

The Honorable Dick Thornburgh Larry D. Thompson

The Issue: Advancing Business Integrity through Corporate Compliance

In this edition of Washington Legal Foundation's CONVERSATIONS WITH, former Pennsylvania Governor and Attorney General of the United States **Dick Thornburgh** discusses the vexing challenges of corporate compliance with former Deputy Attorney General **Larry D. Thompson**. Mr. Thompson draws upon his experiences as a private attorney, a U.S. Attorney, Deputy Attorney General, and general counsel of PepsiCo to explain the legal, financial, and other benefits of designing and maintaining effective corporate compliance programs. He also offers his thoughts on current complicating factors such as the rise of whistleblowing and he advocates for an affirmative defense of an effective compliance plan.

Governor Thornburgh: Let's start by putting the sophisticated compliance programs we see today into context. What was the state of corporate compliance 20 to 25 years ago? How common was it for corporations then to have such programs, and how much commitment to compliance did you see at that time?

Larry Thompson: Corporate compliance programs of any type were not common 20 to 25 years ago.

Compliance programs did exist in specific areas such as antitrust. It has been my experience over the years that businesspeople are generally very honest; whatever compliance efforts that existed previously were well-meaning and undertaken in good faith. What was not understood 20 to 25 years ago was exactly how to implement these programs, how much training was needed under these programs, or even how significant these programs are to a company's business. By today's standards, the compliance programs of that era would mostly be viewed as inadequate.

Governor Thornburgh: Can you note two or three developments over the past several decades that inspired greater commitment to compliance and the formalization of programs?

Mr. Thompson: Yes. Clearly, the promulgation in 1991 of the organizational sentencing guidelines by the U.S. Sentencing Commission has been very important. These guidelines reward corporations for effective compliance programs. But, before that signal event, the development of robust compliance program expectations in the defense industry was huge. Lawyers who counseled businesses closely followed the Defense Industry Initiative on Business Ethics and Conduct and the Department of Defense's Voluntary Disclosure



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Program. Finally, Sarbanes-Oxley’s Section 406, which calls for companies to have ethics programs for key financial executives, has been the “period at the end of the sentence” regarding the necessity for having effective compliance and ethics programs.

Governor Thornburgh: Changes in government enforcement and policies certainly motivate improvement in compliance, but how much of the increased commitment can be attributed to corporate leaders’ drive to be better corporate citizens or display a culture of business integrity?

Mr. Thompson: I don’t believe that today’s business leaders are more committed to business integrity than those of the past. In fact they may have more pressure to achieve short-term financial results for shareholders than did business leaders of the past, who often emphasized other stakeholders in a company’s business in addition to shareholders. What is different today is that a whole cadre of professionals have developed an expertise in developing and implementing effective compliance programs. There is also a recognition by lawyers, academics, and businesspeople that compliance programs alone are not sufficient to address all the ethical issues a business may face. We have all seen situations where something may be technically legal but still problematic from an ethical standpoint. Corporate leaders are getting much more informed advice today on compliance and ethics programs than they did in the past.

Governor Thornburgh: How can a general counsel or chief executive officer

best motivate directors or other officers to embrace a compliance approach inspired by adherence to business integrity, rather than one which seeks baseline legal compliance?

Mr. Thompson: The general counsel and CEO must engage the board of directors and other officers on the importance of compliance and ethics programs. This is the all-important “tone at the top.” They must be committed to the idea that compliance and ethics are extremely important and are the responsibility of everyone in the organization—not just the general counsel or chief compliance officer. And they must keep their personal commitment to compliance and ethics top of mind in the organization. Of course, they must lead by example.

Governor Thornburgh: Is there a competitive advantage in maintaining a “beyond-right” approach to compliance and a culture of business integrity?

Mr. Thompson: Yes, absolutely. What you call the “beyond-right” approach to compliance and a “culture of business integrity” is what I’ve seen over the past 35 years in the very best companies. These companies generally are the most innovative, recruit and retain the best employees, have the most loyal customers, and manage for long-term success and growth in shareholder value. They avoid risky, short-term “fixes.” These companies have solid reputations and operate under a strong set of core values that is exemplified by the phrase, “High Performance with High Integrity,” as Ben Heineman Jr., the former general counsel of General Electric, puts it. Also, based on my experience, things

will almost always, from time to time, go wrong in almost every company. A company's reputation for high integrity is really its best defense in dealing with enforcement officials and government as it goes about sorting things out. This reservoir of good will is very, very valuable. You cannot underestimate how important it is. Finally, I've seen some studies, particularly those by *Ethisphere* and Curtis Verschoor, that support the idea that more ethical companies, however that is all measured, perform better than other companies. I do not know how good these studies are, but they're out there.

Governor Thornburgh: When you were involved on the enforcement side as a U.S. Attorney or as Deputy Attorney General, what shaped your expectations of an "effective compliance program"? Have these expectations changed over the past ten years you have been out of government?

Mr. Thompson: As Deputy Attorney General, especially in the aftermath of corporate scandals like Enron, I was concerned with whether a corporation had a real compliance program and not a pretend or paper one. The question we asked was, "Does the corporation's compliance program work?" We looked at whether there was sufficient staff and other resources devoted to the program. Other considerations involved were whether the corporation's employees were adequately informed about the program and convinced of the corporation's commitment to it. We wanted to know whether there was appropriate discipline, including discipline of higher-ups. Importantly, we understood the realistic

limitations of a compliance program; there is no compliance program that can prevent all criminal activity by a corporation's employees. Nevertheless, we gave real credit to a bona fide, effective compliance program. If the compliance program was effective and solid, it could result in a decision to not charge the corporation and charge only its agents or employees.

Governor Thornburgh: From your experience as a general counsel to a multinational corporation, how can such a company best instill an ethic of integrity and compliance across borders and cultures?

Mr. Thompson: I do not believe there's only one way or right way to do it. My experience is that success in compliance across borders and cultures requires, obviously, hard work and a singular dedication to making it happen. You have to integrate the company's core values for integrity into the way the corporation does business. It is very important that global corporations have global values. It is also very important that, when measuring performance of senior executives, ethics be a paramount consideration. Both results and means have to be important. All of this will require a considerable investment of time, resources, and sweat equity.

Governor Thornburgh: How important is it for a general counsel and a corporate compliance officer to become fully versed in the business in which their company operates? Do they have to be business experts in order to be effective compliance experts?

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Mr. Thompson: I think it is extremely important that the general counsel and chief corporate compliance officer have a deep understanding of the businesses in which their company operates. As Norman Veasey and Christine Di Guglielmo point out in their wonderful new book, *Indispensable Counsel: The Chief Legal Officer in the New Reality*, today’s general counsel, in order to be effective, must be able to “partner” with her corporate colleagues to provide knowledgeable and wise counsel on proposed business strategies. In order to do this, she must understand her company’s business. Relating to both the general counsel and the chief compliance officer, an effective and successful integrity program must be integrated into and with the corporation’s business processes. They clearly must have a good command of the corporation’s businesses to make this integration work.

Governor Thornburgh: In terms of designing programs and lines of reporting and responsibilities, do you feel the general counsel and the chief compliance officer should be separate positions, held by different people?

Mr. Thompson: I am aware that in some corporations the general counsel also serves as chief compliance officer. I prefer that they be separate positions. In coming to this conclusion, it is important to understand that compliance, in my opinion, especially legal compliance, is a core general counsel function. Today’s general counsel are increasingly responsible for managing their respective corporations’ legal and reputational risks. They are the point persons on this front.

The chief compliance officer, on the other hand, is not delivering legal advice to his corporate colleagues. Instead, he is managing and implementing the many moving parts of an effective compliance program. Code of conduct development and training, monitoring hotline calls, working with the legal department, human resources, and internal audits on investigations are all important responsibilities under an effective compliance program. They involve coordination with many different experts, including financial and environmental experts, across the corporation. The coordination of all these processes should be managed with rigor and great integrity. If this is to be done well, it requires a person who is dedicated to it full time.

Governor Thornburgh: To whom should the chief compliance officer most directly report? To the general counsel? To the board of directors?

Mr. Thompson: I know there is a lot of debate surrounding this question. The simple answer is that the chief compliance officer should report to the general counsel. As I have noted, I strongly believe compliance is a core general counsel function. There will be times when it is in the corporation’s interest to have chief compliance officers report to the general counsel. When difficult legal and investigative matters arise, it must be the general counsel’s responsibility to determine how these will be handled. Who will investigate? Will the investigation be a privileged one? What are the legal issues, such as disclosure, surrounding a sensitive occurrence? These are questions only the general counsel should answer, and these answers should

be provided for the benefit of the chief executive officer and, if appropriate, the board. This is not a time for bureaucratic turf wars.

But, to me, this question goes beyond a simple reporting relationship. The chief compliance officer should be a senior member of the management team, which reflects on the importance of compliance and ethics within the organization. In addition, as a senior professional in the corporation, the chief compliance officer should be independent.

This independence can be reflected in a number of ways. The chief compliance officer should not just have the right to go to the chief executive officer or board whenever he believes the corporation is not handling some manner appropriately; his access to the chief executive officer or board should be structured in a more formal way. For example, the chief compliance officer should meet with the chief executive officer alone on a periodic basis, as well as meet alone with the audit committee of the board. The chief compliance officer should not be removed without first notifying the board or a board committee. I think all of this is a good way to balance the legitimate legal interests of the corporation with the need for professional standing and independence of a chief compliance officer. While we are on this subject, we should remember that while the right reporting relationship can be important, it is the culture and core values for integrity that will ultimately lead to success in this area.

Governor Thornburgh: How can a corporation most effectively utilize pri-

vate, outside counsel in matters involving corporate compliance? Is there a role for outside counsel in design and application of programs, or is their role more relevant when responding to a government investigation or action?

Mr. Thompson: Based on my experience, I think it is critically important that a corporation use independent outside counsel and compliance professionals in the design, implementation, and monitoring of compliance and integrity programs. The key word here is “independent.” Using outside counsel and other professionals certainly enhances a program’s reliability. This is important. Moreover, outside input will make the program better and more effective. In-house counsel and compliance professionals will always benefit from hearing different perspectives. Obviously, outside counsel will often need to be brought in to assist in a government investigation or a sensitive internal review.

Governor Thornburgh: Federal and state laws have created new incentives for whistleblowers. How can compliance programs best encourage internal, rather than external, reporting of possible law violations?

Mr. Thompson: This is a major concern. Incentives for whistleblowers can really undermine an effective compliance program and even a culture of integrity. These developments are unfortunate but we now need to deal with them. There was an excellent program on this last year sponsored by the RAND Center for Corporate Ethics and Governance. It is clear that corporations must work even

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harder to make certain there is a culture where internal reporting is valued and encouraged. Corporations really need to spend more time on internal communications regarding the culture of integrity. It should be treated almost like important, albeit internal, advertising. Of course, the culture must be real and authentic. Increased communications will backfire if it is not. I know some have advocated that corporations actually have their own internal compensation or bonuses for whistleblower tips. I would like to see this idea a bit more fully developed before I would recommend its adoption for use by a corporation, especially on a corporate-wide basis.

Governor Thornburgh: In-house and outside counsels are increasingly being targeted by government with either indictments or encouragements to “cooperate.” How must compliance programs react to and manage such situations?

Mr. Thompson: This can be an issue if counsel, both in-house and outside, ever lose sight of their professional obligations. Counsel representing a corporation, especially during an investigative or “crisis” situation must remember that they represent the entity and not any individual. This is absolutely clear from SEC Rule 205.3(a), promulgated under Section 307 of Sarbanes-Oxley. Counsel must calmly get at the facts and make certain that the investigation is thorough, objective, and professional. Counsel cannot let anyone inside the company interfere with an ongoing investigation. In dealing with the government, counsel must make certain that the corporation’s cooperation is authentic, but, again, thoroughly professional. So, for example, it

would be completely inappropriate and unethical to try to “scapegoat” an employee in an effort to satisfy government demands for “cooperation.” The facts are what they are, and the investigation should simply follow the facts.

Governor Thornburgh: Law professor Richard Epstein has written that, “Excessive regulations cause private firms to displace creative officers and entrepreneurial executives with the dull masters of compliance.” Does he have a point?

Mr. Thompson: He most certainly has a point. Simply complying with a long set of rules or rows of compliance manuals on a bookshelf will not only be deleterious to entrepreneurship but will also stifle creativity and risk-taking that is key to successful business. What is needed beyond just compliance is a core set of values that will guide a corporation’s business. So, even as the business moves forward and engages in new ventures and takes appropriate business risks, it will do so in the context of a core set of business values. Even within the framework of an article titled *The Social Responsibility Of Business Is to Increase Its Profits*, Milton Friedman recognized that the general responsibilities of corporate managers will include “conforming to the basic rules of the society”, both those embodied in law and those embodied in ethical custom.

Governor Thornburgh: Last year, a company self-reported Foreign Corrupt Practices Act violations and the Justice Department instituted a deferred because, although DOJ agreed the company had an “effective” compliance

prosecution agreement with them because, although DOJ agreed the company had an “effective” compliance program, the “implementation” was flawed. Is there a risk that compliance fatigue or a sense of cynicism toward compliance might set in if “effective” programs aren’t enough to protect companies from legal peril?

Mr. Thompson: Absolutely. As the Department of Justice recognized in its 2003 guidelines on charging corporations and other entities with crimes, even an effective compliance program cannot prevent every single employee from doing something wrong. This is just being realistic and having a common-sense understanding of what occurs in real life. This is why I believe that an affirmative defense of an effective compliance plan should be allowed before the government can convict an organization of a crime. Today, no matter how effective or gold-plated a compliance program is, a corporation is subject to criminal liability under the strict application of the respondeat superior rule. This is not good policy. There must be situations where a corporation can essentially be “blameless” if it has done all that it should have and has an effective compliance program. I have actually written an article on this called *The Blameless Corporation*. Remember, this is an affirmative defense, and, of course, the government can present rebuttal evidence that the compliance program is not effective or is simply a sham or paper one. Without something like this, business leaders and even employees will begin to devalue compliance programs and, yes, cynicism towards compliance will begin to set in.

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The Honorable Dick Thornburgh is a former Attorney General of the United States, Governor of Pennsylvania, and Under-Secretary-General of the United Nations. He is currently Of Counsel to the international law firm K & L Gates LLP, and Chairman of Washington Legal Foundation's Legal Policy Advisory Board. Governor Thornburgh began his public service career as a United States Attorney in Pittsburgh and an Assistant Attorney General in charge of the Criminal Division. As a private attorney, he was appointed in 2002 as Examiner in the WorldCom bankruptcy proceedings, the largest ever filed, to report on wrongdoing and malfeasance that led to the company's downfall. Governor Thornburgh was also chosen by CBS to conduct an investigation into the *60 Minutes Wednesday* segment on President George W. Bush's service in the Texas Air National Guard.

Larry D. Thompson is the John A. Sibley Chair of Corporate and Business Law at the University of Georgia School of Law. In May 2011, Mr. Thompson retired as senior vice president of government affairs, general counsel, and secretary for PepsiCo. Mr. Thompson previously served as a senior fellow with The Brookings Institution in Washington, D.C. His government career includes serving in the U.S. Department of Justice as Deputy Attorney General and leading the Department's National Security Coordination Council. Mr. Thompson was also chosen to head the Corporate Fraud Task Force, where he led, among others, the Justice Department's ongoing Enron investigation. Previously, he was a partner in the Atlanta law firm King & Spalding, where he practiced in the antitrust and litigation departments. Mr. Thompson also served as the U.S. Attorney for the Northern District of Georgia. In 2009, *Ethisphere Magazine* recognized Mr. Thompson as "one of the most respected and admired general counsel in business today."