
- **CHECK RESULTS PERIODICALLY**



Other sources

- Murphy, 501 IDEAS FOR YOUR COMPLIANCE AND ETHICS PROGRAM, chapter K, “USSGs item 5, other types of checking systems, monitoring techniques, and program evaluations” (SCCE; 2008)
- Kaplan & Murphy, COMPLIANCE PROGRAMS AND THE CORPORATE SENTENCING GUIDELINES: PREVENTING CRIMINAL AND CIVIL LIABILITY, chapter 18, “Measuring the Effectiveness of Compliance & Ethics Programs” (Thomson/West; 1993 & Ann. Supp.)



Other sources

- **SCCE SOCIAL NETWORK,
“AUDITING AND MONITORING
COMPLIANCE NETWORK”**

<http://community.corporatecompliance.org/CORPORATECOMPLIANCE/CORPORATECOMPLIANCE/eGroups/DigestViewer/Default.aspx?GroupID=271>



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QUESTIONS?