Strategies for Successful Compliance Programs

Pitfalls and Traps for the Unwary

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Introduction

In today's regulatory environment, the importance of implementing and maintaining an effective and well-designed legal compliance and training program is hard to overstate. The impediments to establishing and maintaining such a program are, however, often difficult to anticipate and may only become apparent after it's too late.

This program will cover the benefits, key elements, and common pitfalls of implementing an effective compliance program in the context of important issues of **labor and employment**, **antitrust**, and **international law**.

Compliance … With What?

Before discussing the ins and outs of compliance programs, we must first address two basic questions: (1) What are the hot-button concerns that merit a compliance program in the first place? (2) What are the risks of non-compliance?

Antitrust

Significant Areas of Concern

1. Horizontal Restraints (i.e., interactions with competitors)
   - Price Fixing / Bid Rigging
   - Market Division / Customer Allocation
   - Boycotts / Refusals to Deal

2. Vertical Restraints
   - Exclusive Dealing Arrangements
   - Tying/Bundling
   - Resale Price Maintenance

3. Price Discrimination

Risks and Penalties for Non-Compliance

1. Criminal Penalties (Generally Only for "Hardcore" Cartel Behavior)
   - Corporate – fines of up to $100 million or double the gross gains or losses
   - Individual – fines of up to $1 million and up to 10 years in prison
   - Ancillary Criminal Sanctions (e.g., wire fraud, false statements)

2. Civil Claims
   - Treble Damages + Attorneys Fees for Sherman Act Claims
   - High Risk of Direct and Indirect Purchaser Class Actions

Labor & Employment Law

Significant Areas of Concern

1. Federal Anti-Discrimination laws
   - Title VII of the Civil Rights Act (e.g. race, gender and religious discrimination; sexual harassment), Americans with Disabilities Act, Age Discrimination in Employment Act
   - Family and Medical Leave Act, USERRA

2. Immigration Law
   - I-9 Compliance (work authorization)
   - Export Control (see international section)

3. Wage-Hour Law
   - Fair Labor Standards Act (FLSA), state wage payment laws

Risks and Penalties for Non-Compliance

1. Anti-Discrimination - Compensatory and punitive damages; reinstatement; back pay; front pay; attorney's fees
2. I-9 - Fines per each violation that may exceed $1 million or more in the aggregate, depending on employer size; possible criminal sanctions for knowing violations
    a. Export Control (see international section)
3. FLSA – unpaid wages for up to three years; liquidated damages in an equal amount; attorney's fees

International Law

Significant Areas of Concern

1. Export controls: Applicable laws include the following:
    a. Export Administration Act and Export Administration Regulations ("EAR"):
        i. "Exports"
        ii. "Deemed exports"
        iii. Anti-boycott
    b. Arms Export Control Act and International Traffic in Arms Regulations ("ITAR")
    c. Economic and Trade Sanctions ("OFAC")

2. Foreign Corrupt Practices Act ("FCPA")

3. Foreign laws, including:
    a. UK Bribery Act
        - Recently created with similar provisions as the FCPA, but a broader scope
        - Covers both official and commercial bribery
    b. The Organization for Economic Co-operation and Development ("OECD") Anti-Bribery Convention:
        - Adopted by 34 OECD member countries and 5 non-member countries (Argentina, Brazil, Bulgaria, Russia, and South Africa)
        - Establishes legally binding standards to criminalize bribery of foreign public officials in international business transactions and provides for a host of related measures that make this effective
        - Touted as the first and only international anti-corruption instrument focused on the 'supply side' of the bribery transaction.
    c. Competition laws

Risks and Penalties for Non-Compliance

1. Export Controls: sanctions can include:
    a. Civil Fines: Up to the greater of $250,000 or twice the value of the transaction, per violation;
    b. Criminal Sanctions: Fines up to $1 Million and/or up to 20 years imprisonment, per violation;
    c. Administrative Sanctions: Can include permanent or temporary denial of export privileges and cancellation of existing export licenses, among other things.

2. Foreign Corrupt Practices Act ("FCPA"): Sanctions can include:
    a. Criminal Sanctions:
        i. Business entities: fines up to $2 Million
        ii. Officers, directors, stockholders, employees & agents:
            1. Fines up to $100,000 [employer cannot pay]; and/or
            2. Up to 5 years imprisonment
        iii. Alternative Fines Act: up to double the benefit that the defendant sought to obtain by making the corrupt payment
    b. Civil Fines:
        i. Up to $10,000 against entity and individuals acting on behalf of the entity
        ii. Via SEC enforcement action, additional fine which cannot exceed the greater of:

1. The gross amount of pecuniary gain to the defendant as a result of the violation; or
2. The specified limit based on the egregiousness of the conduct involved (ranges from $5,000-$100,000 for natural persons and $50,000 to $500,000 for any other person)

c. Injunctive relief
d. Other government action, such as denial of export licenses, debarment from federal contracts, etc.
e. Private cause of action under RICO (treble damages) or other federal or state laws
f. Whistleblower claims under Dodd-Frank

The Benefits of Compliance

Obviously the ultimate goal of any compliance program is to prevent the company from breaking the law. There are, however, substantial benefits to be gained from detecting a violation before governmental authorities or private plaintiffs discover a violation. Even if misconduct evades detection until it is discovered by governmental authorities, the existence of a compliance program sometimes can be taken into account in assessing penalties.

Antitrust

Benefits of Self-Reporting

- DOJ Leniency Program
  - Amnesty/Amnesty-Plus
  - ACPERA (Substantial Limitations on Civil Damages)
- EC Leniency Program

Effect of Compliance Program on Penalties

- Not Considered by DOJ or EC in Setting Fines or Sentencing

Labor and Employment Law

Benefits of Self-Reporting

No governmental leniency programs, but the existence of a robust and effective compliance program will provide a company with the opportunity to resolve employee issues internally and avoid administrative charges and lawsuits.

Effect of Compliance Program on Penalties

- May help avoid exposure to punitive damages in employment litigation

International Law

Benefits of Self-Reporting

1. EAR:
   - "Voluntary disclosure" meeting EAR requirements: a "great weight" mitigating factor for penalties
   - Prior violation disclosed via a complying voluntary disclosure is discounted in assessing penalties for a subsequent violation
2. ITAR: similar to EAR
3. FCPA:
   - Sentencing guidelines
   - DOJ/SEC approach
   - Whistleblower

Effect of Compliance Program on Penalties

1. EAR:
   - "Great weight" is given if violation was discovered as result of exporter's compliance program and reasonable steps have been taken to prevent reoccurrence
   - Existence of compliance program and overall high level of compliance is a mitigating factor
   - Absence of compliance program if exporting regularly is an "aggravating" factor in assessing penalties
   - Disregard of duties given "great weight" as an aggravating factor in determining penalties
   - As practical matter, without an effective compliance plan, the requisite 5-year records will not likely be available [itself a violation] and also liability may be found for circumstances for which the exporter would not be liable if its actual pre-transaction conduct could be proven (example: exporter's products found in prohibited destination or prohibited use which is actually different than the buyer represented and belief in the purported destination and use by the exporter was reasonable).

2. ITAR:
   - A similar approach is taken to the EAR.

3. FCPA:
   - Factors into whether charges will be brought by DOJ/SEC
   - Lower fines under federal sentencing guidelines

Where Are The Risks In The Organization?

When it comes to compliance programs, one size does not fit all. To develop a relevant, effective compliance program, it is necessary to first conduct a general risk assessment to determine how an organization's business processes and communications intersect with potentially risky conduct.

The nature of the risks faced by the organization and where those risks reside are two of the most important factors that need to be taken into consideration in developing a compliance program. Depending upon the size and sophistication of the organization, it may be possible to conduct this assessment through interviews with senior business leaders and in-house counsel. Risk assessments for larger organizations, however, may entail document review as well as employee interviews and require a cross-functional team led by in-house or outside counsel and the internal audit department.

Regardless of the method chosen to identify and describe the nature of the risks faced by the organization, a risk assessment is an essential first step in designing a compliance program that addresses the substantive areas that present the most risk for the organization and is focused on those individuals that are in a position to affect that risk.

What Does an Effective Compliance Program Look Like?

There are four fundamental components to any effective compliance program: (1) A Written Compliance Policy; (2) Effective and Relevant Training Programs; (3) Methods for Reporting Violations Without Fear of Retaliation; and (4) Routine Monitoring.

The Written Compliance Policy

- Lengthy and Detailed Compliance Policies are Counterproductive.
    - To the extent the client insists on a detailed manual setting forth the precise contours of the relevant law, those materials should remain solely with the legal department as a reference.

- Compliance Manuals for Employees Should be in Clear and Simple Language
    - Avoid legalese.
    - Supply manuals in all of the working languages of the business.

- Compliance Materials Should be Distributed to All Relevant Employees
    - Should require signature acknowledging receipt.

- A Quick-Reference Guide for Employees is Invaluable
    - FAQ's or "Do's and Don'ts"
    - Instructions on how to ask a question or report a compliance concern

Training

- Get Senior Level Employees Invested in Training and Compliance
    - Training that is introduced and sponsored by the business leaders will be considered more important and given more attention.
    - The tone within middle management is, however, just as important.

- Train the Right People at the Appropriate Level of Detail and Sophistication
    - Well-trained employees are the first line of defense.
    - Training should be customized for function and seniority.
    - Depending on the organization, it may be necessary to train large numbers of employees through online training modules.
    - Live, in-person training is, however, key for employees with the ability to create significant legal risk for the organization.
    - Newly hired employees in key areas may require immediate training.

- Use Business Scenarios to Explain Key Principles
    - Steer clear of abstract discussions of the law.
    - The best training uses concrete examples to teach employees how to identify and avoid legal risks.
    - Training should be tailored to the company's geography, industry, and structure.
    - Training should be continuously updated.

- Make Training Interactive
    - Invite employees to be engaged in the training throughout.
    - Consider using tools such as electronic voting systems to overcome employees' natural reluctance to answer questions in front of co-workers.
    - Training should be offered in all of the working languages of the company.

- Track Attendance and Retention
    - Ensure all employees who are required to take the training actually participate.

Reporting Mechanisms

- In any effective compliance program, it must be clear that employees should seek help from subject-matter experts if they have any questions regarding any business practice.

- Similarly, the organization should establish and publicize readily accessible mechanisms for employees to report questionable conduct without fear of retaliation.

- Whistleblower protections are important so that employees feel safe reporting violations internally rather than going directly to the state or federal enforcers.

Monitoring

Merely drafting a compliance policy and holding regular training sessions is not, however, enough. Rather, there must be an established mechanism to determine: (1) how well the compliance program is working; and (2) whether there are actual violations (of either the law or the company's compliance policy) occurring.

- Regular evaluation of how the compliance program is working is often handled by in-house counsel or an internal audit team. This is an ongoing process which entails:
  - Raising awareness of the importance of compliance;
  - Identifying gaps in the compliance program;
  - Ensuring that compliance and training programs are being consistently implemented throughout the relevant businesses.

- Substantive compliance audits can take any number of forms, but often entail the use of outside counsel to conduct a more thorough investigation into the organization's business practices to identify potential violations and to better understand key risk areas.
  - These programs are becoming more and more prevalent, particularly for larger organizations in the area of antitrust law, given the substantial value in being the first to identify and report a violation.
  - Substantive compliance audits should occur on a regular schedule and as needed if issues arise.
    - Employees should not, however, be informed of an impending audit prior to documents being collected in connection with that audit.
  - An effective substantive compliance audit should include a review of business records, including emails and interviews with the right mix of employees.
    - Search terms can be used to pare down email volume to a manageable level;
    - The determination of which employees to interview will often require involvement of senior management and may occasionally be informed by the document review process itself.

- The nature and degree of ongoing monitoring that is required will, of course, vary substantially depending on the nature of the business and the types of legal risks at issue.

- Compliance programs must have teeth to be effective.
    - It is, therefore, important to identify sanctions (including termination of employment) and to keep record of implementation of any sanctions.

Common Pitfalls Faced by Compliance Programs

Because no two compliance programs are the same, each is guaranteed to face its own unique obstacles and challenges. There are, however, a number of pitfalls that are sometimes overlooked but often encountered and for which preparation should be made in advance.

Documentation of Audit Findings

Careless documentation of audit findings can effectively create a road map for plaintiffs or a government agency investigating the organization. Extreme care should, therefore, be used in creating any materials relating to audit findings or any other compliance concerns discovered by the organization.

- Audit reports should be prepared by counsel and should be shared only with business leaders who are directly involved in the audit process.
- Employees should avoid sending emails or creating documents relating to any audit findings.
- Counsel should be present and direct any discussions of audit findings.
- Given the possibility that an organization may ultimately waive the attorney-client privilege, audit reports should be written carefully to avoid creating a self-indicting memo. It is helpful to include, where possible, an explicit statement of how negative findings are being addressed. It is also appropriate, when there are positive findings, to include those findings in the report as well.

Managing Privilege and Work Product Issues

While managing and preserving the attorney-client privilege is second-nature to most attorneys, there are some important issues to take into account in the context of compliance programs.

- In conducting compliance audit interviews, counsel should ensure (as gently as possible) that the employee being interviewed understands that the attorney represents the company, not the employee, and that the privilege belongs to the company.
- Employees need to understand the importance of confidentiality and that it is not appropriate to discuss the substance of the audit interviews outside the presence of company counsel.
- For international audits, European privilege rules may need to be taken into account.
    - There is no single rule on privilege in Europe and each jurisdiction has its own rules.

- The European Union has separate rules that govern all EU antitrust investigations.
    - There is no privilege for communications between the business and its in-house counsel.
    - There is no privilege for communications with external counsel that is not qualified to practice in one of the EU member states.

Managing the Documents

- In many cases, the implementation of a full compliance program will expose deficiencies in an organization's document retention policies. Indeed, the biggest variable in the cost of implementing a external audit is volume of emails retained by individual employees and organizations with no document retention policies may even find it to be prohibitively expensive to conduct an effective audit.
    - Implementing an effective document retention program not only reduces the costs of an audit, but also can substantially reduce litigation costs.

- Audits may also expose gaps in an organization's corporate communications policies. It may be discovered, for instance, that employees regularly communicate with customers or suppliers via text message, private emails, or other ways that are impossible for the organization to control or monitor.
    - These gaps are important areas to explore in the context of any compliance program.

- Privacy laws in Europe and other countries may effectively prevent the company from collecting or reviewing employee emails in connection with a compliance audit.
    - Proactive measures, such as incorporating certain provisions in employment agreements of foreign employees, may better position the company to navigate challenges posed by foreign data privacy laws.