

# *HALLMARK III*

CCO Authority and Compliance Function Resources

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## A. CCO Authority and Independence

The role of the Chief Compliance Officer (CCO) has steadily grown in stature and prestige over the years. In the 2012 FCPA Guidance, under Hallmark Three of the 10 Hallmarks of an Effective Compliance Program, the focus was articulated by the title of the Hallmark, **Oversight, Autonomy, and Resources**. In it the 2012 FCPA Guidance focused on the whether the CCO held senior management status and had a direct reporting line to the Board; stating “In appraising a compliance program, DOJ and SEC also consider whether a company has assigned responsibility for the oversight and implementation of a company’s compliance program to one or more specific senior executives within an organization. Those individuals must have appropriate authority within the organization adequate autonomy from management, and sufficient resources to ensure that the company’s compliance program is implemented effectively. Adequate autonomy generally includes direct access to an organization’s governing authority, such as the board of directors and committees of the board of directors.”

This Hallmark was significantly expanded in both the Evaluation of Corporate Compliance Program (Evaluation) and the new FCPA Corporate Enforcement Policy (Policy). The DOJ’s Evaluation made the following query about the CCO position: **Prong 3. Autonomy and Resources**

**Stature** – *How has the compliance function compared with other strategic functions in the company in terms of stature, compensation levels, rank/title, reporting line, resources, and access to key decision-makers? What has been the turnover rate for compliance and relevant control function personnel? What role has compliance played in the company’s strategic and operational decisions?*

**Autonomy** – *Have the compliance and relevant control functions had direct reporting lines to anyone on the board of directors? How often do they meet with the board of directors? Are members of the senior management present for these meetings? Who reviewed the performance of the compliance function and what was the review process? Who has determined compensation/bonuses/raises/hiring/termination of compliance officers? Do the compliance and relevant control personnel in the field have reporting lines to headquarters? If not, how has the company ensured their independence?*

In the Policy, the DOJ laid out additional factors around CCO authority:

1. The quality and experience of the personnel involved in compliance, such that they can understand and identify the transactions and activities that pose a potential risk;
2. The authority and independence of the compliance function and the availability of compliance expertise to the board;
3. The compensation and promotion of the personnel involved in compliance, in view of their role, responsibilities, performance, and other appropriate factors; and
4. The reporting structure of any compliance personnel employed or contracted by the company.

Clearly the DOJ is articulating that it expects true compliance professionals, who understand the way compliance interacts with and supports the business. The days of a law school trained CCO who cannot read a spreadsheet are consigned to the dustbin of non-compliant history. But more than simply compliance professionalism, companies must compensate and promote compliance professionals within their organization. Simply burying someone in the compliance function of a law department because they cannot cut it will no longer suffice.

There is a new requirement for compliance “independence”. The DOJ has not taken a position on whether a General Counsel (GC) can also be the CCO. However, this new language would seem to signal the death knell for the dual GC/CCO role. It may also signal the larger issue that the CCO should have a separate reporting line to the Board, apart from through the GC. While the DOJ’s stated position that it does not concern itself with whether the CCO reports to the GC or reports independently, it is more concerned about whether the CCO has the voice to go to the Chief Executive Officer (CEO) or Board of Directors directly not via the GC. Even if the answer were yes, the DOJ would want to know if the CCO has ever exercised that right. Yet the Evaluation comes as close to any time previously in articulating a DOJ policy that the CCO be independent of the GC’s office. Therefore, if your CCO still reports up through the GC, you must have demonstrable evidence of both CCO independence and actual line of sight authority to the Board.

[Mike Volkov](#) has said of this change, “The new language includes the addition of “authority” of the compliance function, and the reporting relationship of the compliance function to the board of directors. I am not trying to make a mountain out of a molehill but the term “authority” reinforces the overall trend of maintaining an empowered CCO in corporate governance structures. Additionally, the CCO’s access to the board and regular reporting to the board is emphasized with the new language and reflects increasing concern over the importance of regular reporting by the CCO to the board.”

Here are some questions you should consider in evaluating this prong. First and foremost, is the CCO a part of the senior management or the C-Suite? Is the CCO part of regular meetings of this group? Who can terminate the CCO; is it the CEO, the Audit Committee of the Board or does CCO termination require approval of the entire Board? Most importantly, could a person under investigation or even scrutiny by the CCO fire the CCO? If the answer is yes, the CCO clearly does not have requisite independence.

Additional questions to consider are (a) Who can over-rule a decision by a CCO within an organization? and (b) Who is making the decisions around salary and compensation for the CCO? Is it the CEO, the GC, the Audit Committee of the Board or some other person or group?

Once again for the compliance professional, the Policy makes the importance of a best practices compliance program even more critical. The DOJ is focusing more on the role, expertise and how the compliance function is treated within an organization. Pay your CCO considerably less than your GC? You may now better be able to justify that discrepancy. If you have a legal department budget of \$3MM and compliance department budget of \$500,000; you may be starting behind the 8-ball.

The Evaluation and the Policy build upon the 10 Hallmarks of an Effective Compliance Program and demonstrate the continued evolution in the thinking of the DOJ around the CCO position and the compliance function. Their articulated inquiries can only strengthen the CCO position specifically and the compliance profession more generally. The more the DOJ talks about independence, coupled with resources being made available and authority concomitant with the CCO position, the more corporations will see it is directly in their interest to provide the resources, authority and gravitas to compliance positions in their organizations.

### **Three Key Takeaways**

1. How can you show compliance really has a seat at the senior executive table?
2. What are the professional qualifications of your CCO?
3. Does your CCO have true independence to report directly to the Board of Directors?

## **B. Compliance Function in an Organization**

The role of the compliance professional and the compliance function in a corporation has steadily grown in stature and prestige over the years. In the 2012 FCPA Guidance (Guidance), under Hallmark Three of the 10 Hallmarks of an Effective Compliance Program (Hallmarks), the focus was articulated by the title ***Oversight, Autonomy, and Resources***. When it came to the corporate compliance function the Guidance simply noted the government would “consider whether the company devoted adequate staffing and resources to the compliance program given the size, structure, and risk profile of the business.”

This Hallmark was significantly expanded in both the Department of Justice’s (DOJ’s) Evaluation of Corporate Compliance Programs (Evaluation) and the new FCPA Corporate Enforcement Policy (Policy). The Evaluation made the following query about the CCO position:

### **3. Autonomy and Resources**

***Compliance Role*** – *Was compliance involved in training and decisions relevant to the misconduct? Did the compliance or relevant control functions (e.g., Legal, Finance, or Audit) ever raise a concern in the area where the misconduct occurred?*

***Empowerment*** – *Have there been specific instances where compliance raised concerns or objections in the area in which the wrongdoing occurred? How has the company responded to such compliance concerns? Have there been specific transactions or deals that were stopped, modified, or more closely examined as a result of compliance concerns?*

***Funding and Resources*** – *How have decisions been made about the allocation of personnel and resources for the compliance and relevant control functions in light of the company’s risk profile? Have there been times when requests for resources by the compliance and relevant control functions have been denied? If so, how have those decisions been made?*

The Evaluation added one new set of queries based upon the evolution of corporate compliance programs since 2012.

**Outsourced Compliance Functions** – *Has the company outsourced all or parts of its compliance functions to an external firm or consultant? What has been the rationale for doing so? Who has been involved in the decision to outsource? How has that process been managed (including who oversaw and/or liaised with the external firm/consultant)? What access level does the external firm or consultant have to company information? How has the effectiveness of the outsourced process been assessed?*

In the Policy, the DOJ listed the following as factors relating to a corporate compliance function, that it would consider as indicia of an effective compliance and ethics program:

1. The resources the company has dedicated to compliance;
2. The quality and experience of the personnel involved in compliance, such that they can understand and identify the transactions and activities that pose a potential risk;
3. The authority and independence of the compliance function and the availability of compliance expertise to the board;
4. The compensation and promotion of the personnel involved in compliance, in view of their role, responsibilities, performance, and other appropriate factors; and
5. The reporting structure of any compliance personnel employed or contracted by the company.

1 and the first half of 3 come from the 10 Hallmarks of an Effective Compliance Program. Points 2, the second half of 3, 4 and 5 come from the DOJ's FCPA Pilot Program, Part 3 entitled, "Timely and Appropriate Remediation in FCPA Matters". Clearly the DOJ is articulating that in an operationalized compliance program, it expects true compliance professionals, who understand the way compliance interacts with and supports the business. Companies must compensate and promote compliance professionals within their organization.

### ***Funding and Resources***

You will now have to justify your corporate compliance spend. This means at a minimum you will have to meet some general industry standard. If a corporation tries to low-ball both the pay to compliance professionals, as well as the dollar and head count made available to a compliance function, it will not be viewed positively. Also noted in the Evaluation, a company must be prepared to defend any request for compliance resources which are turned down. Budget requests and allocations are always difficult times in any corporation. There is never enough money to go around and most senior management thinks it is their job to slash all budget requests as a simple matter of course. Now such blanket management will be penalized.

If a compliance function is so hampered by resource restrictions it cannot carry out the basic functions needed for a compliance program to operate, it will not find favor under either the Evaluation or the Policy. If there are compliance projects needed to address basic compliance

risks which are not funded because management failed to heed a Chief Compliance Officers (CCO) or compliance functions budget request, this could be evidence of conscious indifference by senior management.

### ***Role of Compliance and Empowerment***

More than simply throwing money at the compliance function (as if that would ever happen) the DOJ is now inquiring into how the compliance function and its recommendations are treated. If there is business unit over-ride of compliance decisions, there must be an auditable decision trail. This, of course, is anathema to corporate executives who do not want to put themselves at risk.

But more than simply preventing management over-ride, a corporate compliance function has to be empowered by the Board and Chief Executive Officer (CEO) to intervene in business decisions that implicate the company's ethics and compliance issues, compliance with business code of ethics, agent/distributor and supplier codes of conduct, training, communication and internal investigations. If a company considers a business decision or practice that implicates the company's ethical principles, the compliance function must have the internal authority to weigh in and ensure that ethical principles and compliance issues are factored into the business decision.

### ***Outsourcing of Compliance***

This area of compliance practice has arisen largely since the articulation of the Hallmarks in the Guidance. While this might make sense from a cost perspective, it can be largely problematic if it is not managed properly. Rarely do outsiders have the same access as corporate employees, particularly in a function as important as compliance. Additionally, there will never be the trust level with outsiders there is with someone who wears the same color shirt as the employees. Here a company must not only have a rationale in place, which will largely be cost-savings; a company must also have a mechanism in place to assess, on an ongoing basis, any outsourced compliance function. This will be beyond the reach of probably 99% of the companies engaged in such outsourcing.

The Evaluation and new FCPA Corporate Enforcement Policy both demonstrate the continued evolution in the thinking of the DOJ around the corporate compliance function. Their articulated inquiries can only strengthen a corporate compliance function specifically; and the compliance profession more generally. The more the DOJ talks about the independence of the compliance function, coupled with resources being made available and authority concomitant with the corporate compliance function, the more corporations will see it is directly in their interest to provide the resources, authority and gravitas to compliance position in their organizations.

### **Three Key Takeaways**

1. How is compliance treated in the budget process?
2. Has your compliance function had any decisions over-ridden by senior management?

3. Beware outsourcing of compliance as any such contractor must have access to company documents and personnel.