

# In Search of Effective Ethics & Compliance Programs

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## I. INTRODUCTION

In 1991, the U.S. Sentencing Commission's Organizational Guidelines<sup>1</sup> provided firms strong financial incentives to have effective ethics and compliance programs ("ethics programs").<sup>2</sup> Since then, compliance has become big business.<sup>3</sup> To incentivize compliance, some statutes require public firms to disclose their compliance efforts.<sup>4</sup>

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1. U.S. SENTENCING GUIDELINES MANUAL ch. 8 (2013). The U.S. federal courts, while not bound to apply the Guidelines, must take them into account when sentencing organizations for felony and Class A misdemeanor offenses. *Id.* at § 8A1.1. An organization means "a person other than an individual." 18 U.S.C. § 18 (2013). This includes "corporations, partnerships, associations, joint-stock companies, unions, trusts, pension funds, unincorporated organizations, governments and political subdivisions thereof, and non-profit organizations." USSG § 8A1.1, app. n.1 (2013).

2. *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 969 (Del. Ch. 1996) (observing the Guidelines' "powerful incentives for corporations today to have in place compliance programs to detect violations of law, promptly to report violations to appropriate public officials when discovered, and to take prompt, voluntary remedial efforts"); Hon. Patti B. Saris, Chair, U.S. Sentencing Comm'n, Comments at the 12th Annual Compliance & Ethics Institute (Oct. 7, 2013), [http://www.ussc.gov/Guidelines/Organizational\\_Guidelines/Special\\_Reports/saris-remarks-annual-compliance-and-ethics-institute.pdf](http://www.ussc.gov/Guidelines/Organizational_Guidelines/Special_Reports/saris-remarks-annual-compliance-and-ethics-institute.pdf) (noting the Commission's goal "that organizations would come to view this organizational guideline scheme as a powerful financial reason for instituting effective internal compliance programs that, in turn, would minimize the likelihood that the organization would run afoul of the law in the first instance"); CORPORATE LEGAL COMPLIANCE HANDBOOK § 1.04 (2013), 2013 WL 6846847 (concluding that "[t]he combination of the *Caremark* decision, the Sarbanes-Oxley Act, and the revised Sentencing Guidelines now make it more than just a good idea for a corporate board to ensure that its company has an effective compliance program").

3. ETHICS RESOURCE CENTER, *The Federal Sentencing Guidelines for Organizations at Twenty Years: A Call to Action for More Effective Promotion and Recognition of Effective Compliance and Ethics Programs* 29 (2012), <http://www.ethics.org/files/u5/fsgo-report2012.pdf> [hereinafter ERC Report] (noting how the Ethics and Compliance Officer Association grew between 1992 and 2012 from 19 members to over 1,200 members "exclusively comprised of in-house compliance/ethics professionals" and how the Society of Corporate Compliance and Ethics, "a nine-year old group that certifies compliance/ethics professionals, has more than 2,800 members comprised of both in-house and outside compliance/ethics practitioners"); Press Release, Financial Executives International, FEI Survey: Average 2007 SOX Compliance Cost \$1.7 Million (Apr. 30, 2008), available at [http://www.financialexecutives.org/KenticoCMS/News—Publications/Press-Room/2008-press-releases/FEI-Survey—Average-2007-SOX-Compliance-Cost-\\$1-7-.aspx#ixzz2a5AeoQlh](http://www.financialexecutives.org/KenticoCMS/News—Publications/Press-Room/2008-press-releases/FEI-Survey—Average-2007-SOX-Compliance-Cost-$1-7-.aspx#ixzz2a5AeoQlh) (finding from its Sarbanes-Oxley compliance survey of 185 companies, whose annual revenues averaged \$4.7 billion, that average compliance cost for Section 404 during fiscal year 2007 was \$1.7 million); Peter J. Henning, *Lessons From the Glaxo Case in China*, N.Y. TIMES (July 29, 2013), <http://dealbook.nytimes.com/2013/07/29/lessons-from-the-glaxosmithkline-case-in-china/> ("Over the last decade, since the passage of the Sarbanes-Oxley Act in 2002, publicly traded corporations have poured significant resources into their compliance programs to prevent wrongdoing, or to at least be an early warning system for what might become a problem.").

4. Sarbanes-Oxley Act §§ 101(c)(2), 101(g)(3), 103(a), 302, 404 & 406 Pub. L. No. 107-204, 116 Stat. 745 (2002). Sarbanes-Oxley also directed the Sentencing Commission to review and amend the Guidelines to ensure they were "sufficient to deter and punish organizational criminal misconduct." Sarbanes-Oxley Act §

Directors of Delaware corporations owe a duty “to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists.”<sup>5</sup> Companies listed on the New York Stock Exchange<sup>6</sup> and NASDAQ<sup>7</sup> must have an ethics code.

But unethical and illegal corporate conduct is still pervasive. The economic crisis heightened concerns of widespread unethical and illegal conduct among financial institutions, ineffectual compliance, and corporate crime.<sup>8</sup> Thus, the current debate is over what the government can and should do to promote corporate compliance.

One issue is whether a firm should be liable when its employees violate the firm’s express compliance instructions and ethics code. A firm can argue that if it is ultimately responsible for any damages its agent causes, then the agent’s conduct is not intended for the firm’s benefit.<sup>9</sup> This argument proves too much. An ethics program would shelter

805(a)(2)(5).

5. *Caremark*, 698 A.2d at 970 (noting the importance “that the board exercise a good faith judgment that the corporation’s information and reporting system is in concept and design adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations, so that it may satisfy its responsibility” and that “failure to do so under some circumstances may, in theory at least, render a director liable for losses caused by non-compliance with applicable legal standards”); see also *Stone ex rel. AmSouth Bancorp. v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (“Where directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith.”) (internal footnotes omitted). As Wal-Mart Stores, Inc. reported on its bribery scandal, “a number of derivative complaints have been filed in Delaware and Arkansas, also tracking the allegations of the [*New York Times*] story, and naming various current and former officers and directors as additional defendants. The plaintiffs in the derivative suits (in which the Company is a nominal defendant) allege, among other things, that the defendants who are or were directors or officers of the Company breached their fiduciary duties in connection with oversight of FCPA compliance.” Wal-Mart Stores, Inc., Annual Report (Form 10-K) at 25 (Mar. 26, 2013), <http://www.sec.gov/Archives/edgar/data/104169/000010416913000011/wmt10-k.htm>.

6. See NYSE LISTED COMPANY MANUAL § 303A, NYSE (Nov. 25, 2009), [http://nysemanual.nyse.com/LCMTTools/TOCchapter.asp?manual=/lcm/sections/lcmsections/chp\\_1\\_4/default.asp&selectedNode=chp\\_1\\_4\\_3](http://nysemanual.nyse.com/LCMTTools/TOCchapter.asp?manual=/lcm/sections/lcmsections/chp_1_4/default.asp&selectedNode=chp_1_4_3) (requiring listed companies to “adopt and disclose a code of business conduct and ethics for directors, officers and employees, promptly disclose any waivers of the code for directors or executive officers” and “proactively promote compliance with laws, rules and regulations, including insider trading laws”).

7. NASDAQ Rule 4350(n), [http://www.sec.gov/rules/other/nasdaqllcf1a4\\_5/nasdaqllcamendrules4000.pdf](http://www.sec.gov/rules/other/nasdaqllcf1a4_5/nasdaqllcamendrules4000.pdf) (last visited Apr. 20, 2014) (“Each company must adopt a code of conduct applicable to all directors, officers and employees. The code must satisfy the definition of a ‘code of ethics’ . . . set out in the Sarbanes-Oxley Act of 2002, and it must be publicly available. A company may adopt multiple codes applicable to different types of employees. Any waivers to the Code of Conduct made to directors or executive officers must be approved by the board and publicly disclosed.”).

8. See, e.g., Nico W. Van Yperen et al., *To Win, or Not to Lose, At Any Cost: The Impact of Achievement Goals on Cheating*, 22 BRIT. J. MGMT. S5, S5 (2011) (“The numerous ethical scandals concerning high-profile firms and business executives but also outcomes of scientific research have raised many concerns about the emergence of unethical and irresponsible behaviour in organizations.”); MICHAEL D. GREENBERG, PERSPECTIVES OF CHIEF ETHICS AND COMPLIANCE OFFICERS ON THE DETECTION AND PREVENTION OF CORPORATE MISDEEDS: WHAT THE POLICY COMMUNITY SHOULD KNOW, RAND CENTER FOR CORPORATE ETHICS AND GOVERNANCE (2009); Blake E. Ashforth et al., *Re-Viewing Organizational Corruption*, 33 ACAD. MGMT. REV. 670, 670 (2008).

9. The legal doctrine of *respondeat superior* already affects a firm’s compliance efforts. A firm may be criminally liable for the actions of its agents, who were acting within the scope of their authority, or apparent authority, and who intended, at least in part, for the firm to benefit. See, e.g., *United States v. Ionia Mgmt. S.A.*, 526 F. Supp. 2d 319, 323–24 (D. Conn. 2007), *aff’d* 555 F.3d 303 (2d Cir. 2009) (summarizing the legal

firms from criminal liability, thereby lessening their incentive to comply with the law. Moreover, many corporate crimes, such as price-fixing and bribery, can benefit the firm—at least initially—and violate its compliance code. Consequently, an ethics program cannot automatically immunize firms from criminal liability.<sup>10</sup>

A second issue is the extent to which courts and agencies should consider a firm's ethics program (or its absence) in determining the appropriate fine and other penalties.<sup>11</sup> A third issue is whether the agencies and courts should require firms in any settlement or sentence to implement an ethics program. If so, can the agencies and courts accurately assess whether the firm is indeed implementing an effective ethics program?<sup>12</sup>

No consensus exists on these issues. Some argue that firms should be criminally liable only if the prosecutor proves beyond a reasonable doubt that the firm “failed to have reasonably effective policies and procedures to prevent the conduct.”<sup>13</sup> A second approach is to provide firms an affirmative defense for their compliance efforts.<sup>14</sup> A third approach is that an ethics program is legally relevant, but not determinative, in determining corporate liability and sentencing.<sup>15</sup> A fourth approach is to leave ethics

doctrine of *respondeat superior*); *United States v. Koppers Co.*, 652 F.2d 290, 298 (2d Cir. 1981) (defining a firm's agent as “an officer of the corporation or an agent of the corporation having duties of such responsibility that his conduct may fairly be assumed to represent the corporation”); *United States v. Automated Med. Labs.*, 770 F.2d 399, 407 (4th Cir. 1985) (noting the purpose in “requiring that an agent have acted with the intent to benefit the corporation . . . is to insulate the corporation from criminal liability for actions of its agents which be *inimical* to the interests of the corporation or which may have been undertaken solely to advance the interests of that agent or of a party other than the corporation”). Accordingly, juries can consider a firm's compliance policy in determining whether its employees intended, at least in part, for the firm to benefit: “If you find that the agent was acting within the scope of his employment, the fact that the agent's act was illegal, contrary to his employer's instructions, or against the corporation's policies will not relieve the corporation of responsibility for it. However, you may consider the fact that the agent disobeyed instructions or violated company policy in determining whether the agent intended to benefit the corporation, or was acting within this authority.” *Ionia Mgmt.*, 526 F. Supp. 2d at 324 (quoting 1 LEONARD B. SAND ET AL., MODERN FEDERAL JURY INSTRUCTIONS—CRIMINAL ¶ 2.01, Instr. 2-7 (2007)).

10. *United States v. Twentieth Century Fox Film Corp.*, 882 F.2d 656, 660 (2d Cir. 1989); *United States v. Basic Const. Co.*, 711 F.2d 570, 573 (4th Cir. 1983) (holding that a corporation may be held criminally responsible for violations committed by its employees “if they were acting within the scope of their authority, or apparent authority, and for the benefit of the corporation, even if . . . such acts were against corporate policy or express instructions”).

11. Organisation for Economic Co-operation and Development, *Policy Roundtable: Promoting Compliance with Competition Law* 2011, OECD, at 22 (Mar. 27, 2012) [hereinafter OECD], available at <http://www.oecd.org/daf/competition/promotingcompliancewithcompetitionlaw2011.pdf>.

12. David M. Uhlmann, *Deferred Prosecution and Non-Prosecution Agreements and the Erosion of Corporate Criminal Liability*, 72 MD. L. REV. 1295, 1327 (2013).

13. Brief for the Association of Corporate Counsel et al. as Amici Curiae Supporting Appellant, *United States v. Ionia Mgmt. S.A.*, No. 07-5801-CR, 2008 WL 8626038, at \*23 (2d Cir. June 12, 2008) (quoting Andrew Weissmann & David Newman, *Rethinking Criminal Corporate Liability*, 82 IND. L.J. 411, 414 (2007)).

14. MODEL PENAL CODE § 2.07(5) (1962) (stating that defendant can prove “by a preponderance of evidence that the high managerial agent having supervisory responsibility over the subject matter of the offense employed due diligence to prevent its commission”); Ellen S. Podgor, *Educating Compliance*, 46 AM. CRIM. L. REV. 1523, 1529 n.39 (2009) (collecting scholarship advocating “a good faith defense” where the company took sufficient measures to comply with the law but an employee failed to abide to the established company norms).

15. CANADA COMPETITION BUREAU, *Bulletin: Corporate Compliance Programs*, 14 (Sept. 2010), available at [http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/CorporateCompliancePrograms-sept-2010-e.pdf/\\$FILE/CorporateCompliancePrograms-sept-2010-e.pdf](http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/vwapj/CorporateCompliancePrograms-sept-2010-e.pdf/$FILE/CorporateCompliancePrograms-sept-2010-e.pdf) [hereinafter CANADA COMPETITION BUREAU]; U.K. OFFICE OF FAIR TRADING, *Guidance: How Your Business Can Achieve Compliance With*

programs as a discretionary factor that prosecutors may consider.

Nor is there consensus within the U.S. Department of Justice (DOJ) on these issues. For many corporate crimes, such as the Foreign Corrupt Practices Act (FCPA) violations, the DOJ treats a compliance program as a potential exonerating or mitigating factor:

An assessment of a company's compliance program, including its design and good faith implementation and enforcement, is an important part of the government's assessment of whether a violation occurred, and if so, what action should be taken. In appropriate circumstances, DOJ and SEC may decline to pursue charges against a company based on the company's effective compliance program, or may otherwise seek to reward a company for its program, even when that program did not prevent the particular underlying FCPA violation that gave rise to the investigation.<sup>16</sup>

One notable exception is antitrust, which often involves corporate liability and significant criminal fines.<sup>17</sup> The DOJ does not factor the firm's compliance efforts in determining the antitrust liability<sup>18</sup> or fine.<sup>19</sup> For the DOJ's Antitrust Division, "the true benefit of compliance programs is to prevent the commission of antitrust crimes, not to enable organizations that commit such violations to avoid prosecution for them."<sup>20</sup> Thus, ethics programs play a "very limited role" when the DOJ exercises its prosecutorial discretion for antitrust crimes.<sup>21</sup> To increase compliance, some argue that the Antitrust Division should adopt and promote the Guidelines' incentive,<sup>22</sup> but others disagree.<sup>23</sup>

*Competition Law*, 31–32 (June 2011) [hereinafter OFT Guidance], available at [http://oft.gov.uk/shared\\_oft/cand-cartels/competition-awareness-compliance/oft1341.pdf](http://oft.gov.uk/shared_oft/cand-cartels/competition-awareness-compliance/oft1341.pdf) (firm can seek to reduce its penalty by providing evidence of the "adequate steps" it took to achieve "a clear and unambiguous commitment to competition law throughout the organisation, risk identification, risk assessment, risk mitigation, and review").

16. CRIMINAL DIV. OF THE U.S. DEP'T OF JUSTICE & ENFORCEMENT DIV. OF THE U.S. SECURITIES & EXCH. COMM'N, *FCPA: A RESOURCE GUIDE TO THE U.S. FOREIGN CORRUPT PRACTICES ACT 56* (2012), available at <http://www.justice.gov/criminal/fraud/fcpa/guide.pdf> [hereinafter FCPA Guide]; see also U.S. DEP'T OF JUSTICE, U.S. ATTORNEYS' MANUAL: PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS § 9-28.800 (Aug. 2008), available at <http://www.justice.gov/opa/documents/corp-charging-guidelines.pdf> [hereinafter U.S. ATTORNEYS' MANUAL] (laying out general considerations in prosecuting business organizations)

17. U.S. ATTORNEYS' MANUAL, *supra* note 16, at § 9-28.800 (noting "the nature of some crimes, e.g., antitrust violations, may be such that national law enforcement policies mandate prosecutions of corporations notwithstanding the existence of a compliance program").

18. *Id.* at § 9-28.400 (noting the Antitrust Division's firm and well-established policy, "understood in the business community, that credit should not be given at the charging stage for a compliance program and that amnesty is available only to the first corporation to make full disclosure to the government").

19. USSG §§ 2R1.1(d), 8A1.2, app. n.3(C).

20. Gary R. Spratling, Deputy Ass't Attorney General, Antitrust Div., U.S. Dep't of Justice, *The Experience and Views of the Antitrust Division* (Sept. 8, 1995), <http://www.justice.gov/atr/public/speeches/speech1grs.htm>.

21. *Id.* at Part II ("Once a violation occurs, a compliance program can do little, if anything, to persuade the Division not to prosecute the offense."). See William J. Kolasky, Deputy Ass't Attorney General, Antitrust Div., U.S. Dep't of Justice, *Antitrust Compliance Programs: The Government Perspective* (July 12, 2002), <http://www.justice.gov/atr/public/speeches/224389.htm> (explaining the Antitrust Division's guidance on what constitutes an effective compliance program).

22. See generally Joseph Murphy & William Kolasky, *The Role of Anti-Cartel Compliance Programs in Preventing Cartel Behavior*, 26 ANTITRUST 61 (2012) (advancing the Guidelines' incentive); D. Daniel Sokol, *Cartels, Corporate Compliance, and What Practitioners Really Think About Enforcement*, 78 ANTITRUST L.J.

Nor is there any consensus on when, and for which crimes, firms should be required to implement an ethics program. Some organizations condition leniency on the firm's adoption of an ethics program.<sup>24</sup> Some want the Antitrust Division to do the same.<sup>25</sup> But the Division does not require, as part of its leniency program, that applicants (even recidivists) implement an effective antitrust compliance program.<sup>26</sup> One plea agreement reflects the "apparent 'split personality' within the DOJ on the role of compliance programs."<sup>27</sup> Bridgestone Corporation (Bridgestone) violated both the Sherman Act and FCPA by conspiring to fix prices for over eight years and bribing foreign officials who worked in state-owned entities.<sup>28</sup> Bridgestone's antitrust and anti-bribery compliance efforts were clearly deficient. Yet the DOJ required Bridgestone to remedy the deficiencies only in its FCPA compliance policies.<sup>29</sup>

Nor is there a global consensus on the legal significance of corporate ethics programs in assessing liability and the appropriate fine.<sup>30</sup> Some jurisdictions, including the United Kingdom, France, Israel, Canada, and India, may reduce an antitrust offender's fine on account of its compliance efforts.<sup>31</sup> Other jurisdictions, notably the European Union, do not.<sup>32</sup>

Every jurisdiction encourages firms to promote compliance. But jurisdictions diverge over whether, when, and to what extent an ethics program should be an exonerating or mitigating factor. To help address this issue, this Article examines the

201, 225 (2012).

23. See generally Wouter P. J. Wils, *Antitrust Compliance Programmes and Optimal Antitrust Enforcement*, 1 J. ANTITRUST ENFORCEMENT 52 (2013) (arguing against an extrinsic incentive, such as the Guidelines', to antitrust offenses).

24. Firms with contracts related to projects financed or supported by the World Bank can avoid being barred ten years for their misconduct by disclosing their misconduct and adopting "a robust 'best practice' corporate governance Compliance Program," monitored for three years by a compliance monitor. World Bank, *VDP Guidelines for Participants* 8 (2011), [http://siteresources.worldbank.org/INTVOLDISPRO/Resources/VDP\\_Guidelines\\_2011.pdf](http://siteresources.worldbank.org/INTVOLDISPRO/Resources/VDP_Guidelines_2011.pdf). The firm breaches the terms and conditions of the World Bank's voluntary disclosure if it "[k]nowingly or recklessly fails to implement a Compliance Program." *Id.* at 12.

25. Murphy & Kolasky, *supra* note 22, at 63.

26. That may be changing. In 2012, "for the first time, the [D]ivision recommended that a criminal antitrust defendant be required, as a condition of its probation, to retain an independent corporate monitor to develop and implement an effective antitrust compliance program." BILL BAER, ASS'T ATTORNEY GENERAL, ANTITRUST DIV., U.S. DEP'T OF JUSTICE, Prepared for the Georgetown Law 7th Annual Global Antitrust Enforcement Symposium: *Remedies Matter: The Importance of Achieving Effective Antitrust Outcomes* (Sept. 25, 2013), 2013 WL 5429290 (F.T.C.), at \*6.

27. J. Thomas Rosch, Comm'r, Federal Trade Comm'n, U.S. Enforcement of the Foreign Corrupt Practices Act of 1977: Some Observations and Thoughts 23 (Sept. 13, 2012), <http://www.ftc.gov/speeches/rosch/120913FCPAenforcement.pdf>.

28. The FCPA generally "prohibits offering to pay, paying, promising to pay, or authorizing the payment of money or anything of value to a foreign official in order to influence any act or decision of the foreign official in his or her official capacity or to secure any other improper advantage in order to obtain or retain business." FCPA Guide, *supra* note 16, at 10.

29. Plea Agreement, United States v. Bridgestone Corp., Attachment B (Corporate Compliance Program), No. 4:11-cr-00651 (S.D. Tex. Oct. 5, 2011), available at <http://www.justice.gov/criminal/fraud/fcpa/cases/bridgestone/10-05-11bridgestone-plea.pdf>.

30. See, e.g., OECD, *supra* note 11, at 18 (observing the lack of international consensus on whether corporate antitrust violators should receive lighter or stiffer sanctions based on their compliance efforts).

31. *Id.* at 19.

32. *Id.* at 19 n. 80; Wils, *supra* note 23, at 2.

underlying problem: why, despite the Guidelines' financial incentive, do ineffective compliance and corporate crime persist?

Part II outlines the problem. Firms have independent reasons to exercise due diligence to prevent and detect criminal conduct and promote an organizational culture that encourages ethical conduct and a commitment to comply with the law. Moreover, for over 20 years, the Guidelines promoted a financial incentive to induce firms to develop an ethical organizational culture. Nonetheless, many firms' compliance efforts remain ineffective, and corporate crime persists.

Part III explores whether the problem of ineffective compliance is attributable to three assumptions underlying the Guidelines, namely: (i) an ethics program can effectively deter and prevent unethical and illegal conduct; (ii) an effective ethics program is attainable; and (iii) courts and agencies can distinguish between effective and otherwise ineffective or sham ethics programs. The empirical research, while developing, suggests that compliance efforts can be effective, and that effective compliance is attainable. Although several criteria that the courts and DOJ use to assess ethics programs raise concerns, the problem does not stem from these three assumptions.

Part IV then identifies one important, yet unexplored, reason why corporate compliance, despite the Guidelines' incentive, remains ineffective. To promote compliance, the courts and the DOJ take an extrinsic, incentive-based approach, which assumes that compliance is primarily undertaken for the Guidelines' financial incentive. Compliance is perceived as a "cheap insurance policy" against later liability.<sup>33</sup> Parts IV.A and B discuss the inherent difficulties in telling firms exactly what they must do to earn the Guidelines' incentive, and in articulating objective, easy-to-administer standards to assess compliance efforts. Parts IV.C and D examine how an extrinsic, incentive-based approach can encumber an ethical organizational culture.

Rather than mix two approaches, the government, as Part V proposes, should consistently promote an intrinsic, ethics-based approach. Here, the expectation is that a firm seeks an ethical organizational culture for its own end, for a strategic competitive advantage, or to prevent being competitively disadvantaged.

The available information—economic logic, sentencing data, behavioral insights, survey results, and (most importantly) the persistence of significant corporate crime—indicates that the current extrinsic, incentive-based approach to compliance is ineffective. The alternative—an intrinsic, ethics-based approach—is already in the Guidelines but is de-emphasized. It should be given greater emphasis. To be sure, there is no definitive evidence that an intrinsic, ethics-based approach will necessarily foster an ethical organizational culture across firms. However the current approach is not working, and there are important reasons to believe, based on the behavioral literature to date, that an intrinsic, ethics-based approach would be superior. Given what we know now, an intrinsic, ethics-based approach should become the preferred approach. Once we have more experience with it, we should rigorously evaluate its effectiveness, but at present, it is the best route forward.

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33. Wils, *supra* note 23, at 17; Milton C. Regan, Jr., *Risky Business*, 94 GEO. L.J. 1957, 1966 (2006) (arguing that "legal compliance is a matter not of obeying commands with intrinsic normative value, but adding the prospect of liability to the scales when weighing the costs and benefits of different courses of action. This instrumental approach to rule compliance is insufficient to ensure robustly ethical conduct because its motives for compliance are relatively shallow and contingent.").

## II. THE PROBLEM OF CORPORATE CRIME AND INEFFECTIVE CORPORATE COMPLIANCE DESPITE THE GUIDELINES' INCENTIVE

Underlying the debate over whether, and to what extent, an ethics program should be an exonerating or mitigating factor is the assumption that firms require an additional extrinsic financial incentive to implement effective ethics programs. One issue is whether firms would undertake these compliance efforts unilaterally. If market forces would pressure firms in competitive markets to “(1) exercise due diligence to prevent and detect criminal conduct; and (2) otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law,”<sup>34</sup> then the Guidelines' incentive is superfluous.

### A. Independent Demand for an Ethical Organizational Culture

There are many reasons why firms would exercise due diligence to prevent and detect criminal conduct and promote an ethical organizational culture. Firms have a general obligation to ensure that their agents act lawfully on their behalf.<sup>35</sup> In complying with the law, firms can better avoid criminal indictment, which for some “can be a life-or-death matter.”<sup>36</sup> In preventing criminal behavior, firms can better avoid the attendant prosecutions and follow-on private civil litigation, which beside the cost, can disrupt their daily operations.<sup>37</sup> Firms can also better avoid the escalating fines,<sup>38</sup> the loss of

34. USSG § 8B2.1(a).

35. See, e.g., DEL. CODE ANN. TIT. 8, § 101(b) (West 2014) (“A corporation may be incorporated or organized . . . to conduct or promote any lawful business or purposes, except as may otherwise be provided by the Constitution or other law of this State.”); CANADA COMPETITION BUREAU, *supra* note 15, at 3; see also Rebecca Henderson & Karthik Ramanna, *Managers and Market Capitalism* 28 (Harv. Bus. School, Working Paper No. 13-075 (2013)), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2231526](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2231526) (“[M]anagers in corporations are agents for both shareholders of the corporation and the society that grants corporations the license to generate profits.”).

36. Brief for the Association of Corporate Counsel et al., *supra* note 13, at \*20.

37. For example, in connection with the bribery scandal in its fiscal year 2013, Wal-Mart Stores, Inc. incurred \$157 million in costs “in conducting [its] on-going review and investigations and in responding to requests for information or subpoenas seeking documents, testimony and other information in connection with the government investigations and in defending the existing and any additional shareholder lawsuits and any governmental proceedings that are instituted against [it] or any of [its] current or former officers.” Wal-Mart Form 10-K, *supra* note 5, at 22. During the three months prior to April 30, 2013, Wal-Mart's expenses relating to the scandal grew to “approximately \$73 million,” including approximately \$44 million in costs “for the ongoing inquiries and investigations” and \$29 million for its “global compliance review, program enhancements and organizational changes.” Wal-Mart Stores, Inc. Form 10-Q for the quarterly period ending April 30, 2013, at 16 (June 7, 2013). The FCPA investigations also “may require the involvement of certain members of [Wal-Mart] senior management that could impinge on the time they have available to devote to other matters relating to [Wal-Mart's] business.” Wal-Mart Form 10-K, *supra* note 5, at 22; see also CANADA COMPETITION BUREAU, *supra* note 15, at 3, 4; OFT Guidance, *supra* note 5, at 6; OECD, *supra* note 11, at 24 (noting firms' desire to “avoid the diversion of the company's attention that competition investigations and litigation cause”).

38. Diana E. Murphy, *The Federal Sentencing Guidelines for Organizations: A Decade of Promoting Compliance and Ethics*, 87 IOWA L. REV. 697, 709 (2002) (finding from the first ten years of sentencing under the Guidelines, nearly 1500 organizations sentenced, \$2.3 billion in fines imposed, nearly \$279 million in restitution, and over 3000 years of probation); OECD, *supra* note 11, at 27 (noting for the periods 1990–94 and 2005–09, the average corporate fine for cartel violations increased in the E.U. and U.S. by approximately 2200% and 9000% respectively); Alexandre H. Rene et al., *Anti-Corruption: Minimizing FCPA Risk on Two*



business—including government contracts—that results from criminal or civil liability,<sup>39</sup> and the damages to the firms' and their employees' reputation.<sup>40</sup>

Apart from avoiding losses, a firm can seek an ethical organizational culture for its own end, for a strategic competitive advantage, or to prevent being competitively disadvantaged. A recent business ethics survey found that “a values-based culture does not detract from high performance, but instead provides a competitive advantage.”<sup>41</sup> An ethical culture can help firms attract and retain customers,<sup>42</sup> investors,<sup>43</sup> and employees.<sup>44</sup> An ethical culture can increase the significance of the employees' tasks<sup>45</sup> and well-being (as the employees derive greater moral meaningfulness from their labors<sup>46</sup>), which can increase profitability.<sup>47</sup> In signaling the firm's ethics and

*Fronts: Through Corporate Policy and Corporate Culture*, BLOOMBERG LAW REPORTS—CORPORATE COUNSEL (Feb. 13, 2012) (noting that 2010 saw eight of the ten largest monetary settlements for FCPA violations).

39. 48 C.F.R. § 9.406-1(a) (2013) (noting that among the factors in determining whether to debar government contractor is “[w]hether the contractor had effective standards of conduct and internal control systems in place at the time of the activity which constitutes cause for debarment or had adopted such procedures prior to any Government investigation of the activity cited as a cause for debarment”); U.S. Dep't of Health & Human Services, Office of Inspector General & American Health Lawyers Association, *An Integrated Approach to Corporate Compliance: A Resource for Health Care Board of Directors* 4 (July 1, 2004), available at <http://oig.hhs.gov/fraud/docs/complianceguidance/Tab%204E%20Appendx-Final.pdf> [hereinafter HHS & AHLA] (stating that “failure to appropriately monitor compliance with the complex health care regulatory requirements” can lead to firm's exclusion from participating in federal health care programs); CANADA COMPETITION BUREAU, *supra* note 15, at 3; Murphy, *supra* note 38, at 713.

40. See, e.g., Wal-Mart Form 10-K, *supra* note 5, at 22 (anticipating among the negative consequences from the bribery scandal “additional news articles . . . that could impact the perception of our role as a corporate citizen among certain audiences”); OECD, *supra* note 11, at 3; CANADA COMPETITION BUREAU, *supra* note 15, at 3; OFT Guidance, *supra* note 15, at 5.

41. LRN Corp., 2013 Ethics & Compliance Leadership Survey Report 23 (2013), available at <http://www.lrn.com/operational-guidance-whitepapers/2013-ethics-compliance-leadership-survey-report> [hereinafter 2013 Leadership Survey].

42. Muel Kaptein, *The Ethics of Organizations: A Longitudinal Study of the U.S. Working Population*, 92 J. BUS. ETHICS 601, 601 (2010).

43. *Id.* (“[E]thical and sustainable investing in the U.S. increased from \$639 billion in 1995 to \$2,159 billion in 1999 and from \$2,290 billion in 2005 to \$2,711 billion in 2007 . . .”).

44. CANADA COMPETITION BUREAU, *supra* note 15, at 5; Ronald F. Piccolo et al., *The Relationship Between Ethical Leadership and Core Job Characteristics*, 31 J. ORGANIZATIONAL BEHAV. 259, 271 (2010) (finding in their study an association between ethics and assessments of job characteristics, which perhaps reflects “the desire for employees in the modern workplace to seek employment at organizations in which they can take pride, and to earn job assignments that offer an opportunity to have a meaningful impact on the lives of others” and how “[e]mployees join organizations with expectations that policies and leaders will be supportive and fair, and that companies will operate in ethical and socially responsible ways”).

45. Piccolo et al., *supra* note 44, at 261–66 (describing task significance as “the degree to which a job and its assignments have ‘substantial impact’ on the lives of people, whether those people are in the immediate organization or in the world at large,” including “the extent to which one's work supports the [organization's] mission and values” and “offers a means by which one can realize his or her personal values”) (internal citation omitted).

46. Douglas R. May & Matthew T. Luth, *The Effectiveness of Ethics Education: A Quasi-Experimental Field Study*, 19 SCI. ENG. ETHICS 545, 551–52 (2013); Itai Beer et al., *Advancing Ethics in Public Organizations: The Impact of an Ethics Program on Employees' Perceptions and Behaviors in a Regional Council*, 112 J. BUS. ETHICS 59, 64 (2013) (describing literature on how “organizational ethics is one of the most influential factors affecting” quality of work life, including increasing employee “satisfaction, trust, and commitment of employees”); Piccolo et al., *supra* note 44, at 261 (“By emphasizing fair treatment, shared values, and integrity in common personnel and business transactions, ethical leaders inspire favorable behaviors

trustworthiness, an effective ethics program can make the firm more attractive to potential acquirers and joint venturers.<sup>48</sup> The compliance efforts can reduce the acquiring company's concerns over unexpected litigation or illegal activity inflating the target company's value.<sup>49</sup> In addition, ethics programs are a prerequisite for various government procurement contracts.<sup>50</sup>

Compliance efforts may help firms detect any illegality early.<sup>51</sup> By reporting such misconduct and taking corrective actions, firms may receive leniency or reduced penalties.<sup>52</sup> Employees, sensitive to compliance and ethical issues, may have greater awareness of illegal behavior of competitors, suppliers, and customers.<sup>53</sup> In promoting ethical behavior, the firm can more realistically encourage its suppliers and downstream purchasers to promote compliance.<sup>54</sup> This, in turn, may make it less likely that the firm will be the victim or otherwise suffer the brunt of its suppliers' or customers' crimes (such as paying higher prices, which reflect its suppliers' legal fees and fines). In knowing the rules of the game, employees can compete aggressively but fairly.<sup>55</sup>

Employees also have independent incentives for effective compliance. Employees, aware of risky behavior, can better avoid criminal liability, imprisonment (especially when prison sentences are increasing in length and frequency for certain corporate

among employees, encourage high levels of pride and commitment to the organization, and shape the way employees perceive the work context.”).

47. Piccolo et al., *supra* note 44, at 266 (“[W]hen employees are motivated by jobs that have a positive and meaningful impact on other people, they work harder by exhibiting high levels of effort, which then lead to higher job performance.”).

48. CANADA COMPETITION BUREAU, *supra* note 15, at 5; JOSEPH E. MURPHY, A COMPLIANCE & ETHICS PROGRAM ON A DOLLAR A DAY: HOW SMALL COMPANIES CAN HAVE EFFECTIVE PROGRAMS 5 (2011); 1 CORPORATE COUNSEL'S GUIDE TO ACQUISITIONS & DIVESTITURES § 3:5 (updated Mar. 2014) (noting that as part of due diligence, counsel should inquire whether the target company has an ethics code and if it does not, to obtain, as Sarbanes–Oxley requires, an explanation from the target company).

49. FCPA Guide, *supra* note 16, at 28 (“Contracts obtained through bribes may be legally unenforceable, business obtained illegally may be lost when bribe payments are stopped, there may be liability for prior illegal conduct, and the prior corrupt acts may harm the acquiring company's reputation and future business prospects.”).

50. Federal Acquisition Regulation § 52.203-13(b) (“Within 30 days after contract award, unless the Contracting Officer establishes a longer time period, the Contractor shall—(i) Have a written code of business ethics and conduct; [and] (ii) Make a copy of the code available to each employee engaged in performance of the contract.”); Clay Hagedorn & Chadd Tierney, *Designing and Implementing an Ethical Compliance Program: A Primer*, ASPATORE, 2011 WL 2117933, at \*3 (May 2011).

51. Wils, *supra* note 23, at 9.

52. OFT Guidance, *supra* note 15, at 6 (noting that one advantage of the “competition law compliance culture” is “taking appropriate steps to comply with competition law might result in an up to 10 per cent reduction in the amount of the financial penalty imposed by the OFT for a competition law infringement, depending upon the circumstances”).

53. *Id.* (stating that one advantage of a “competition law compliance culture” would include “employees being able to recognise the potential signs that another business might be infringing competition law, particularly in situations where their own business might be the victim of such an infringement and might decide to take appropriate action”); CANADA COMPETITION BUREAU, *supra* note 15, at 5.

54. USSG § 8B2.1 cmt. n.2(C)(ii) (“As appropriate, a large organization should encourage small organizations (especially those that have, or seek to have, a business relationship with the large organization) to implement effective compliance and ethics programs.”).

55. OFT Guidance, *supra* note 15, at 6.

crimes, such as price-fixing<sup>56</sup>), and the collateral consequences of a felony conviction. Risk-averse individuals may not join the board of directors of companies with inadequate ethics programs.<sup>57</sup>

Finally, an ethical organizational culture can confer a positive externality on the community. Firms benefit from a culture where the rule of law is obeyed, government officials can be trusted, laws are generally respected, and no firm gains a relative competitive advantage by violating the law.<sup>58</sup>

### *B. Extrinsic Incentives to Increase Compliance Efforts*

Part I.A discusses how an effective ethics program can provide significant advantages. Firms in competitive markets should exercise due diligence to prevent and detect criminal conduct and promote an ethical organizational culture. Yet no one seriously contends that most firms have effective ethics programs; otherwise, corporate illegality would be rare. Courts would rarely order firms to implement effective ethics programs as part of sentencing.

Policymakers can respond to insufficient compliance efforts in several ways. One way is to increase corporate fines and jail time.<sup>59</sup> Perhaps firms are not exercising due

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56. OECD, *supra* note 11, at 2, 9 (noting that between 1990–94 and 2005–09 the average number of persons per year receiving prison sentences in the U.S. for price fixing increased in the proportion of individuals imprisoned, and how the average sentence increased from 247 to 717 days).

57. CORPORATE LEGAL COMPLIANCE HANDBOOK, *supra* note 2, at § 1.04. Having said this, directors are well protected from liability for a breach of their fiduciary duties, especially under Delaware corporate law. A stockholder derivative action against directors for a breach of fiduciary duty must overcome significant procedural hurdles. FED. R. CIV. P. 23.1; *Shenker v. Laureate Educ., Inc.*, 983 A.2d 408, 423 (Md. 2009); Lisa M. Fairfax, *Spare the Rod, Spoil the Director? Revitalizing Directors' Fiduciary Duty Through Legal Liability*, 42 HOUS. L. REV. 393, 408 (2005) (discussing how “the procedural rules related to shareholder suits for fiduciary duty breaches make it difficult for shareholders to even bring an action challenging director conduct in this area”). In addition, director decision-making may be reviewed under the business judgment rule, a doctrine of judicial restraint in evaluating director action. *See id.* at 409–10 (explaining the justification for the business judgment rule). Moreover, director liability for monetary damages for a breach of the duty of care may be limited or eliminated by an exculpation provision in the corporation’s charter. DGCL § 102(b)(7); MBCA § 202(b)(4); Fairfax, *supra*, at 412 (“Even if shareholder plaintiffs overcome the procedural hurdles necessary to get their day in court and convince the sitting judge to hold directors liable for breach of fiduciary duty by successfully rebutting the nearly insurmountable presumption of the business judgment rule, the combination of exculpatory statutes, indemnification provisions, and directors’ and officers’ . . . liability insurance . . . means that such directors generally will not bear any out-of-pocket liability for their breach.”). In addition, indemnification or insurance may pay or reimburse directors for their monetary damages for a breach of fiduciary duty. DGCL § 145; MBCA §§ 8.50-8.59.

58. OECD, *supra* note 11, at 12–13 (explaining in general terms the deterrents in place in a number of countries and the effectiveness of those deterrents).

59. Although this Article focuses on the Guidelines’ incentive, the Guidelines provide several sticks. In determining the fine within the applicable guideline range, courts consider whether the firm failed to have, at the time of the offense, an effective ethics program. USSG § 8C2.8(a)(11). Moreover, courts may impose a fine above the guideline range if the firm was legally required to have an effective ethics program at the time of the offense, but did not. *Id.* § 8C4.10. Four aggravating factors can increase the organization’s culpability score: (i) if high-level personnel (or substantial authority personnel) participated in, condoned, or were willfully ignorant of the organization’s criminal activity; (ii) a prior history of misconduct; (iii) if the organization violated a condition of probation, judicial order or injunction; or (iv) “if the organization willfully obstructed or impeded, attempted to obstruct or impede, or aided, abetted or encouraged obstruction of justice during the investigation, prosecution, or sentencing of the instant offense.” U.S. Sentencing Comm’n, Office of General Counsel,

diligence to prevent criminal conduct because crime still pays.<sup>60</sup> If the gains from noncompliance are large enough, and the risks and costs of detection are low enough, one profit-maximizing strategy is to violate the law and camouflage violations with a superficially attractive compliance program. But some are concerned that higher corporate fines and longer prison sentences will be counterproductive.<sup>61</sup> Others recommend disqualifying individuals who violated the law from serving as a director or officer of a company.<sup>62</sup>

Even if the penalties were optimal, corporate crime may persist above the optimal level. One reason involves the asymmetrical incentives of the executives and the firm,<sup>63</sup> as well as the firm's senior executives and lower-level employees.<sup>64</sup> Another reason is that executives—given their dispositional biases, their imperfect willpower, and the prevailing situational factors—do not behave like their rational neoclassical economic counterparts.<sup>65</sup>

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*Chapter Eight Fine Primer: Determining the Appropriate Fine Under the Organizational Guidelines 4–5* (Mar. 2013) [hereinafter Sentencing Comm'n Primer], available at [http://www.ussc.gov/Legal/Primers/Primer\\_Organizational\\_Fines.pdf](http://www.ussc.gov/Legal/Primers/Primer_Organizational_Fines.pdf).

60. See generally John M. Connor & Robert H. Lande, *Cartels as Rational Business Strategy: Crime Pays*, 34 CARDOZO L. REV. 427 (2012) (discussing antitrust fines).

61. Higher fines may bankrupt firms. With fewer competitors, “consumers might pay higher prices, receive poorer service, or benefit from less innovation.” OECD, *supra* note 11, at 28; Douglas Ginsburg & Joshua Wright, *Antitrust Sanctions*, 6 COMPETITION POLICY INT’L 3, 6, 12 (2010) (evaluating the merits of fines and imprisonment, as well as debarment of guilty individuals). Taxpayers bear the cost of longer incarcerations. Longer incarcerations, if disproportionate to the conduct’s moral outrage, increase the risk of nullification by courts and juries. See OECD, *supra* note 11, at 30–34 (discussing the efficacy of imprisonment as a deterrent); see generally Maurice E. Stucke, *Morality and Antitrust*, 2006 COLUM. BUS. L. REV. 443 (2006) (discussing the problems with optimal deterrence theory). Some authorities, like the European Commission, may be averse to criminalizing certain offenses (such as competition law) out of concern of the issues that would pose for some member states opposed to criminalizing that conduct.

62. U.K. OFFICE OF FAIR TRADING, DRIVERS OF COMPLIANCE AND NON-COMPLIANCE WITH COMPETITION LAW 16 (May 2010), available at [http://www.offt.gov.uk/shared\\_offt/reports/comp\\_policy/oft\\_1227.pdf](http://www.offt.gov.uk/shared_offt/reports/comp_policy/oft_1227.pdf) (noting that businesses perceived director disqualification as second most important sanction, after criminal penalties, in deterring infringements of competition law).

63. OECD, *supra* note 11, at 29 (“Furthermore, practical considerations suggest that high corporate fines alone cannot provide sufficient deterrence. For example, the interests of individuals in a company may not align perfectly with the best interests of the company. If executives or officers believe they can advance more rapidly, collect higher bonuses, or gain prestige by padding profits via cartel activity, they may be inclined to do so even though the company could eventually be fined as a result. By then, the responsible individuals may have moved on to another company. Even if they did not, it is unlikely that the costs imposed on those individuals will match the costs imposed on the company. Simply put, a divergence of interests is likely to be a problem whenever directors, officers, or managers believe they personally have more to gain from committing a violation than they stand to lose if their company is fined.”).

64. Senior executives can immediately profit from lower-level employees’ secretly fixing prices, allocating markets, or bribing officials to secure profitable contracts. If, and when, the crimes are detected and prosecuted, the senior executives are not necessarily criminally prosecuted, nor do their reputation and wealth necessarily diminish. Even if individual fines and jail terms increase, senior managers may set aggressive financial goals that are difficult for their subordinates to achieve legally. See Donald C. Langevoort, *Monitoring: The Behavioral Economics of Corporate Compliance with Law*, 2002 COLUM. BUS. L. REV. 71, 80 (2002).

65. See Maurice E. Stucke, *Am I a Price-Fixer? A Behavioral Economics Analysis of Cartels*, in CRIMINALISING CARTELS: A CRITICAL INTERDISCIPLINARY STUDY OF AN INTERNATIONAL REGULATORY MOVEMENT (Caron Beaton-Wells & Ariel Ezrachi eds., Hart Publishing Oxford 2011) (examining these factors

Although stiffer penalties and more prosecutions remain options to increase compliance efforts and deter corporate crime, the Guidelines provide two more mechanisms. First, courts can order the guilty organization, as part of probation, to “develop and submit to the court an effective compliance and ethics program” and periodically report its progress in implementing its program.<sup>66</sup> But this piecemeal approach only reaches organizations that are caught, prosecuted, convicted, and sentenced. A court-ordered ethics program can lower the offender’s risk of recidivism. But court-ordered ethics programs, unless draconian in expense or control, will not necessarily increase the incentives of non-offending firms to invest in compliance.

Second, the Guidelines “offer incentives to organizations to reduce and ultimately eliminate criminal conduct by providing a structural foundation from which an organization may self-police its own conduct through an effective compliance and ethics program.”<sup>67</sup> To incentivize organizations to undertake compliance and ethics measures before any crime is committed, the Guidelines lower a qualifying organization’s culpability score by three points for a subsequent crime.<sup>68</sup> This significantly reduces the organization’s criminal fine.<sup>69</sup> Although the Guidelines seek to deter corporate crime,<sup>70</sup>

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in much greater detail); OECD, *supra* note 11, at 25 (“When individuals in a company believe they are above the law or that they are so smart that they will not get caught or convicted, they are more likely to violate the law.”). As a compliance expert and antitrust lawyer officer observed, “Although the threat of huge fines and jail would seem to be an effective deterrent to cartel conduct, companies are by nature insular. The internal pressures tend to outweigh more remote, external threats. The need to keep a tough boss happy can overshadow any remote concern about laws and government. Moreover, responsibility is dispersed, so individuals do not necessarily perceive the same elements of culpability that companies do. . . . Moreover, one of the most striking characteristics of the types of senior level executives who often engage in cartels is arrogance; they view themselves as too smart to be caught. If offenders believe they will never be caught, deterrence through severe sanctions alone is likely to be ineffective.” Murphy & Kolasky, *supra* note 22, at 63.

66. USSG ch. 8, introductory cmt. & § 8D1.4(b)(1). For some recent cases where the court ordered an ethics program, see *United States v. CITGO Petroleum Corp.*, CRIM.A. C-06-563, 2012 WL 4127800 (S.D. Tex. Sept. 18, 2012) (involving various crimes); *In re Chiquita Brands Int’l, Inc. Alien Tort Statute & S’holder Derivative Litig.*, 792 F. Supp. 2d 1301, 1310 (S.D. Fla. 2011) (regarding payments to the AUC and transportation of 3000 rifles out of Nicaragua); *United States v. Guidant LLC*, 708 F. Supp. 2d 903, 919 (D. Minn. 2010) (requiring in the probation order that the defendant invest in charitable foundations, in addition to implement a compliance program).

67. USSG ch. 8, introductory cmt. (noting that two mitigating factors when sentencing organizations are (i) an effective ethics program and (ii) self-reporting, cooperation, or acceptance of responsibility).

68. See USSG § 8C2.5(f)(1) (explaining that “an effective compliance and ethics program” will lower the overall culpability score).

69. An organization starts with a culpability score of five points, which four aggravating factors can increase by as much as 12 points and two mitigating factors can decrease by as much as eight points. See USSG § 8C2.5 (explaining the factors in detail). The net culpability score, using the table set out in USSG § 8C2.6, determines the applicable minimum and maximum fine multipliers. To illustrate, suppose Firms *A* and *B* have the same base fine (\$10.5 million) and initially the same culpability score (five). But Firm *A*’s culpability score, on account of its ethics program, is reduced to two. Multiplying the base fine (\$10.5 million) with the culpability score’s minimum and maximum multiplier (which is one and two for a score of five and .4 and .8 for a score of two), Firm *B*’s fine will range between \$10.5 million and \$21 million, whereas Firm *A*’s fine will range between \$4.2 million and \$8.4 million. See Sentencing Comm’n Primer, *supra* note 59, at 5 (explaining in general terms the calculations above).

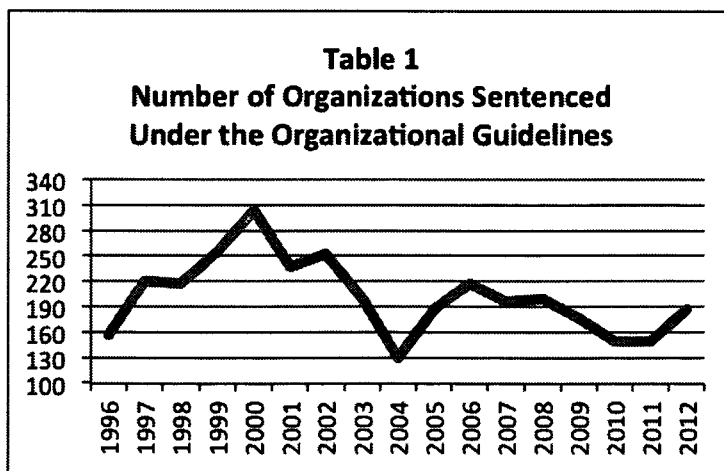
70. See USSG ch. 8, intro. cmt. (noting that the Guidelines are “designed so that the sanctions imposed upon organizations and their agents, taken together, will provide just punishment, adequate deterrence, and incentives for organizations to maintain internal mechanisms for preventing, detecting, and reporting criminal conduct”); Murphy, *supra* note 38, at 703 (noting how Guidelines “are geared toward deterrence”).

the payoff ironically comes *after* the firm's agents commit a crime for which the firm is liable and sentenced. In short, the Guidelines' financial reward comes after the firm breaks the law.

*C. Despite the Guidelines' Incentive, Corporate Crime and Ineffective Compliance Persist*

As Part II.B discusses, for over 20 years, the Guidelines have promoted a financial incentive to induce firms' senior management to exercise due diligence and foster an ethical organization culture. This Part assesses the incentive's effectiveness, starting with the sentencing data to see how frequently courts find organizations' compliance efforts effective.

Unlike data on individual offenders, data on organizations convicted and sentenced under the Guidelines are limited. But the limited data provide some insights. First, the number of individuals sentenced under the Sentencing Guidelines has increased significantly over the past 15 years, while the number of organizations sentenced annually has fluctuated between 130 and 304.<sup>71</sup> But this fact alone does not suggest that corporate crime has abated. At times, the DOJ prosecutes only the firm's executives.<sup>72</sup> The DOJ may not criminally prosecute the firm, when it would impose "disproportionate harm to shareholders, pension holders, employees, and others not proven personally culpable" and adversely impact the public.<sup>73</sup> At times, the DOJ opts for civil litigation, where it can obtain, with a lower burden of proof, similar remedies and relief.<sup>74</sup>

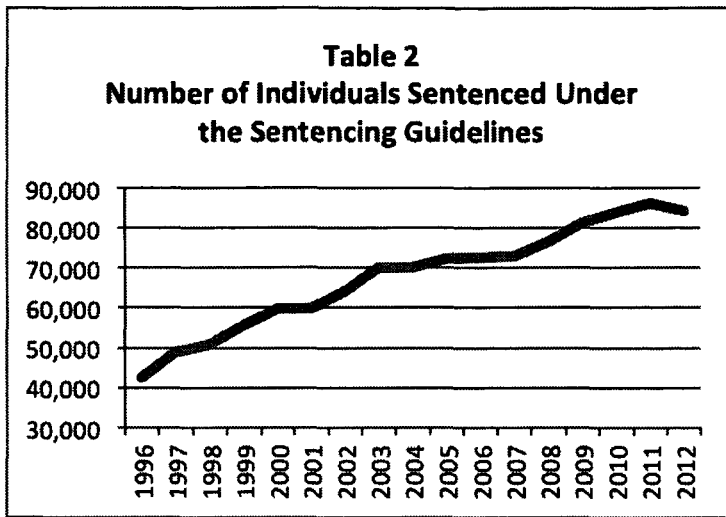


71. Data for each fiscal year (Oct. 1–Sept. 30) taken from U.S. SENTENCING COMM'N, SOURCEBOOK OF FEDERAL SENTENCING STATISTICS, Introduction, available at [http://www.ussc.gov/Research\\_and\\_Statistics/Annual\\_Reports\\_and\\_Sourcebooks/Archives.cfm](http://www.ussc.gov/Research_and_Statistics/Annual_Reports_and_Sourcebooks/Archives.cfm).

72. U.S. ATTORNEYS' MANUAL, *supra* note 16, at § 9-28.400 (noting the Tax Division's "strong preference for prosecuting responsible individuals, rather than entities, for corporate tax offenses").

73. *Id.* § 9-28.300.

74. *Id.* § 9-28.1100 (listing considerations regarding adequacy of civil alternatives to prosecution).



Consequently, relative to the tens of thousands of individuals sentenced annually, organizations are sentenced infrequently.<sup>75</sup> Even when organizations are sentenced, only a subset will have ethics programs, of which a percentage will be found effective.<sup>76</sup> This percentage (0.0873%) is surprisingly tiny.<sup>77</sup>

Based on the Sentencing Commission's public data, the federal district courts between 1996 and 2012 sentenced 3435 organizations.<sup>78</sup> Only three times did the court reduce an organization's culpability score due to it having an effective ethics program at the time of the offense.<sup>79</sup>

75. Compare *supra* Table 1 with Table 2.

76. See *infra* Table 3.

77. *Id.*

78. *Supra* Table 1.

79. Apparently two more organizations received credit between 1992 and 1996. ERC Report, *supra* note 3, at 37 (noting for fiscal years 1992-2010, only five of 3433 organizations sentenced received credit for a compliance/ethics program).

Table 3<sup>80</sup>

	<i>Organization Found to Have an Effective Ethics Program-§8C2.5(f)</i>	<i>Organization Had No Ethics Program</i>	<i>Organization Had an Ethics Program that Was Not Effective</i>	<i>Organization Did Not Have an Effective Ethics Program</i>
<b>2012</b>	0	63	(data not provided)	--
<b>2011</b>	0	74	--	--
<b>2010</b>	0	60	--	--
<b>2009</b>	0	96	--	--
<b>2008</b>	0	93	--	--
<b>2007</b>	1	88	--	--
<b>2006</b>	0	108	--	--
<b>2005 Post-Booker</b>	0	69	--	--
<b>2005 Pre-Booker</b>	0	20	--	--
<b>2004 Post-Blakely</b>	0	20	--	--
<b>2004 Pre-Blakely</b>	0	49	--	--
<b>2003</b>	0	90	0	--
<b>2002</b>	0	143	0	--
<b>2001</b>	0	90	2	--
<b>2000</b>	0	118	14	--
<b>1999</b>	1	--	--	91

80. Data for each fiscal year (Oct. 1–Sept. 30) taken from SOURCEBOOK, *supra* note 71, Table 54 (Table 52 in 1998 & 1997, Table 47 in 1996): Organizations Sentenced Under Chapter Eight: Culpability Factors. As the total in Table 3 is less than the total number of organizations sentenced annually (*see supra* Table 1), it appears that a compliance program is not always brought to the sentencing court's attention.



2014]	<i>In Search of Effective Ethics and Compliance Programs</i>			785
<i>1998</i>	0	--	--	118
<i>1997</i>	1	--	--	112
<i>1996</i>	0	--	--	94
<i>Total</i>	3	1181	16	415

The federal courts are not opposed to ethics programs. For example, between 2000 and 2012, the sentencing court found only one organization to have an effective ethics program, but ordered 17% of all organizations to institute an effective ethics program as part of probation.<sup>81</sup> Moreover, with the exception of 2008 and 2009, the federal courts have increasingly ordered (based on the percentage of all organizations sentenced) organizations to implement an effective ethics program.

**Table 4<sup>82</sup>**

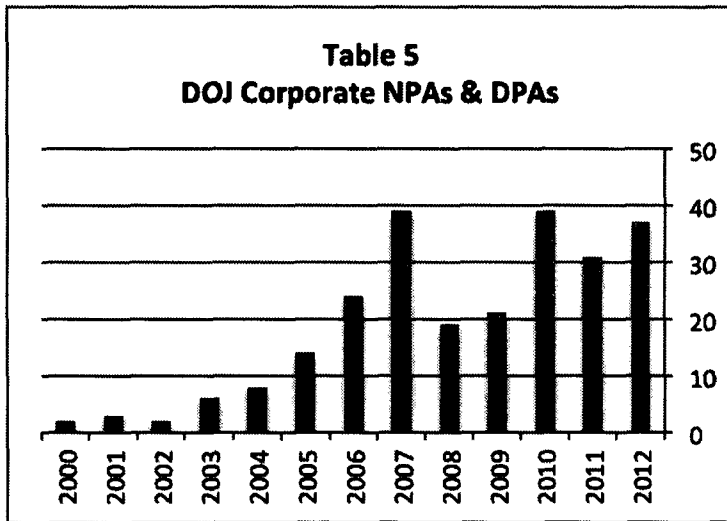
<i>Court-Ordered Ethics Program</i>	<i>Program Ordered</i>	<i>No Program Ordered</i>	<i>% of All Organizations Sentenced</i>
<i>2012</i>	66	120	35.48%
<i>2011</i>	31	129	19.38%
<i>2010</i>	42	107	28.19%
<i>2009</i>	9	168	5.08%
<i>2008</i>	12	183	6.15%
<i>2007</i>	47	148	24.10%
<i>2006</i>	41	166	19.81%
<i>2005</i>	28	113	19.86%
<i>Post-Booker 2005</i>	7	38	15.56%
<i>Pre-Booker 2004</i>	11	33	25.00%
<i>Post-Blakely 2004</i>	10	76	11.63%
<i>Pre-Blakely 2003</i>	24	176	12.00%
<i>2002</i>	38	213	15.14%

81. *Supra* Table 3.

82. Data for each fiscal year (Oct. 1–Sept. 30) taken from SOURCEBOOK, *supra* note 71, Table 53: Chapter Eight Organizational Sentencing Components.

<b>2001</b>	40	198	16.81%
<b>2000</b>	42	258	14.00%
<b>Total</b>	448	2126	17.40%

Given the Guidelines' significant financial incentive for compliance, why have the federal courts so rarely found firms to have effective ethics programs? Why are courts increasingly ordering firms to revise or implement ethics programs? One possible explanation is that the sentencing data do not reflect the corporate universe. If firms with effective ethics programs are likelier to avoid criminal prosecution, then the federal courts will likely sentence firms without effective ethics programs, thereby skewing the sentencing data. Firms with effective ethics programs may avoid criminal prosecution if the DOJ instead opts for deferred prosecution agreements (DPAs) or non-prosecution agreements (NPAs).<sup>83</sup> The number of publicized DPAs and NPAs has increased since 2002.<sup>84</sup>



Second, if the firm has an effective ethics program, the DOJ may elect to prosecute only the employees,<sup>85</sup> or may consider civil or regulatory alternatives, where the

83. U.S. ATTORNEYS' MANUAL, *supra* note 16, § 9-28.1000; *see also* FCPA Guide, *supra* note 16, at 53 (noting among the nine factors considered "in conducting an investigation, determining whether to bring charges [against a corporation], and negotiating plea or other agreements" are "the existence and effectiveness of the corporation's pre-existing compliance program" and its "remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one"); ERC Report, *supra* note 3, at 3.

84. 2013 Mid-Year Update on Corporate Deferred Prosecution Agreements (DPAs) and Non-Prosecution Agreements (NPAs), Publications, GIBSON DUNN (July 9, 2013), <http://www.gibsondunn.com/publications/pages/2013-Mid-Year-Update-Corporate-Deferred-Prosecution-Agreements-and-Non-Prosecution-Agreements.aspx> (noting at least 20 such agreements per year); Uhlmann, *supra* note 12, at 1301 (noting that the DOJ's Criminal Division uses such agreements more than other divisions).

85. U.S. ATTORNEYS' MANUAL, *supra* note 16, § 9-28.500 (recognizing the inappropriateness of

Guidelines do not apply.<sup>86</sup> Third, even if prosecuted, firms may be found not guilty on account of their ethics programs.<sup>87</sup> Fourth, firms that were found guilty might have had an effective ethics program but ran afoul of the Guidelines' other requirements.<sup>88</sup>

The problem is that no one, except the DOJ, knows the extent to which firms' compliance efforts resulted in their avoiding criminal liability or a lower fine. The compliance industry complains about the lack of "hard evidence that organizations are receiving the promised consideration for their compliance programs," that "prosecutors rarely point to compliance/ethics programs when publicly discussing case resolutions," and about the "very few cases where DOJ acknowledged granting credit for—or even carefully assessing—a pre-existing compliance/ethics program."<sup>89</sup> Corporate ethics officers have asked the DOJ for greater guidance on when and why ethics programs played an important mitigating or exonerating role.<sup>90</sup> But unlike its detailed statistics on individual offenders, the DOJ does not publicize declinations, its reasons for entering into DPAs or NPAs, and the extent to which the firm's compliance efforts factored in its opting for a DPA or NPA.<sup>91</sup>

But it is doubtful that most firms—other than those prosecuted—have effective compliance programs. First, DPAs and NPAs do not explain the 1996–2002 time period when the DOJ rarely relied on them,<sup>92</sup> and the federal courts found only two instances of an effective ethics program out of the hundreds of organizations sentenced. Moreover, the DPAs and NPAs generally require the firms to implement or improve their compliance efforts significantly, which suggests that the firms' pre-existing compliance efforts were subpar.<sup>93</sup>

imposing "liability upon a corporation, particularly one with a robust compliance program in place, under a strict *respondeat superior* theory for the single isolated act of a rogue employee").

86. *Id.* § 9-28.1100 (listing considerations regarding adequacy of civil alternatives to prosecution).

87. Few individual and organizational defendants go to trial; between 2008 and 2012, over 96% pled guilty. U.S. SENTENCING COMM'N, 2012 SOURCEBOOK OF FEDERAL SENTENCING STATISTICS, Figure C: Guilty Pleas and Trial Rates Fiscal Years 2008–2012, available at [http://www.ussc.gov/Research\\_and\\_Statistics/Annual\\_Reports\\_and\\_Sourcebooks/2012/sbtoc12.htm](http://www.ussc.gov/Research_and_Statistics/Annual_Reports_and_Sourcebooks/2012/sbtoc12.htm).

88. Sentencing Comm'n Primer, *supra* note 59, at 5 (noting how under USSG § 8C2.5(f)(2) & (3), courts should not reduce the firm's culpability score "if the organization unreasonably delayed reporting the offense to the appropriate governmental authorities or under specified instances in which high-level or substantial authority personnel participated in, condoned, or were willfully ignorant of the offense").

89. ERC Report, *supra* note 3, at 3.

90. *The Release of Statistics on Ethics and Compliance Programs in Enforcement Decisions: A Joint Report to the U.S. Department of Justice*, ETHICS RESOURCE CENTER 7 (Jan. 27, 2011), <http://www.ethics.org/files/u5/FinalDOJ.pdf> (requesting the DOJ to provide (i) "[g]eneral statistics on the consideration given [ethics and compliance] programs in enforcement decisions"; (ii) "[d]escriptions (without identifying information) of individual cases in which [ethics] programs were a mitigating factor in enforcement decisions"; (iii) "[i]nformation about what specific aspects of an [ethics] program factored into enforcement decisions"; and (iv) "[i]nformation about the benefits of an effective [ethics] program, such as helping avert a decision to prosecute or avoidance of other sanctions such as appointment of a monitor").

91. FCPA Guide, *supra* note 16, at 77.

92. Uhlmann, *supra* note 12, at 1307–08, 1311.

93. *Id.* at 1323; U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-10-110, CORPORATE CRIME: DOJ HAS TAKEN STEPS TO BETTER TRACK ITS USE OF DEFERRED AND NON-PROSECUTION AGREEMENTS, BUT SHOULD EVALUATE EFFECTIVENESS, 23, 33 (Dec. 2009), available at <http://www.gao.gov/new.items/d10110.pdf> (noting how "companies are often required to establish or enhance internal controls or company compliance programs, or engage in training to detect and prevent further wrongdoing" and that 45 of the 57 DPAs and NPAs reviewed required the company to improve or enhance its compliance program).

Second, one enduring complaint is that firms continue to underinvest in compliance. The Guidelines have helped galvanize the industry's support for compliance, which has significantly increased over the past 20 years.<sup>94</sup> Nonetheless, despite the Guidelines' incentive, few firms have all the components that the Guidelines expect of an effective ethics program.<sup>95</sup> The compliance industry complains about ineffective, half-hearted, check-the-box compliance:

In short, the managements of too many companies aim for what they perceive as minimally required when it comes to compliance/ethics—in essence, they aim for the bottom. A major flaw in this thinking is that—quite apart from the question of what good corporate citizens should be doing on their own without the threat of enforcement—the fact is that minimalistic, check-the-box compliance/ethics programs do not even satisfy the intent of the Guidelines.<sup>96</sup>

Despite the Organizational Guidelines' and the UK's Office of Fair Trading's (OFT) financial incentives for effective ethics programs, 13% of surveyed U.S. and U.K.

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94. Kaptein, *Longitudinal Study*, *supra* note 42, at 606 (showing the percentage of 12,196 Americans surveyed in 2008 who reported their employers having: (1) a code of ethics that articulates the organization's values and standards (81.62%), (2) communication and training to employees on their code of conduct (76.34%), (3) policies to hold employees accountable for code of conduct violations (70.98%), (4) policies to investigate and take corrective action if misconduct is alleged (70.64%), (5) background investigations on prospective employees (66.52%), (6) confidential and anonymous ethics hotline (57.44%), (7) senior-level ethics or compliance officer (56.15%), (8) monitoring and auditing of employee compliance with code of conduct (48.84%), and (9) incentive policies to uphold the code of conduct (24.92%)); *The 2011 National Business Ethics Survey*, ETHICS RESOURCE CENTER 48 (Jan. 5, 2012) [hereinafter 2011 ERC Survey], available at <http://www.ethics.org/news/2011nbes> (showing percentage of U.S. employees who reported in 1994, 2000, 2003, 2005, 2007 and 2011 their firms having: (i) written standards for ethical conduct (increasing from 66% to over 80%); (ii) training on company standards of ethical workplace conduct (increasing from 37% to over 70%); (iii) a mechanism for seeking ethics-related advice or information (declining and then returning to over 60%); (iv) a mechanism for reporting misconduct anonymously (71% in 2011 survey); (v) ethical conduct assessed as a part of employee performance evaluations (declining from 71% in 2003 to 67% in 2011); and (vi) employees who violate the organizations standards or the law disciplined (85% in 2011)).

95. Kaptein, *Longitudinal Study*, *supra* note 42, at 615 (finding from surveyed employees of organizations with over 200 employees from 11 industries that only 15.6% of their organizations adopted all seven of the Guidelines' components and that 18.38% of their organizations lacked an ethics code).

96. ERC Report, *supra* note 3, at 67 ("Unfortunately, the practices of these best-in-class organizations have not been adopted by many companies where there is still an overwhelming emphasis on government enforcement to 'make the case' for compliance/ethics efforts. In a recent survey of compliance/ethics professionals, the majority of respondents indicated that one of the most important reasons they desired more information from the DOJ was that they needed help in reminding company leaders about the value of the investment in their compliance/ethics programs."); Uhlmann, *supra* note 12, at 1332; GREENBERG, *supra* note 8, at viii. This also applies to antitrust compliance, where the Guidelines' incentive does not apply. See Murphy & Kolasky, *supra* note 22, at 61 ("Unfortunately, experience teaches that too few companies—especially non-U.S. companies—invest the time, resources, and imagination necessary to develop and implement effective anti-cartel compliance programs."). Antitrust counsel in one telephone survey "nearly universally stated that compliance programs do not seem to become embedded within the firm. Senior management and general counsel are sensitive to cartel matters; however, this does not seem to translate to other managers . . . . A number of practitioners provided anecdotes of visiting the offices of cartel participants and finding antitrust compliance training binders in the office. The cartel participants usually claimed that they had never participated in compliance training, nor had they been informed that cartel participation was illegal. In one case the cartelist in question even attended an antitrust compliance training the previous month." Sokol, *supra* note 22, at 227.

companies, whose annual company revenues ranged between \$200 million and \$100 billion, reported having *no* established budget for compliance, with an additional 28% indicating their budgets were \$500,000 or less.<sup>97</sup>

Third, the Guidelines increase an organization's culpability score if its high-level personnel "participated in, condoned, or were willfully ignorant of the offense" or "tolerance of the offense by substantial authority personnel was pervasive throughout the organization."<sup>98</sup> As Table 6 reflects, courts often increase the culpability score of smaller organizations (fewer than 200 employees). This likely reflects different base rates. Small firms far outnumber large ones.<sup>99</sup> Moreover, it is more likely, and easier to prove, that senior executives in small firms knew or participated in the offense. What is surprising are the 168 instances where senior management in larger firms (200+ employees) promoted an unethical organizational culture.

**Table 6: Involvement in or Tolerance of Criminal Activity<sup>100</sup>**

<i>Number of Employees</i>	<i>Total 1998-2012</i>
<i>5,000+</i>	31
<i>1,000+</i>	37
<i>200+</i>	100
<i>50+</i>	228
<i>10 or more employees</i>	447

Fourth, corporate crime has not meaningfully abated. Cartels, as the Organisation for Economic Cooperation and Development (OECD) recognized, "remain a substantial problem, as do recidivists."<sup>101</sup> Despite the record number of convictions and jail time for

97. *Deeper Insight for Greater Strategic Value: State of Compliance: 2013 Survey*, PWC (June 2013), <http://www.pwc.com/us/en/risk-management/assets/soc-survey-2013-final.pdf> (providing a survey of nearly 800 U.S. and UK executives in 19 industries). One explanation is that the companies had but did not separately budget their compliance efforts. For example, 80% of the companies (79% U.S. and 86% UK) had an assigned Chief Compliance Officer. For firms without a CCO, the functions that typically managed compliance oversight were within the legal (39%) and internal audit (21%) departments. *Id.* at 9. But, as the survey found, "despite incentives in the [Organizational] Guidelines that encourage the CCO to have a formal reporting relationship to the board, this has continued to decrease when compared to 2012." *Id.* at 10.

98. USSG § 8C2.5(b).

99. Of the 5,734,538 firms in the U.S. with paid employees, 3,575,240 firms had fewer than five employees, 968,075 had five to nine employees, 617,089 had 10–19 employees, 475,125 had 20–99 employees, 81,773 had 100–499 employees, and 17,236 had 500+ employees. *2010 Statistics of U.S. Businesses*, U.S. CENSUS BUREAU, <http://www.census.gov/econ/susb/>.

100. Data for the fiscal years (Oct. 1, 1997–Sept. 30, 2012) taken from Table 54 in 1999. Table 52 in 1997–98 & Table 47 in 1996: *Organizations Sentenced Under Chapter Eight Culpability Factors*, see SOURCEBOOK, *supra* note 71.

101. OECD, *supra* note 11, at 2 (noting that "[b]etween 1990 and 2005, 174 companies violated laws

cartel participants, “the available evidence shows that the number, size and harm to consumers of discovered cartels are still increasing.”<sup>102</sup> Indeed, price-fixing cartels represent a unique failure of corporate compliance. Cartels involve multiple competitors within an industry. The competitors, often market leaders, collude to fix prices, rig bids or allocate markets. Thus, a bribery case reflects the long-term ineffectiveness of a firm’s compliance efforts; a price-fixing cartel reflects the ineffectiveness of an industry’s compliance efforts, often over long time periods. Moreover, price-fixing cartels by definition implicate executives who have the power to set or negotiate prices, typically senior management.<sup>103</sup>

Cartels are not the only distressing reminder of a weak ethical organizational culture. The 2000s began and ended with corporate scandals. The United States has stepped up its investigations of the major Wall Street banks.<sup>104</sup> In a recent insider trading prosecution, the U.S. criticized a leading hedge fund for failing on many occasions “to employ effective compliance procedures or practices to prevent . . . insider trading.”<sup>105</sup> The DOJ and SEC continue to investigate bribery and corruption,<sup>106</sup> including whether Wal-Mart Stores bribed officials in “a number of foreign markets,” including Mexico, Brazil, China and India.<sup>107</sup> The number of FBI cases involving corporate fraud, securities and commodities fraud, health care fraud, and mortgage fraud has increased.<sup>108</sup>

against price-fixing at least twice, with some reoffending as many as 26 times—that we know of”); Murphy & Kolasky, *supra* note 22, at 61; Sokol, *supra* note 22, at 202 n.7.

102. OECD, *supra* note 11, at 11; Caron Beaton-Wells & Brent Fisse, *U.S. Policy and Practice in Pursuing Individual Accountability for Cartel Conduct: A Preliminary Critique*, 56 ANTITRUST BULL. 277 (2011); see also *Fine and Jail Charts Through Fiscal Year 2013*, U.S. DEP’T OF JUSTICE, [www.justice.gov/atr/public/criminal/264101.html](http://www.justice.gov/atr/public/criminal/264101.html) (last visited Apr. 21, 2014) (showing record fines and lengths of prison sentences).

103. Wils, *supra* note 23, at 5 (collecting some of the empirical literature).

104. See, e.g., Ben Protess & Jessica Silver-Greenberg, *JPMorgan’s Legal Hurdles Expected to Multiply*, N.Y. TIMES (Sept. 23, 2013), [http://dealbook.nytimes.com/2013/09/23/jpmorgans-legal-hurdles-expected-to-multiply/?\\_php=true&\\_type=blogs&\\_r=0](http://dealbook.nytimes.com/2013/09/23/jpmorgans-legal-hurdles-expected-to-multiply/?_php=true&_type=blogs&_r=0) (discussing several legal challenges JP Morgan currently faces).

105. Indictment at 4, United States v. S.A.C. Capital Advisors, LP, 13 Crim 541 (S.D.N.Y. 2013).

106. Press Release, BDO United States, Public Boards Have Multiple Concerns With Proxy Advisory Firms and Strongly Opposed to Mandatory Audit Rotation According to BDO USA, LLP (Sept. 25, 2012) (on file with author), available at <http://www.bdo.com/news/pr/2273>; PricewaterhouseCoopers, *Global Economic Crime Survey 7* (2009), available at [http://www.pwc.com/en\\_GX/gx/economic-crime-survey/pdf/global-economic-crime-survey-2009.pdf](http://www.pwc.com/en_GX/gx/economic-crime-survey/pdf/global-economic-crime-survey-2009.pdf) (“Globally, 27% of respondents experiencing economic crime reported having experienced bribery and corruption cases in the last 12 months.”); 2011 ERC Survey, *supra* note 94, at 46 (“In 2011, 9% of [American] employees observed a potential FCPA violation compared to 5% in 2009.”); BDO, *2012 BDO BOARD SURVEY 2*, 4 (2012) (33% of surveyed corporate directors of public company boards with revenues between \$250 million and \$750 million found corruption/bribery as the greatest fraud risk facing their businesses; of those companies conducting international business, “a majority (57%) say they deal with foreign officials and almost one-third (32%) of those believe compliance risks related to bribery of government officials has increased over the past two years, compared to just four percent reporting a decrease”).

107. Wal-Mart Form 10-K, *supra* note 5, at 22.

108. FED. BUREAU OF INVESTIGATION, FINANCIAL CRIMES REPORT TO THE PUBLIC: FISCAL YEARS 2010–2011 (Oct. 1, 2009–Sept. 30, 2011), available at <http://www.fbi.gov/stats-services/publications/financial-crimes-report-2010-2011>; see also Lisa M. Krigsten, *Recent Amendments to the Sentencing Guidelines: New Incentives to Create Effective Compliance Programs and Disclose Criminal Activity*, 13 J. HEALTH CARE COMPLIANCE 61, 62 (2011) (noting that in fiscal year 2010, DOJ opened 1116 distinct criminal health care fraud investigations and filed charges against 931 defendants, a 16% increase over the previous year and a 43% increase over the number of defendants charged five years earlier).

Employees in recent surveys continue to identify frequent corporate wrongdoing.<sup>109</sup> Financial services employees were grimmer.<sup>110</sup> When auditor Ernst & Young surveyed nearly 400 chief financial officers, the findings were disturbing:

When presented with a list of possibly questionable actions that may help the business survive, 47 per cent of CFOs felt one or more could be justified in an economic downturn.

Worryingly, 15 per cent of CFOs surveyed would be willing to make cash payments to win or retain business and 4 per cent view misstating a company's financial performance as justifiable to help a business survive.

While 46 per cent of total respondents agree that company management is likely to cut corners to meet targets, CFOs have an even more pessimistic view (52 per cent).<sup>111</sup>

Consequently, despite the Guidelines' financial incentive, ineffective compliance and corporate crime persist.

### III. WHETHER THE PROBLEM ARISES FROM THE GUIDELINES' THREE FUNDAMENTAL ASSUMPTIONS

To help understand why corporate crime and concerns of ineffective compliance persist, despite the Guidelines' financial incentive, this Part explores whether the problem arises from the Guidelines' three fundamental assumptions: first, ethics programs can

109. See Muel Kaptein, *Understanding Unethical Behavior by Unraveling Ethical Culture*, 64 HUM. RELATIONS 843, 843 (2011) [hereinafter Kaptein, *Understanding Unethical Behavior*] (discussing one recent survey where 74% of U.S. managers and employees observed unethical behavior in the preceding 12 months in their organizations); *Global Economic Crime Survey*, *supra* note 106, at 7 (2009 survey found a significant increase in firms experiencing accounting fraud, attributable in part to "financial targets being more difficult to achieve" and "senior management wanting to report a desired level of financial performance"); see GREENBERG, *supra* note 8, at 1 (discussing the recent legal outlook for corporate ethics and compliance). A 2011 survey of 4683 employees in the for-profit sector had mixed findings. 2011 ERC Survey, *supra* note 94. Fewer employees witnessed misconduct in the U.S. workplace (45% in 2011, lower than the 49% in 2009 and 55% in 2007), and a higher percentage of employees reported bad behavior (65% up from 63% in 2009, and 53% in 2005). *Id.* at 12. But more employees who reported misconduct said they experienced some form of retaliation (22% in 2011 versus 12% in 2007 and 15% in 2009). *Id.* More employees perceived pressure to compromise standards to do their jobs (13% versus 8% in 2007). *Id.* And the share of companies with weak ethics cultures climbed to near record levels at 42% up from 35% two years ago. *Id.*

110. *Wall Street Professional Survey Reveals Widespread Misconduct, Acceptance of Illegal Activities and Disregard of Client Interests*, LABATON SUCHAROW LLP, at 3 (July 16, 2013), <http://www.labaton.com/en/about/press/Wall-Street-Professional-Survey-Reveals-Widespread-Misconduct.cfm> (52% of the surveyed 250 financial services employees felt their competitors likely engaged in illegal or unethical behavior; 24% felt their colleagues at their own company likely engaged in misconduct to get ahead; 23% reported observing or having first-hand knowledge of wrongdoing in the workplace; 29% believed that "financial services professionals may need to engage in illegal or unethical behavior to be successful"; 28% "felt the industry does not put the interests of clients first and 24% admitted they would engage in insider trading [to make \$10 million] if they could get away with it").

111. *12th Global Fraud Survey Growing Beyond: A Place for Integrity, CFOs in the Spotlight*, ERNST & YOUNG, [http://www.ey.com/Publication/vwLUAssets/Global-Fraud-Survey-a-place-for-integrity-12th-Global-Fraud-Survey/\\$FILE/EY-12th-GLOBAL-FRAUD-SURVEY.pdf](http://www.ey.com/Publication/vwLUAssets/Global-Fraud-Survey-a-place-for-integrity-12th-Global-Fraud-Survey/$FILE/EY-12th-GLOBAL-FRAUD-SURVEY.pdf).

111. USSG § 8B2.1 (2014).

effectively deter and prevent criminal conduct; second, effective ethics programs are attainable; and third, courts can distinguish between effective and otherwise ineffective or sham ethics programs.

#### A. Can Ethics Programs Effectively Deter and Prevent Criminal Conduct?

The Guidelines assume that an ethics program can be “generally effective in preventing and detecting criminal conduct.”<sup>112</sup> If firms, despite their earnest efforts, cannot deter or prevent crime and promote ethical conduct, then their compliance efforts will always be found ineffective. Besides fluke cases, no one will receive the Guidelines’ financial incentive, firms will not invest in additional compliance, and corporate crime will persist.

One empirical issue is whether ethics programs can effectively prevent and detect crimes, and if so, the extent of their effectiveness.<sup>113</sup> One positive trend is the increase over the past 30 years in empirical work on business ethics.<sup>114</sup> The empirical studies suggest that the Guidelines are on the right track: firms can prevent and deter unethical and illegal behavior by promoting an ethical organizational culture.<sup>115</sup> One study, for example, found a work group’s ethical culture was inversely related to the frequency of unethical behavior observed within the work group.<sup>116</sup> To reduce the likelihood of

112. USSG § 8B2.1 (2014).

113. Kimberly D. Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L. Q. 487, 510 (2003) (discussing how “little evidence exists at all concerning the effectiveness of internal compliance structures as a means to reduce socially harmful conduct, a fact that, in and of itself, is troubling given the legal system’s enthusiastic embrace of such structures as a liability determinant . . . [T]he evidence that does exist is decidedly mixed, with many of the most methodologically sound studies indicating the lack of effectiveness of such structures”); see also ERC Report, *supra* note 3, at 100 (recognizing that the “academic literature does not provide much detail about the specific program practices that yield the greatest effects when it comes to compliance and ethics”); Beeri et al., *supra* note 46, at 59; Max H. Bazerman & Francesca Gino, *Behavioral Ethics: Toward a Deeper Understanding of Moral Judgment and Dishonesty*, 8 ANNU. REV. LAW SOC. SCI. 85, 89 (2012).

114. See Jana L. Craft, *A Review of the Empirical Ethical Decision-Making Literature: 2004–2011*, J. BUS. ETHICS (Oct. 9, 2012), available at <http://link.springer.com/article/10.1007/s10551-012-1518-9/fulltext.html> (reviewing 84 articles); Michael J. O’Fallon & Kenneth D. Butterfield, *A Review of The Empirical Ethical Decision-Making Literature: 1996–2003*, 59 J. BUS. ETHICS 375, 375 (2005) (reviewing 174 articles).

115. See Hal E. Hershfield et al., *Short Horizons and Tempting Situations: Lack of Continuity to Our Future Selves Leads to Unethical Decision Making and Behavior*, 117 ORGANIZATIONAL BEHAV. & HUM. DECISION PROCESSES 298, 299 (2012) (discussing causes of unethical behavior); Alexandre Ardichvili et al., *Minding the Gap: Exploring Differences in Perceptions of Ethical Business Cultures Among Executives, Mid-Level Managers and Non-Managers*, 15 HUM. RES. DEV. INT’L 337, 340 (2012) (citing research finding a “relationship among leader’s values, morality and ethical role modeling, the quality of ethical business cultures of their organizations and ethical or unethical behavior of subordinates”); Kaptein, *Understanding Unethical Behavior*, *supra* note 109, at 847–51 (identifying clarity of ethical standards, management and supervisors’ role model for ethical behavior, managers’ and employees’ commitment to behave ethically, and the likelihood of managers and employees being punished for behaving unethically and rewarded for behaving ethically); O’Fallon & Butterfield, *supra* note 114, at 379 (surveying over two decades of research and finding that “idealism and deontology are positively related to ethical decision-making, whereas relativism and teleology [and other factors, such as economic orientation] are negatively related [to ethical decision-making]”); Craft, *supra* note 114 (summarizing research on decision making); Ashforth et al., *supra* note 8, at 677 (noting how the “organization-level research has shown, the optimal approach emphasizes aspirations and values backed by accountability to laws and regulations”).

116. Kaptein, *Understanding Unethical Behavior*, *supra* note 109, at 863.



unethical behavior, management should create an organization that promotes at least six dimensions of an ethical culture, in which

- 1) management and 2) supervisors act as ethical role models, 3) realistic moral standards are set and sufficient means are provided to behave ethically, 4) managers and employees are supported and committed to behave ethically, 5) adequate opportunity is provided to discuss ethical issues and dilemmas, and 6) unethical behavior is punished and ethical behavior is appreciated.<sup>117</sup>

The empirical foundation of effective compliance, however, remains incomplete. The research on different corporations' ethical cultures is still developing, perhaps because quantifying executives' and corporations' ethical values is difficult.<sup>118</sup> Nor is there strong empirical evidence that "the instruction of ethics within business schools provides any discernible impact on the ethicality of students," and if the ethics instruction is effective, "how or why it is effective."<sup>119</sup> Some studies find that university ethics instruction "is at best minimally effective in enhancing ethics among students and business people."<sup>120</sup> Consequently, an ethics code and ethics training do not necessarily provide greater ethical awareness, a stronger ethical culture, or less unethical, illegal behavior.<sup>121</sup>

117. *Id.*

118. Lee Biggerstaff et al., *Unethical Culture, Suspect CEOs and Corporate Misbehavior* 39 (Nat'l Bureau of Econ. Research, Working Paper No. 19261, 2013), [http://www.nber.org/papers/w19261.pdf?new\\_window=1](http://www.nber.org/papers/w19261.pdf?new_window=1) (noting the dearth of literature, but finding, consistent with the "upper echelons theory" of corporate behavior, that after hiring outsider CEOs with suspect ethics, as evidenced by their systematically backdating their option grants and exercises, firms are "more likely to just meet or narrowly beat analyst earnings expectations" and "use more earnings-increasing discretionary accruals in the quarters when they meet these thresholds"); May & Luth, *supra* note 46, at 548 (noting the few empirical findings on how to improve ethical awareness, decision-making, and behavior to science and engineering students); O'Fallon & Butterfield, *supra* note 114, at 399 (noting that no empirical study had examined in its entirety Rest's multi-step model of identifying an issue's moral nature, making a moral judgment, establishing moral intent of placing the moral concerns over other concerns, and engaging in moral action); Ashforth et al., *supra* note 8, at 679 ("Despite a vast body of literature on control in organizations, little research has focused on corruption control, and even less work has attempted to provide a comprehensive and systematic approach to understanding how organizations and their leaders can limit corruption through the varied control mechanisms at their disposal."); Krawiec, *supra* note 113, at 487 (noting the little empirical data that internal compliance structures reduce the incidence of prohibited conduct within organizations).

119. Ethan P. Waples et al., *A Meta-Analytic Investigation of Business Ethics Instruction*, 87 J. BUS. ETHICS 133, 134 (2009) (emphasis omitted) (arguing that although ethics courses (or discussion of ethics issues in other courses) are not useless per se, legal educators should engage in more inquiry on ways to design courses to achieve greater ethical awareness among diverse participants); see also Craft, *supra* note 114 (discussing some of the ethics literature); Bazerman & Gino, *supra* note 113, at 89 (citing literature that ethicists do not necessarily behave more ethically because they devote their careers to studying and teaching morality).

120. Waples et al., *supra* note 119, at 146; May & Luth, *supra* note 46, at 555, 559 (finding no statistically significant difference in the moral judgment of students who had the ethics-based courses and students in the regular courses; the study used "a 30-question multiple-choice assessment of the core concepts and standards in responsible conduct of research," whereby the total number of correct answers was used as the participant's knowledge).

121. Kaptein, *Longitudinal Study*, *supra* note 42, at 602, 607 (while finding that "86% of the Fortune Global 200 companies had a[n] ethics code in 2007, compared to 49% in 1999" and that the surveyed participants' scope of ethics programs increased between 2004 and 2008, data did not reflect any significant change in seven dimensions of the firms' ethical culture); Muel Kaptein, *Toward Effective Codes: Testing the*

More empirical research is needed to better understand when and why ethics programs work. But the available data do suggest that an ethics program—if part of the organization’s efforts to promote an ethical organizational culture—can effectively prevent and deter criminal conduct.<sup>122</sup> Logically this makes sense. If a sole proprietor can behave ethically, then adding one person to the firm should not automatically destroy its ethical culture. Maintaining the ethical culture can be difficult as more people join the firm. But the evidence does not identify a firm size when compliance efforts, however earnest, become ineffective. Thus, the Guidelines’ first assumption appears sound.

### *B. Are Effective Ethics Programs Attainable?*

The Guidelines next assume that an ethics program can “be reasonably designed, implemented, and enforced so that the program is generally effective in preventing and detecting criminal conduct.”<sup>123</sup> Even if an ethics program can theoretically promote an ethical organizational culture and deter and prevent unethical and illegal behavior, corporate crime will persist if effective compliance is too difficult or costly for many firms to achieve. If the DOJ’s and courts’ conception of an effective ethics program is unrealistic (say akin to expecting executives to run a sub-four minute mile), then few, if any, firms could obtain the Guidelines’ incentive. Executives would view effective compliance like the prospect of running a sub-four minute mile: theoretically possible, but practically unrealistic. Few firms would invest, on account of the Guidelines’ incentive, in additional compliance.

So is the courts’ and DOJ’s conception of an effective ethics program as unrealistic as asking executives to run a 3:59.4 minute mile? Here, too, the Guidelines’ assumption appears realistic. Policymakers generally defer to companies to tailor compliance measures to their specific business, the “risks associated with that business,”<sup>124</sup> and their size and resources.<sup>125</sup> Accordingly, the agencies and courts reject compliance as one-

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*Relationship with Unethical Behavior*, 99 J. BUS. ETHICS 233, 234 (2011) [hereinafter “*Toward Effective Codes*”] (noting 79 empirical studies’ divergent findings on a business ethics code’s effectiveness, where 35% of the studies found the code effective, 16% found a weak relationship, 33% found no significant relationship, and 14% yielded mixed results); Joseph A. McKinney et al., *The Effects of Ethical Codes on Ethical Perceptions of Actions Toward Stakeholders*, 97 J. BUS. ETHICS 505, 506–08 (2010) (citing varying results of empirical assessments of ethical codes’ effectiveness, but finding in their samples of over 2800 business professionals (albeit with a low response rate of roughly 18% and 12%) that employees at firms with ethical codes of conduct tend to perceive the ethically questionable behavior depicted in a series of vignettes to be less acceptable than employees at firms without an ethics code); Beeri et al., *supra* note 46, at 65 (noting that “studies are equivocal about the degree to which ethics codes, by themselves, have the power to affect ethical outcomes and recreate the moral reality”); Krawiec, *supra* note 113, at 511 (“Despite the pervasiveness of ethics codes in corporate America and the insistence by many legal compliance professionals on their importance as a deterrence tool, little evidence exists to support the theory that ethics codes modify employee behavior.”).

122. See *supra* notes 115–116.

123. USSG § 8B2.1.

124. FCPA Guide, *supra* note 16, at 56; OFT Guidance, *supra* note 15, at 8.

125. Int’l Competition Network, *Cartel Working Group Subgroup 2: Enforcement Techniques, Anti-Cartel Enforcement Manual: Chapter on Cartel Awareness, Outreach and Compliance* 20 (Mar. 2012) [hereinafter ICN], available at <http://www.internationalcompetitionnetwork.org/uploads/library/doc835.pdf> (noting that competition agencies “that have done research and work in the compliance area mention the importance of businesses developing a tailor-made approach which suits their particular situation”).

size-fits-all.<sup>126</sup> A “‘box-ticking’, ‘one size fits all’ approach to compliance,”<sup>127</sup> one agency’s case study found, “may well be counterproductive to instilling a compliance culture.”<sup>128</sup> Instead the DOJ and courts expect the ethics program’s designers and implementers to assess the potential risks of illegality, taking into account the industry dynamics, firm’s business, business model and objectives, various corporate strategies to achieve these objectives, including potential illegal strategies, and firm’s incentive structure.<sup>129</sup>

Besides recognizing compliance as firm-specific, courts and the DOJ recognize that compliance measures are inherently “dynamic and evolve as the business and the markets change.”<sup>130</sup> Firms must periodically assess the risk of criminal conduct, given changes in their business, industry, or culture.<sup>131</sup> Consequently, courts and agencies expect more than compliance manuals or training programs,<sup>132</sup> but provide firms wide latitude in how best to promote an ethical organization culture.<sup>133</sup> The DOJ, for example, eschews “formulaic requirements” to assess an ethics program’s effectiveness; prosecutors instead use “a common-sense and pragmatic approach to evaluating compliance programs, making inquiries related to three basic questions: Is the company’s compliance program well designed? Is it being applied in good faith? Does it work?”<sup>134</sup>

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126. FCPA Guide, *supra* note 16, at 57 (“When it comes to compliance, there is no one-size-fits-all program.”); OFT Guidance, *supra* note 15, at 4 (recognizing “that a ‘one size fits all’ approach is not appropriate for competition law compliance and that the appropriate actions to achieve a compliance culture will vary, for example depending on the size of business and the nature of the risks identified”); ICN, *supra* note 125, at 24 (“The ideas of how compliance should be practiced seem to have shifted over the years from a so called “check box” approach to a more risk-based approach.”).

127. OFT Guidance, *supra* note 15, at 25.

128. *Id.*; see also FCPA Guide, *supra* note 16, at 57 (warning how compliance programs “that employ a ‘check-the-box’ approach may be inefficient and, more importantly, ineffective”).

129. HHS & AHHA, *supra* note 39, at 5 (“Specifically, the Board must not only be knowledgeable about the corporate compliance program, but also be able to evaluate and recommend modifications to the program in light of ongoing organizational risk assessments. Thus, the Board needs to be knowledgeable of any major risks of unlawful conduct facing the organization to evaluate the adequacy of its compliance program in mitigating those risks.”); CANADA COMPETITION BUREAU, *supra* note 15, at 6 (the person or group responsible for compliance, to act effectively, must have “a solid understanding of what is taking place within the business”).

130. FCPA Guide, *supra* note 16, at 56.

131. USSG § 8B2.1(c) & cmt. n.7 (an organization, at the onset of its ethics and compliance efforts and periodically thereafter, must assess the risk of criminal conduct and take “appropriate steps to design, implement, or modify each requirement” set out in the Guidelines “to reduce the risk of criminal conduct identified through this process”); see also CANADA COMPETITION BUREAU, *supra* note 15, at 8, 10 (noting that “senior management should conduct risk assessments annually to better assess compliance priorities”); OFT Guidance, *supra* note 15, at 14 (highlighting “common potential competition law risks”); Murphy & Kolasky, *supra* note 22, at 61 (“Periodically assess the risks of cartel conduct occurring, including identifying ‘at risk’ personnel and focusing the program and allocating resources based on that assessment.”).

132. Murphy & Kolasky, *supra* note 22, at 62 (observing that “a company may no longer claim that written manuals and a few lectures constitute a compliance program. Today, anything less than the rigorous application of a broad range of management tools does not qualify as an effective compliance program”).

133. Paula Desio, Deputy General Counsel, *An Overview of the Organizational Guidelines*, U.S. SENTENCING COMM’N, [http://www.ussc.gov/sites/default/files/pdf/training/organizational-guidelines/ORG OVERVIEW.pdf](http://www.ussc.gov/sites/default/files/pdf/training/organizational-guidelines/ORG%20OVERVIEW.pdf) (last visited Apr. 21, 2014) (noting how the Guidelines criteria “embody broad principles that, taken together, describe a corporate ‘good citizenship’ model, but do not offer precise details for implementation”).

134. FCPA Guide, *supra* note 16, at 56 (Prosecutors answer these questions by considering “the

While not offering a model program, the Guidelines do expect effective ethics programs to have seven attributes:

1. Clear Compliance Standards and Procedures Designed to Prevent and Detect Criminal Conduct for Different Business Units Based on the Risks that May Likely Arise<sup>135</sup>
2. Senior Management's Knowledge, Commitment, Oversight and Support for Compliance<sup>136</sup>
3. Screen for Unethical Employees in Hiring and Promoting<sup>137</sup>

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comprehensiveness of the compliance program; the extent and pervasiveness of the criminal misconduct; the number and level of the corporate employees involved; the seriousness, duration, and frequency of the misconduct; and any remedial actions taken by the corporation, including, for example, disciplinary action against past violators uncovered by the prior compliance program, and revisions to corporate compliance programs in light of lessons learned. Prosecutors should also consider the promptness of any disclosure of wrongdoing to the government"); U.S. ATTORNEYS' MANUAL, *supra* note 16, at § 9-28.800.

135. USSG § 8B2.1(b); ERC Report, *supra* note 3, at 23. The standards should include codes of conduct and organizational policies tailored for each business unit. FCPA Guide, *supra* note 16, at 57 ("As DOJ has repeatedly noted in its charging documents, the most effective codes are clear, concise, and accessible to all employees and to those conducting business on the company's behalf."); CANADA COMPETITION BUREAU, *supra* note 15, at 8.

136. The firm's governing body, typically its Board of Directors, must be "knowledgeable about the content and operation of the compliance and ethics program." USSG § 8B2.1(b); *see also* CANADA COMPETITION BUREAU, *supra* note 15, at 7 (emphasizing senior management must brief the Board of Directors periodically about the compliance program). The Board must "exercise reasonable oversight with respect to the implementation and effectiveness of the compliance and ethics program." USSG § 8B2.1(b); *see also* U.S. ATTORNEYS' MANUAL, *supra* note 16, at § 9-28.800 (prosecutors consider whether "the corporation's directors exercise independent review over proposed corporate actions rather than unquestioningly ratifying officers' recommendations," whether internal audit functions are "conducted at a level sufficient to ensure their independence and accuracy," and whether "the directors established an information and reporting system in the organization reasonably designed to provide management and directors with timely and accurate information sufficient to allow them to reach an informed decision regarding the organization's compliance with the law"). Second, the firm's "high-level personnel" must "ensure that the organization has an effective compliance and ethics program;" at least one high-level personnel must be "assigned overall responsibility for the compliance and ethics program." USSG § 8B2.1(b)(2)(B). "High-level personnel" are "individuals who have substantial control over the organization or who have a substantial role in the making of policy within the organization" and "includes: a director; an executive officer; an individual in charge of a major business or functional unit of the organization, such as sales, administration, or finance; and an individual with a substantial ownership interest." USSG § 8A1.2, cmt. n.3(B); *see also* CANADA COMPETITION BUREAU, *supra* note 15, at 8 (advocating that "a member of senior management should be appointed as a compliance officer, responsible for ensuring compliance and for dealing with all questions and concerns pertaining to compliance with the Acts" and "[s]enior management should report to the board of directors on any compliance issues"). Finally, at least one firm employee must have "day-to-day operational responsibility for the compliance and ethics program," "report periodically to high-level personnel and, as appropriate, to the governing authority, or an appropriate subgroup of the governing authority, on the effectiveness of the compliance and ethics program," and "be given adequate resources, appropriate authority, and direct access to the governing authority or an appropriate subgroup of the governing authority." USSG § 8B2.1(b); CANADA COMPETITION BUREAU, *supra* note 15, at 6.

137. The organization must "use reasonable efforts not to include within the substantial authority personnel of the organization any individual whom the organization knew, or should have known through the exercise of due diligence, has engaged in illegal activities or other conduct inconsistent with an effective compliance and ethics program." USSG § 8B2.1(b)(3). "Substantial authority personnel" are "individuals who within the scope of their authority exercise a substantial measure of discretion in acting on behalf of an organization." USSG § 8A1.2, cmt. n.3(C). In implementing this, the firm must hire and promote individuals so as to ensure that all

4. Ongoing Training and Education<sup>138</sup>5. Monitoring, Auditing and Reporting Requirements and Periodic Self-Assessments of the Program's Effectiveness<sup>139</sup>6. Disciplinary Enforcement and Incentives Consistent with Compliance<sup>140</sup>7. Taking Corrective Measures After Detecting Criminal Conduct[.]<sup>141</sup>

The compliance industry does not claim that these seven steps are unrealistic. Instead the Guidelines' "seven-step standards for compliance/ethics programs have become the de facto framework for U.S. corporations and also serve as a reference point

high-level personnel and those with substantial authority "perform their assigned duties in a manner consistent with the exercise of due diligence and the promotion of an organizational culture that encourages ethical conduct and a commitment to compliance with the law." USSG § 8B2.1, cmt. n.4. This does not mean a blanket refusal to hire or promote individuals with a criminal record. A blanket prohibition could lead to civil liability. Tess Stynes, *EEOC Files Suits Against BMW Manufacturing, Dollar General*, WALL ST. J. (June 11, 2013), <http://online.wsj.com/article/BT-CO-20130611-706879.html>. Instead the firm should "consider the relatedness of the individual's illegal activities and other misconduct (i.e., other conduct inconsistent with an effective compliance and ethics program) to the specific responsibilities the individual is anticipated to be assigned and other factors such as: (i) the recency of the individual's illegal activities and other misconduct; and (ii) whether the individual has engaged in other such illegal activities and other such misconduct." USSG § 8B2.1, cmt. n.4.

138. The firm must "take reasonable steps to communicate periodically and in a practical manner its standards and procedures, and other aspects of the compliance and ethics program . . . by conducting effective training programs and otherwise disseminating information appropriate to such individuals' respective roles and responsibilities." USSG § 8B2.1(b)(4)(A). This includes not only its employees, but where appropriate, its agents. USSG § 8B2.1(b)(4)(B). Besides communicating general principals, the training must be tailored for the different business units to "demonstrate to staff, in a practical way, how compliance policies and procedures affect their daily activities." CANADA COMPETITION BUREAU, *supra* note 15, at 9; OFT Guidance, *supra* note 15, at 23 ("Many businesses find that competition law compliance training can be most effective if it focuses on training staff how to recognise potential competition law risks likely to be relevant to the business and prevent competition infringements from occurring in the first place."). This also includes opportunities "for extensive discussions on questions and answers." CANADA COMPETITION BUREAU, *supra* note 15, at 9.

139. The firm must take reasonable steps to ensure that its ethics program is being followed, "including monitoring and auditing to detect criminal conduct." USSG § 8B2.1(b)(5); *see also* CANADA COMPETITION BUREAU, *supra* note 15, at 11 (listing monitoring, auditing, and reporting as essential to an effective system); OECD, *supra* note 11, at 42. The firm must "evaluate periodically the effectiveness" of its ethics program and "publicize a system, which may include mechanisms that allow for anonymity or confidentiality, whereby the organization's employees and agents may report or seek guidance regarding potential or actual criminal conduct without fear of retaliation." USSG § 8B2.1(b)(5).

140. The firm must promote and enforce consistently its ethics program "throughout the organization through (A) appropriate incentives to perform in accordance with the compliance and ethics program; and (B) appropriate disciplinary measures for engaging in criminal conduct and for failing to take reasonable steps to prevent or detect criminal conduct." USSG § 8B2.1(b)(6); *see also* CANADA COMPETITION BUREAU, *supra* note 15, at 12 (firm's efforts, to be "credible and effective," should "explicitly state that disciplinary actions (for example, suspension, demotion, dismissal and even legal action) will be taken where an employee contravenes the Acts" and with respect to incentives, compliance efforts can be considered "for the purposes of employee evaluations, promotions and bonuses"); OECD, *supra* note 11, at 42 ("It should be made clear that violations, especially price fixing, will not be tolerated, i.e. that the company will not defend or support violators and that they will lose their jobs.").

141. "After criminal conduct has been detected, the organization shall take reasonable steps to respond appropriately to the criminal conduct and to prevent further similar criminal conduct, including making any necessary modifications to the organization's . . . ethics program." USSG § 8B2.1(b)(7). The court should not reduce the corporate fine "if the organization unreasonably delayed reporting the offense to the appropriate governmental authorities." Sentencing Comm'n Primer, *supra* note 59, at 5.

for many U.S. regulatory and enforcement agencies,” and “most companies today with serious compliance/ethics programs carefully calibrate their programs to the Guidelines compliance/ethics program criteria.”<sup>142</sup>

Consequently, in recognizing effective compliance as company specific and dynamic, the courts and DOJ do not impose an unrealistic or impractical model ethics program. The Guidelines provide the expectations of an effective ethics program: namely that management and employees “(1) exercise due diligence to prevent and detect criminal conduct; and (2) otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.”<sup>143</sup> Besides the seven steps, the Guidelines leave the details to the firm. As the U.K.’s Office of Fair Trading observes, “The key point is that businesses should find an effective means of identifying, assessing, mitigating and reviewing their competition law risks in order to create and maintain a culture of compliance with competition law that works for their organisations.”<sup>144</sup> Thus effective compliance (like running a sub-20 minute mile) is attainable.

### C. Can Courts and Agencies Assess an Ethics Program’s Effectiveness?

The Guidelines assume that courts can distinguish between effective and otherwise ineffective or sham ethics programs. Suppose courts often err, finding ineffective ethics programs to be effective, and effective programs to be ineffective. Firms with effective programs often will not get the Guidelines’ incentive, while competitors with cosmetic, ineffective programs will get the incentive. It is like a county fair contest for the best home-cooked pie. If the judges cannot distinguish between store-bought and home-cooked pies, and if store-bought pies are cheaper and more convenient to enter, then imagine the frustration when store-bought pies get the prize. Many firms, to obtain the Guidelines’ incentive, would simply invest in cosmetic, off-the-shelf compliance programs (sufficient for the court to make a Type I, false positive error), but not necessarily genuine, firm-specific compliance (given the risk of the court making a Type II, false negative error). As a result, cosmetic (rather than effective) compliance and corporate crime would persist.

Are error costs causing the problem here? No one seriously contends that an ethics program should automatically immunize a firm from liability or reduce its fine.<sup>145</sup> If *any* ethics program suffices, firms would invest in cosmetic compliance. Few would

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142. ERC Report, *supra* note 3, at 2, 30.

143. USSG § 8B2.1(a); *see also* ICN, *supra* note 125, at 21–22 (“The most important goal in any case is to achieve an effective culture of compliance within the business. For some businesses this may mean a change of behaviour within the organization.”).

144. OFT Guidance, *supra* note 15, at 4.

145. *See, e.g.*, Murphy, *supra* note 38, at 713 (“The mere presence of a compliance program, however, ‘does not immunize the corporation from liability when its employees, acting within the scope of their authority, fail to comply with the law.’”) (internal citation omitted); Murphy & Kolasky, *supra* note 22, at 61 (“No company should receive credit for merely going through the motions and paying lip service to compliance.”); *E.E.O.C. v. Xerxes Corp.*, 639 F.3d 658, 669 (4th Cir. 2011) (“[M]ere promulgation of an anti-harassment policy, no matter how well-conceived, will not suffice to show the requisite level of care where the employer has administered the policy in bad faith or has rendered it ineffectual by acting unreasonably.” (quoting *Spriggs v. Diamond Auto Glass*, 242 F.3d 179, 187 (4th Cir. 2001))).

necessarily promote an ethical culture that effectively deters wrongdoing.<sup>146</sup> Nor can effectiveness mean failsafe.<sup>147</sup> As the DOJ recognizes, “no compliance program can ever prevent all criminal activity by a corporation’s employees.”<sup>148</sup> Requiring failsafe compliance nullifies the Guidelines’ financial incentive of a reduced fine, which the firm obtains after being found (or pleading) guilty. Thus, the Guidelines only require that the program “be reasonably designed, implemented, and enforced so that the program is generally effective in preventing and detecting criminal conduct.”<sup>149</sup> Consequently, courts must distinguish generally effective (but not failsafe) compliance efforts from ineffective or sham efforts.<sup>150</sup>

The sentencing data do not suggest that error costs are contributing to ineffective compliance. If error costs were high, courts would often find ineffective ethics programs to be effective. That is clearly not the case. But as the next Part addresses, four criteria that the courts and DOJ use to assess an ethics program’s effectiveness have significant problems, which can diminish the value of the Guidelines’ financial incentive.

#### IV. PROBLEMS WITH AN EXTRINSIC, INCENTIVE-BASED APPROACH TO COMPLIANCE

As Part II addresses, ineffective ethics programs and corporate crime persist despite the Guidelines’ incentive. This problem, as addressed in Part III, is not attributable to three key assumptions. One may conclude that the Guidelines’ financial incentive is insufficient. To induce firms to promote an ethical organizational culture, courts should give even greater credit for compliance programs when determining the corporate fine.

One outstanding empirical issue is whether the Guidelines’ financial incentive is optimal. One Sentencing Commissioner, after Enron, noted the “considerable evidence” that the Guidelines’ mitigation for effective ethics programs, “and the powerful fine mitigation incentives embodied within it, have resulted in substantial beneficial effects over the past decade by advancing corporate ethics, improving corporate governance, and preventing crime.”<sup>151</sup> Unfortunately this cannot be verified mathematically. The costs and benefits of the Guidelines’ incentive are not quantifiable.<sup>152</sup> As one competition law

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146. OECD, *supra* note 11, at 26 (“[C]ompanies will have incentives merely to implement low-cost, low-maintenance, superficial [ethics programs] that do not actually contribute much to prevention.”).

147. USSG § 8B2.1(a)(2) (“The failure to prevent or detect the instant offense does not necessarily mean that the program is not generally effective in preventing and detecting criminal conduct.”).

148. U.S. ATTORNEYS’ MANUAL, *supra* note 16, at § 9-28.800.

149. USSG § 8B2.1(a)(2).

150. OECD, *supra* note 11, at 22.

151. John R. Steer, Member & Vice Chair, U.S. Sentencing Comm’n, *The Sentencing Commission’s Implementation of the Sarbanes-Oxley Act 22 (2003)*, available at [http://www.uscc.gov/Guidelines/Organizational\\_Guidelines/Selected\\_Articles/Steer-PLI-2003.pdf](http://www.uscc.gov/Guidelines/Organizational_Guidelines/Selected_Articles/Steer-PLI-2003.pdf).

152. To illustrate, suppose policymakers agreed to reduce the antitrust corporate fines by X percent or Y amount if the violator had an effective ethics program at the time of the offense. Also assume that firms predictably respond to monetary incentives, that the potential reduction in fines actually increases the firms’ compliance efforts, which in turn reduces corporate crime, and that policymakers can control the other variables that may affect the firms’ investment in compliance or cause corporate crime to decline. To ascertain the incentive’s benefits, policymakers would have to quantify the incremental investment in corporate compliance caused by the incentive, the reduction in corporate crime as a result, the societal benefits from this reduction in crime, and any other societal benefits from the firms’ incremental increase in compliance. Policymakers next must ascertain the incentive’s costs, including the agencies’ and courts’ administrative costs to determine whether the defendants’ ethics programs are indeed effective, the lost revenue from the lower fines, and the

scholar observed, "There have been no attempts in the literature to estimate empirically the general effects, positive or negative, of antitrust compliance programmes."<sup>153</sup> The same is true of the Guidelines' incentive.

Consequently, debating the size of the Guidelines' incentive, without an empirical basis, will not bring consensus. One can instead examine whether an extrinsic, incentive-based approach to compliance works. If an extrinsic approach is at odds with the Guidelines' three assumptions discussed in Part III, then the size of the incentive (whether doubled or halved) is less important. This Part examines several shortcomings of the Guidelines' extrinsic, incentive-based approach to compliance, and why it is contributing to ineffective corporate compliance.

*A. Under an Extrinsic, Incentive-Based Approach to Compliance, Firms Will Demand Specific Guidance on What Exactly They Must Do to Obtain the Incentive*

An extrinsic, incentive-based approach implicitly encourages firms to analyze the costs and benefits of an effective ethics program. This has several implications. First, for the incentive to work, a firm must be able to assess the return on its investment in extra compliance. Here the firm must assess the likelihood of receiving the incentive and its magnitude. Second, to assess its compliance costs, the firm must know what specific additional steps it must undertake, for how long, and the cost to undertake these steps. Third, to incentivize firms to improve their compliance efforts, the Guidelines adopt an implied contract. If a firm undertakes compliance, including Part III.B's seven steps, then courts will reduce the firm's future penalty by a specified amount.<sup>154</sup>

Under an extrinsic, incentive-based approach, firms will demand to know what is expected of them to receive the incentive, and courts and the DOJ should anticipate the compliance industry's demand for "a greater use of 'plain English.'"<sup>155</sup> Not surprisingly, the compliance industry complains about the lack of guidance as to what firms must specifically do to obtain the Guidelines' incentive:

Many compliance/ethics programs fall short of their potential because portions of the [Guidelines] remain underemphasized or unclear. The ability of business managers to embrace and implement the... criteria outlined in the [Guidelines] is tied to their ability to understand the specific actions or decisions expected of them.<sup>156</sup>

As these concerns reflect, absent specific guidance from the courts and DOJ, companies are reluctant to invest in compliance: "Particularly in times of shrinking

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amount spent on compliance that is socially wasteful (i.e., does not actually promote compliance and deter crime). Finally policymakers must ascertain whether the incentive's size is optimal. The incentive cannot be too generous (i.e., reducing fines beyond what is necessary to induce optimal compliance) or meager (as firms will underinvest in compliance).

153. Wils, *supra* note 23, at 62.

154. ABA Section of Business Law, Corporate Compliance Committee, *Survey—Corporate Compliance*, 60 BUS. LAWYER 1759, 1762 (2005) [hereinafter ABA Compliance Survey] (noting that the key to incentive-based approach is "that the government has made a credible (if not always legally binding) commitment to offer some credit to organizations with a qualifying ethics and compliance program").

155. ERC Report, *supra* note 3, at 5.

156. *Id.* at 4.



budgets and restricted resources it would be very helpful to have some evidence to demonstrate why a solid compliance program is needed—and why a better program is worth the effort versus a bare bones minimum.”<sup>157</sup>

One fundamental problem with an extrinsic, incentive-based approach is that the courts and DOJ cannot supply the answer.<sup>158</sup> They cannot identify—aside from Part III.B’s seven steps—what additional steps that firms must undertake to improve their ethical culture significantly and lower the risk of unethical and illegal behavior by their employees. Given the dynamic, firm-specific nature of compliance, neither the courts nor DOJ can offer a model ethics program or “formulaic requirements” that will effectively deter unethical and illegal conduct (an impossible task with over 4000 federal crimes<sup>159</sup>). Moreover, the consensus is that such a checklist is counterproductive. A “‘check the box’ type of mentality” may be easier for companies to undertake and for the courts and DOJ to review, but that mentality “discourages critical judgment about how to instill effectiveness.”<sup>160</sup>

*B. Under an Extrinsic, Incentive-Based Approach, Firms Will Demand Uniform Standards that Accurately, Predictably, Objectively, Quickly & Inexpensively Assess an Ethics Program’s Effectiveness*

An incentive’s value also depends on the firm’s ability to assess its likelihood of obtaining it. To illustrate, suppose you told a painter, “Paint me a pleasing picture, and you will receive \$10 million.” Surely the painter would want as much information as possible as to what you consider a pleasing picture. Firms, using the courts’ criteria, should accurately predict the likelihood of their ethics program being found effective. Besides being accurate, the courts’ evaluative criteria should be easy and inexpensive to apply.<sup>161</sup> Accordingly for an extrinsic, incentive-based approach to succeed, firms will demand, and the courts and DOJ must supply, uniform, clear, and objective evaluative standards and a public accounting of how and when ethics programs are taken into account.

One problem, according to the compliance industry, is that the agencies and courts do not have such criteria.<sup>162</sup> While the record of ethics programs “getting consideration

157. *Id.* at 44 (“The current DOJ approach allows cynical executives to conclude that any violation justifies a DOJ conclusion that the compliance program was ineffective no matter how robust the program was in preventing other problems. As a result, additional resources are diverted elsewhere, an outcome potentially harmful to society at large and in opposition to what the DOJ probably intended.”).

158. *See, e.g.,* McKinney et al., *supra* note 121, at 506 (noting how “the legal and regulatory system cannot be sufficiently detailed to anticipate every conceivable situation within which unethical behavior might take place nor is it likely to evolve at a rate fast enough to keep up with that of the constantly changing business environment”).

159. Podgor, *supra* note 14, at 1529, 1532 n.56.

160. ERC Report, *supra* note 3, at 5; *see also* Ashforth et al., *supra* note 8, at 677 (noting how detailed conduct “regulation can also have harmful consequences if it causes organizations to focus on following rules imposed by external regulators, rather than focusing internally on creating aspirational ethical cultures”).

161. *See, e.g.,* OECD, *supra* note 11, at 352 (noting “that the call appears to be for competition authorities to think about what a good compliance programme would entail and setting standards that firms can follow”) & 358 (noting that “if competition authorities want to promote compliance with competition law, it is arguably the responsibility of competition authorities to engage in a discussion with the business community and work together towards some common standards”).

162. ERC Report, *supra* note 3, at 10 (“The dearth of information about the impact of [ethics programs] in

in the settlement of cases is thin, the standards and processes by which compliance and ethics programs are measured for effectiveness are thinner.”<sup>163</sup> The compliance industry notes the “lack of consistency in policies toward [ethics programs] across the various government agencies that play a role in corporate law enforcement and regulation because there is neither a requirement that these policies be aligned nor a mechanism available for doing so.”<sup>164</sup> Thus, the industry demands a “common set of criteria, assessment framework, methodology, or work steps . . . to measure the effectiveness of compliance and ethics programs,” so that “two different prosecutors confronting similarly-situated compliance programs will arrive at similar conclusions in assessing those programs.”<sup>165</sup>

A greater problem, however, is that no such evaluative criteria exist.<sup>166</sup> The key attribute of an effective ethics program—whether the defendant’s organizational culture genuinely encourages ethical conduct and a commitment to comply with the law—is not susceptible to a uniform evaluative standard that broadly applies across industries; is sufficiently objective so that firms, agencies, and courts likely reach the same conclusion; and is easy for firms, courts and agencies to administer without requiring too much time or expense. Effective ethics programs are both dynamic and tailored to the firm’s size, industry, organizational culture, informal norms, leadership style, business and legal environment, and financial condition. Measures effective for one firm are not necessarily effective for another.

This has several implications. First, courts cannot benchmark the defendant’s ethics program against a model program. Second, the talisman of effective compliance cannot be the presence of specific objective components, such as training materials or an ethics code, which alone do not prevent criminal conduct and promote an ethical organizational culture.<sup>167</sup> Third, because the DOJ and courts discourage firms from taking a checklist, one-size-fits-all approach to compliance, it would be counterproductive if they used a checklist of compliance measures to assess an ethics program’s effectiveness. Otherwise firms would base their compliance efforts on the government’s checklist.

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DOJ decision-making undermines the [Guidelines’] policy of incentivizing the development of best practice compliance/ethics programs. DOJ should provide a public accounting of the impact of [ethics programs] in DPAs and require that press releases and other statements regarding cases of corporate or other organizational misconduct explicitly discuss the role played by compliance/ethics. It also should collect and publish aggregate data on the role of [ethics programs] in such cases.”)

163. *Id.* at 49.

164. *Id.* at 4 (noting how it “is often difficult to determine what elements agencies look for in evaluating compliance/ethics programs. While some agencies rely heavily on the [Guidelines’] framework, others do not. Nor is it always clear that an agency, in fact, grants credit for effective programs even when that agency has a policy that ostensibly supports their adoption”).

165. *Id.* at 50.

166. Wils, *supra* note 23, at 68–69 (noting the impossibility “for authorities and courts to distinguish reliably and at reasonable cost between situations where antitrust compliance programmes are part of a culture and practice of real compliance and situations of symbolic or cosmetic compliance”).

167. Kaptein, *Understanding Unethical Behavior*, *supra* note 109, at 858 (finding that an organization having an ethics program per se said “very little about the frequency of observed unethical behavior,” which is consistent with the other empirical literature that “the mere existence of an ethics program does not imply that it is effective,” since effectiveness “is determined by the manner in which it is developed, implemented, and embedded—as well as by the content and quality of each component”).

As a result, few objective criteria exist to assess an ethics program's effectiveness.<sup>168</sup> The Guidelines do provide, as Part III.B discusses, seven measures expected from an effective ethics program.<sup>169</sup> Although the absence of a measure suggests ineffective compliance, the seven steps are not sufficient to promote an ethical organizational culture. Moreover, several evaluative criteria that the DOJ and courts use, as the next four subparts discuss, have inherent problems that diminish the effectiveness of an extrinsic, incentive-based approach.<sup>170</sup>

### *1. Failure to Follow Others*

One Guidelines' criterion is whether the firm failed "to incorporate and follow applicable industry practice or the standards called for by any applicable governmental regulation."<sup>171</sup> Presumably, industry-wide compliance practices or standards must be effective to promote compliance (otherwise why would so many firms follow them). Moreover, the Guidelines endorse small organizations to model their "own compliance and ethics program on existing, well-regarded compliance and ethics programs and best practices of other similar organizations."<sup>172</sup>

But the fact that the industry's compliance practices and standards coalesce says little about their effectiveness in promoting an ethical culture and preventing criminal conduct. Firms, for example, can have strong economic incentives to follow other firms' compliance practices if doing so lowers their compliance costs (by avoiding the costs of independently designing and tailoring the practices) and provides safety in numbers. Moreover, industry practices are probably less dynamic than the customized, risk-based approach that the Guidelines otherwise endorse.<sup>173</sup>

Second, in concluding that the firm, having followed industry-wide compliance practices and procedures, reasonably promoted compliance, the DOJ and courts become more susceptible to the fundamental attribution error. They can attribute the criminal behavior to the dispositional flaws of a few bad apples, who—despite the company's efforts—were pre-disposed to crime.<sup>174</sup> In overvaluing dispositional or personality-based

168. USSG § 8B2.1 cmt. n.2(A).

169. *Id.* ("Each of the requirements set forth in this guideline shall be met by an organization.").

170. One criterion that does not appear problematic is whether the firm earlier engaged in misconduct, "similar in nature to the conduct underlying the instant offense, without regard to whether or not such conduct violated the same statutory provision." USSG § 8A1.2 cmt. n.3(F). "Recurrence of similar misconduct creates doubt regarding whether the organization took reasonable steps to meet the requirements of this guideline." USSG § 8B2.1 cmt. n.2(D). A history of similar misconduct "may be probative of a corporate culture that encouraged, or at least condoned, such misdeeds, regardless of any compliance programs." U.S. ATTORNEYS' MANUAL, *supra* note 16, at § 9-28.600 ("Criminal prosecution of a corporation may be particularly appropriate where the corporation previously had been subject to non-criminal guidance, warnings, or sanctions, or previous criminal charges, and it either had not taken adequate action to prevent future unlawful conduct or had continued to engage in the misconduct in spite of the warnings or enforcement actions taken against it.").

171. USSG § 8B2.1 cmt. n.2(B).

172. USSG § 8B2.1 cmt. n.2(C)(iii).

173. ICN, *supra* note 125, at 18 ("[I]t is no longer considered sufficient for businesses to create a static compliance program which describes in general the overall risks of breaching competition law. 'Risk-based' means that the approach is tailored to the specific risks faced by the business. The risks identified will necessarily vary, and each business must take appropriate actions according to the specific risks which that particular business faces.").

174. Ashforth et al., *supra* note 8, at 672 ("[W]e are most accustomed to thinking about corrupt behavior in

explanations for other individuals' observed unethical or illegal conduct, they can undervalue or ignore the effect of situational factors that promote unethical behavior.<sup>175</sup> Stanley Milgram's famous experiment showed how, contrary to most people's expectations, many ordinary adults administered what they believed to be a 450-volt electrical shock to an unresponsive volunteer.<sup>176</sup> The courts may not inquire, for example, how the firm could have prevented the employee's temptation in the first place.<sup>177</sup>

Compliance can overemphasize screening employees for dispositional flaws<sup>178</sup> and discount or ignore the harder-to-fix situational factors within that firm or industry that foster criminality.<sup>179</sup> For example, in one study, corporate higher-ups viewed price-fixing as primarily the result of a few employees' dispositional flaws, i.e., "isolated incidents of human weakness tempted by the prevailing low morals in a few isolated industry subcultures."<sup>180</sup> In contrast, mid-level managers closer to those convicted for price-fixing emphasized the prevailing situational factors, namely, the conflicting company goals or moral gray zones where "[t]he need to survive conflicts with the drive to be super clean."<sup>181</sup>

A third problem in encouraging firms to follow industry-wide compliance practices is its inviting greater subjectivity and arbitrariness in the government's assessment, thereby reducing the extrinsic incentive's value. Returning to competition law, suppose the major firms had similar compliance practices. Nonetheless the firms colluded on price. How would the DOJ and court assess which firms had effective ethics programs? Suppose Firm *A* convinced the DOJ that its ethics program was effective. In treating Firm *A* leniently, the DOJ effectively tells the other defendants that their ethics programs,

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organizations primarily in microlevel terms. It is comforting to assume that one bad apple or renegade faction within an organization is somehow responsible for the corruption we too often observe.").

175. See, e.g., Kimberly Kirkland, *Self-Deception and the Pursuit of Ethical Practice: Challenges Faced by Large Law Firm General Counsel*, 9 U. ST. THOMAS L.J. 593, 594 (2011) (many general counsel interviewed appeared to view character flaws as a primary cause of lawyer misconduct); Ashforth et al., *supra* note 8, at 672-73 ("[O]therwise decent people can end up engaging in questionable practices as a result of their immersion in, and socialization into, the social and cultural environment of a corrupt organization."); Francesca Gino et al., *See No Evil: When We Overlook Other People's Unethical Behavior* 4 (Harv. Bus. School, Working Paper No. 08-045, 2008), available at [http://www.hbs.edu/faculty/Publication%20Files/08-045\\_18339ad6-e675-48ee-9db8-72a3e6ef3f03.pdf](http://www.hbs.edu/faculty/Publication%20Files/08-045_18339ad6-e675-48ee-9db8-72a3e6ef3f03.pdf); Robert A. Prentice, *Good Directors and Bad Behavior*, 55 BUS. HORIZONS 535, 539 (2012).

176. See generally STANLEY MILGRAM, *OBEDIENCE TO AUTHORITY* (1974) (describing a series of experiments to see how far human subjects would go to obey authority); PHILIP ZIMBARDO, *THE LUCIFER EFFECT: UNDERSTANDING HOW GOOD PEOPLE TURN EVIL* (1st ed. 2007) (explaining an "attempt to understand the processes of transformations at work when good or ordinary people do bad or evil things"); Bazerman & Gino, *supra* note 113, at 92.

177. Regan, *supra* note 33, at 1964 ("A sound risk management program identifies what are most likely to be occasions of temptation and attempts to adopt measures that reduce their potency. As situationism recommends, it focuses on a point earlier in the causal chain than the ultimate ethically significant decision.").

178. Managers may also overestimate their abilities to detect dispositional flaws. Langevoort, *supra* note 64, at 88.

179. *Id.* at 84; Ashforth et al., *supra* note 8, at 672 ("This internal locus of attribution suggests that corruption can be eliminated if only organizations can root out and keep out corrupt individuals").

180. Jeffrey Sonnenfeld, *Executive Apologies for Price Fixing: Role Biased Perceptions of Causality*, 24 ACAD. MGMT. J. 192, 195 (1981).

181. *Id.* at 196.

unlike Firm A's, were ineffective or shams. This will strike Firm A's competitors as arbitrary since they, like Firm A, followed the same industry practices. The DOJ's decision to treat Firm A leniently will likely rest on less tangible, more subjective factors.<sup>182</sup> Companies can affect compliance through myriad factors, many not visible to the public, agencies, courts, and other firms. Firm A's competitors would question the accuracy and objectivity of the DOJ's decision, thereby increasing the DOJ's costs to defend its decision. Thus, for some, the fair outcome is to hold every conspirator liable.<sup>183</sup> Anticipating this outcome, firms may discount the value of Guidelines' incentive, thereby reducing its effectiveness to promote compliance.

## 2. Assessing the Tone at the Top

The Guidelines assume that an ethics program is ineffective "if an individual—(i) within high-level personnel of a small organization; or (ii) within substantial authority personnel, but not within high-level personnel, of any organization, participated in, condoned, or was willfully ignorant of, the offense."<sup>184</sup> This criterion dovetails with the courts' overall assessment of the senior executives' commitment to promote an ethical organizational culture. To set the proper tone, the firm's executives in their assigned duties must promote "an organizational culture that encourages ethical conduct and a commitment to compliance with the law."<sup>185</sup> The Guidelines and business ethics literature recognize that any program's effectiveness depends on senior management's unequivocal and visible commitment, involvement, and support.<sup>186</sup> Thus, for agencies

182. Wils, *supra* note 23, at 66 (illustrating how "ostensibly identical antitrust compliance programmes can be part of a culture and practice of real compliance, an irrelevant sideshow, or part of a calculated attempt to project a misleading image of compliance").

183. *Id.* at 74 ("Given the many and complex ways in which companies can influence the likelihood of antitrust infringements being committed by their employees, the impossibility of reliably capturing all these ways in a list of characteristics of supposedly 'effective' compliance programmes that can be applied by competition authorities or courts at reasonable cost, and the fact that companies financially benefit from antitrust infringements irrespective of how exactly they were committed, company liability for all antitrust infringements engaged in by their employees is both efficient and fair.").

184. USSG § 8C2.5(f)(3)(B); Sentencing Comm'n Primer, *supra* note 59, at 4. This presumption does not apply if—(i) The individual or individuals with operational responsibility for the compliance and ethics program . . . have direct reporting obligations to the governing authority or an appropriate subgroup thereof (e.g., an audit committee of the board of directors); (ii) The compliance and ethics program detected the offense before discovery outside the organization or before such discovery was reasonably likely; (iii) The organization promptly reported the offense to appropriate governmental authorities; and (iv) No individual with operational responsibility for the compliance and ethics program participated in, condoned, or was willfully ignorant of the offense." USSG § 8C2.5(f)(3)(C).

185. USSG § 8B2.1(b).

186. CANADA COMPETITION BUREAU, *supra* note 15, at 6 ("Fostering a culture of compliance must start at the top. Senior management must set the tone and recognize that it is part of their leadership role to ensure compliance with the law and with any court order imposed on their business."); OECD, *supra* note 11, at 24; OFT Guidance, *supra* note 15, at 10 ("Senior management, especially the board, must demonstrate a clear and unambiguous commitment to competition law compliance. Without this commitment, any competition law compliance efforts are unlikely to be successful."); Kaptein, *Toward Effective Codes*, *supra* note 121, at 237 (collecting studies on the importance of the board's and executives' commitment to effectuate firm's ethics code); John M. Schaubroeck et al., *Embedding Ethical Leadership Within and Across Organization Levels*, 55 ACAD. MGMT. J. 1053, 1058 (2012) (discussing recent studies finding "when individuals perceive their leader as a proponent and exemplar of ethical behavior, they report individual and work unit psychological states that

and courts, “compliance begins with the board of directors and senior executives setting the proper tone for the rest of the company.”<sup>187</sup> The role and conduct of senior management are the “most important” factors to assess how pervasive wrongdoing was within the firm.<sup>188</sup>

At times, the senior management’s indifference or hostility to an ethical organizational culture is apparent. One egregious example is Archer Daniels Midland Co. (ADM). While illegally colluding to fix prices in a hotel conference room, ADM’s President told his competitor that ADM’s corporate slogan, which “penetrated the whole company,” was “Our competitors are our friend. Our customers are the enemy.”<sup>189</sup> The business ethics literature shows how “rewarding unethical behavior tends to increase the frequency of such behavior, while effective sanctioning systems tend to decrease such behavior.”<sup>190</sup> Thus, the government can easily assess the tone at the top when the senior executives themselves are committing the crimes or are directly rewarding employees to violate the law.

It is questionable, however, that the government can accurately, predictably, objectively, quickly, and inexpensively assess the tone at the top when senior executives send out mixed signals. Management can exhort employees to behave ethically, yet require financial targets that in the employees’ mind can be realistically achieved only through illegal and unethical means: “If there is any ambiguity in management’s commitment to compliance, whether at the senior, middle or lower levels, then staff may feel that infringing competition law is ‘worth the risk’, in order to achieve extra sales to meet an internal target.”<sup>191</sup> For example, after being involved in over a dozen antitrust cases in the 1940s, General Electric (GE) disseminated in the 1950s its written policy that

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are conducive to more ethical conduct” and when “they perceive stronger ethical leadership, followers are more likely to engage in prosocial behaviors and less likely to engage in deviant or counterproductive behaviors”); NATIONAL ASSOCIATION OF CORPORATE DIRECTORS, REPORT OF THE NACD BEST PRACTICES COUNCIL: COPING WITH FRAUD AND OTHER ILLEGAL ACTIVITY 1, 11 (1998) [NACD] (discussing how setting the “tone at the top” is an effective deterrent to fraud and other illegal activity).

187. FCPA Guide, *supra* note 16, at 57.

188. U.S. ATTORNEYS’ MANUAL, *supra* note 16, at § 9-28.500; *see also* CANADA COMPETITION BUREAU, *supra* note 15, at 17 (noting that if senior management participated in or condoned such illegal conduct, “it will be apparent to the Bureau that senior management’s commitment to compliance was not serious and the program was neither credible nor effective”).

189. Scott D. Hammond, Dir. of Criminal Enforcement, U.S. Dep’t of Justice, Antitrust Div., *The Fly On The Wall Has Been Bugged—Catching An International Cartel In The Act* (May 15, 2001), *available at* <http://www.justice.gov/atr/public/speeches/8280.htm>.

190. O’Fallon & Butterfield, *supra* note 114, at 398.

191. OFT Guidance, *supra* note 15, at 11; *see also* OECD, *supra* note 11, at 3 (observing how “company’s top executives might express support for competition law compliance, but simultaneously give signals in other contexts that they really do not care how sales targets are met, just as long as they are met”); *Global Economic Crime Survey*, *supra* note 106, at 5 (finding that 68% of fraud practitioners attributed greater risk of fraud to increased “incentives or pressures” to engage in misconduct); Kaptein, *Toward Effective Codes*, *supra* note 121, at 237 (discussing the empirical literature on how management’s financial targets can influence compliance); Niki A. Den Nieuwenboer & Muel Kaptein, *Spiraling Down into Corruption: A Dynamic Analysis of the Social Identity Processes that Cause Corruption in Organizations to Grow*, 83 J. BUS. ETHICS 133, 138 (2008) (collecting studies finding corruption related to performance pressure from performance targets); Ashforth et al., *supra* note 8, at 673 (noting the “widely and long-held notion that senior leaders are often responsible for corrupt actions by setting unrealistic financial goals and modeling, condoning, or simply turning a blind eye to the means underlings use to achieve them”).

employees must “conform strictly to the antitrust laws.”<sup>192</sup> But GE executives were under tremendous corporate pressure to meet their departments’ financial goals. Each year, these managers had to budget for more profit as a percent of net sales as well as a larger percentage of available business. These “reach” goals were unattainable, according to some mid-level GE executives, absent collusion. If they failed to meet these “reach” goals, the GE executives could expect to be fired. As one GE executive rationalized, collusion may have been illegal “but it wasn’t unethical.”<sup>193</sup>

Senior executives can have strong economic incentives to send mixed signals:

Given that antitrust infringements can bring great financial benefit to companies, that a company can easily encourage antitrust infringements, notwithstanding any antitrust compliance programme, in particular by setting excessive financial targets and incentives, and that the cost of setting up a compliance programme is low compared to the potential benefits from antitrust infringements, companies would have a clear incentive to set up a compliance programme so as to obtain immunity from fines, while maximizing antitrust infringements through excessive performance targets and incentives.<sup>194</sup>

Mixed signals go beyond financial goals. One study found that the type of goal—interpersonal performance goals (i.e., pitting oneself against others) versus intrapersonal mastery goals (i.e., striving to do better, and avoid doing worse, than one has done before)—affected the participants’ intentions to cheat. Those with performance goals reported stronger intentions to cheat than those with mastery goals.<sup>195</sup> Moreover, the performance goal participants cheated significantly more than the mastery goal participants.<sup>196</sup> If employees are pitted against one another and if some achieve their performance goals through illegal means and are not punished, then a race to the bottom ensues.<sup>197</sup> So if the executives intentionally select interpersonal performance goals, which foster unethical behavior, should courts find the firm’s compliance efforts ineffective, however earnest?

Besides deciphering mixed-signals, courts and the DOJ will have a hard time accurately, predictably, and easily reconciling conflicting perspectives of the tone at the top and the firm’s ethical culture. At times, fans of opposing football teams perceive the action on the field differently. In a Dartmouth–Princeton football game, for example, nearly “all Princeton students judged the game as ‘rough and dirty;’” almost 90% of the Princeton students thought the Dartmouth players started the rough play; the Princeton students saw the Dartmouth team make over twice as many infractions as their team made.<sup>198</sup> A majority of the Dartmouth students, however, thought both sides were to

192. Richard Austin Smith, *The Incredible Electrical Conspiracy (Part I)*, FORTUNE, Apr. 1961, at 135.

193. *Id.*

194. Wils, *supra* note 23, at 18.

195. Van Yperen et al., *supra* note 8, at S6, S9 (experiment involving 264 undergraduates (76% women)).

196. *Id.* at S10 (experiment involving 159 undergraduates (77% women) randomly assigned to one of the four goal conditions or the no-goal control condition).

197. Den Nieuwenboer & Kaptein, *supra* note 191, at 138–39 (discussing how “performing well through corruption will automatically increase the threat to identity, starting a self-perpetuating spiral of increasing pressures to commit corruption” and a “cross-level field study among 187 employees from 35 groups in 20 organizations . . . showed that the level of corruption exhibited by an individual was positively related to the level of corruption exhibited by their co-workers”).

198. Albert H. Hastorf & Hadley Cantril, *They Saw A Game: A Case Study*, 49 J. ABNORMAL PSYCHOL.

blame and saw both teams make about the same number of infractions.<sup>199</sup> So too can the senior executives', mid-level management's, and staff's versions of events differ.<sup>200</sup> Employees, for example, may rationalize their illegal conduct with the belief that corruption is widespread or condoned,<sup>201</sup> when it is not, or perceive the senior executives' signal as mixed—promoting ethics while condoning illegal behavior—which may not be the case.

One criticism of the rational ethical decision-making models is that one knows when one is confronted with an ethical dilemma, knows the ethical and unethical responses, and deliberates over the benefits and costs of ethical and unethical behavior.<sup>202</sup> Critics argue that the model, which presupposes rational individuals with willpower, is “incomplete and potentially misleading.”<sup>203</sup> An emerging field, behavioral ethics, uses insights from psychology to better understand how people actually behave when confronted with ethical dilemmas.<sup>204</sup> Bounded ethicality examines “the psychological processes that lead even good people to engage in ethically questionable behavior that contradicts their own preferred ethics.”<sup>205</sup>

People can morally disengage when ethical principles conflict with unethical behavior. Persons that cheat, for example, “reduce the degree to which they view cheating as morally problematic.”<sup>206</sup> People, despite their unethical behavior, continue to believe in their moral superiority.<sup>207</sup> Prisoners, in one study, rated themselves as kinder

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129–30 (1954).

199. *Id.* at 130–31.

200. Ardichvili et al., *supra* note 115, at 344–45 (discussing literature on different perspectives of management and employees on firms' ethical cultures, with their study finding that senior executives in the U.S., Brazil, and Germany rated their organizations' ethical culture significantly higher than did the mid-level managers, who rated the culture higher than non-managerial employees); Ziva Kunda, *The Case for Motivated Reasoning*, 108 PSYCHOL. BULL. 480, 480 (1990) (examining the behavioral literature in “explor[ing] the possibility that motivation may affect reasoning through reliance on a biased set of cognitive processes: strategies for accessing, constructing, and evaluating beliefs”).

201. *Global Economic Crime Survey*, *supra* note 106, at 5, 13–14 (survey identifying three risk factors for misconduct: (i) the incentive or pressure to engage in misconduct, (ii) the opportunity to commit fraud, and (iii) the perpetrators' ability “to rationalise or justify their actions;” of those “who attributed greater levels of fraud to increased rationalisation within their organisations, 35% identified ‘others do it so it's okay’ as being a contributory factor”). Courts and agencies can assess the pervasiveness of cynicism. But the cynicism may arise from labor issues (e.g., management's poorly-executed strategy while taking higher bonuses), and affect the employees' perception of management's commitment to an ethical culture.

202. MAX H. BAZERMAN & ANN E. TENBRUNSEL, *BLIND SPOTS: WHY WE FAIL TO DO WHAT'S RIGHT AND WHAT TO DO ABOUT IT* 4, 29 (2011).

203. *Id.* at 29.

204. *Id.* at 4; Bazerman & Gino, *supra* note 113, at 90 (defining behavioral ethics “as the study of systematic and predictable ways in which individuals make ethical decisions and judge the ethical decisions of others, ways that are at odds with intuition and the benefits of the broader society”).

205. BAZERMAN & TENBRUNSEL, *supra* note 202, at 5.

206. *Id.* at 72 (discussing how “moral disengagement allows us to behave contrary to our personal code of ethics, while still maintaining the belief that we are ethical people”); Shaul Shalvi et al., *Ethical Manoeuvring: Why People Avoid Both Major and Minor Lies*, 22 BRITISH J. MGMT. S16, S25 (2011) (finding that while their experiments' participants “knew to distinguish right from wrong (as suggested by their tendency to justify their unethical behaviour) they still lied under the right circumstances”).

207. See Ann E. Tenbrunsel et al., *The Ethical Mirage: A Temporal Explanation as to Why We Aren't as Ethical as We Think We Are*, 2 (Harv. Bus. School, Working Paper No. 08-012, 2009), available at [www.hbs.edu/faculty/Pages/download.aspx?name=08-012.pdf](http://www.hbs.edu/faculty/Pages/download.aspx?name=08-012.pdf) (exploring the biased perceptions people hold of



to others, and more honest, trustworthy, dependable, generous, compassionate, self-controlled, and moral than the average community member.<sup>208</sup> The only trait that the prisoners viewed themselves on par with the average citizen was law abidingness.<sup>209</sup> Ninety-nine percent of surveyed high school students agreed that it was important for them “to be a person with good character;” 93% were satisfied with their own ethics and character; and 81% believed that when it came to doing what was right, they were better than most people they knew. But many students admitted to copying someone else’s homework (74%); lying to a teacher about something significant (54%); cheating on a school exam (52%); sometimes lying to save money (38%); stealing something from a store (20%); stealing something from parents and relatives (18%); stealing something from friends (14%); and not answering some of the survey questions truthfully (30%).<sup>210</sup>

Individuals can morally disengage. They blame their boss or co-workers, perceive the unethical conduct as widespread,<sup>211</sup> or otherwise rationalize their misconduct.<sup>212</sup> They inaccurately predict how they will behave when confronted with an ethical dilemma, their actual unethical behavior, and their rationalizations to maintain their ethical self-image.<sup>213</sup>

In recent cheating scandals, students rationalized their unethical conduct and blamed school administrators for tolerating cheating. Approximately 70 Harvard University students were disciplined for cheating on a government class take-home final.<sup>214</sup> Some students claimed that cheating was common or accepted behavior.<sup>215</sup> Likewise, New

their own behavior).

208. Constantine Sedikides et al., *Behind Bars But Above the Bar: Prisoners Consider Themselves More Prosocial Than Non-prisoners*, 52 *BRITISH J. OF SOCIAL PSYCHOL.* 4–5 (Dec. 23, 2013 Epub ahead of print), available at <http://onlinelibrary.wiley.com/doi/10.1111/bjso.12060/abstract?sessionid=DA4949AB4F422DE43803C300A07BAB79.f04t04> (survey of 85 convicted prisoners in the south of England).

209. *Id.*

210. Josephson Institute of Ethics, *2012 Report Card on the Ethics of American Youth, Installment 1: Honesty and Integrity* (Nov. 20, 2012), available at [http://charactercounts.org/programs/reportcard/2012/installment\\_report-card\\_honesty-integrity.html](http://charactercounts.org/programs/reportcard/2012/installment_report-card_honesty-integrity.html).

211. Ernst Fehr & Urs Fischbacher, *The Economics of Strong Reciprocity*, in *MORAL SENTIMENTS & MATERIAL INTERESTS: THE FOUNDATIONS OF COOPERATION IN ECONOMIC LIFE* 167 (Herber Gintis et al. eds. 2005) (“[I]f people believe that cheating on taxes, corruption, or abuses of the welfare state are widespread, they themselves are more likely to cheat on taxes, take bribes, or abuse welfare state institutions.”).

212. Bazerman & Gino, *supra* note 113, at 93 (citing literature of how the “more room a situation provides for people to rationalize their behavior, the more likely they are to behave unethically”); see also Den Nieuwenboer & Kaptein, *supra* note 191, at 137 (discussing literature how “people who commit corruption negate the illegitimacy of their acts through rationalizations” and “by using language that enables them to look at [criminal conduct] as non-criminal, as justified, or as something for which they themselves are not to blame”); NACD, *supra* note 186, at 13.

213. BAZERMAN & TENBRUNSEL, *supra* note 202, at 63.

214. Richard Pérez-Peña, *Students Accused of Cheating Return Awkwardly to a Changed Harvard*, *N.Y. TIMES* (Sept. 16, 2013), available at [http://www.nytimes.com/2013/09/17/education/students-accused-of-cheating-return-awkwardly-to-a-changed-harvard.html?\\_r=0](http://www.nytimes.com/2013/09/17/education/students-accused-of-cheating-return-awkwardly-to-a-changed-harvard.html?_r=0) (noting that “[i]nstructions on the take-home final allowed the use of books, notes and the Internet, but forbade discussing it with others. But in grading the exams, Dr. Platt found strong similarities among some of them, even verbatim repetition, down to the same typographical errors.”); Richard Pérez-Peña, *Students Disciplined in Harvard Scandal*, *N.Y. TIMES* (Feb. 1, 2013), available at <http://www.nytimes.com/2013/02/02/education/harvard-forced-dozens-to-leave-in-cheating-scandal.html>.

215. Richard Pérez-Peña, *At Harvard, Suspects in Cheating Take a Leave*, *N.Y. TIMES* (Sept. 11, 2012), available at <http://www.nytimes.com/2012/09/12/education/harvard-cheating-suspects-go-on-leave.html> (noting

York's Stuyvesant High School students rationalized when cheating was acceptable and unacceptable:

By the time they graduate, many have internalized a moral and academic math: Copying homework is fine, but cheating on a test is less so; cheating to get by in a required class is more acceptable than cheating on an Advanced Placement exam; anything less than a grade of 85 is "failing"; achieve anything more than a grade-point average of 95, and you might be bound for the Massachusetts Institute of Technology or Yale . . . "I'm sure everybody understood it was wrong to take other people's work, but they had ways of rationalizing it," said Karina Moy, a 2010 graduate of the school. "Everyone took it as a necessary evil to get through."<sup>216</sup>

So in assessing the tone at the top, courts perhaps can assess whether employees were adequately informed about the ethics program's policies.<sup>217</sup> But assessing whether the employees were "convinced of the corporation's commitment to it" will be harder.<sup>218</sup> The government will have a hard time assessing whether employees were rationalizing their crimes or accurately perceiving a mixed signal from senior executives.

Finally, courts and the DOJ at times cannot easily determine whether the senior executives' ignorance of ethical transgressions was willful. At times managers and co-workers fail "to notice others' unethical behavior when seeing that behavior would harm the observer."<sup>219</sup> Financial incentives can motivate ethical blindness. The behavioral ethics literature questions the objectivity of auditors, managers, and lawyers, who have a significant pecuniary interest in the transaction or outcome.<sup>220</sup> Furthermore, money,

how some interviewed students "acknowledged collaborating with fellow students, despite explicit instructions on the test not to do so, but said that behavior was widely accepted"); Richard Pérez-Peña, *Harvard Students in Cheating Scandal Say Collaboration Was Accepted*, N.Y. TIMES (Aug. 31, 2012), available at <http://www.nytimes.com/2012/09/01/education/students-of-harvard-cheating-scandal-say-group-work-was-accepted.html?ref=education>.

216. Vivian Yee, *Stuyvesant Students Describe the How and the Why of Cheating*, N.Y. TIMES (Sept. 25, 2012), available at <http://www.nytimes.com/2012/09/26/education/stuyvesant-high-school-students-describe-rationale-for-cheating.html>. This was not an isolated event. Stuyvesant's student newspaper surveyed 2045 students who "anonymously filled out 13 questions regarding the frequency of their cheating habits." The Editorial Board, *This Was Probably Plagiarized*, THE SPECTATOR (Mar. 11, 2012), <http://issuu.com/stuy-spectator/docs/spectator-issue-11>. About 80% of the surveyed students admitted cheating in some way. *Id.* ("For each grade, more than 72% of students had copied homework at least once, with more than 28% copying at least weekly . . . and 79% of all students, and about 90% of seniors, admitted to learning about questions before tests at least once a year."). A study of more than 5000 business (mostly MBA) and nonbusiness graduate students at U.S. and Canadian colleges and universities during the 2002–2003 and 2003–2004 academic years found that graduate business students cheat more than their nonbusiness-student peers. Donald L. McCabe et al., *Academic Dishonesty in Graduate Business Programs: Prevalence, Causes, and Proposed Action*, 5 ACAD. MGMT. LEARNING & EDUC. 294, 299 (2006). Cheating was positively correlated with the student's perception that his or her peers were also cheating. *Id.* at 298.

217. *But see* Lisa L. Shu et al., *Dishonest Deed, Clear Conscience: When Cheating Leads to Moral Disengagement and Motivated Forgetting*, 37 PERSONALITY & SOC. PSYCHOL. BULL. 330 (2011) (finding how dishonest behavior increased moral disengagement and motivated forgetting of moral rules).

218. U.S. ATTORNEYS' MANUAL, *supra* note 16, at § 9-28.800.

219. BAZERMAN & TENBRUNSEL, *supra* note 202, at 81 ("When party A has an incentive to see party B in a favorable light, party A will have difficulty accurately assessing the ethicality of party B's behavior.").

220. *Id.* at 82–83; Scott Killingsworth, 'C' is for Crucible: Behavioral Ethics, Culture, and the Board's Role in C-Suite Compliance, RAND CENTER FOR CORPORATE ETHICS AND GOVERNANCE SYMPOSIUM (May

friendship and a sense of loyalty can motivate reasoning. Managers may seek a benign explanation for a well-liked employee's ambiguous conduct.<sup>221</sup> As one compliance officer (CO) reported,

In a worse situation where the CO's advice on critical compliance concerns is ignored, what would be the duty of the CO? Some are brave to escalate to the top management or even to authorities. But in such situations there would be concerns 1) What if the CO's good-faith judgment is wrong since anyone could make mistakes; 2) If a CO makes a wrong judgment, the CO would violate one of the code of conduct: following the right instructions from their supervisors; 3) If a CO makes correct judgment, that would normally take years to prove in case of court procedures. In any of the above cases, the CO would have to endure unfavorable personal results out of his/her insistence for a long time. The majority of COs would not take such risks.<sup>222</sup>

Consequently, the value and effectiveness of the Guidelines' incentive are further diminished given the inherent difficulty in assessing: (i) how the firm's agents "construe the legitimacy of what senior management says,"<sup>223</sup> (ii) whether the agents' jaded assessment is accurate or biased by self-serving rationalizations, and (iii) when ignorance is willful or due to ethical blindness.

### *3. Evaluating the Company's Risk Assessment*

Because effective compliance is inherently dynamic and firm-specific, one issue is the DOJ's and courts' ability to evaluate the defendant's risk-assessment efforts. "Effective [compliance] policies and procedures," the DOJ and SEC recognize,

require an in-depth understanding of the company's business model, including its products and services, third-party agents, customers, government interactions, and industry and geographic risks. Among the risks that a company may need to address include the nature and extent of transactions with foreign governments, including payments to foreign officials; use of third parties; gifts, travel, and entertainment expenses; charitable and political donations; and facilitating and expediting payments.<sup>224</sup>

Achieving that in-depth understanding is daunting for in-house compliance officers, especially when the risk of illegality for some corporate crimes is unknown or conjecture.<sup>225</sup> How, then, will prosecutors and courts—less familiar with the industry and

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29, 2013), available at <http://ssrn.com/abstract=2271840>; Jane Goodman-Delahunty et al., *Insightful or Wishful: Lawyers' Ability to Predict Case Outcomes*, 16 PSYCHOL. PUB. POL'Y & L. 133, 149 (2010) (finding from a sample of 481 U.S. lawyers evidence of unrealistic litigation goals, of vastly overconfident predictions of cases' outcomes, and that the overconfidence bias did not vary significantly with the litigators' experience).

221. Langevoort, *supra* note 64, at 86.

222. Michael Scher, *The Majority of Compliance Officers Wouldn't Take Such Risks*, FCPA BLOG (Aug. 7, 2013, 2:08 AM), <http://www.fcpablog.com/blog/2013/8/7/the-majority-of-compliance-officers-wouldnt-take-such-risks.html>.

223. Langevoort, *supra* note 64, at 107.

224. FCPA Guide, *supra* note 16, at 58.

225. Stucke, *Morality*, *supra* note 61, at 452–57; *Global Economic Crime Survey*, *supra* note 106, at 17 (surveys finding a gap between perception and reality for asset misappropriation and accounting fraud).

firm's business model—know whether the firm diligently adjusted its compliance efforts to changing risks? As the DOJ recognizes, “[m]any corporations operate in complex regulatory environments outside the normal experience of criminal prosecutors.”<sup>226</sup> Although prosecutors can “consult with relevant federal and state agencies with the expertise to evaluate the adequacy of a program’s design and implementation,”<sup>227</sup> there is no assurance that the other agencies fully understand the firm’s risks.

Firms can be required to document their compliance efforts sufficiently “so that they can be not only proven in the event of a breach, but studied with regard to what went wrong and then improved.”<sup>228</sup> But this assesses what the firm did—not what the firm could have done, but failed to do, to ensure that its compliance efforts remain effective. Compliance risks can change, for example, when the firm enters new markets or hires personnel in key positions.<sup>229</sup> As the risk of illegal activities changes, the compliance efforts tailored to that risk must change too.<sup>230</sup>

A second issue involves the firms’, agencies’, and courts’ ability to assess risk objectively. Compliance professionals may intentionally “overstate legal risks because to do so is a wealth-maximizing strategy.”<sup>231</sup> Employees, prosecutors, and courts may also unintentionally skew the legal risks.<sup>232</sup> One cognitive heuristic, the availability heuristic, occurs when one assesses an event’s probability by how readily available it comes to mind.<sup>233</sup> For example, the government publishes statistics on the likelihood of different causes of deaths.<sup>234</sup> But many people in one study judged accidental deaths to be likelier than deaths caused by stroke (which at the time caused twice as many deaths as all accidents combined), and death by tornado as likelier than death by asthma (which at the time caused 20 times more deaths).<sup>235</sup> A sensational news story about insider trading may prompt, under the availability heuristic, more resources to deter that crime, even though insider trading is less likely to occur within that firm than other less-publicized corporate crimes. The availability heuristic can affect prosecutors, who in easily recalling a recent case handled by their office or whose department focuses on particular crimes (e.g., the Antitrust Division) may overestimate the risk of particular crimes, and fault firms for not devoting more compliance efforts to deter that crime.

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226. U.S. ATTORNEYS’ MANUAL, *supra* note 16, at § 9-28.800.

227. *Id.*

228. OECD, *supra* note 11, at 22.

229. *Id.* at 21.

230. *Id.*; OFT Guidance, *supra* note 15, at 19–23; 1 CORPORATE COUNSEL’S GUIDE TO ACQUISITIONS & DIVESTITURES § 3:5 (database updated Mar. 2014).

231. Krawiec, *supra* note 113, at 531–32 (citing studies).

232. See generally Ann H. Harvey et al., *Monetary Favors and Their Influence on Neural Responses and Revealed Preference*, 30 J. NEUROSCI. 9597 (2010) (study showing how money can bias one’s judgment, even where the subjects did not believe it should); Langevoort, *supra* note 64, at 94 (“If salaries and promotions are dependent on being perceived as a team player rather than an aggressive watchdog, compliance personnel will not really want to find problems and will fail to properly process the information that passes before them.”).

233. Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, 185 SCIENCE 1124, 1127 (1974) (noting situations where people assess the “frequency of a class or the probability of an event by the ease with which instances or occurrences can be brought to mind”).

234. Robert Roy Britt, *The Odds of Dying*, LIVE SCIENCE (Jan. 6, 2005, 2:00 AM), <http://www.livescience.com/3780-odds-dying.html>.

235. DANIEL KAHNEMAN, THINKING, FAST AND SLOW 138 (2011) [hereinafter KAHNEMAN, THINKING].

Courts and agencies may also be susceptible to hindsight bias, where knowledge of the outcome, such as a bribe to a foreign official, increases their belief “about the degree to which . . . [they] would have predicted that outcome without the benefit of that knowledge.”<sup>236</sup> A risk may appear far greater to the prosecutor after the bribe occurred than to the compliance officer and management before the crime. Not only may one overstate the risk, the hindsight bias research shows how one is “far more likely to condemn unethical behavior when the behavior leads to a bad rather than a good outcome—even when controlling for the action of the actor being judged.”<sup>237</sup>

A third issue involves the DOJ’s and courts’ second-guessing the firm’s methods to address legal risks. In evaluating a firm’s risk assessment for bribes, the DOJ and SEC warn firms against focusing “on low-risk markets and transactions to the detriment of high-risk areas.”<sup>238</sup> The agencies state that “a \$50 million contract with a government agency in a high-risk country warrants greater scrutiny than modest and routine gifts and entertainment.”<sup>239</sup> For the government, “[d]evoting a disproportionate amount of time policing modest entertainment and gift-giving instead of focusing on large government bids, questionable payments to third-party consultants, or excessive discounts to resellers and distributors may indicate that a company’s compliance program is ineffective.”<sup>240</sup>

This is intuitively appealing. After all, a firm should focus its limited compliance resources on high-risk, big-ticket contracts. Focusing on small, routine contracts might appear hypocritical.

But the government’s criterion can undermine effective compliance. Suppose Firm A, in reviewing the business ethics literature, believes that significant misbehavior can arise from minor infractions.<sup>241</sup> Seeing others engage in seemingly minor, yet unethical, behavior can loosen one’s moral constraints.<sup>242</sup> One’s behavior is influenced by the

236. MAX H. BAZERMAN & DON A. MOORE, *JUDGMENT IN MANAGERIAL DECISION MAKING* 38 (7th ed., Wiley 2008).

237. Bazerman & Gino, *supra* note 113, at 96.

238. FCPA Guide, *supra* note 16, at 58.

239. *Id.* at 58–59.

240. *Id.* at 58.

241. DAN ARIELY, *THE (HONEST) TRUTH ABOUT DISHONESTY* 200–14 (2012) [hereinafter ARIELY, DISHONESTY]; Ashforth et al., *supra* note 8, at 671 (nothing that if “corrupt individual acts are left unchecked, they can spread to other individuals and magnify in scope and audacity, in ways that can eventually transcend individuals and groups and become embedded in the very culture of an organization and industry” and the “resulting corruption becomes systemic, deeply embedded, and intractable, as seen, for example, in the web of organizations caught in the Enron scandal”); *Global Economic Crime Survey*, *supra* note 106, at 13 (warning that even “a relatively minor incident can cause significant reputational damage” and that “senior executives who appear unconcerned about fraud within their organisation may—through a lack of attention and focus—unwittingly foster environments where certain types of fraud are perceived to be permissible”). The trustworthiness of someone dishonest in small things has been long questioned. See Luke 16:10 (“The person who is trustworthy in very small matters is also trustworthy in great ones; and the person who is dishonest in very small matters is also dishonest in great ones.”).

242. Craft, *supra* note 114, at 239 (discussing recent literature of how peers and social groups affect ethical decision-making); ARIELY, DISHONESTY, *supra* note 241, at 200 (assessing the increase in cheating when participants observed a confederate blatantly cheating, with participants claiming to have answered on average 15 of the 20 problems, in contrast to average of seven right answers by the control group where cheating was not possible, and 12 right answers where cheating was possible but without anyone blatantly cheating); Kees Keizer et al., *The Spreading of Disorder*, 322 *SCIENCE* 1681, 1681 (2008) (experiments’ finding “that, when people observe that others violated a certain social norm or legitimate rule, they are more likely to violate other

behavior of others, particularly those within one's social group.<sup>243</sup> Minor individual infractions transcend themselves and corrode an ethical organizational culture.<sup>244</sup> A dishonest act seemingly unrelated to the employees' corporate responsibilities can loosen the employees' moral constraints.<sup>245</sup> As the employees grow comfortable engaging in unethical conduct, their moral constraints loosen further and their conduct worsens.<sup>246</sup> As Ariely concludes from his behavioral experiments, "As long as we see other members of our own social groups behaving in ways that are outside the acceptable range, it's likely that we too will recalibrate our internal moral compass and adopt their behavior as a model for our own."<sup>247</sup> To rationalize their unethical conduct, individuals, like the cheating Harvard and Stuyvesant students, may believe others are engaging in similar conduct.<sup>248</sup> Given management's influence in shaping in-group norms, the tone from the top takes greater importance.<sup>249</sup> Thus, Ariely, among others, recommends being "more vigilant in our efforts to curb even small infractions."<sup>250</sup>

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norms or rules, which causes disorder to spread").

243. In experiments with Carnegie Mellon students, the cheating confederate was either within ("one of us," wearing a plain t-shirt and jeans) or outside ("one of them" wearing a blue-and-gold University of Pittsburgh sweatshirt) the participants' social group. When the cheater was an outsider, the Carnegie Mellon students still cheated, claiming on average nine out of 20 possible right answers compared to the control group, which could not cheat and solved on average seven out of 20 problems. But they did not cheat as much as students who observed someone from their social group cheat (claiming on average 15 right answers), or the students who did not observe anyone cheat (claiming on average 12 right answers). ARIELY, DISHONESTY, *supra* note 241, at 206; *see also* Prentice, *supra* note 175, at 536 (discussing how conformity bias, among other factors, can cause unethical employee behavior); Den Nieuwenboer & Kaptein, *supra* note 191, at 139 (citing research on how "individuals base their assessment of prototypical behavior of the in-group mainly on the people who provide the most critical information about behavior and norms"); Bazerman & Gino, *supra* note 113, at 93 (citing literature of how "actions of other people can influence our own in the ethics domain," including the moral actions of just one person or an in-group member's unethical behavior); Stephen Coleman, Minnesota Dep't of Revenue, *The Minnesota Income Tax Compliance Experiment State Tax Results 1-25* (1996), available at [http://www.revenue.state.mn.us/research\\_stats/research\\_reports/19xx/research\\_reports\\_content\\_compliance.pdf](http://www.revenue.state.mn.us/research_stats/research_reports/19xx/research_reports_content_compliance.pdf) (discussing an experiment where a letter to state taxpayers that appealed to a social norm about tax compliance (namely that the overwhelming majority accurately report the income taxes they owe) had a "moderately significant effect on the entire sample and a stronger effect within a large subgroup of taxpayers" than the letter that made a rational argument for paying taxes (describing how the income tax dollars were spent)).

244. ARIELY, DISHONESTY, *supra* note 241, at 214.

245. In one experiment, the female participants received Chloé designer sunglasses and were randomly assigned to three conditions. *Id.* at 124. One group was told they were wearing real Chloé sunglasses; the second group was told they were wearing counterfeit Chloé sunglasses; the third group was not told anything about the sunglasses being authentic or counterfeit. Participants in all three groups cheated on the subsequent arithmetic exercise, but more participants in the counterfeit group (74%) cheated than those in the no-information (42%) and authentic (30%) groups. *Id.* at 125-26. Moreover, the amount of cheating increased as the experiment continued, especially among those wearing the counterfeit sunglasses. *Id.* at 130 (noting the sharp transition for many participants where "they suddenly graduated from engaging in a little bit of cheating to cheating at every single opportunity").

246. ARIELY, DISHONESTY, *supra* note 241, at 130.

247. *Id.* at 207.

248. *Id.* at 132-33.

249. Den Nieuwenboer & Kaptein, *supra* note 191, at 139; OECD, *supra* note 11, at 25 ("To the people who work in them, large organizations' internal priorities and incentive systems may have a much greater bearing on their behavior than the seemingly distant threat of external rules.").

250. ARIELY, DISHONESTY, *supra* note 241, at 214.

Suppose Firm *A*, to promote an ethical culture, scrutinizes even modest, routine gifts and entertainment to signal its intolerance to corruption, however minor. Firm *A* believes it cannot foster an ethical culture when unethical, albeit petty, bribes are tolerated. Unethical behavior, once tolerated, becomes harder to punish (as the firm cannot credibly delineate between minor and major ethical transgressions).<sup>251</sup>

So how should Firm *A* allocate its resources to promote an ethical organizational culture that deters crime? Should it devote more resources to police routine entertainment and gift-giving or large government bids? Here, the DOJ lacks a counterfactual, namely what would have happened had Firm *A* allocated its resources differently.

Another problem is when the government assesses Firm *A*'s compliance efforts based on its relative efforts rather than absolute levels. To illustrate, suppose Firms *A* and *B* allocate their compliance resources differently. To prevent bribes, Firm *B* spends ten times more examining big-ticket government contracts (worth over \$50 million) than it spends examining modest routine gifts. Firm *A*, in contrast, spends twice the amount examining modest routine gifts than it spends examining big-ticket contracts. The DOJ can conclude that Firm *A* spends a disproportionate amount policing modest entertainment and gift-giving. But this does not tell us whether Firm *A*'s compliance efforts are less effective than Firm *B*'s. If Firms *A* and *B* both spend the same amount to assess the FCPA risks of big-ticket contracts, then it follows that Firm *A* simply spends more to prevent petty bribes. Consequently, although Firm *A* spends relatively more policing low-risk versus high-risk transactions, its overall compliance budget far exceeds Firm *B*'s.

The DOJ and courts, of course, would not penalize Firm *A* when contrasting its efforts with Firm *B*'s. But given the dynamic, tailored nature of compliance, the DOJ and courts often will lack a baseline of the minimum time and expense needed to review and monitor big-ticket contracts. It will be easier to examine Firm *A*'s compliance efforts in relative rather than absolute terms. Thus, in warning companies against "performing identical due diligence on all third-party agents, irrespective of risk factors" as "often counter-productive, [in] diverting attention and resources away from those third parties that pose the most significant risks,"<sup>252</sup> the DOJ and SEC assume that the firm overspends on low-risk activities and underinvests on high-risk activities. This may be true. But it is also possible that the company, like Firm *A*, is committed to an ethical organizational culture, and sets its review of the high-risk agents as the base-line for reviewing all agents' conduct.

Given the government's inherent difficulty in assessing objectively, accurately, and reliably whether the firm minimized the risk of specific misconduct most likely to occur in that industry and locale at that time,<sup>253</sup> the value of the Guidelines' incentive diminishes further.

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251. Den Nieuwenboer & Kaptein, *supra* note 191, at 139–40 (citing research where managers "who do not consistently follow through with (ethics) policies run a greater risk that their subordinates will engage in corruption").

252. FCPA Guide, *supra* note 16, at 59.

253. USSG § 8B2.1, cmt. n.7 ("If, because of the nature of an organization's business, there is a substantial risk that certain types of criminal conduct may occur, the organization shall take reasonable steps to prevent and detect that type of criminal conduct.").

#### 4. Surveillance Versus Trust

The Guidelines instruct firms to take “reasonable steps to ensure that [their] compliance and ethics program is followed, including monitoring and auditing to detect criminal conduct.”<sup>254</sup> The Guidelines do not elaborate how firms should monitor their employees, or the regularity and intrusiveness of the monitoring. The Guidelines recognize that the “formality and scope of actions” will depend on the firm’s size.<sup>255</sup> Smaller firms can monitor “through regular ‘walk-arounds’ or continuous observation while managing the organization.”<sup>256</sup>

This raises two issues. First, do regular walk-arounds and continuous observation promote within large or small firms an organizational culture that genuinely encourages ethical conduct and a commitment to comply with the law? Second, in assessing the effectiveness of larger firms’ compliance efforts, do courts and the DOJ expect larger firms to undertake more formal and intrusive monitoring?

Neoclassical economic theory posits that to optimally deter crime, the penalty should equal at least the crime’s expected net harm to others (plus enforcement costs) divided by the probability of detection and proof of the violation.<sup>257</sup> Accordingly, the government can deter crime by increasing the fine and/or probability of detection and prosecution. Likewise, in increasing their internal monitoring and auditing, firms can increase the probability of detecting employees’ illegal behavior.

Behavioral economists, in testing optimal deterrence theory, find several important deviations. Many in the experiments cheat, but not to the extent neoclassical economic theory suggests.<sup>258</sup> In one study, for example, participants could cheat without being caught or punished.<sup>259</sup> Most participants cheated, but only a little bit.<sup>260</sup> Even when the financial incentives to cheat increased, cheating did not increase.<sup>261</sup> In fact, participants who stood to gain \$10 per correct answer cheated on average less than participants who received 25 cents, 50 cents, one dollar, two dollars, or five dollars per correct answer.<sup>262</sup> Consequently, although many people cheated, their cheating did not increase when the probability of detection was zero or the economic gains increased. As Ariely concluded

254. USSG § 8B2.1(b)(5).

255. USSG § 8B2.1 cmt. n.2(C)(i). Large organizations are expected to “devote more formal operations and greater resources in meeting the requirements of this guideline” than small organizations. *Id.* at n.2(C)(ii). Small organizations must demonstrate “the same degree of commitment to ethical conduct and compliance with the law as large organizations,” but courts should expect “less formality and fewer resources than would be expected of large organizations.” *Id.* at n.2(C)(iii). Small organizations can train employees “through informal staff meetings,” use “available personnel, rather than employing separate staff, to carry out the . . . ethics program,” and have their governing authority “directly manage the organization’s compliance and ethics efforts.” *Id.*

256. *Id.* at cmt. n.2(C).

257. See Gary S. Becker, *Nobel Lecture: The Economic Way of Looking at Behavior*, 101 J. POL. ECON. 385, 389–90 (1993); Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169, 169–217 (1968) (discussing optimal deterrence theory).

258. See Shalvi et al., *supra* note 206, at S16.

259. ARIELY, DISHONESTY, *supra* note 241, at 18 (claiming on average six out of 20 matrices correct versus the control group who answered four out of 20 matrices correctly).

260. *Id.* at 19.

261. *Id.*

262. *Id.* Participants cheated by the same degree (claiming six correct answers) even when told that other participants on average answered four or eight correctly. *Id.* at 22.



from these studies, “we cheat up to the level that allows us to retain our self-image as reasonably honest individuals.”<sup>263</sup>

If these experiments’ findings hold true across firms, then firms can maintain an ethical culture and deter illegal behavior without having to increase their surveillance of employees with more to gain by cheating. In fact, the behavioral experiments found that providing ethical<sup>264</sup> or subtle<sup>265</sup> reminders—just before the temptation to cheat—effectively deterred cheating.

More fundamentally, the Guidelines assume that monitoring promotes, rather than undermines, an ethical organizational culture. We often see drivers slow down upon seeing a highway patrol car. But we also see drivers resume speeding once safely past the patrol car. Increased monitoring may deter workers’ incentive to cheat, but it does not necessarily make them more ethical.

One locally-owned supermarket my family frequents prides itself that the customer is always right. At the check-out line, the cashier always asks us how many bagels or ears of corn are in our paper bag. The cashier never opens the bag to verify our count nor does our family abuse that trust by undercounting.<sup>266</sup> No doubt, as Ariely’s cheating experiments show, some likely abuse that trust. But the supermarket not only signals trust, but also enables its customers to behave ethically and to habituate that ethical conduct. For Aristotle, knowledge of virtue and virtuous behavior was insufficient.<sup>267</sup> “[N]ature gives us the capacity to receive them,” he wrote, “and capacity comes to maturity by habit.”<sup>268</sup> Virtue is attained only through practice and exercise as the conduct

263. ARIELY, DISHONESTY, *supra* note 241, at 23, 27; *see also* Shalvi et al., *supra* note 206, at S23 (similarly finding participants’ avoiding major lies and lies for a minor profit “even in a completely private and anonymous setting”).

264. In one experiment, half of the 450 participants were asked to write down as many of the Ten Commandments as they could recall before the test. ARIELY, DISHONESTY, *supra* note 241, at 39; DAN ARIELY, PREDICTABLY IRRATIONAL: THE HIDDEN FORCES THAT SHAPE OUR DECISIONS 207 (2008) [hereinafter ARIELY, PREDICTABLY IRRATIONAL]. That group could, but did not, cheat (compared to the group asked to recite beforehand ten books they read in high school, which did cheat). *Id.* at 207–08. In another set of experiments, MIT students were divided into three groups, and were financially rewarded for correct answers on a math test. *Id.* at 212. The control group could not cheat and solved on average three problems; the second group could cheat as they self-reported the number of right answers and reported solving on average 5.5 problems on the same test. *Id.* at 212. The third group, like the second group, could cheat, but they signed at the beginning of the test the statement “I understand that this study falls under the MIT honor system.” *Id.* MIT did not, in fact, have an honor code. The third group self-reported on average three problems, the same number as the control group, which could not cheat. ARIELY, PREDICTABLY IRRATIONAL, *supra* at 212–13. Likewise, even though Yale does not have an honor code, its students, who signed the statement, did not cheat. ARIELY, DISHONESTY, *supra* note 241, at 42.

265. KAHNEMAN, THINKING, *supra* note 235, at 57–58 (discussing how priming can deter unethical conduct); Melissa Bateson et al., *Cues of Being Watched Enhance Cooperation in a Real-World Setting*, 2 *BIOL. LETT.* 412 (2006) (finding from experiment that people paid on average 2.76 times more money (relative to the amount of tea or coffee consumed) in the weeks when a photo of human eyes was above the university kitchen’s moneybox than when a photo of flowers was above the moneybox, with contribution levels always increasing with the transition from flowers to eyes and decreasing with the transition from eyes to flowers).

266. Deborah Franklin, *The Psychology of the Honor System at the Farm Stand*, NPR, June 11, 2012, <http://www.npr.org/blogs/thesalt/2012/06/11/154750001/the-psychology-of-the-honor-system-at-the-farm-stand> (discussing trust at farm stands like the Swanton Berry Farm with unattended moneyboxes).

267. ARISTOTLE, *NICOMACHEAN ETHICS*, Book X, ch. 9, available at <http://www.perseus.tufts.edu/hopper/text?doc=Perseus:text:1999.01.0054:book=10:chapter=9>.

268. *Id.* at Book II, ch. 1, sec. 3, available at <http://www.perseus.tufts.edu/hopper/text?doc=Perseus%3A>

develops into habit.<sup>269</sup> Consequently, if the Guidelines require firms to continuously monitor their employees, then besides the cost, the surveillance does not provide employees opportunities to fully develop moral habits. Granted, in undertaking specific conduct mechanically and involuntarily, employees can habituate that conduct. But employees, as a result of the surveillance, do not understand how to behave ethically in new or unforeseen situations.

Finally increased surveillance can be counter-productive. Intrusive monitoring raises, as one district court wrote, its own liability risks:

At the risk of stating the obvious, employers can investigate allegations of employee misconduct. Employers have many traditional tools available in that regard. Covert video surveillance is not a traditional tool. We pride ourselves on our respect for individual privacy. Outside of a strip search or a body cavity search, a covert video search is the most intrusive method of investigation a government employer could select. Secret videotaping goes against the grain of our strong anti-Orwellian traditions. Secret videotaping should be reserved for those extreme and rare circumstances involving serious transgressions where it is highly improbable that less odious techniques will be effective. The intrusiveness of the search must be commensurate with the seriousness of the suspected misconduct. Although some investigation into . . . [the employee's] alleged misconduct may certainly have been appropriate, the court concludes that a secret video surveillance search was excessively intrusive. The status of being an employee does not carry with it the elimination of personal dignity.<sup>270</sup>

The Guidelines do not address when employee monitoring turns the workplace into a prison. Compliance lawyers taking the insights from the behavioral social sciences are questioning the benefits of “command-and-control” compliance programs.<sup>271</sup> Increased surveillance can reduce the employees’ trust, productivity, engagement, and commitment to comply with the law.<sup>272</sup> In its intrusive monitoring, the firm may communicate

text%3A1999.01.0054%3Abook%3D2%3Achapter%3Dpos%3D16%3Asection%3D3.

269. *Id.* at Book X, ch. 9, sec. 2, available at <http://www.perseus.tufts.edu/hopper/text?doc=Perseus%3Atext%3A1999.01.0054%3Abook%3D10%3Achapter%3D9%3Asection%3D2>. Aristotle recognized that not everyone was properly raised to habituate virtuous conduct; they need the law to regulate their upbringing and pursuits and to punish them when they disobey. *Id.* at sec. 4, available at <http://www.perseus.tufts.edu/hopper/text?doc=Perseus%3Atext%3A1999.01.0054%3Abook%3D10%3Achapter%3D9%3Asection%3D4>.

270. *Richards v. Cnty. of Los Angeles*, 775 F. Supp. 2d 1176, 1184 (C.D. Cal. 2011).

271. See Scott Killingsworth, *Modeling the Message: Communicating Compliance Through Organizational Values and Culture*, 25 *GEO. J. LEGAL ETHICS* 961, 966, 968 (2012) [hereinafter *Modeling the Message*] (noting command-and-control “programs and their associated communications aim to govern employee behavior largely through concrete incentives, principally deterring misconduct via monitoring and detection mechanisms and the threat of punishment,” which can have adverse effects, including resentment, an “us-versus-them” attitude towards management, and a reverse-Pygmalion effect where employees may tend to “live down” to the projection of low expectations upon them); Langevoort, *supra* note 64, at 104–06 (discussing the merits of a integrity- or ethics-based monitoring system instead of a costly command-and-control system).

272. GEORGE A. AKERLOF & RACHEL E. KRANTON, *IDENTITY ECONOMICS: HOW OUR IDENTITIES SHAPE OUR WORK, WAGES, AND WELL-BEING* 52 (2010) (discussing how strict supervision can yield “more information regarding workers’ efforts, enabling the principal to fine-tune monetary incentives,” while loose supervision, although providing less information on workers’ effort, promotes workgroup identification, and greater autonomy and effort); Regan, *supra* note 33, at 1970 (“One fairly robust finding is that aggressive compliance monitoring can have an unfavorable effect on the motivation of agents to comply with rules. When

unintentionally that wrongdoing is widespread, making it easier for employees to rationalize their unethical conduct.<sup>273</sup> Given trust's importance in the workplace, firms may prefer an integrity-based system, where employees pledge an honor code similar to the College of William and Mary's,<sup>274</sup> and provide ethical reminders in response to the opportunity to cheat.<sup>275</sup>

Now envision the firm's dilemma when designing its ethics program: should it veer toward an integrity-based or command-and-control system? The firm must assess, not only which approach is more effective, but which approach the government would likely find effective. Although the Guidelines encourage the compliance officer to select the means to promote an ethical culture, one risk is that the DOJ and court will be more impressed by "ongoing monitoring"<sup>276</sup> than an integrity-based system.<sup>277</sup>

If the firm chooses the latter, the government lacks a counterfactual of how much more or less effective the command-and-control approach would be. Nor can the DOJ and courts consider what other firms in the industry do. We see, for example, different approaches at law schools. Students at my law school take final examinations in an unsupervised classroom. At some law schools, students select the days when they take

employees regard supervision as unreasonably pervasive and intrusive, they can develop an adversarial attitude toward the company, its supervisors, and the rules themselves. They may come to attribute their own compliance as motivated by coercion, rather than by their own desire to act properly. In their eyes, people act ethically because the system forces them to, not because they are motivated to do so."); Samuel Bowles, *Policies Designed for Self-interested Citizens May Undermine "The Moral Sentiments": Evidence from Economic Experiments*, 320 SCIENCE 1605, 1608 (2008) (discussing empirical literature where manager's signaling distrust engenders lower profits); Tim Dixon, *The Privacy Comm. of New S. Wales, No. 67, Invisible Eyes: Report on Video Surveillance in the Workplace* § 3.4 (Aug. 1995), available at <http://www.austlii.edu.au/au/other/CyberLRes/1995/video/index.html> (discussing how employers' video surveillance substantially harmed the working environment in undermining workplace morale and creating distrust and suspicion between employees and management).

273. See Regan, *supra* note 33, at 1971 (stating that compliance systems that use penalties send a negative signal to the office about what kind of ethical behavior they can expect from fellow employees); Fehr & Fischbacher, *supra* note 211, at 167.

274. *The Honor Code & Honor Councils*, College of William & Mary, DEAN OF STUDENTS: STUDENT CONDUCT, COLLEGE OF WILLIAM & MARY, available at <http://www.wm.edu/offices/deanofstudents/services/studentconduct/honorcodeandstudentconduct/honorcode/index.php> (last visited May 23, 2014) ("As a member of the William and Mary community, I pledge on my honor not to lie, cheat, or steal, either in my academic or personal life. I understand that such acts violate the Honor Code and undermine the community of trust, of which we are all stewards.").

275. AKERLOF & KRANTON, *supra* note 272, at 35. In the behavioral experiments, it was not the ethics code itself (as neither Yale nor MIT had an honor code), but the ethical reminder immediately before the opportunity to cheat that significantly deterred cheating. Ariely and his colleagues conducted this experiment at Princeton University, which according to its website, has one of the older Honor Codes in the country; its Code, "a revered tradition," is "a center of academic integrity" and "contributes to a feeling of trust that pervades the campus." Luchi M. Megwa, *Undergraduate Honor Code*, PRINCETON UNIV. (last visited Apr. 21, 2014), <http://www.princeton.edu/honor/>. All incoming Princeton students receive a copy of the Honor Code (Princeton University, Constitution of the Honor System, art. VIII (amended 2012)), and a "letter from the chair of the Honor Committee explaining the honor system." The Trustees of Princeton University, *Honor Code*, PRINCETON UNIV., [http://www.princeton.edu/honor/about\\_us/](http://www.princeton.edu/honor/about_us/) (last visited Apr. 8, 2014). Nonetheless, two weeks after their ethics training, Princeton students cheated on average as much as the participants in the other studies. ARIELY, DISHONESTY, *supra* note 241, at 43. But, like the MIT and Yale students, the Princeton students, who were reminded of the Honor Code immediately before the opportunity to cheat, did not cheat. *Id.*

276. FCPA Guide, *supra* note 16, at 19.

277. Langevoort, *supra* note 64, at 105.

their finals unproctored.<sup>278</sup> At other schools, exams are proctored.<sup>279</sup> Which approach most effectively deters cheating and/or promotes an ethical organizational culture? Arguably all three can, although that is unclear.<sup>280</sup> Simply because some law schools monitor their students does not mean an integrity-based system is inadequate.

Moreover, natural experiments can yield the wrong conclusion. Suppose a firm, after switching from an honors code to close surveillance, detects more wrongdoing. The thorny issue is whether the surveillance (i) simply detects pre-existing wrongdoing or (ii) itself *causes* more wrongdoing by signaling distrust. If the latter, then the government, failing to account surveillance's causation of wrongdoing, can conclude incorrectly that the earlier integrity-based system was deficient. A downward spiral results where the firm detects the illegality its surveillance promotes.

### C. Problem of Copycat Compliance Under an Extrinsic, Incentive-Based Approach

Part IV. Subsections A and B discuss the inherent difficulties in telling firms exactly what they must do to earn the Guidelines' incentive, and in articulating objective, easy-to-administer standards to assess compliance efforts. These difficulties diminish the effectiveness of the Guidelines' financial incentive. This Part and Part IV.D take a different tack and examine how an extrinsic, incentive-based approach can encumber an ethical organizational culture.

The Guidelines' assessment of compliance is pass/fail. Courts determine whether the compliance program is effective, not exemplary. Firms with D- or A+ compliance programs get the same incentive. If compliance departments compete for firm resources, and if firms undertake compliance primarily to secure the Guidelines' financial incentive, then firms would reduce their compliance costs to the bare minimum necessary.<sup>281</sup> To reduce compliance costs, a firm likely would copy other firms' compliance efforts.

One example of copycat compliance arose under the Sarbanes–Oxley Act of 2002. Companies subject to the reporting requirements of Section 13(a) or 15(d) of the Securities Exchange Act must disclose whether they adopted a code of ethics for their principal executive officer, principal financial officer, principal accounting officer or

278. Washington & Lee University Student Handbook, 2013–14 10 (Aug. 2013), available at <http://www.wlu.edu/Documents/student-life/student-conduct/student-handbook.pdf>.

279. *Exam Policies*, WAKE FOREST UNIVERSITY SCHOOL OF LAW, <http://registrar.law.wfu.edu/exams/> (last visited July 20, 2014) (“All examinations will be monitored by the faculty member in his/her discretion or by a staff person assigned by the Dean. . . . Monitors for scheduled exams are present to enforce the rules set by the professors.”); *Exam Information*, UNIVERSITY OF DAYTON SCHOOL OF LAW, <http://www.udayton.edu/law/registrar/exams.php#Exam%20Standards%20of%20Conduct> (last visited July 20, 2014).

280. Michael Musheno, *Book Review*, 45 LAW & SOC'Y REV. 1063 (2011) (reviewing AARON KUPCHIK, *HOMEROOM SECURITY: SCHOOL DISCIPLINE IN AN AGE OF FEAR* (2010) and TORIN MONAHAN, *CULTURES OF CONTROL IN PUBLIC EDUCATION* (Rodolfo D. Torres eds. 2010) (noting that the long-term effects of surveillance on students, while not fully realized, raise concern)).

281. Regan, *supra* note 33, at 1976 (“An organization that treats its compliance program as an insurance policy will find it rational to incur expenses for such a program only up to the point at which it will be deemed sufficiently effective to gain lenient treatment for the organization. Given the difficulty of determining whether a compliance program is effective, companies may enhance the likelihood of receiving these benefits simply by establishing programs with certain formal features.”).

controller, and persons performing similar functions.<sup>282</sup> The SEC defined code of ethics broadly as

written standards that are reasonably designed to deter wrongdoing and to promote:

- (1) Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships; . . .
- (3) Full, fair, accurate, timely, and understandable disclosure in reports and documents that a company files with, or submits to, the Commission and in other public communications made by the company;
- (4) Compliance with applicable governmental laws, rules and regulations;
- (5) The prompt internal reporting to an appropriate person or persons identified in the code of violations of the code; and
- (6) Accountability for adherence to the code.<sup>283</sup>

The SEC rejected suggestions that it “set forth additional ethical principles that the code of ethics should address” or “specify every detail that the company must address in its code of ethics, or prescribe any specific language that the code of ethics must include.”<sup>284</sup> The SEC stated “that ethics codes do, and should, vary from company to company and that decisions as to the specific provisions of the code, compliance procedures and disciplinary measures for ethical breaches are best left to the company.”<sup>285</sup>

Despite the SEC’s statement, one study found significant conformity among ethics codes of many S&P 500 firms.<sup>286</sup> The authors studied the publicly-posted ethics codes for 497 of the S&P 500 firms as well as 100 smaller firms.<sup>287</sup> The S&P 500 firms’ ethical codes were generally longer, “an average of 226.7 sentences compared to 117.2 sentences for small firms,” but many S&P 500 firms had substantially similar sentences in their codes,<sup>288</sup> and a few had substantially similar ethics codes even though they operated in different industries.<sup>289</sup> Among the sentences copied were:

282. Disclosure Required by Sections 406 & 407 of the Sarbanes–Oxley Act of 2002, Exchange Act Release Nos. 33-8177; 34-47235; File No. S7-40-02 (Jan. 24, 2013) (codified at 17 CFR Parts 228, 229 & 249), available at [http://www.sec.gov/rules/final/33-8177.htm#footbody\\_42](http://www.sec.gov/rules/final/33-8177.htm#footbody_42).

283. *Id.*

284. *Id.*

285. *Id.*

286. Margaret Forster et al., *Commonality in Codes of Ethics*, 90 J. BUS. ETHICS 129, 139 (2009).

287. *Id.* at 134.

288. *See id.* at 133 (finding the “average number of exact sentence matches is 36.8 for S&P firms while the median is only 4. Thus, while for one-half of the sample there are only four or fewer exact sentences in their codes of ethics overlapping other S&P 500 codes, for the other half of the sample, there is a significantly higher number of sentences that match other codes. So, for the average firm, about 37 sentences in their code of ethics are exactly repeated in other S&P 500 codes. At the 95th percentile, there is a huge overlap (222 sentence matches).”). Only 64 S&P 500 firms had ethics codes that did not overlap in part with any other S&P firm’s codes. *Id.* at 136.

289. *Id.* at 134 (finding that the “Abercrombie & Fitch and Home Depot codes contain a list consisting of approximately 480 words that differ by less than a handful of words” and that the codes of Qualcomm and TSR

- “Obeying the law, both in letter and in spirit, is the foundation on which this company’s ethical standards are built.”
- “Due to the complexity of our business and the competitive realities of the marketplace, we must be clear about our corporate values and maintain a vigorous commitment to acting with integrity.”
- “The company is committed to promoting the values of honesty, integrity, and fairness in the conduct of its business and sustaining a work environment that fosters mutual respect, openness, and individual integrity.”
- “We are honest and treat people with respect, courtesy, fairness, and dignity, and we work hard to make . . . a great place to work and a company that is respected for the quality of its people and products.”
- “In order to sustain that success for future generations, it is our responsibility to preserve and strengthen our core ethical beliefs and the values upon which our company was founded.”
- “There are no shortcut formulas or automatic answers to the choices we have to make in business today, however we should decide these questions in ways that are consistent with . . . ’s values.”
- “We have a responsibility to ourselves—integrity is at the heart of who we are.”<sup>290</sup>

Granted, at times, firms will look at other ethics programs to see what is genuinely helpful, to identify a problem that they overlooked, or perhaps to articulate better an important principle. This is not objectionable. But widespread plagiarism of ethics codes raises significant concerns about the firms’ commitment to an ethical culture.<sup>291</sup> An ethics code, if genuinely believed and instilled, should arise from within the firm to reflect its values and culture; it should not be a cut-and-paste affair.

But firms motivated under an extrinsic, incentive-based approach seek to minimize their compliance costs while ensuring that their compliance efforts conform with ethics programs found effective. Given the paucity of data of effective ethics programs, firms opt for the second best and find safety in numbers. Indeed, Part IV.B.1 discusses how the Guidelines encourage firms to follow industry compliance practices and procedures. By copying other firms’ ethics codes and compliance practices, firms can minimize their compliance costs and reduce the risk that their compliance program is found to depart from industry standards. However, copycat compliance will likely be ineffective.

#### *D. Problem of Market Norms Crowding Out Ethical and Social Norms That Effectively Deter Unethical and Illegal Conduct*

Should firms pay their employees to attend religious services (or be faulted if they did not)? The business ethics literature suggests a positive relationship between religion

Inc., which were in different industries, were “essentially identical”).

290. Forster et al., *supra* note 286, at 137.

291. BAZERMAN & TENBRUNSEL, *supra* note 202, at 119.

and ethical decision-making.<sup>292</sup> If the Guidelines seek to promote an ethical organizational culture through financial incentives, then the Guidelines should incentivize firms to incentivize their employees to behave ethically.<sup>293</sup> This raises the issue of market norms crowding out social and ethical norms, which can more effectively promote an ethical organizational culture that deters crime.<sup>294</sup> Introducing financial incentives to behave ethically can undermine, rather than promote, an ethical culture.

An incentive-based approach to ethics can also perversely promote the incentives to violate the law.<sup>295</sup> An extrinsic, incentive-based approach puts a price tag on behaving ethically. Firms using this approach will assess whether crime pays. The Guidelines' incentive must continually adjust to the returns of illegality. As two economists observed, "If jobholders have only monetary rewards and only economic goals, they will game the system insofar as they can get away with it."<sup>296</sup> In one experiment, more participants in the condition without a compliance program saw the decision as an ethical one than participants in the condition with a compliance program, who saw the decision as a business one (e.g., the likelihood of getting caught and the likely cost).<sup>297</sup> Indeed in a recent insider trading case, the firm's compliance program, instead of promoting an ethical culture, provided employees innovative ways to avoid detection.<sup>298</sup>

Moreover, people can engage in unethical and illegal conduct for tempting, short-term gains (sometimes for the firm, sometimes only for the individual) at the expense of

292. O'Fallon & Butterfield, *supra* note 114, at 392.

293. USSG § 8B2.1(b); ERC Report, *supra* note 3, at 7 (requesting that the Guidelines "[m]ore strongly encourage companies to use incentives to promote their programs, including compliance/ethics as a key component of employee evaluations and reviews"); Saris, *supra* note 2, at 19 (noting the requests to the Sentencing Commission for "guidance on ways to improve the compliance and ethics program, such as describing appropriate incentives for employees").

294. For a thoughtful discussion of how markets can crowd out morals see MICHAEL J. SANDEL, WHAT MONEY CAN'T BUY: THE MORAL LIMITS OF MARKETS 93–130 (2012); Regan, *supra* note 33, at 1970–71 (noting how "employees' interpretation of their compliance as motivated by external influence may 'crowd out' any tendency to attribute compliance to their own intrinsic desire to act in accordance with the law"; "drain the compliance program of any inherent moral value, so that it is conceptualized as simply a set of rules that attach prices to certain types of behavior"; and "may undermine employees' perception of themselves as honest and ethical people who would abide by the law even in the absence of monitoring").

295. BAZERMAN & TENBRUNSEL, *supra* note 202, at 109–10.

296. AKERLOF & KRANTON, *supra* note 272, at 59.

297. BAZERMAN & TENBRUNSEL, *supra* note 202, at 111.

298. SAC Indictment ¶ 23; James B. Stewart, *At SAC, Rules Compliance with an 'Edge'*, N.Y. TIMES (July 27, 2013), available at [http://www.nytimes.com/2013/07/27/business/at-sac-rules-compliance-with-an-edge.html?pagewanted=2&\\_r=0](http://www.nytimes.com/2013/07/27/business/at-sac-rules-compliance-with-an-edge.html?pagewanted=2&_r=0) ("The training seems only to have alerted some employees to the type of activity they needed to conceal—not to stop it. One new SAC employee, in an instant message to Mr. Cohen conveying information about Nokia, said he'd just gotten a lecture from SAC's head of compliance, 'So I won't be saying much,' he wrote. 'Too scary.' The government noted that this didn't prompt any reaction from Mr. Cohen."). Likewise in an antitrust case, New York alleged, "Intel's illegal conduct occurred despite its much-touted antitrust compliance program. As described in the Harvard Business Review (June, 2001), the program featured mock raids and staged cross-examinations of Intel managers before audiences of other executive staff. One of the 'Don'ts' said to be inculcated by the program was 'no exclusive contracts where microprocessors were concerned.' Whatever the intention, internal Intel emails strongly suggest that the actual effect of the program was to school Intel executives in cover-up, rather than compliance. In some instances, Intel executives were told to use less transparent language to mask their tactics because of 'legal' or 'antitrust' concerns. Notably absent is any suggestion that the conduct itself—paying for exclusivity—might be objectionable." Complaint, *New York v. Intel Corp.*, No. 09-CV-00827, 2009 WL 3628013 (D. Del. Nov. 3, 2009).

long-term gains or risk.<sup>299</sup> Individuals may be particularly likely to do this in the face of short-term (individual or company) losses. These biases also undermine the effectiveness of extrinsic incentives that stochastically occur well into the future.

Even when illegal behavior is discovered, executives may find it cheaper to mitigate the costs of the illegal behavior rather than promote an ethical culture.<sup>300</sup> Take Apple, for example. Its website promotes how the computer, mobile phone and software manufacturer conducts its business “ethically, honestly, and in full compliance with all laws and regulations. This applies to every business decision in every area of the company worldwide.”<sup>301</sup> Among Apple’s principles of business are (i) “Honesty” (i.e., demonstrating “honesty and high ethical standards in all business dealings”) and (ii) “Compliance” (ensuring “that business decisions comply with all applicable laws and regulations”).<sup>302</sup> Apple’s compliance policies expressly prohibit price-fixing.<sup>303</sup> Two recent civil prosecutions undermine Apple’s public pronouncements. In 2010, the DOJ alleged that Apple’s senior executives illegally agreed with executives at Adobe, Google, and Pixar executives not to poach each other’s employees by cold-calling them.<sup>304</sup> Although not a garden-variety price-fixing case, senior executives cannot secretly agree to reduce competition for their employees’ services. Not surprisingly, Apple and the other defendants settled. Then in 2012, the DOJ alleged, and the trial court found, that Apple conspired with the major book publishers to raise the retail price of e-books.<sup>305</sup> Besides the egregiousness of Apple’s anticompetitive behavior, the court’s opinion questioned other conduct,<sup>306</sup> including the honesty of two Apple executives and its Associate General Counsel.<sup>307</sup> Despite two antitrust violations, Apple, to the trial court’s frustration, remained unrepentant.<sup>308</sup> Moreover, the court “expressed dissatisfaction that

299. Hershfield et al., *supra* note 115, at 299 (discussing how “[m]any (but not all) decisions that carry with them the possibility of unethical behavior can thus be framed as inter-temporal choices, or choices that have consequences at different points in time (i.e., both the present and the future)”).

300. Langevoort, *supra* note 64, at 102.

301. *Business Conduct*, APPLE, INC., (Dec. 2012), [http://files.shareholder.com/downloads/AAPL/3111172668x0x443008/5f38b1e6-2f9c-4518-b691-13a29ac90501/business\\_conduct\\_policy.pdf](http://files.shareholder.com/downloads/AAPL/3111172668x0x443008/5f38b1e6-2f9c-4518-b691-13a29ac90501/business_conduct_policy.pdf).

302. *Id.*

303. Apple Inc. Annual Report (Form 10-K) (Sept. 24, 2011), Ex. 14.1, Business Conduct, *available at* <http://www.sec.gov/Archives/edgar/data/320193/000119312511282113/d220209d10k.htm>.

304. Complaint, United States v. Adobe Systems, Case No. 1:10-cv-01629 (D.D.C. filed Sept. 24, 2010), <http://www.justice.gov/atr/cases/f262600/262654.htm>.

305. United States v. Apple, Inc., 952 F. Supp. 2d 638, 708 (S.D.N.Y. 2013).

306. *Id.* at 656 n.15 (noting that “Apple had considered proposing to Amazon that they simply divide the e-market for books and music”). Had Apple proposed this, and Amazon accepted, their executives would likely have been criminally prosecuted for illegally allocating markets, in violation of section 1 of the Sherman Act. United States v. Topco Assocs., Inc., 405 U.S. 596, 607–08 (1972).

307. *Apple*, 952 F. Supp. 2d at 661 n.19, 672–73 n.38, 678 n.47, & 681 n.52 (finding testimony of Eddy Cue, Apple’s Senior Vice President of Internet Software and Services, not credible); *id.* at 682 n.53 (finding testimony of Keith Moerer, Director of Apple’s iTunes, not credible); *id.* at 702–03 n.66 (finding that besides Cue’s “unreliable” testimony, other “witnesses who were noteworthy for their lack of credibility included Moerer” and Apple’s Associate General Counsel Kevin Saul).

308. Joab Jackson, *Judge Scolds Apple for Lack of Remorse in Ebook Antitrust Case*, COMPUTERWORLD (Aug. 9, 2013, 8:38 PM), [http://www.computerworld.com/s/article/9241573/Judge\\_scolds\\_Apple\\_for\\_lack\\_of\\_remorse\\_in\\_e\\_book\\_antitrust\\_case?pageNumber=1](http://www.computerworld.com/s/article/9241573/Judge_scolds_Apple_for_lack_of_remorse_in_e_book_antitrust_case?pageNumber=1) (“None of the publishers nor Apple have expressed any remorse’ about colluding to fix electronic book prices in 2010, said District Judge Denise Cote, of the US District Court for the Southern District Court of New York. ‘They are, in a word, unrepentant.’”).



Apple had not taken any steps to modify its business practices, such as establishing internal compliance monitoring, to prevent it from undertaking similar behaviour in the future.”<sup>309</sup> Apple unsuccessfully appealed to the Second Circuit about its court-ordered compliance officer.<sup>310</sup>

One compliance lawyer summed it well:

The command-and-control approach is based on the assumption that workers will behave like the “rational actors” of economic theory: they will weigh the costs and benefits of compliance versus rule-breaking and make a rational, self-interested decision to avoid the risk of punishment. The greater the emphasis on monitoring, detection, and punishment, the more this assumption rises to the surface.

The implicit message, then, is one of pursuing self-interest (avoiding punishment) rather than one of doing the right thing: the employee is encouraged to frame the question in terms of personal risks and rewards. And if you frame compliance as an essentially economic proposition, you invite misconduct whenever its reward is significant and either the risk of detection, or the punishment if caught, is perceived as acceptably low. Instead of conveying the message that compliance is non-negotiable, risk/reward framing implies that it may be negotiable if the price is right.<sup>311</sup>

#### V. AN INTRINSIC, ETHICS-BASED APPROACH

This Article’s goal is to explore how the Guidelines’ extrinsic, incentive-based approach to compliance contributes to the persistence of ineffective compliance. Some may disagree, but for over 20 years, the Guidelines have offered firms a significant financial incentive to develop an ethical organizational culture. Nonetheless, corporate crime persists. Too many ethics programs remain ineffective.

If the Guidelines’ current approach is not working, the debate turns to what the Sentencing Commission should do next. An alternative approach—an intrinsic, ethics-based approach toward compliance—exists, is gaining traction in the compliance industry, and should be given greater emphasis in the Guidelines. The details of implementing an intrinsic, ethics-based approach require fuller attention in a separate article. My aim here is to argue that a superior viable alternative exists and quickly sketch some of its benefits and risks.

##### *A. How an Intrinsic, Ethics-Based Approach to Compliance Differs from an Extrinsic, Incentive-Based Approach*

First, under an extrinsic approach, compliance is primarily undertaken for the Guidelines’ financial incentive. An ethics-based approach emphasizes that firms are (or should be) intrinsically motivated to promote an ethical organizational culture: “A crucial

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309. *Id.*

310. Andrew Albanese, *Second Circuit Denies Apple’s Monitor Appeal*, PUBLISHERS WEEKLY (Feb. 10, 2014), <http://www.publishersweekly.com/pw/by-topic/digital/content-and-e-books/article/61012-second-circuit-denies-apple-s-monitor-appeal.html>.

311. *Modeling the Message*, *supra* note 271, at 966–67.

part of this process involves senior management empowering and motivating employees ‘to do the right thing, because it is the right thing to do.’”<sup>312</sup> The expectation is that a firm, as Part II.A discusses, should seek an ethical organizational culture for its own end, for a strategic competitive advantage, or to prevent being competitively disadvantaged. Firms should be intrinsically motivated to develop an ethical culture where employees use their skills for the improvement and benefit of others, and employees align their identity with an organization of high ethical ideals.

Second, an extrinsic approach fosters a compliance culture that asks: “What can I legally do?”, “What are the costs and return on investment of the extra compliance?”, and “Will the measure help us persuade the DOJ or court that our compliance program is effective and thereby lower any fine?” An intrinsic approach fosters an ethical culture that asks: “What is the right and ethical thing to do?”, an inquiry that permeates daily decisions.<sup>313</sup> The firm’s core values are aligned with day-to-day operations.<sup>314</sup> Ethical leaders “stress moral values and purpose in their decision making”; they tell followers “how the tasks and efforts of group members contribute to the achievement of important goals,” and “how performing tasks contribute to the achievement of socially responsible goals, and make salient to followers the purpose, morality, and ethicality of work, likely enhancing the significance of group members’ tasks.”<sup>315</sup>

Finally, firms under an extrinsic approach, as Part IV discusses, demand to know what is expected of them from the government, namely what specific steps they must undertake to meet the regulator’s narrow legalistic requirements of effective compliance.<sup>316</sup> This is not a recipe for success.<sup>317</sup> Under an intrinsic approach, a firm develops an ethical organizational culture for its own sake or for the sake of increasing employee well-being and profitability. As the Sentencing Commission’s Chair and ethics industry recognize, an ethical organization is more proactive than a compliant one.<sup>318</sup>

312. *Global Economic Crime Survey*, *supra* note 106, at 14; *see also* Piccolo et al., *supra* note 44, at 263 (“Ethical leaders can be trusted, emphasize business ethics and values to employees, and ask, ‘What is the right thing to do?’”).

313. GREENBERG, *supra* note 8, at 12 (“In principle, the CECO is supposed to be the voice for doing the right thing because it is the right thing to do, and for engaging management in asking questions about what is ‘right’ in different situations.”); 2013 Leadership Survey, *supra* note 41, at 10.

314. 2013 Leadership Survey, *supra* note 41, at 10.

315. Piccolo et al., *supra* note 44, at 262; *see also* 2013 Leadership Survey, *supra* note 41, at 10 (discussing how successful ethics programs “[c]elebrate employee acts of ethical leadership, both in team meetings, and other company communications vehicles”).

316. GREENBERG, *supra* note 8, at 15 (noting one “recurring” theme in the compliance conference “was the importance of corporate ethical ‘culture’ as a facet of a robust ethics and compliance program, and the role of the CECO as a guardian of that culture” and “[t]o the extent that ethical corporate culture ultimately involves a set of assimilated values, it is in that sense the opposite of a check-the-box approach to meeting narrowly legalistic requirements for controls and governance, imposed from the outside”).

317. John Henry Calvinist, *Book Review*, THE NEW HUMANITIES (reviewing JOHN KAY: THE TRUTH ABOUT MARKETS: WHY SOME NATIONS ARE RICH, BUT MOST REMAIN POOR (2004) (citing “In regulating corporate America, the prescriptive approach—which allowed players freedom within rules—failed, [as] the rules did not so much exclude the unacceptable as define the limits of the permissible.”)), *available at* <http://www.thenewhumanities.net/books/Book%20Reviews58.html> (last visited May 23, 2014).

318. Murphy, *supra* note 38, at 716 (“An ethical organization will develop ways in which ethical dilemmas are to be resolved by management and employees. An ethical organization will also foster and protect reporting mechanisms and reward ethical conduct.”); 2013 Leadership Survey, *supra* note 41, at 13, 21; Timothy L. Fort, *Steps for Building Ethics Programs*, 1 HASTINGS BUS. L.J. 194, 202 (2005) (“If one puts off considering ethical

Intrinsically-motivated firms should not demand a compliance checklist from regulators.<sup>319</sup>

This is not to say that legal compliance is abolished. Firms in heavily regulated industries will still need compliance training to help employees avoid technical regulatory violations. Regulatory requirements at times can appear counterintuitive (and debatable) to employees. Many regulatory requirements lack moral or ethical content. So, depending on the industry, technical compliance training will likely continue. But, as organizational cultures become more ethical, hopefully the need for command-and-control regulations will be reduced.

### *B. Benefits of an Intrinsic, Ethics-Based Approach to Compliance*

An ethics-based approach is likelier to promote an ethical organizational culture. An ethical organizational culture cannot be established through external mandates.<sup>320</sup> The key to an effective ethics program is not whether the firm has an ethics code per se, but the extent to which the code is embedded in regular decision-making.<sup>321</sup> As one study found, “the quality of communication” in an ethics code “had a stronger [negative] relationship with unethical behavior” than the code’s content.<sup>322</sup> And the code’s content, in turn, had a stronger negative relationship with unethical behavior than the mere existence of a code of ethics.<sup>323</sup> As several ethics scholars wrote:

Although such formal systems can help to prevent unethical behavior, research suggests that they can also be easily decoupled from the organization’s daily life. Organizations can adopt a “check-off” approach: Do we have a code and do we tell everyone about it? Check. Do we provide regular training? Check.

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dilemmas until, for example, oil is floating in the Prince William Sound, it is too late. The way to approach the problem is to be prepared for such contingencies. This requires ongoing consideration of ethical issues rather than waiting to consider them when a problem arises.”)

319. CANADA COMPETITION BUREAU, *supra* note 15, at 6 (“Policies, procedures and training are, on their own, insufficient to ensure compliance. To be effective, all policies, procedures and training must be part of a larger culture that instills compliance as a fundamental value.”).

320. GREENBERG, *supra* note 8, at ix (listing the difficulty of establishing ethical culture by external mandate as one of the major points of agreement at the compliance roundtable).

321. McKinney et al., *supra* note 121, at 513 (noting how “[e]thical leadership behavior is gaining attention as a factor that influences employee behavior and plays a critical role in creating the ethical climate of the organization” and how ethics codes “will be undoubtedly more effective to the extent that leaders are themselves following the code, communicating it frequently, and holding employees accountable for compliance”). One business professor asked his executive education students: “First, do their companies have a code of conduct? Second, when was the last time they read it or know of any efforts to make the code part of the day-to-day dialogue occurring at work? Nearly everyone answers “yes” to the first question and are mute to the second.” Fort, *supra* note 318, at 196.

322. Kaptein, *Toward Effective Codes*, *supra* note 121, at 245 (finding that (i) the “more diverse the perceived content” of the business ethics code, (ii) the “higher the perceived quality” of communications surrounding the ethics code (in that the meaning and implications for behavior were understood and that individuals were equipped to apply the ethics code in practice), and (iii) “the better the perceived embedment” of the ethics code by senior and local management (i.e., management’s commitment to integrate the ethics code in the company’s daily practices), the lower the perceived frequency of unethical behavior in the workplace; the factor most inversely related to observed unethical behavior was senior and local management’s embedment of the ethics code).

323. *Id.*

Do we have a hotline? Check. And so on. But if codes land in employees' circular files, if training amounts to little more than a brief online annual hassle, and if the hotline is answered by some third party, employees can easily come to view this elaborate infrastructure as mere "window dressing." In fact, Andersen still had its ethics code . . . as did Enron.

So a formal ethics infrastructure does not guarantee a corruption-free organization. What is required is a culture that embeds support for ethical conduct throughout its formal and informal systems.<sup>324</sup>

Not surprisingly, the compliance industry endorses an ethics-based approach. As two ethics scholars observed, "In today's business, values-based management—rather than compliance-based management—is increasingly popular."<sup>325</sup> A values-based approach makes business sense. It generates, a 2013 survey found, the highest return on ethics and compliance investment.<sup>326</sup> Ethics and compliance leaders are "increasingly seeing an ethical culture as key to driving long-term business value."<sup>327</sup>

Granted the compliance industry wants greater guidance from the DOJ to arm compliance officers with greater resources and authority in their negotiations with senior officers and directors. But the industry recognizes that successful compliance must be ethics-based:

When companies have successfully integrated compliance/ethics into the company's DNA, it is in great part because the board and management have defined the mission of the company as comprising both financial performance and an equally strong commitment to acting with integrity. Doing this is more than merely adopting the right words in a values or mission statement.<sup>328</sup>

An ethics-based approach is also consistent with the Guidelines' key assumptions. The Guidelines originally did not mention ethics, relying on compliance and incentives.<sup>329</sup> But the Guidelines evolved.<sup>330</sup> Since 2004, the Guidelines emphasize both

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324. Ashforth et al., *supra* note 8, at 673–74 (citations omitted); *see also* 2011 ERC Survey, *supra* note 94, at 33 (stating that data from its 2011 survey and earlier research "provide a clear model for building an ethically healthy organization where: few employees feel pressure to compromise standards, misconduct is rare, observations of misbehavior are properly reported, and those who report do not experience retaliation," namely "[i]nvest in building a strong ethics and compliance program; and [c]ommit to ethical leadership and building an ethics-focused business culture"); Fort, *supra* note 318, at 196–97.

325. Den Nieuwenboer & Kaptein, *supra* note 191, at 139 (citing several studies where "values-based management styles are more effective and create better cultures").

326. 2013 Leadership Survey, *supra* note 41, at 7 (noting how its survey "clearly shows that a values-based approach to the core elements of an [ethics] program generates the highest return on the [compliance] investment"); *see also id.* at 12 (noting how four out of five respondents in 2013 saw "performance and value-creation as the greatest benefits of an ethical culture, surpassing compliance for the first time").

327. *Id.* at 5.

328. ERC Report, *supra* note 3, at 68; *see also id.* at 6 (recognizing that "[u]ltimately, when companies are truly committed, the board and management have defined the very mission of the company as fusing financial performance with an equally strong commitment to integrity"); ICN, *supra* note 125, at 23 (expecting compliance to be "a fundamental part of the business policy"); GREENBERG, *supra* note 8, at vii (noting how the importance of organizational culture has emerged as a priority for compliance officers); ABA Compliance Survey, *supra* note 154, at 1787 (arguing that "without a healthy, ethical corporate culture, an organization cannot maintain an effective compliance program").

329. Murphy, *supra* note 38, at 714.

compliance and an ethical organizational culture: “the Commission’s message is clear—good corporate conduct means above all else ethical conduct.”<sup>331</sup> The Guidelines, consistent with an intrinsic ethics-based approach, now assess a program’s effectiveness in part on the firm’s strong ethical culture. The Guidelines start with a compliance *and* ethics objective.<sup>332</sup> The Guidelines’ seven steps, which Part III.B discusses, are meant to promote “an organizational culture that encourages ethical conduct.”<sup>333</sup> The belief is that the organization’s ethical values, as one study found,<sup>334</sup> will cascade down the organization.<sup>335</sup>

Since an ethics-based approach is consistent with the Organizational Guidelines’ key assumptions, the Commission does not have to overhaul the Guidelines. Instead, the emphasis would shift. Under an intrinsic approach, courts can still reduce an organization’s culpability score based on its compliance efforts. But the reduction is framed as a fairness issue.<sup>336</sup>

Suppose the intrinsically motivated Firm *A* has a strong ethical organizational culture. Accordingly, Firm *A* unilaterally investigates an alleged violation, promptly brings any illegal behavior to the DOJ’s attention, cooperates fully with the prosecutors, makes restitution to the victims, disciplines the employees responsible for the activity and those who willfully ignored the conduct, and undertakes remedial measures (including examining any contributing situational factors) to deter future violations. Suppose Firm *B*

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330. Press Release, U.S. Sentencing Comm’n, Commission Tightens Requirements for Corporate Compliance and Ethics Programs (May 3, 2004), available at [http://www.usssc.gov/Legislative\\_and\\_Public\\_Affairs/Newsroom/Press\\_Releases/20040503\\_Press\\_Release.htm](http://www.usssc.gov/Legislative_and_Public_Affairs/Newsroom/Press_Releases/20040503_Press_Release.htm) (noting the “focus on ethical corporate behavior in [the 2004 Guidelines] amendment reflects a shift in the legal landscape since the promulgation of the original organizational guidelines in 1991,” and that the amendments seek to enhance “the rigor and detail” of the Guidelines’ requirements, including “[a]s a fundamental proposition, that organizations must promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law”).

331. U.S. Sentencing Comm’n, Public Meeting, Minutes of the April 8, 2004 Public Meeting, available at [http://www.usssc.gov/Legislative\\_and\\_Public\\_Affairs/Public\\_Hearings\\_and\\_Meetings/20040408/4\\_08\\_04.htm](http://www.usssc.gov/Legislative_and_Public_Affairs/Public_Hearings_and_Meetings/20040408/4_08_04.htm); ABA Compliance Survey, *supra* note 154, at 1787 (noting the 2004 Amendments’ “overarching theme” is “[c]ulture trumps compliance”).

332. USSG § 8B2.1(a)(2) (firms must “otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law”).

333. USSG § 8B2.1(b).

334. Schaubroeck et al., *supra* note 186, at 1070 (finding that ethical leadership influenced the ethical culture within each of the U.S. Army’s hierarchical levels, that “ethical culture cascades across hierarchical levels to a substantial extent . . . thus enabling a new and previously unstudied pathway for leadership influence to transmit across levels,” and that “leaders who exhibit a high level of ethical leadership may facilitate the influence of subordinate leaders’ ethical leadership on their followers”).

335. FCPA Guide, *supra* note 16, at 57 (“By adhering to ethical standards, senior managers will inspire middle managers to reinforce those standards. Compliant middle managers, in turn, will encourage employees to strive to attain those standards throughout the organizational structure.”); USSG § 8B2.1 cmt. n.3 (“High-level personnel and substantial authority personnel of the organization . . . shall perform their assigned duties consistent with the exercise of due diligence, and shall promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.”); ICN, *supra* note 125, at 23 (explaining that a firm’s commitment “must come from the top down,” senior management and the executive board are ultimately accountable for ensuring compliance, they must “demonstrate their commitment clearly and unambiguously,” and they “must foster a culture of compliance within the business organization by playing an active and visible role in promoting compliance”).

336. Damien Geradin, *Antitrust Compliance Programmes and Optimal Antitrust Enforcement: A Reply to Wouter Wils*, 1 J. ANTITRUST ENFORCEMENT 325, 338–39 (Oct. 2013).

is unwilling to undertake these measures. Is it fair to find both firms equally culpable? Notice here Firm *A* neither demands nor expects an incentive. Its executives undertake these measures—not for an extrinsic reward—but because they understand how the misconduct can undermine their organization’s ethical culture and competitive advantage. Rather, society deems it unfair to treat Firms *A* and *B* similarly.<sup>337</sup> Reframing the reduction in culpability score as a fairness consideration returns the DOJ and Commission to their initial view of compliance.<sup>338</sup>

Finally, since an ethics-based approach highlights the firm’s intrinsic motivation, there should be less pressure on the government to tell firms exactly what they must do, and less pressure for ineffective, or counter-productive, compliance check-lists. The DOJ already considers “the commitment of corporate leaders to a ‘culture of compliance’ and look[s] to see if this high-level commitment is also reinforced and implemented by middle managers and employees at all levels of a business.”<sup>339</sup> The government’s message will now be consistent; it does not want compliance *per se*, but ethical “institutional cultures that discourage criminal conduct.”<sup>340</sup>

### *C. Concerns of an Intrinsic, Ethics-Based Approach*

One likely concern is that an intrinsic, ethics-based approach, if feasible, would have obviated the need of the Guidelines’ incentives. An intrinsic approach, like Sophocles, depicts “men as they ought to be,” whereas the extrinsic, incentive-based approach, like Euripides, depicts men “as they were.”<sup>341</sup> But it is questionable if firms act as self-interested as some lawyers and economists presuppose.<sup>342</sup> Regardless, self-interested firms should adopt an intrinsic approach when it confers a competitive advantage (or avoids the firm being competitively disadvantaged). If an intrinsic approach provides

337. As Wouter Wils reminded me, apart from the most important fact that Firm *A* is less likely to get involved in an alleged violation, and is more likely to have ended its involvement earlier and thus to have a shorter duration and for that reason a lower penalty, Firm *A* could get a rebate for cooperation with the prosecutors, and possibly also one for prompt restitution.

338. U.S. ATTORNEYS’ MANUAL, *supra* note 16, at § 9-28.500 (“A corporation can only act through natural persons, and it is therefore held responsible for the acts of such persons fairly attributable to it.”); ERC Report, *supra* note 3, at 21 (“Initially, for reasons simply of fairness, the Commission wanted the FSGO to draw distinctions among quite different organizational defendants,” namely “an organization in which the management had diligently tried to prevent misconduct, but nevertheless had an employee deliberately break the rules, and an organization in which the management was directly complicit in the offense could be convicted of precisely the same crime.”).

339. FCPA Guide, *supra* note 16, at 57.

340. Desio, *supra* note 133.

341. ARISTOTLE, THE RHETORIC AND THE POETICS 261 (Modern Library 1984).

342. An OFT-commissioned study examined, *inter alia*, the perceived importance of several factors in deterring competition law violations. *The Deterrent Effect of Competition Enforcement*, U.K. OFFICE OF FAIR TRADING (Nov. 2007), available at [http://www.of.gov.uk/shared\\_of/reports/Evaluating-OFTs-work/of962.pdf](http://www.of.gov.uk/shared_of/reports/Evaluating-OFTs-work/of962.pdf). After (i) 30 interviews with lawyers, economists and companies; (ii) a telephone survey of 234 senior competition lawyers based in the UK and Brussels; and (iii) a telephone survey of 202 UK companies, the study found a divergence between lawyers and companies. On a scale from 1 (not at all important) to 4 (very important), lawyers on average perceived criminal penalties (3.50) as the most important, followed by fines (3.31), disqualification of directors (3.06), adverse publicity (2.79), and private damages actions (2.49). Companies also rated criminal penalties (3.51) as the most important, but found disqualification of directors (3.38) and adverse publicity (3.25) more significant than fines (3.13) and private damages actions (2.93). *Id.* at 72.

firms a competitive advantage in attracting and retaining well-qualified employees, and increasing employee well-being and profitability, then firms, faced with strong competitive pressure, should promote an ethical organizational culture. An extrinsic approach is needed to induce only those self-interested firms that believe an ethical culture is not worth its cost and will not be punished by market forces for not promoting an ethical culture. Thus, weak enforcement and industry competition are other possible contributing factors to the underlying problem of ineffective compliance.

Moreover, unlike jurisdictions that must decide which approach to undertake, the United States, except for antitrust crimes, is beyond that point. For over 20 years, the Guidelines mixed both approaches. For federal corporate crimes, the issue is whether policymakers should accentuate the Guidelines' intrinsic, ethics-based message or its financial incentive. There is no strong empirical evidence that the Guidelines' incentive successfully promoted within most firms an ethical organizational culture.

A second concern is whether an intrinsic, ethics-based approach raises its own unique risks, like moral balancing,<sup>343</sup> moral hypocrisy,<sup>344</sup> or duping the agency. The DOJ and court ultimately assess not whether the defendant has an ethics program, but whether its organizational culture genuinely encouraged ethical conduct and a commitment to comply with the law. One *Harvard Business Review* article, for example, praised Intel's antitrust compliance program as an "integral element" of Intel's successful business strategy and how senior management embedded "antitrust compliance deep into Intel's corporate memory."<sup>345</sup> But the European Commission and the Federal Trade Commission (FTC) found otherwise.<sup>346</sup> Intel's alleged misconduct included plainly illegal and unethical practices, such as deceiving consumers and the public.<sup>347</sup> Suppose in a high-profile case, a firm avoids prosecution on account of its compliance efforts. Later the public learns that the firm was violating other laws. The DOJ will look foolish or corrupt. Smarting from this experience, the DOJ will unlikely publicize its non-prosecution of firms based on their ethics programs.

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343. Bazerman & Gino, *supra* note 113, at 94 (discussing how individuals, in deciding whether to engage in unethical behavior, "consider their previous moral and immoral actions"; "keep track of their moral balance between moral credits (past good deeds) and moral debits (past bad deeds)"; and "compute a personal moral balance based on their actions that are morally relevant within a given time frame and do not go below their minimum," so that "a prior moral act can license later morally questionable behavior").

344. *Id.* at 95 (explaining that where people "desire to appear moral without bearing the actual cost of being moral").

345. David B. Yoffie & Mary Kwak, *Playing by the Rules: How Intel Avoids Antitrust*, HARV. BUS. REV., June 2001, at 119–20 ("Rather than wait for antitrust problems to develop, Intel would do everything in its power to ensure that the issue would never arise.").

346. The European Commission fined Intel a record amount (over one billion euros) for engaging in "naked" (i.e., plainly anticompetitive) restrictions to thwart its smaller competitor. James Kanter, *Europe Fines Intel \$1.45 Billion in Antitrust Case*, N.Y. TIMES (May 13, 2009), available at [http://www.nytimes.com/2009/05/14/business/global/14compete.html?pagewanted=all&\\_r=0](http://www.nytimes.com/2009/05/14/business/global/14compete.html?pagewanted=all&_r=0). The FTC alleged that Intel's unfair methods of competition began in 1999—two years before the *Harvard Business Review* article—and continued through 2009. Administrative Compl., *FTC v. Intel Corp.*, Docket No. 9341 (Dec. 16, 2009), available at <http://www.ftc.gov/sites/default/files/documents/cases/091216intelcmpt.pdf>.

347. Intel Compl. ¶ 10. Intel eventually settled. Decision & Order, *In re Intel Corp.*, filed Aug. 4, 2010, [http://www.ftc.gov/sites/default/files/documents/cases/2010/08/100804inteldo\\_0.pdf](http://www.ftc.gov/sites/default/files/documents/cases/2010/08/100804inteldo_0.pdf).

## VI. CONCLUSION

For over 20 years, the Guidelines have offered firms a significant financial incentive to develop an ethical organizational culture. Nonetheless, too many ethics programs remain ineffective and corporate crime persists. The compliance industry complains that “[t]oo many business executives take a ‘check the box’ approach to their programs, rather than satisfying the full intent of the [Guidelines].”<sup>348</sup>

The complaint, as this Article discusses, reflects the conflict between an extrinsic, incentive-based approach and the DOJ and courts’ expectations of effective compliance. The Guidelines seek to incentivize firms to develop an ethical organizational culture. But the compliance industry and government complain about the extrinsic approach’s side effects, including a mechanistic, copycat approach to compliance.<sup>349</sup> In short, the Commission cannot take an extrinsic, incentive-based approach to compliance, and expect managers to be intrinsically motivated to develop an ethical organizational culture.

As this Article explores, the Guidelines’ extrinsic, incentive-based approach to compliance does not cure, and likely contributes to, the problem. The extrinsic approach is hard to administer. It does not instill an ethical culture. As the Sentencing Commission Chair recognized, “It is questionable whether a compliance program can be truly effective if it does not have an ethics component.”<sup>350</sup> And it is doubtful that monetary incentives can effectively promote an ethical organizational culture necessary to deter and prevent corporate crimes.

Rather than mix two approaches, the courts and DOJ should emphasize an intrinsic, ethics-based approach. The intrinsic approach, in promoting shared value, will likely provide the firm with a competitive advantage. In aligning and embedding the firm’s core ethical values with daily operations, the approach will likely strengthen ethical leadership and an ethical organizational culture. It will likely deter and prevent unethical and illegal corporate behavior. Some may disagree. But the current approach is not working. The Guidelines’ incentive, as the sentencing data over the past 20 years reveals, was rarely received. Nor is there much hope of its inducing companies, after the economic crisis, to become more ethical.

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348. ERC Report, *supra* note 3, at 5.

349. *Id.* at 6 (“Merely ‘going through the motions’ in implementing a compliance/ethics program will neither meet the intent of the FSGO standards nor result in the kind of ethical cultures in companies that society increasingly expects.”).

350. Murphy, *supra* note 38, at 716.