

The Corporate Compliance Monitor's Role in Regulatory Settlement Agreements

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Former Siemens Managing Board Director, Uriel Sharef, conspired with several executives to make approximately $1.4 billion in payments to government officials around the world in direct violation of the Foreign Corrupt Practices Act ("FCPA"). Siemens' top management, aware of ongoing internal investigations, did little to strengthen the company's internal compliance program. As a result, Siemens pleaded guilty to criminal violations of the FCPA brought by the Department of Justice ("DOJ") and agreed to pay fines of $448.5 million and an additional $1.15 billion to settle charges brought by the Securities and Exchange Commission ("SEC"). In addition, Siemens agreed to the appointment of a corporate monitor to ensure the implementation of a robust and functioning compliance program focusing on internal controls that would seek to avoid future violations of the FCPA and other regulatory measures.

As exemplified in the Siemens matter, the use of corporate monitors by judicial and regulatory government agencies as an instrument for verifying an organization's compliance with settlements agreements and orders resolving corporate criminal or regulatory accountability continues to rise. From 1993 through September 2009, companies agreed to the implementation of a corporate monitor 30% of the time in DOJ or SEC deferred prosecution agreements ("DPA") and non-prosecution agreements ("NPA").[1] From 2004 through 2010, the use of a corporate monitor increased to over 40%.[2] Corporate monitors are also frequently used in non-criminal matters, such as in mergers or acquisitions, where a regulator may want to ensure adherence to the terms of an agreement. It is expected that corporate monitors will continue to be used as a way for the government to track compliance with settlement agreements and that their use will continue to rise in-line with more recent utilization.

This article will help to define a corporate monitor, how a monitor is selected, the responsibilities of a monitor after its selection, and the effectiveness of a monitor in assisting companies enhance its corporate compliance programs.

Corporate Monitors Defined

Corporate monitors are primarily responsible for assessing and reporting to a government agency on the effectiveness of the corporate compliance and ethics programs of companies that have had significant legal or regulatory issues resolved by DPA, NPA, and administrative settlements (collectively "Settlement Agreements"), among others. Judge Rakoff, in his judgment in the *SEC v. WorldCom, Inc.*, stated:

[1] Warin, F. J., Diamant, M. S., & Root, V. S. "Somebody's Watching Me: FCPA Monitorships and How They Can Work Better." *University of Pennsylvania Journal of Business Law* 13:2 321, 328 (2011).
[2] Ibid. at 322.

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While the Corporate Monitor's efforts were initially directed at preventing corporate looting and document destruction, his role and duties have steadily expanded, with the parties' full consent, to the point where he now acts not only as financial watchdog (in which capacity he has saved the company tens of millions of dollars) but also as an overseer who has initiated vast improvements in the company's internal controls and corporate governance.[3]

In other words, the corporate monitor's roll is to ensure that the company not only meets the financial terms of its settlement agreement, but, more importantly, how the company enhances its compliance and ethics program, policies, procedures, and processes to not allow the same issues to occur again.

Selection of a Corporate Monitor

Not all cases require the appointment of a corporate monitor. The selection begins with the identification of a need for a corporate monitor and there are a set of factors that the DOJ and SEC consider when determining whether a monitor is appropriate. These factors include:

- Severity of the offense
- Duration of the misconduct
- Pervasiveness of the misconduct, including whether the conduct cuts across geographic and/or product lines
- Nature and size of the company
- Quality of the company's compliance program at the time of the misconduct
- Subsequent remediation efforts[4]

Once the need for a corporate monitor is identified, a selection process that evaluates the qualifications of the proposed monitor ensues. These specifications include:

- The necessary qualifications for a monitor based on the facts and circumstances of the case
- The monitor must be selected based on the merits
- The selection process should be designed to: 1) select a highly qualified and respected person or entity based on suitability for the assignment and all of the circumstances; 2) avoid potential and actual conflicts of interests; and 3) otherwise instill public confidence[5]

A fair amount of emphasis is placed on avoiding conflicts of interest and perceived conflicts of interest.[6] The term of a corporate monitor spans anywhere from a few months to many years, with an average of between 18 and 36 months.[7]

Guidelines Governing a Corporate Monitor

Once a corporate monitor is in place, it is duty bound to adhere to certain principles, a number of which are outlined below.

Independence: The monitor must be an independent third party, not an employee or agent of the company or the Government.

Oversight: The monitor should regularly assess the company's compliance with the terms of the Settlement Agreement(s) designed to reduce the risk of recurrence of the company's misconduct, including internal controls, corporate ethics, and compliance programs.

Scope of Oversight: The monitor should address the areas of misconduct covered by the Settlement Agreement(s) and the scope of work should be no broader than necessary to address and reduce the risk of recurrence of the company's misconduct.

Reporting: The Government, the company, and the monitor should communicate freely and the monitor should make periodic written reports where appropriate.

Implementation of Monitor's Recommendations: The company is not required to implement the recommendations of the monitor. However, the Government must be notified if the company refuses and may consider this in evaluating whether the company has satisfied its obligations under its Settlement Agreement(s).

Recurrence of Misconduct: The Settlement Agreement(s) should clearly identify the types of misconduct that should be reported directly to the Government. The monitor shall also have discretion to report evidence of other misconduct to the Government, the company, or both.

Duration: The duration of the monitor's appointment should be specific to the problems that exist and the types of measures necessary for the monitor to satisfy its mandate.

Extension and Early Termination: The Settlement Agreement(s) should provide for an extension of the monitor's service at the discretion of the Government and should provide for early termination when appropriate.[8]

[3] *SEC v. WorldCom, Inc.*, 273 F. Supp. 2d 431, 432 (S.D.N.Y. 2003).
[4] Criminal Division of the U.S. Department of Justice and Enforcement Division of the U.S. Securities and Exchange Commission. *A Resource Guide to the U.S. Foreign Corrupt Practices Act* p. 71 (2012).
[5] Morford, Craig. "Selection and Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations." *Criminal Resource Manual* 163 (March 7, 2008).
[6] Ibid.
[7] Ford, Christie & Hess, David. "Can Corporate Monitorships Improve Corporate Compliance?" *The Journal of Corporation Law* 34:3, 679, 683 (2009).
[8] Morford, Craig. "Selection and Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations." *Criminal Resource Manual* 163 (March 7, 2008).

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Execution of a Corporate Monitor's Responsibilities

The corporate monitor begins executing its duties by developing a work plan that will include a timeline for reaching certain milestones such as:

- Receipt and review of documents and information relevant to the company's compliance and ethics program, as well as reports or investigations discussing past misconduct
- Interviews and discussions with the Board of Directors, Audit Committee, senior management, and company personnel
- Identification of markets or geographies for potential site visits
- Deadlines for informal and formal reporting of the corporate monitor's findings

Inherent in the corporate monitor's work plan is the ability to learn about and get to know the company, the company's clients or customers, and the people in the company. This allows the corporate monitor to ascertain the culture and risk tolerance throughout the company.

After finalization of the work plan, the corporate monitor will begin executing that work plan. Assessing the compliance of the company is the main duty of the corporate monitor. To that end, a continuous and open line of communication between the corporate monitor, the company, and the Government will only help to facilitate a robust and productive monitorship.

An accurate assessment of the company's adherence to the settlement agreement requires truthful and exact reporting of a corporate monitor's observations to the company and the regulatory body. This is in the best interest of the company and the monitor. The formalized communication of this assessment is usually the final step in a monitor's work plan, or at least a major milestone along the path of the work plan.

Effectiveness of Corporate Monitors

The mere presence of a corporate monitor can help to change the culture of a company and how it approaches its internal controls and compliance and ethics programs. Corporate monitors force the company to direct attention and resources to compliance and ethics that more often than not were missing historically. With the introduction of a corporate monitor, companies are routinely obligated to implement stronger internal controls and fortify their compliance programs. This emphasis on compliance and ethics can only help to create a stronger control system throughout the company. Both the regulatory body and the company routinely come out ahead because both entities do not have to expend what would otherwise be a large amount of resources on an investigation and trial.

While there are a number of perceived benefits to monitorships, companies have voiced their concerns in appointing a corporate monitor. Some companies worry about "scope creep," wherein the company and corporate monitor disagree about the extent of the corporate monitor's role and purview. However, since 2010, the DOJ has recommended including language in any Settlement Agreements that would explain what role the DOJ can play in resolving any disagreements between the corporate monitor and the company.[9]

Another concern is the inherent disruption that a corporate monitor can have on existing operations. Much of this disruption will occur in the form of time and resources that would otherwise be dedicated to other corporate functions. For example, a large amount of time will be spent by the individuals liaising with the corporate monitor. In addition, the members of the Board of Directors and senior management will invariably be asked to contribute some of their already limited time to discussions and even reorganization of the compliance and ethics function.

Finally, the cost of the corporate monitor is paid for by the company. The length of the monitorship, the complexity of the Settlement Agreement(s), the state of the company's existing compliance and ethics program, and the geographic markets and industries in which the company operates will dictate the cost. More often than not, however, this cost is far less than what the company would otherwise pay in fines, possible debarment, or legal fees in defending an enforcement action through trial.

Conclusion

Although corporate monitors are often perceived as outsiders looking to "catch" a company in an act of misconduct, in reality the monitor can bring great value to all parties involved in a Settlement Agreement. Allowing an independent third party to take an unbiased look at the practices of a company's ethics and compliance program, and adherence to the terms and conditions of a Settlement Agreement, can often save the parties millions of dollars. The monitor's ultimate value can be seen in the recommendations and implementation of best practices previously employed in other similarly situated companies and as outlined by regulators.

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[9] Grindler, Gary. "Additional Guidance on the Use of Monitors in Deferred Prosecution Agreements and Non-Prosecution Agreements with Corporations." *Criminal Resource Manual* 166 (May 25, 2010).

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