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COMPLIANCE AND ETHICS REQUIREMENTS TO BE TIGHTENED

The U.S. Federal Sentencing Commission's guidelines for organizations (including corporations, partnerships, associations, trusts, pension funds and not-for-profit organizations) are the foundation for many current compliance and ethics programs. First promulgated in 1991, the guidelines set forth minimum sentences to be imposed on individuals and organizations found guilty of a federal crime, and further define what qualifies as an effective organizational compliance and ethics program. The Sarbanes-Oxley Act required the Commission to review and amend the guidelines to ensure that they are sufficient to deter and punish organizational criminal conduct. The Commission has recently proposed amendments to the guidelines to strengthen the rigor and increase the detail of the guidelines' requirements.

An effective compliance and ethics program has the benefit of potentially mitigating the often severe criminal penalties and civil damage awards associated with financial and oversight offenses. Further, a sound, enforced compliance program may deter prosecutors from pursuing criminal action against an organization in the first place.

The Commission specifies seven minimum requirements for organizational compliance and ethics programs. Under the new amendments, an organization would not receive any sentence reduction unless all of the seven requirements are met.

(1) Establish organizational standards and practices to prevent and detect criminal conduct.

This primary requirement is changed in so far as the amendments strengthen and add detail to the remaining requirements of an organization's standards.

(2) Identify both high-level personnel responsible for overseeing the program, as well as personnel with day-to-day operational responsibility.

Under the proposed amendments, primary responsibility for knowledge about and reasonable oversight of the compliance and ethics program is placed on the organization's governing authority, typically the Board of Directors. Furthermore, high-level personnel are required to become more involved in the implementation and enforcement of the program. One high-level individual must be designated and assigned "overall responsibility" for the program.

(3) Monitor substantial authority personnel for conduct inconsistent with the program.

The standard of care for selecting "substantial authority personnel" (high-level personnel and managers with discretionary authority) has been heightened such that the organization is now responsible to ensure that these individuals have not engaged in illegal activity or activity inconsistent with the compliance and ethics program.

(4) Conduct effective organization-wide training programs.

The mandate for effective training now includes not only employees and agents, but also members of the governing authority (i.e., the board of directors), high level personnel, and substantial authority personnel. Training is expected to be more intensive and ongoing with periodic updates.



(5) Take reasonable steps, including audits and effectiveness evaluations, to ensure adherence to the program.

The proposed amendments additionally suggest an anonymous and confidential reporting system so that guidance may be sought by employees without fear of retaliation. The organization is now also expected to undertake periodic audits of the compliance and ethics plan as well as study the overall effectiveness of the program.

(6) Enforce the compliance and ethics standards consistently.

New to this requirement is emphasis on (a) organizational incentives to reinforce compliant behavior and (b) organizational punishments for both violations of the compliance plan but also specifically for those who fail to take "reasonable steps to prevent or detect criminal conduct."

(7) Respond to criminal conduct in a preventative fashion.

This requirement remains basically unchanged, but emphasis is placed on the organization's duty to continually monitor and change its compliance and ethics program so as to avoid future misconduct.

In addition to changes to the seven program requirements, the amendments also create a new obligation that organizations perform a "risk assessment" which is to include: (1) an assessment of the nature and seriousness of potential criminal conduct; (2) an assessment of the type of criminal conduct likely to occur due to the nature of the organization's business; and, (3) an assessment of the organization's history of criminal conduct. The organization should use the results of such a risk assessment to aid in the further development and implementation of its compliance and ethics program.

The amendments to the requirements will become effective November 1, 2004 unless the Congress rejects the Commission's proposals.

For further information on how to update your organization's compliance and ethics programs to reflect industry best practices and to prepare for these future amendments, contact your BS&K attorney or one of the attorneys listed below.

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