

5 Need-to-Know Developments for the Audit/Compliance Committee

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By Michael W. Peregrine

The board's audit and compliance committee may benefit from a briefing on several new developments that raise important risk and compliance oversight issues. These developments affect upstream reporting relationships of the general counsel; the expanding role of the general counsel; increased liability concerns of compliance officers; and a prominent new report on compliance program effectiveness. The typical committee charter will be implicated by each of these developments, and the general counsel is well situated to present this briefing.

1. "Reporting Up" This first development, arising from a recent decision of a state bar disciplinary commission, implicates the "upstream" organizational reporting obligations of the general counsel's office to, and through, the committee.

According to [various media reports](#), the Michigan Attorney Grievance Commission declined to pursue six former General Motors Co. in-house counsel for failing to disclose to consumers the safety risks of an alleged defective automotive product. The reporting practices (or lack thereof) by members of the GM in-house counsel department were a major part of that company's broader ignition switch controversy.

The professional rules in question were those that (a) refine the role of lawyers in supporting the flow



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of information and analysis on legal compliance matters within the corporation they represent; and (b) clarify the limitations placed on the lawyer's ability to disclose to third parties confidential information about the client's potential criminal or fraudulent conduct. As such, the Michigan decision provides a useful opportunity for the committee to address the practical confluence of its risk oversight responsibilities, and in-house counsel's professional responsibilities regarding "reporting up" and "reporting out."

2. Expanded Role for General Counsel This second development concerns the manner in which the committee interacts with the general counsel.

On April 2, [NYSE Governance Services and BarkerGilmore released its survey report, "The Rise of the GC: From Legal Adviser to Strategic Adviser."](#) The principal conclusions are that the role

of the corporate general counsel continues to expand and evolve, and as this role shifts, the perspectives of the general counsel are “uniquely positioned” to advise the board and management team on risk management and strategic decisions. In that regard, 97% of the survey respondents were of the view that general counsel would be a part of the executive management team by 2020.

This is consistent with the perspectives of leading corporate responsibility commentators, such as Ben Heineman Jr. and E. Norman Veasey, that the role of the modern general counsel includes not only providing legal advice (broadly defined), but also serving as a member of the “business team” and offering business and risk management advice.

These survey results and related confirmation should prompt the committee to consider a broader role for the general counsel in committee operations—i.e., not merely as staff to the committee, but also as an active participant in its agenda.

3. Compliance Officer Liability Exposure This third development involves the manner by which the committee provides appropriate support and encouragement to the chief compliance officer in the performance of his/her duties.

Over the last several months, compliance officers have grown increasingly concerned about possible individual liability exposure. These concerns have been prompted by the application of the U.S. Department of Justice’s Yates Memorandum, by DOJ’s appointment of a “compliance officer” within its Fraud Division and by a series of controversial government enforcement actions against compliance officers.

These include actions initiated by the Securities and Exchange Commission against several compliance officers working in the investment adviser sector, and a separate fine applied by the Treasury Department to the former compliance officer of a financial ser-

vices company for certain alleged compliance plan and reporting failures. In addition, FINRA recently fined and suspended a former compliance officer at a financial services firm for allegedly failing to implement satisfactory anti-money laundering procedures. Perhaps in response to such concerns, Andrew Weissmann (Chief of the Department of Justice’s Fraud Section) recently commented that DOJ is “not going after compliance officers for criminal liability.”

The collective “anxiety” of the compliance industry was given a more public presence by the recent issuance of a **comprehensive survey of compliance and risk officers**. Notably, a large percentage of surveyed corporate compliance and legal officers expressed significant concerns regarding their personal liability, arising from what they perceived to be increased government scrutiny of compliance personnel.

This third development should be of particular concern to the committee. It could serve to limit the effectiveness of the compliance program in general, and the performance of the compliance officer in particular. It may prompt a discussion by the committee of the most appropriate means by which compliance officers can be provided tangible support and encouragement by the corporation.

4.The Ethics and Compliance Initiative (ECI) Report This fourth development is about the manner by which the committee monitors the effectiveness of the organization’s compliance program.

On April 25, the nonprofit ECI released the report of its blue ribbon panel, **“Principles and Practices of High-Quality Ethics Programs.”** Membership of the panel included a cross section of prominent current and former legislators, government enforcement officials and compliance officers. The stated purpose of the report was to identify specific principles and practices that the panel believes characterize “high quality ethics and compliance programs”— i.e., those

that transcend minimum effectiveness standards such as the ones set forth in the Federal Sentencing Guidelines. Principles specifically cited by the report as characteristic of high quality compliance programs include:

- Ethics and compliance is considered as an essential element within every element of corporate operation.
- Ethics and compliance risks are identified, *owned* [emphasis added], managed and mitigated across the organization.
- Leaders across all organizational levels are responsible for developing and sustaining a culture of integrity.
- The organization supports an environment that encourages, protects and values the reporting of compliance concerns and suspected wrongdoing.
- The organization quickly takes action and holds itself accountable when wrongdoing is identified.

The premise of the report is that compliance programs based on the Sentencing Guidelines actually reflect only minimum practices – and thus there may be value in considering more comprehensive approaches. Accordingly, there may be value for the committee to review the report and compare its recommendations and identified principles against the core elements of the organization's existing compliance program. At the same time, the committee should receive a short briefing on the provocative new law review article, "[Corporate Governance in an Era of Compliance](#)." This article boldly confronts what are likely to be incipient concerns in many boardrooms and executive suites — whether compliance programs 'have gone too far'; whether they are incompatible with traditional models of governance efficiency.

This implicates the committee's expected practice of periodically reviewing the effectiveness of the organization's compliance and ethics program.

5. Program Benchmarking The Committee should be aware of promised guidance from DOJ's Fraud Division on how it proposes to evaluate the existence and effectiveness of individual corporate compliance plans. A recent, detailed "open letter" to DOJ's new Compliance Counsel (published in the [Harvard Business Law Review](#)) serves in part to provide recommendations on how DOJ should implement this goal of establishing industry-specific benchmarks by which individual programs may be evaluated. In that regard, the "open letter" provides a useful overview of the categories of compliance program benchmarking that DOJ may ultimately apply.

The Bottom Line

Individually and collectively, these developments have direct application to the risk and compliance program oversight obligations of the committee. They are sufficiently material as to warrant informing the committee in the normal course of the management briefing process. Because the developments all share a foundation in law and legal compliance, the general counsel (perhaps in consultation with the chief compliance officer) is the most appropriate corporate officer to present on them.

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