

The Business Case for an Effective Compliance Program

As the global regulatory and enforcement focus on financial and corporate fraud, corruption, and national security crimes intensifies, a compliance and ethics program has never provided more value to companies. An effective compliance program demonstrates a company's commitment to responsible conduct and can result in substantial and direct benefits to a company's bottom line.

What are the bottom line benefits of an effective corporate compliance and ethics program?

Prevention of violations: A compliance plan tailored and implemented to address the real risks faced by a company should prevent most violations. In preventing violations, a compliance program can more than justify associated costs and investments. The cost of non-compliance includes not only fines and other judicial penalties, but also the expense of internal investigations, the legal defense of the company and its employees, and possible collateral consequences such as debarment from public contracts, denial of licensing privileges, the avoidance of contracts, and the loss of business relationships.

The mere threat of fines and these additional consequences can weaken a company's credit profile, liquidity, and rating. Accordingly, a company's access

to financing may be constrained during the pendency of an investigation, regardless of its final resolution, Fitch Ratings reported recently¹.

In order to be effective, a program needs to have a demonstrated commitment to compliance at the highest levels, Board of Directors' oversight, an empowered compliance infrastructure, relevant training, regular auditing and monitoring, reporting procedures, remediation, discipline, and recordkeeping.

Competitive advantage: A compliant company "will have a more resilient business, be an employer of choice for recruiting and can gain a competitive advantage as a preferred choice of ethically concerned customers, investors, suppliers and other stakeholders."² Compliant companies also offer the stability derived from avoidance of the delays and disruptions caused by investigations, interim suspension orders, intensive licensing reviews, or other, more stark, penalties. By implementing an effective compliance program, a company can highlight its commitment to stable and enduring business relationships, putting to rest anxieties about global trading and risk management pitfalls.

Exiting investments: The intensification of focus by authorities on corruption has carried over into investors' due diligence.

Key issues

What are the bottom line benefits of an effective corporate compliance and ethics program?

Conclusion

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¹ "U.S. Foreign Corrupt Practices Act—No Minor Matter," Fitch Ratings (June 1, 2010).

² "The 2010 UK Bribery Act Adequate Procedures: Guidance on Good Practice Procedures for Corporate Anti Bribery Programmes, Transparency International," at 5 (July 2010).

Investors are becoming more and more concerned about historic compliance breaches and practices of target companies and the extent to which compliance has been monitored by a target. A lax attitude to compliance by a target is likely to mean that investors will insist on onerous warranties and indemnity protections or that investors will walk away from a deal. An effective compliance program will ease investors' concerns about legacy liability issues.

Early detection of problems and investigative control: An effective compliance program can offer companies the opportunity to discover a breach ahead of regulators and take proactive steps to contain and correct it. For example, in the case of cartel violations, many jurisdictions now offer significant 'rewards' to companies that report violations ahead of their being uncovered by a regulator, including immunity from substantial fines and criminal prosecution.

When companies without operative means of detecting violations find themselves the subject of an investigation, they are disadvantaged as they try to conduct internal investigations to 'catch up' with investigators' knowledge. This can obviously affect a company's ability to respond to and (where applicable) negotiate with authorities, as well as its ability to continue its day-to-day business.

As a result of recent legislation, it is also more likely that potential violations of certain laws will be brought to the attention of relevant authority. The Dodd-Frank Wall Street Reform and Consumer Protection Act signed into law by President Obama contains in Section 922³ a new whistleblower incentive program that would reward certain whistleblowers with between 10 per cent and 30 per cent of the total sum collected in a successful Securities and

Exchange Commission enforcement action for which the whistleblower provided 'original information.' This would include, for instance, covered enforcement actions for the violation of the FCPA accounting provisions. An effective compliance program would ensure that a company was aware of and could address internally any potential violations of these provisions before they are disclosed to appropriate authorities.

Minimising potential charges: A company's preparedness to address its legal obligations will often influence the way it is treated by investigative agents and authorities. For example, in the United States, when agents begin an investigation, they will give the benefit of doubt to a company with a strong compliance program. Instead of search warrants and grand jury subpoenas, a company may face less intrusive (which often correlates to less costly) requests for documents and informational interviews.

In the United States, the likelihood of prosecution decreases when a company can convince the government that it has discovered and fully remediated the problem so that recurrence is sufficiently unlikely. After a violation occurs, the objective is to convince the government to forego making an example of the company for deterrent effect. This objective is more likely to be achieved when a company has discovered and self-disclosed the violation to the relevant agency, when appropriate. Most US agencies, including the Department of Justice, will give credit for an effective compliance program by declining or deferring prosecution or reducing the penalty imposed.

Defending charges: The importance of implementing compliance procedures for all companies with global operations was highlighted by the recent passage of the

Bribery Act in the United Kingdom.⁴ The Bribery Act creates a new corporate criminal offence for failing to prevent bribery by an associated person. This new "corporate offence" applies to any commercial organisation incorporated under the laws of the United Kingdom and any overseas entity that carries on a business or part of a business in the United Kingdom. A foreign company which carries on any part of its business in the UK could be prosecuted for failure to prevent bribery, even where the bribery takes place wholly outside the UK and the benefit or advantage to the company is intended to accrue outside the UK. A company's only defense to this new offence is if it can show that it had adequate procedures in place designed to prevent persons associated with it from undertaking bribery.

The UK Secretary of State will issue guidance as to what constitutes "adequate procedures," but in the interim a company must look for other guidance to benchmark or develop its compliance program. Transparency International UK (a leading non-governmental anti-corruption organization) has published comprehensive guidance on adequate procedures under the UK Bribery Act.⁵ Clifford Chance provided advice on the legal aspects of this text. A company following those guidelines may have reasonable assurance that it has aligned to what is generally viewed as current good practice and thereby represents "adequate procedures."

Penalty mitigation: An effective compliance program can reduce penalties imposed on a company in sentencing. For example, in the US if the government decides to proceed with prosecution, most agencies will mitigate penalties for companies that self-disclose or that have in place an effective compliance program. The Department of Commerce gives up to 25 per cent

¹ "U.S. Foreign Corrupt Practices Act—No Minor Matter," Fitch Ratings (June 1, 2010).

² "The 2010 UK Bribery Act Adequate Procedures: Guidance on Good Practice Procedures for Corporate Anti Bribery Programmes, Transparency International," at 5 (July 2010).

³ Pub. Law. 111-203, § 922 (modifying the Securities Exchange Act of 1934 (15 U.S.C. 78a et. seq) by adding a new Sec. 21f).

⁴ The UK Bribery Act received Royal Assent on April 8, 2010, and will come into force in April 2011.

⁵ http://www.transparency.org.uk/attachments/138_adequate-procedures.pdf

mitigation credit for effective export compliance programs. Similarly, the Department of Treasury Office of Foreign Assets Control may give as much as 50 per cent mitigation credit for effective compliance programs. In criminal cases, the U.S.

Sentencing Guidelines, which provide uniform sentencing policies for certain crimes (including FCPA and anti-trust offences), allows a three-point reduction (30 per cent) in the penalty calculation for companies shown to have an effective compliance and ethics program.

In order to receive credit for having an "effective" compliance and ethics program, a company must:

(1) exercise due diligence in preventing and detecting criminal conduct; and
(2) encourage ethical behaviour within the company by:

- ensuring that the company's board is knowledgeable about, and encourages the implementation of, the
- compliance and ethics program;
- taking reasonable measures to ensure that company personnel do not engage in conduct that is inconsistent
- with administering an effective compliance and ethics program;
- ensuring the program is communicated to all employees (including through training);
- ensuring that the program is periodically evaluated and that employees can anonymously seek guidance
- regarding potential criminal conduct;
- ensuring that the program is promoted and enforced appropriately and consistently; and
- ensuring that reasonable steps are taken to remediate any violations that occur.

Even if "high level personnel" are involved, companies are still eligible for compliance

credit as long as: (1) compliance officers have direct reporting obligations to a company's governing authority; (2) the misconduct is discovered internally before it is discovered by third parties, including government officials; (3) the company promptly self-reports the violation; and (4) no person responsible for the administration of the compliance and ethics program was involved in the wrongdoing.⁶

Conclusion

With heightened liability risks for companies, directors, and individuals, companies must make sure that they have robust, up-to-date, and effective compliance policies and systems. Effective compliance strengthens a company's business position, prevents violations, and mitigates any potential penalties should the worst occur.

⁶ Proposed amendment to the US Sentencing Guidelines, scheduled to be implemented November 1, 2010.

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