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# ‘Mandavolent’ Compliance

By Joe Murphy

In 1986, when Jay Sigler and I were writing our first book on voluntary corporate compliance, the idea of large scale, vigorous company compliance programs was essentially an untested concept. There had been legal areas where voluntary efforts had been growing—the defense industry after the 1980s’ Ill Wind scandal, environment, antitrust—but the idea that there could be an entire field known as corporate compliance was a novel approach that was met with skepticism in many quarters. By 1991, the U.S. Sentencing Commission’s adoption of a carrot-and-stick system to promote such programs touched off a development that has reached global proportions. Today, voluntary compliance programs are springing up around the globe. After the shock of Enron, WorldCom and similar cases, there is certainly debate about what it takes for these programs to be fully effective. But the acceptance of these programs is well established.

## Another less-obvious trend

Success, however, is not without its risks. Accompanying this trend toward voluntary compliance programs is another trend that few have noticed, but which has the potential to dramatically alter the meaning of compliance programs. This change stems from a fairly simple exercise of government logic. The reasoning goes as follows:

- 1) Voluntary compliance programs are good because they can help prevent and detect violations of law. They are valuable because companies are applying their own resources and expertise to this socially beneficial task.
- 2) Not all companies have these programs, and more could be done even in the ones that exist.
- 3) Therefore, if voluntary programs are beneficial, but there are not enough of them, then let’s make the voluntary programs mandatory. Then everyone will have voluntary programs that meet every risk the legislature or regulatory agencies want addressed.

What we have been witnessing, perhaps without realizing it, is a new phenomenon—the birth of mandatory voluntary compliance programs. To match this trend I thought it would be appropriate to find an expression that is easier than repeating “mandatory voluntary” compliance.

Being a believer in the evolution of language, it occurred to me that what was missing was a descriptive term to capture this logic and its new dynamic. After several intense minutes of thought, I came upon the answer, so I am introducing the term

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*mandavolent compliance*. Its origins are straightforward, just combining parts of the two words into a more compact new word (emphasis in the second syllable, if anyone wants to try it).

### **Some recent examples**

What are the examples of mandavolent compliance?

*Sarbanes-Oxley*. In 2002 Congress ventured into the world of corporate compliance, albeit without doing any significant research, and decided to require certain compliance elements for publicly traded companies. So today listed companies need to have reporting systems for auditing and accounting issues. They also must have codes of conduct for their CFO and CEO (or have the unusual courage to report to the world that they do not need such a code). They must also have systems for their securities lawyers to escalate certain compliance issues up the ladder in their companies.

The stock exchanges, following the direction of the SEC under Sarbanes-Oxley, but going even further, required codes that went beyond the law, to cover all employees and directors. The New York Stock Exchange (NYSE) even added an open-ended requirement for someone (it is not made clear who) to reach all the independent directors to express their “concerns.”

*Sexual harassment training*. While Sarbanes–Oxley has the visibility, it was not the first venture into mandavolent compliance. Maine and Connecticut determined that preventing sexual harassment was important enough to require companies to teach it to their employees. Not to be outdone, California in 2004 enacted a requirement for any company in that state employing 50 or more employees to have two hours of supervisor training in this area every two years.

*Pharmaceutical company programs*. Lest anyone think that the Republican administration in California would lead to reduced legal adventurism, California decided in 2004 to impose compliance programs on all pharmaceutical companies doing business in that state. What standard must those companies follow? Not the nationally recognized Sentencing Guidelines standards, but the *guidance* standards established by the Office of Inspector General (OIG) of the Department of Health and Human Services. This will be a challenge for the industry, since the OIG guidance is written expressly as just that—a guidance, not a mandatory standard.

*Mutual funds and advisors*. The SEC, having been

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apparently upstaged by state enforcers, has decided to jump ahead in this trend. It has ordered mandavolent compliance efforts for mutual funds and advisors, who will all now have compliance officers.

*Consent decrees and corporate integrity agreements*. Incrementally, mandavolent compliance has become a standard product of government enforcement efforts. From baby steps just a few years ago, there are now hundreds of negotiated decrees and orders imposing mandavolent compliance programs on companies in a broad range of industries, although the healthcare field is by far the leader.

*Privacy*. In the U.S., the Health Insurance Portability and Accountability Act of 1996 (HIPAA) has mandated privacy compliance officers to protect healthcare records. But just so no one mistakes mandavolent compliance for an American aberration, this tool has found its way onto the global stage. In Canada, for example, the national government has mandated privacy compliance program elements to protect individuals’ records held by companies. Germany has mandated designation of privacy officers.

### **No end in sight**

These examples show the movement that has been widening as we watch. As things stand today, it is difficult to see a natural stopping point for this trend. Why would California stop at pharmaceutical companies, if mandavolent compliance is a good idea? Why not take on the next industry that gets in trouble? And why would this approach stop at the West Coast? If it works in California, why would the New York legislature ignore it? Why not require every organization in the country to have a full-blown compliance program? Why not the world as well?

If this is a force that is upon us, is there anything those in compliance and ethics should be doing about it? Consider the recent record of the compliance and ethics profession, particularly in regard to Sarbanes-

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Oxley. The Sarbanes-Oxley Act of 2002 was passed in response to massive corporate wrongdoing. It was the public's representatives' plan to prevent a recurrence. But where were the compliance and ethics professionals? Where in Sarbanes-Oxley can be found any trace of our experience or knowledge? The law speaks of auditors, lawyers, financial managers—but not one single reference to compliance officers or compliance programs. And what is actually in the law? The (throwback) belief that merely adopting codes of conduct will have a significant impact (apparently glossing over the fact that Enron, among others, had a code). A requirement for a reporting system limited to a narrow financial area—and one that requires the impossible: confidentiality and anonymity (did any of the lawyers in Congress ask about what happens to the “confidential” records when there is a subpoena or discovery request in litigation, for example?). And an escalation system for lawyers that channels them through the general counsel and CEO (ignoring the recent cases involving too many instances of misconduct at the senior level) without so much as a “hello” to the compliance officer—who is typically already responsible for channeling just such reports to the audit committee.

The lesson of Sarbanes-Oxley to the compliance and ethics profession is that we have been asleep at the switch. We have neither ears to hear what is happening among policy makers, nor a voice to make our concerns heard. We cannot blame anyone else—the fault is on our own shoulders.

So where does this take us in dealing with the trend toward mandavolent compliance? If nothing changes we will see an exact repeat of Sarbanes-Oxley. Legislators and regulators who know less about this area than even the most junior compliance staff person will be dictating to us how to do our jobs. Instead of innovation and efforts to achieve effectiveness, we will be following the orders of the lawyers who will tell us exactly what the law requires us to do.

Is mandavolent compliance a bad thing? The point here is not that I have the answer—it is that we are not

even asking ourselves the question. For purposes of moving this question along, I offer here some possible pros and cons (I am sure a little imagination could produce even more):

**The ‘pros’ of ‘mandavolent’ compliance**

*Levels the playing field.* If all companies must have programs, then those who do so are not disadvantaged. Companies can feel freer to apply resources to the effort, knowing that competitors have to do so also. (This assumes having a program is a net loss and not a business advantage. Many of us would dispute that.)

*It gets everyone doing this.* If programs are required, then everyone will have to have one. That certainly expands the compliance field and could bring to bear more expertise. More programs would mean more compliance and ethics people, which might help the community to grow into a more effective force.

*It moves us past wasted arguments about whether to do things.* One of the great benefits of the Sentencing Guidelines is that they moved the field past endless debate and set a floor for the minimum needed for a program. If legislators and regulators proceed down that path and set standards that resolve issues that are still being debated, they could accelerate the compliance effort.

*One legal standard can avoid having to meet a plethora of standards.* As compliance programs have become more popular, more standards have been cropping up. If Congress made programs mandatory for everyone and set the standard, then there would be just one standard that all could follow.

*Government intervention has driven development.* Proponents of mandavolent compliance can fairly note that it was the Sentencing Commission that kick-started this entire field, and that messages from government, such as the Thompson memo and the *Caremark* case have continued to propel it along. Government mandates would just be the next logical step.

*Incentive-based systems have not driven development enough.* Policy makers could point to Enron, WorldCom and similar debacles and argue that incentive-based systems have not prevented these violations, so more is needed. Perhaps applying the lessons of these cases could lead to pervasive systems that could prevent, or detect these corporate crime waves at a much earlier time.

*Legislation can change values.* How often have we

heard the statement, “you can’t legislate morality”? At least some of the empirical evidence suggests, however, that legislation does, in fact, change society’s ideas of right and wrong. Certainly a good case could be made that criminalizing the infliction of environmental harm, and making discrimination and harassment illegal have at least molded society’s standards for acceptable conduct. So perhaps making compliance programs mandatory could, over time, make them part of the culture, and acceptable business conduct.

### **The ‘cons’ of ‘mandavolent’ compliance?**

*It can drive everyone down to the minimum necessary.* The problem with setting a legally mandated minimum is that it can quickly become the practical maximum. If California requires two hours of harassment training every two years, will that mean that few companies will now have such training on an annual basis? Will such laws elevate form over substance?

*Mandatory minimums can freeze development.* One weakness of government-imposed standards is that they can freeze the development and growth of the field. This is an area where the Sentencing Commission got it right. The standards provide structure, but beyond that they essentially require companies to keep innovating and working to stay up to or ahead of “industry practice.” But a mandatory standard may need to be more precise than voluntary guidelines. Once the government tells us that two hours training every two years is enough, why bother to see if other things work.

*What drove development before, was providing an incentive, not a dictate.* Development of innovative efforts came not from mandates, but from incentives. An incentive-based system leads people to experiment and strive to improve. Legal minimums can have exactly the opposite effect.

*Standards are typically set by people who do not know or understand compliance programs.* The experience with Sarbanes-Oxley is not encouraging. One phenomenon that is unfortunately too common in this field is that those who do not take the time to study the field believe it to be a simple, intuitive matter. Ignoring the years of experience that are now available, they sit down at their isolated desks, detached from the day-to-day reality of compliance people, and come up with standards that are outdated, ineffective, and in some cases counter-productive.

While the Sentencing Commission had the wisdom

*One risk of ‘mandavolent’ compliance is that it could lead to the lawyerization of compliance.*

to solicit input from actual compliance and ethics people, the California legislature, Congress, and other regulators apparently considered this a waste of time. There are no signs today that this would change, absent compliance and ethics people becoming organized and making their presence known.

*Mistakes in mandatory standards lead to misallocation of resources.* Here is another lesson from Sarbanes-Oxley. Companies have dived into the process of writing codes of conduct with great vigor. They have spent millions making sure they have “control systems” over minor expenditures. Meanwhile, major compliance risks are given the second seat while these legally “important,” although sometimes trivial, steps are attended to.

*Leads to the lawyerization of compliance.* In the beginning days of compliance, everything was done by lawyers. Codes were written by lawyers (and, judging from the prose, *for* lawyers as well). Company policies rivaled legislation in their complexity. When training was part of the mix, lawyers would give lectures on what the laws said. The Sentencing Guidelines forced a change toward making programs “effective,” and before long companies realized that “by lawyers, for lawyers” was not a formula for success. This lesson appeared to be taking hold, until Sarbanes-Oxley and the recent growth of mandavolent compliance. More and more we are seeing lawyers’ commentary on the meaning of Sarbanes-Oxley, and whether company efforts meet the minutiae of the NYSE standards for codes (which, after all, only tell us what we “should” do, although the NYSE’s proffered code language speaks in mandatory terms, and a plaintiff’s lawyer might use failure to follow the NYSE standards as an absence of diligence, but then . . . ) Will legislated standards for compliance shift the focus back, away from what really works, to a new obsession with what “the law” means? Certainly some of the experiences with Sarbanes-Oxley suggest this could be the wave of the future.

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as part of the settlement of a class-action race-discrimination lawsuit in 2000, for example.)

Nonetheless, “the momentum is building,” says Howard. “More companies will do this going forward, and not just because they got whacked.” It’s inevitable as the workforce becomes more diverse and compliance departments become more effective that employees “fear they may get caught in the middle.” The ombuds office can help them out, guide them.

The office has its limitations, Friede cautions. “We’re not decision makers.” They can’t change company

*‘It’s a great job.’ An ombudsperson has access to all lines of business, domestic and overseas. They develop a company-wide perspective. They can have an impact on the organization.*

policy. Above all, the office is meant to be accessible. It’s one more way to send the message to employees—“We do care.” □

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### ‘Mandavolent’ Compliance . . . *Cont’d. from p. 11*

*Can lead to a multitude of legal standards.* If we could be sure there would be only one legal standard, there might be at least some relief for company compliance managers. But why think there would be only one mandatory standard? Why would not each state and each agency mandate what was to be done? And what force would cause these to be similar, or even consistent? Will we end up, for example, with one standard that tells us exactly how to conduct investigations and another that tells us that following the first standard will violate that jurisdiction’s privacy compliance standards?

### A boost or threat?

Pro or con, which is right? Is mandavolent compliance the boost that our field has been waiting for, or is it a threat to push the entire field backward? Is it possible to harness this trend so that we benefit from the positives but avoid the risks?

The compliance and ethics profession could answer these questions and take its future into its own hands. Or it could be completely passive, letting down our clients and ourselves while abdicating key decisions to those who know little or nothing about compliance. The choice may still be ours, but not for long. □

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### Shell Oil and Lubrizol . . . *Continued from page 7*

annually and are reviewed by the board’s audit committee and other senior executives. Annual reports are sent to key managers and are publicized in in-house publications. They try to be as transparent as possible, adds

*Explaining why her company opted for a third-party vendor to manage the helpline, Caremark’s chief compliance officer said, ‘Because they don’t have caller ID.’*

Meister, and attempt to share anecdotes wherever possible. Meister also holds private sessions with the board’s audit committee each time it meets.

Discretion is critical when it comes to reporting such

matters. “I’ve had grown men and women cry in my office,” says Meister. You have to preserve their confidentiality.

The helpline was recently audited by Lubrizol’s internal audit team, who were monitoring for Sarbanes-Oxley compliance. The auditors wanted to know how quickly the office responded to helpline calls. “We passed,” recalls Meister.

Again, it is critical for employees to believe that if they call the helpline, something will be done. About the time that Meister first arrived at the company, in 1994, there was a senior sales person who was running a separate business—apart from Lubrizol—one that involved all kinds of self-dealing and conflicts of interest. “People tried to bring it forth, and nothing was done about it,” he recalls. That can be fatal for a helpline. In the end, “People have to believe that you’ll actually do something.” □



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