

Use of Ethics Officers to Oversee Corporate Ethics Programs

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The recent turmoil and scandal that has embroiled directors and senior officers at Hewlett-Packard has led to criminal charges and renewed focus on privacy issues, conduct of internal investigations and appropriate corporate standards and practice with respect to business ethics. At this point, the scope of actual legal liability for the persons involved in the investigation of leaks of sensitive and confidential information by directors is far from settled; however, several people have lost their jobs and legislative action has already been taken against the controversial practice of "pretexting" (i.e., lying to obtain the personal phone records of others). In addition, it is clear the companies should take a moment to revisit their practices regarding the conduct of internal investigations and consider the need to formalize their ethics programs by creating a separate ethics officer position.

One of the ironic twists about the criminal charges brought against the chief ethics officer of HP is that the company had been widely recognized as one of the top corporate citizens based on its proactive programs to promote diversity and improve the communities within which the company operated. In spite of these efforts, the business reputation of the company has now been badly shaken by what appears to be a breakdown among the senior executives vested with responsibility for legal compliance and ethical behavior. This is not the first time such a thing has happened. For example, Fannie Mae was ranked as one of the best corporate citizens in 2004; yet, within a year, it found itself embroiled in controversy following accusations of accounting improprieties and claims that executives had benefited from improper compensation packages. Lessons learned from these two companies have caused other companies to take a hard look at how they staff their compliance and ethics functions and what other steps can be taken to build and maintain ethical goodwill among investors, customers, business partners, regulators and the general public.

For any business to deal with the demands of legal compliance, an effort must be made to establish and maintain a comprehensive legal compliance program. The program serves many purposes, the most important of which is monitoring the legal health of the business and identifying problems and, in some cases, new opportunities that may develop as the business grows and changes and new laws and regulations are implemented. While establishing and maintaining a compliance program is a time-consuming and often expensive project, there are clearly significant legal and business advantages to the company. Compliance programs can be used to educate employees and set standards for acceptable conduct in all the company's operations around the world. There also seems to be a direct link between companies that score high on integrity factors and those that perform well financially. According to one study, the five companies perceived as having the strongest integrity (i.e., General Electric, IBM, Microsoft, Toyota and Wal-Mart) were the same ones that topped the list of companies that created the most value for their shareholders. Other studies focusing generally on

corporate governance, of which compliance is an important element, have verified that firms with the best governance practices tend to be relatively more profitable, more valuable and offer their shareholders a higher return on their investment.

The compliance program will only be as good as the people appointed to the compliance team, and the directors need to make some fundamental decisions in this regard at the time that the program is initially endorsed by the board. As the company grows, it will typically establish a compliance office to exercise overall control over the compliance activities of the company. The compliance office will be responsible for establishing compliance policies and procedures throughout the company and may also be involved in other functions such as crisis management. Responsibility for operation of the compliance office should be vested in a chief compliance officer ("CCO") who is considered to be a member of the senior management group of the company and who reports to the chief executive officer and, as necessary, to the audit committee of the board of directors. Every effort should be made to protect the independence of the CCO by providing a separate employment contract to him or her. Given the demands of the CCO position, it is not surprising that companies often look to attorneys, internal auditors, or former investigative agency employees. In any event, the CCO must have a broad compliance background and specific experience working with organizations that have operated in the same product and geographic markets. The CCO should be at a sufficiently high organizational level to ensure the cooperation of all personnel in the event that a compliance investigation is required or a compliance reform is necessary. Selection of a top official is helpful in persuading employees that compliance is an important and valued goal for the company.

Recently, more and more companies have decided to appoint an ethics officer to oversee a wide range of regulatory and ethical matters and launch and coordinate initiatives to ensure that the business objectives and culture of the company are aligned with acknowledged and accepted ethical values and practices. Ethical issues arise frequently in the modern business environment, and trained ethics officers can develop and suggest solutions and make sure the company actually follows the policies, guidelines and ethical standards that it promotes. In particular, ethics officers can and should be available on a daily basis to work with employees to assist them in making decisions that are fair, lawful and ethical since it is unlikely that employees have even the most basic education and training in the theory and practice of business ethics. More specific reasons for creating an ethics officer position include:

- To provide assistance with meeting regulatory compliance through development and implementation of ethics training programs and ongoing measurement of results that can be reported back to top management;
- To improve the reputation and perception of the company with employees, regulators and the general public; and
- To create and implement an infrastructure for reporting and managing ethical issues.

When creating the position of chief ethics officer, the company should prepare a comprehensive job description in advance. The scope of the duties of the chief ethics officer will depend on several factors, including the business activities of the company; the geographic reach of the company's activities, including the countries in which the company regularly deals with customers and other business partners; the specific laws and regulations that are applicable to the business activities of the company; and whether or not the company also has a CCO as part of its top management team. It is important to note that companies have a variety of options when deciding how an ethics officer would fit into their overall organization:

- While not all ethical issues are legal issues, there is certainly significant overlap, and many companies recognize this by creating a combined legal compliance and ethics officer position.
- Another approach is to split the jobs and put them both under the supervision of the general counsel of the company.
- Still another option is for the chief legal officer (i.e., general counsel) to also be the CCO and then create a separate ethics officer position within the general counsel's office.
- Finally, some companies rely on independent consultants to fulfill many of the responsibilities of an ethics officer outlined below.

In all cases, to be recognized by regulators as a meaningful attempt at ensuring ethical and legal compliance, the position must operate at "substantial authority" level of management, and the incumbent must have regular access to senior management and the audit or other committees of the board of directors exercising responsibility for ethical and compliance issues.

In any event, among the chief ethics-oriented responsibilities of the position might be the following:

- Responsibility and accountability for developing and directing the ethics and business conduct function for the entire company;
- Providing leadership, oversight, and expert advice to ensure appropriate development, interpretation, and implementation of the ethics policies and programs;
- Accountability for all program activities relating to standards of conduct, including ethical relationships with employees, customers, contractors, suppliers, shareholders, and other stakeholders;

- Accountability for the company-wide confidential reporting program (such as a Helpline) allowing employees, customers, suppliers, and other stakeholders to report violations of ethics-related policies and guidelines without fear of retaliation;
- Establishing and administering a long-term strategy for improving the ethical profile of the company through training programs and regular communications around ethical and business conduct issues;
- Integrating new acquisitions into the ethics practices of the parent company;
- Coordinating investigations into alleged violations of the company's ethics policies and making recommendations for resolution of ethics-related problems and misconduct;
- Developing systems and methods for measuring and quantifying the efficacy of the company's ethics-related programs and policies; and
- Making regular reports to senior management and the audit and other committees of the board of directors regarding the company's ethics program and policies.

Since the ethics officer position is relatively new, there is no standard set of educational and experience requirements that can be applied in all circumstances. In fact, since one of the most important roles of the ethics officer is to serve as the "conscience of the company," the choice often comes down to factors and impressions that are difficult to objectively measure. Ethics officers are drawn from a wide array of disciplines include legal, human resources, finance, auditing, security, or line operations; however, the top candidates generally are strong communicators, objective and thoughtful, politically savvy and able to establish and maintain trust and credibility throughout the company, able to assimilate and analyze information quickly, have common sense, and have a record that demonstrates the highest level of personal and professional integrity. The ethics officer must also have strong management skills, particularly when the officer is given personnel and budgetary resources to launch and maintain the ethics program, and have experience with developing and implementing training programs. Finally, the ethics officer must have a thorough working knowledge of the business strategies of the company, specific risk factors to which the company may be subject, and the laws and regulations directly applicable to the business activities of the company.

Given the very specific duties and responsibilities of an ethics officer, it is strongly recommended that persons occupying that position be subject to a formal written employment agreement that specifically references all or most of the responsibilities listed above. The agreement should clearly describe the authority of the ethics officer and the reporting channels that apply to the position. For example, if the ethics officer position is placed within the office of the general counsel, the agreement should indicate that the officer will report to the general counsel. If the ethics officer is given budgetary responsibility, the agreement should provide guidance as to how the officer should prepare a proposed budget, obtain approval for the budget and administer the budget over

the course of the fiscal year. In some cases, the agreement will go beyond a general description of responsibilities to incorporate specific targets for a given quarter or year such as promulgating a code of ethics for the company, completing a minimum number of training programs, establishing a Hotline procedure and launching compliance programs in specified areas.