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The Compliance Process

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THE COMPLIANCE PROCESS

VERONICA ROOT*

Even as regulators and prosecutors proclaim the importance of effective compliance programs, failures persist. Organizations fail to ensure that they and their agents comply with legal and regulatory requirements, industry practices, and their own internal policies and norms. From the companies that provide our news, to the financial institutions that serve as our bankers, to the corporations that make our cars, compliance programs fail to prevent misconduct each and every day. The causes of these compliance failures are multifaceted and include general enforcement deficiencies, difficulties associated with overseeing compliance programs within complex organizations, and failures to establish a culture of compliance throughout the organizational structure. In short, creating an effective compliance program is an inherently difficult task.

And yet, it may be that organizations can improve compliance within their organizations by rethinking the way they approach the compliance challenge. This Article—drawing on insights from cognitive psychology, behavioral economics, and behavioral ethics—sets forth a new method of evaluating compliance failures that focuses on the compliance process, which has the distinct, albeit interrelated, stages of prevention, detection, investigation, and remediation. The Article argues that utilizing a process frame will assist industry leaders, regulators, and policymakers in conducting more effective root-cause analyses of compliance failures, which will lead to the creation, implementation, and better evaluation of compliance programs. Delineating clear boundaries for the stages within the compliance process is difficult, but getting these distinctions right is essential when confronted with significant or complex compliance failures, particularly when an organization lacks a robust commitment to compliance. Additionally, the process frame can be utilized across regulatory areas and corporate forms, which serves to cement compliance as its own proper field worthy of further inquiry and study. By focusing on “The Compliance Process,” organizations, policymakers, and scholars will improve the tools available for them to assist in the creation and implementation of effective compliance programs.

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INTRODUCTION

Regulators, prosecutors, corporations, and their members dedicate a great deal of time and resources to implement the ever-elusive “effective compliance program.” Compliance refers to a firm’s effort to ensure that it and its agents adhere to legal and regulatory requirements, industry practice, and the firm’s own internal policies and norms. Organizations from all over the world, out of fear of sanction, harm, retribution, or ridicule, initiate programs aimed at making certain that their employees and members maintain compliance with external and internal norms and requirements. Yet every year seems to bring another set of significant scandals within organizations.

From fake accounts to faulty ignition switches to bribed foreign officials, serious and pervasive corporate misdeeds continue to occur, and these misdeeds are very often labeled “a compliance failure.”¹ When compliance failures occur, organizations inevitably end up focusing on how the compliance program itself failed, so that the firm can implement a compliance program that will ensure that future, similar misconduct does not occur. For the most complex of compliance failures, however, inquiries framed from the perspective of how a compliance program failed can be relatively broad and potentially unwieldy. As this Article demonstrates, however, an organization’s compliance program consists of four distinct stages within a compliance process: prevention, detection, investigation, and remediation. When compliance failures are assessed through a process frame, greater clarity regarding the nature of the compliance program’s failure may be discerned.

For example, starting in July 2016, a sexual harassment scandal emerged at Fox News, which is owned by a subsidiary of Twenty-First Century Fox, Inc.,² leading to the dismissal of Roger Ailes, the former chief executive officer of Fox News, among others.³ The public scandal began when a former Fox News anchor, Gretchen

1. The amorphous “compliance failure” distinction covers a huge swath of behavior across dozens of industries in public and private firms, which is perhaps unsurprising when one considers that a diverse set of firms will be subject to different legal and regulatory requirements.

2. Fox News provides reporting on current and political events occurring within the United States and across the world. It is owned by Fox Entertainment Group, which is a subsidiary of Twenty-First Century Fox, Inc. Twenty-First Century Fox has a “portfolio[] of cable, broadcast, film, pay TV and satellite assets spanning six continents across the globe.” It “[r]each[es] more than 1.8 billion subscribers in approximately 50 local languages every day.” *Investor Relations*, 21ST CENTURY FOX, <https://www.21cf.com/investor-relations> [<https://perma.cc/SZP4-C4DH>].

3. Jonathan Stempel, *21st Century Fox in \$90 Million Settlement Tied to Sexual Harassment Scandal*, REUTERS (Nov. 20, 2017, 6:02 PM), <https://www.reuters.com/article/us-fox-settlement/21st-century-fox-in-90-million-settlement-tied-to-sexual-harassment-scandal-idUSKBN1DK2NI> [<https://perma.cc/E3MB-6MTT>].

Carlson, filed a lawsuit accusing Roger Ailes of engaging in sexual harassment.⁴ Prior to being dismissed from Fox News and filing suit, Carlson recorded all private meetings between herself and Ailes for over a year and a half.⁵ The recordings included remarks from Ailes such as, “I think you and I should have had a sexual relationship a long time ago, and then you’d be good and better and I’d be good and better.”⁶ Upon Carlson filing suit, several other women alleged similar accounts detailing experiences of sexual harassment from Ailes.⁷ Ailes departed as chief executive officer of Fox News about two weeks after Carlson filed suit,⁸ but her complaint triggered a reckoning within the organization.⁹

Upon reviewing the events at Fox News, one natural conclusion is that the organization failed to create, implement, and execute an effective compliance program that would properly address and respond to sexual harassment in the workplace. That conclusion, given the depth and breadth of the alleged misconduct at Fox News, provides an insufficient basis for fully assessing the root causes of the compliance failure. But when a process frame is employed, additional details appear explaining why the sexual harassment program failed.

First, it appears Fox News failed to engage in activities likely to effectively *prevent* sexual harassment in the workplace. For example, Fox News,¹⁰ like many organizations,¹¹ relied on sexual harassment training to prevent misconduct in its workplace. Organizations rely on training to prevent misconduct, in part, because of two Supreme Court rulings from the late 1990s.¹² However, in 2015 “the EEOC established a task force to investigate workplace harassment and concluded that ‘much of the training done over the last 30 years has not worked as a prevention

4. Tom Huddleston Jr., *Roger Ailes Resigns: A Timeline of His Downfall*, FORTUNE (July 21, 2016), <http://fortune.com/2016/07/21/roger-ailes-resigned-scandal-timeline> [<https://perma.cc/75GK-JHFA>].

5. Michael M. Grynbaum & John Koblin, *Fox Settles with Gretchen Carlson over Roger Ailes Sex Harassment Claims*, N.Y. TIMES (Sept. 6, 2016), <https://www.nytimes.com/2016/09/07/business/media/fox-news-roger-ailes-gretchen-carlson-sexual-harassment-lawsuit-settlement.html> [<https://perma.cc/2G33-WBRE>].

6. *Id.*

7. Huddleston, *supra* note 4.

8. *Id.*

9. Emily Steel & Michael S. Schmidt, *Bill O'Reilly Settled New Harassment Claim, Then Fox Renewed His Contract*, N.Y. TIMES (Oct. 21, 2017), <https://www.nytimes.com/2017/10/21/business/media/bill-oreilly-sexual-harassment.html> [<https://perma.cc/FR6L-YCBY>].

10. Non-Monetary Relief at 1–2, 14, *City of Monroe Emps.’ Ret. Sys. ex rel. Twenty-First Century Fox, Inc. v. Murdoch*, No. 2017-0833-AGB (Del. Ch. Nov. 20, 2017) (As part of this agreement, Fox News agreed to “continue to conduct ‘live’ harassment and discrimination training for every employee.”).

11. Claire Suddath, *Why Can’t We Stop Sexual Harassment at Work?*, BLOOMBERG BUSINESSWEEK (Nov. 28, 2016), <https://www.bloomberg.com/features/2016-sexual-harassment-policy> [<https://perma.cc/8UVV-RPSQ>].

12. *See Burlington Indus., Inc. v. Ellerth*, 524 U.S. 742, 765 (1998) (creating a two-part affirmative defense allowing employers to avoid sex discrimination liability when following best practices); *Faragher v. City of Boca Raton*, 524 U.S. 775, 807 (1998) (adopting the same two-part affirmative defense).

tool.”¹³ Thus, while Fox News was likely complying with industry standards and best practices when utilizing sexual harassment training, the training activities it engaged in may not have been likely to prevent workplace sexual harassment. And Fox News failed to respond to new information and guidance that revealed the pitfalls and drawbacks of relying primarily on training to prevent sexual harassment in the workplace.¹⁴ Additionally, Fox News allegedly developed a culture where men were valued for making robust commentary while women were valued for their physical attributes.¹⁵ It does not appear that Fox News engaged in activity to prevent the commodification of women within its workforce.

Second, Fox News failed to *detect* sexual harassment within its organization. Sexual harassment, like many employment law issues, puts the onus on the victim to self-report misconduct. At Fox News, an alleged culture existed where women were afraid of reporting harassment. For instance, Megyn Kelly, a former Fox News television journalist who also alleged sexual harassment by Ailes, stated she believes the men at the center of the sexual harassment scandals “actively worked to suppress them and scare the other women.”¹⁶ Additionally, the detection mechanisms established at Fox News would have allowed Ailes to effectively stifle any

13. Suddath, *supra* note 11. One reason posited for why training is an ineffective prevention tool is “that both managers and workers regard it as a pro forma exercise aimed at limiting the employer’s legal liability.” Yuki Noguchi, *Trainers, Lawyers Say Sexual Harassment Training Fails*, NPR (Nov. 8, 2017, 4:30 PM), <https://www.npr.org/2017/11/08/562641787/trainers-lawyers-say-sexual-harassment-training-fails> [https://perma.cc/7H2N-SVYU]. Focusing on the legality of the harassment is a problem because “the letter of the law prohibits ‘severe or pervasive’ harassment when, in fact . . . there are plenty of examples that might not meet that standard but clearly should not be tolerated in the workplace.” *Id.* Further, most training courses are online, which do not appropriately engage employees. *Id.*

At best, research has found, [online sexual harassment] training succeeds in teaching people basic information, like the definition of harassment and how to report violations. At worst, it can make them uncomfortable, prompting defensive jokes, or reinforce gender stereotypes, potentially making harassment worse. Either way, it usually fails to address the root problem: preventing sexual harassment from happening in the first place.

Claire Cain Miller, *Sexual Harassment Training Doesn’t Work. But Some Things Do.*, N.Y. TIMES: THE UPSHOT (Dec. 11, 2017), <https://www.nytimes.com/2017/12/11/upshot/sexual-harassment-workplace-prevention-effective.html> [https://perma.cc/3PYY-BHHE].

14. While the EEOC still emphasizes that training is better than no training, it wants companies to “supplement training with initiatives that emphasize broader topics such as civility and respect.” Suddath, *supra* note 11.

15. Fox News developed a reputation for “[b]lustery male commentators and women, just as qualified, who were showcased for their looks with revealing clothes and camera shots.” Mike Snider, *Sexual Harassment at Fox News: Murdochs Overhaul Culture with Eyes on Sky*, KITSAP SUN (July 17, 2017, 2:49 PM), <https://www.kitsapsun.com/story/money/business/2017/07/17/sexual-harassment-fox-news-murdochs-overhaul-culture-eyes-sky/460303001> [https://perma.cc/6YWT-MP8B].

16. Dominic Patten, *Megyn Kelly on Why Harvey Weinstein’s “Done”, Sexual Harassment Solutions, Doubling Down & Rising Ratings*, DEADLINE (Nov. 9, 2017, 7:45 AM), <http://deadline.com/2017/11/megyn-kelly-sexual-harassment-interview-harvey-weinstein-fox-news-roger-ailes-experiences-1202203810> [https://perma.cc/C9LB-H9CE].

investigations because human resources, the department that would receive sexual harassment claims, reported to Roger Ailes.¹⁷

Third, Fox News initially failed to *investigate* sexual harassment when alerted to potential misconduct. For example, a biography of Ailes published in 2014 included multiple stories of women, the majority of which remained unnamed, who reported being sexually harassed by Ailes.¹⁸ It does not appear that this information was acted upon by appropriate channels within Fox News or Twenty-First Century Fox. After becoming aware of Carlson's allegations, Twenty-First Century Fox did, however, retain an external law firm to initiate an internal investigation into the alleged sexual harassment by Ailes. Based on the findings of the internal review, at least six additional women claimed Ailes behaved inappropriately toward them.¹⁹

Fourth, Fox News struggled to *remediate* and properly address sexual harassment claims. For example, after Ailes was dismissed from Fox News, allegations were brought against then Fox News megastar Bill O'Reilly.²⁰ These were not the first allegations brought against O'Reilly, as settlements were entered into for claims alleging sexual harassment by O'Reilly in 2002, 2004, 2011, as well as two in 2016.²¹ Twenty-First Century Fox allowed O'Reilly to designate the latter allegations as a "personal matter" and permitted him to settle the sixth claim in January 2017 without disclosing the parameters of the settlement to Twenty-First Century Fox.²² The settlement amount, which was subsequently disclosed to the public, was \$32 million.²³ Despite this history and awareness of conduct that resulted in repeated settlements for alleged sexual harassment, in February 2017, Twenty-First Century Fox granted O'Reilly a four-year contract extension that paid him \$25 million a year.²⁴ Additionally, upon learning of Ailes and O'Reilly's alleged repeat misconduct, instead of sending a strong signal regarding the need to conduct an extensive overhaul of its policies and procedures regarding sexual harassment, then executive cochairman of Twenty-First Century Fox, Rupert Murdoch, stated in December 2017 that the Fox News sexual harassment scandal was "[a]ll nonsense, there was a problem with our chief executive, sort of, over the years, isolated incidents."²⁵ Yet, more than two dozen women came forward with sexual harassment

17. *Id.* During an interview after Ailes's alleged misconduct became public, Kelly argued that human resources, where employees report discrimination and harassment, should not report to the chief executive officer to avoid conflicts of interest. *Id.*

18. Callum Borchers, *Book: Roger Ailes Has Been Soliciting Sex from Female Journalists Since the 1980s*, WASH. POST: THE FIX (July 6, 2016), https://www.washingtonpost.com/news/the-fix/wp/2016/07/06/book-roger-ailes-has-been-soliciting-sex-from-female-journalists-since-the-1980s/?noredirect=on&utm_term=.033f10a4519e [https://perma.cc/G8NP-S8NY].

19. Jim Rutenberg, Ben Protess & Emily Steel, *Internal Inquiry Sealed the Fate of Roger Ailes at Fox*, N.Y. TIMES (July 20, 2016), <https://www.nytimes.com/2016/07/21/business/media/as-an-internal-inquiry-sinks-ailes-questions-about-fox-newss-fate.html?mtrref=www.google.com> [https://perma.cc/DN3L-BPQR].

20. Steel & Schmidt, *supra* note 9.

21. *Id.*

22. *Id.*

23. *Id.*

24. *Id.*

25. Erik Wemple, *Rupert Murdoch Expertly Returns the Sexual Harassment Spotlight to*

allegations against Roger Ailes, the former chief executive officer, in addition to complaints against other employees.²⁶ Despite Murdoch's statements, Twenty-First Century Fox has engaged in some potentially robust remediation efforts, as evidenced by the fact that it (i) dismissed Ailes and O'Reilly,²⁷ (ii) entered into multiple settlements in summer 2016 regarding Ailes's alleged misconduct,²⁸ (iii) agreed to implement governance and compliance enhancements aimed at preventing sexual harassment,²⁹ and (iv) expressed its commitment to preventing sexual harassment, racial discrimination, and retaliation in its Statement of Corporate Governance.³⁰

As demonstrated by this description, labeling the challenges faced by Twenty-First Century Fox and Fox News as a failure in creating and maintaining an effective sexual harassment compliance program does not prompt one to see the depth and breadth of the potential deficiencies present. The root causes of the compliance failures at Twenty-First Century Fox and Fox News appear multifaceted. At a minimum, the causes may include (i) poor guidance and policy from Supreme Court jurisprudence, (ii) a need to adjust reporting lines within the firms, (iii) a more robust and responsive investigative process when confronted with allegations of sexual harassment, and (iv) improved leadership responses to allegations of sexual harassment and possible dysfunctional cultural realities within the firms. These multilayered, contributing causes become more apparent when one confronts the corporate misconduct using a process frame.

While the emerging field of compliance is perceived by many as a narrow component of general corporate governance efforts,³¹ the sheer breadth and diversity of issues compliance programs must confront makes implementing effective compliance programs an intensely challenging endeavor.³² Today's organizations are responsible for ensuring proper compliance in many different areas. Whether it is General Motors's failure to properly address a faulty ignition switch or Wells Fargo's decision to ignore fraudulently opened accounts—one common challenge

Fox News, WASH. POST (Dec. 16, 2017), https://www.washingtonpost.com/blogs/erik-wemple/wp/2017/12/16/rupert-murdoch-expertly-returns-the-sexual-harassment-spotlight-to-fox-news/?utm_term=.eab74cecd1ad [<https://perma.cc/X59P-LPWD>].

26. *Id.*

27. Steel & Schmidt, *supra* note 9.

28. Stipulation and Agreement of Settlement, Compromise, and Release at 3, City of Monroe Emps.' Ret. Sys. *ex rel.* Twenty-First Century Fox, Inc. v. Murdoch, No. 2017-0833-AGB (Del. Ch. Nov. 20, 2017). This agreement as well as the subsequent non-monetary relief agreement were approved by the court on February 9, 2018. Jeff Montgomery, *Fox's 'Unusual' \$90M Scandal Deal Gets Chancery's OK*, LAW360 (Feb. 9, 2018, 7:11 PM), <https://www.law360.com/articles/1011154/fox-s-unusual-90m-scandal-deal-gets-chancery-s-ok> [<https://perma.cc/J4M9-FWUK>].

29. Non-Monetary Relief, *supra* note 10.

30. *Id.* at 2.

31. Lawrence A. Cunningham, *Deferred Prosecutions and Corporate Governance: An Integrated Approach to Investigation and Reform*, 66 FLA. L. REV. 1, 14 (2014). *But see* Sean J. Griffith, *Corporate Governance in an Era of Compliance*, 57 WM. & MARY L. REV. 2075 (2016) (arguing that compliance does not fit within traditional models of corporate governance).

32. *See* Eric C. Chaffee, *Creating Compliance: Exploring a Maturing Industry*, 48 U. TOL. L. REV. 429, 430–31 (2017).

confronting modern organizations is how to appropriately assess and resolve compliance questions. As a result, misconduct by and within organizations continues to be a topic of significance for courts, regulators, prosecutors, and the individuals affected or harmed, which, in turn, makes the field of compliance of great societal import.³³ Yet despite its recognized importance, significant compliance failures persist.

Because compliance failures continue to occur, scholars, governmental actors, and industry leaders are constantly proposing, implementing, and questioning strategies aimed at improving organizations' compliance programs. For example, legal scholarship has discussed the importance of focusing on cultures of compliance,³⁴ the need for robust incentives from governmental actors,³⁵ and the propriety of permitting governmental actors to dictate corporate governance reforms.³⁶ Additionally, governmental actors are constantly experimenting with methods for encouraging more compliant behavior by organizations, as evidenced by the publication of recent guides on compliance programs³⁷ and the Department of Justice's (DOJ) adoption of a pilot program meant to motivate self-disclosure and cooperation by organizations.³⁸ Similarly, industry leaders, such as the Association

33. See Cunningham, *supra* note 31, at 14 (explaining that the roots of compliance are anchored in the intensification of organizational criminal liability).

34. Donald C. Langevoort, *Cultures of Compliance*, 54 AM. CRIM. L. REV. 933 (2017).

35. Veronica Root, *Coordinating Compliance Incentives*, 102 CORNELL L. REV. 1003 (2017).

36. See Renee M. Jones & Michelle Welsh, *Toward a Public Enforcement Model for Directors' Duty of Oversight*, 45 VAND. J. TRANSNAT'L L. 343 (2012) (arguing in favor of a public enforcement model for the fiduciary duties of corporate directors). Compare Cunningham, *supra* note 31 (arguing that prosecutors should invest in corporate governance by contemplating it at the outset and articulating rationales for changes), and Griffith, *supra* note 31 (arguing for a more limited governmental role in designing corporate governance mechanisms), with Brandon L. Garrett, *Rehabilitating Corporations*, 66 FLA. L. REV. F. 1 (2014) (responding to Cunningham's argument).

37. See, e.g., William H. Jordan, Edward T. Kang & Jason D. Popp, *Government & Internal Investigations Advisory: DOJ Releases Guidance on Compliance Programs*, ALSTON & BIRD (Mar. 22, 2017), <https://www.alston.com/en/insights/publications/2017/03/doj-releases-guidance-on-compliance-programs> [https://perma.cc/8JMB-5MQH] (discussing a publication from DOJ Fraud explaining how it measures compliance programs and providing information meant to help shape compliance policies); *OIG Publishes Compliance Program Effectiveness Guide*, ARNALL GOLDEN GREGORY (Apr. 25, 2017), <http://www.agg.com/Compliance-Program-Effectiveness-Guide-Published-by-OIG-04-25-2017> [https://perma.cc/8QL2-J38T] (discussing document issued by the Health and Human Services Office of the Inspector General on how to measure a compliance program's effectiveness).

38. Press Release, U.S. Dep't of Justice, Criminal Division Launches New FCPA Pilot Program (Apr. 5, 2016), <https://www.justice.gov/archives/opa/blog/criminal-division-launches-new-fcpa-pilot-program> [https://perma.cc/2EA8-PUQB] (discussing the new DOJ Pilot Program, which provides significant mitigation credit and, in some instances, a declination to prosecute for companies confronting a Foreign Corrupt Practices Act (FCPA) violation); see also Rod J. Rosenstein, Deputy Attorney Gen., U.S. Dep't of Justice, Remarks at 34th International Conference on the Foreign Corrupt Practices Act (Nov. 29, 2017), <https://www.justice.gov/opa/speech/deputy-attorney-general-rostenstein-delivers-remarks-34th-international-conference-foreign> [https://perma.cc/7TWS-FKFA] (some elements of the pilot

of Corporate Counsel, often publish guidance and best practices aimed at assisting organizations in their compliance efforts.³⁹ Finally, the American Law Institute has brought together a variety of constituencies in an effort to provide “a set of recommended standards and best practices on the law of compliance and risk management.”⁴⁰

This Article contributes to the effort to improve compliance within organizations by proposing a new method for evaluating compliance failures that focuses on the discrete stages that make up the compliance process—prevention, detection, investigation, and remediation. Importantly, the compliance process outlined is applicable even when an organization has previously failed to demonstrate a robust commitment to creating a culture of compliance. Additionally, because the proposed compliance process frame may be utilized across regulatory areas and corporate forms, this Article helps to cement the field of compliance as a discrete area of study.

Part I of this Article discusses the origins of the “effective compliance program” mandate and its commonly accepted limitations. Part II sets forth the four stages within a compliance process in an effort to provide a new framework for evaluating compliance failures. Currently, organizations that experience a compliance failure enter into a relatively broad inquiry focused on why their compliance program failed. This Article, however, argues that firms facing complex compliance failures may benefit from instead asking where within the compliance process did failure or failures occur. Part III draws on insights from the fields of cognitive psychology, behavioral economics, and behavioral ethics and argues that by assessing compliance failures through the process frame proposed by this Article, organizations will be able to better assess and understand the root cause of the breakdowns in their compliance programs.⁴¹ Once the root cause, or causes, of a compliance failure is understood, an organization will be better equipped to take appropriate measures aimed at ensuring long-term change. Part IV addresses benefits and potential concerns raised by the Article’s proposed framework.

program were subsequently made permanent via a new FCPA corporate enforcement policy); Jonathan Sack, *DOJ Announces It Will Extend FCPA “Pilot Program,”* FORBES (Mar. 13, 2017, 11:16 AM), <https://www.forbes.com/sites/insider/2017/03/13/doj-announces-it-will-extend-fcpa-pilot-program/#4db34c31d3e1> [<https://perma.cc/XS4F-RNLJ>].

39. Kwamina Williford & Daniel Small, *Establishing an Effective Compliance Program: An Overview to Protecting Your Organization*, ASS’N CORP. COUNS. (Jan. 25, 2013), <http://www.acc.com/legalresources/quickcounsel/eaecp.cfm> [<https://perma.cc/ZGK8-DX2R>].

40. *Principles of the Law: Compliance, Enforcement, and Risk Management for Corporations, Nonprofits, and Other Organizations*, AM. L. INST., https://www.ali.org/projects/show/compliance-enforcement-and-risk-management-corporations-nonprofits-and-other-organizations/#_participants [<https://perma.cc/3K99-E4MT>].

41. The importance of engaging in a root-cause analysis was acknowledged by the DOJ when discussing a program aimed at evaluating corporate compliance programs within firms. U.S. DEP’T OF JUSTICE, *EVALUATION OF CORPORATE COMPLIANCE PROGRAMS 1*, <https://www.justice.gov/criminal-fraud/page/file/937501/download> [<https://perma.cc/MM7N-NPBM>].

I. THE (ELUSIVE) EFFECTIVE COMPLIANCE PROGRAM

Establishing an effective Compliance and Ethics Program (“Program”) has become a necessity to protect any highly regulated organization.
– Association of Corporate Counsel⁴²

Organizations accept the need to establish an effective compliance and ethics program as a relatively uncontroversial reality. Thus, organizations understand that they and their agents must adhere to legal and regulatory requirements, industry practices, and the organization’s own internal policies and norms. This current understanding of compliance has evolved, in part, due to (i) an increase in regulatory requirements associated with a more complex administrative state, (ii) the addition of duty of care obligations for boards of directors and other corporate managers, and (iii) the increasing nature of governmental actors to pursue organizational criminal liability.⁴³

This Part begins by describing some of the rules, standards, and mandates that require firms to implement compliance programs. The Part then explains how a variety of incentives from enforcement agencies and prosecutors also exist to encourage organizations to adopt compliance programs that are effective, despite being imperfect. The Part concludes by outlining why perfect compliance would lead to an inefficient amount of self-policing and, therefore, is generally not pursued.

A. Rules, Standards & Mandates

The field of compliance, like many areas of the law, consists of a mix of bright-line rules and less precise standards. The mix of rules and standards work together to establish the minimum levels of conduct firms must adopt to ensure that they have created effective compliance programs. If an organization does not meet these rules and standards, it becomes subject to certain consequences.

For example, the United States requires “truthful declarations to U.S. Customs and Border Protection,” which allows “[c]ustoms officers . . . to scrutinize cultural property . . . and prevent the inappropriate entry of such property.”⁴⁴ This is a bright-line rule with which, in theory, compliance should be relatively easy. In addition to this bright-line rule, there are industry standards governing the sale and trade of certain antiquities, which can be more complicated to implement into a compliance program. For example, experts in the antiquities field know that “the acquisition of

42. Williford & Small, *supra* note 39.

43. Chaffee, *supra* note 32, at 429–30; *see also* Cunningham, *supra* note 31, at 14. This Part does not include a discussion on the responsibilities of board of directors for compliance efforts because these issues are briefly highlighted in Part II of the Article and more thoroughly discussed in other works of legal scholarship. *See, e.g.*, Symposium, *The Caremark Decision at 21—Corporate Compliance Comes of Age*, 90 TEMP. L. REV. 597 (2018).

44. Press Release, U.S. Attorney’s Office, E. Dist. of N.Y., U.S. Dep’t of Justice, United States Files Civil Action to Forfeit Thousands of Ancient Iraqi Artifacts Imported by Hobby Lobby (July 5, 2017), <https://www.justice.gov/usao-edny/pr/united-states-files-civil-action-forfeit-thousands-ancient-iraqi-artifacts-imported> [https://perma.cc/B24F-QMWY] [hereinafter Hobby Lobby Press Release].

cultural property likely from Iraq, including cuneiform tablets and cylinder seals, carries a risk that such objects may have been [improperly] looted from archaeological sites in Iraq.”⁴⁵ Thus, businesses dealing in antiquities should ensure that (i) their customs declarations are truthful and honest and (ii) their compliance program has policies in place that govern how to properly handle antiquities from Iraq and other countries prone to antiquity theft.

In 2017, Hobby Lobby Stores, Inc. (“Hobby Lobby”) entered into a settlement with the U.S. government because it violated the operative rules and standards controlling the acquisition of certain antiquities, including cuneiform tablets—clay tablets with an ancient system of writing “that was used in ancient Mesopotamia thousands of years ago.”⁴⁶ It improperly shipped cultural artifacts into the United States with falsified records regarding the artifacts’ country of origin and labeled the contents of the shipments as “ceramic tiles.”⁴⁷ Hobby Lobby engaged in these illegal activities despite having received warnings from “an expert on cultural property law” that Hobby Lobby itself retained.⁴⁸ Thus, Hobby Lobby failed to have an effective ethics and compliance program as it relates to the acquisition of antiquities.

The consequence of Hobby Lobby’s compliance failure is that it was forced to forfeit many of the antiquities “and an additional sum of \$3 million” to resolve a civil action brought against it by the United States.⁴⁹ Hobby Lobby also “agreed to adopt internal policies and procedures governing its importation and purchase of cultural property, provide appropriate training to its personnel, hire qualified outside customs counsel and customs brokers, and submit quarterly reports to the government on any cultural property acquisitions for the next eighteen months.”⁵⁰ In short, Hobby Lobby was required to create an ethics and compliance program with respect to the purchase of antiquities. Thus, in addition to having to comply with the bright-line rule and standards issued by the government, Hobby Lobby now also has a mandate, in the form of a civil settlement agreement with the government that requires Hobby Lobby to create a compliance program that addresses the purchase of antiquities.

The mandate to adopt certain compliance programs can come, as it did in the case of Hobby Lobby, through a settlement agreement, but mandates are also sometimes found directly within statutory or regulatory requirements. For example, the Bank Secrecy Act requires banks to adopt compliance programs that include “[i]nternal policies, procedures, and controls,” as well as the “[d]esignation of a compliance officer” and “[o]ngoing employee training programs.”⁵¹ As such, an organization subject to the Bank Secrecy Act and its corresponding regulations has a mandate to adopt an ex ante ethics and compliance program. However, at the same time government actors and scholars recognize that compliance programs must be tailored

45. *Id.*

46. *Id.*

47. *Id.*

48. *Id.*

49. *Id.*

50. *Id.*

51. See, e.g., FDIC, *Bank Secrecy Act, Anti-Money Laundering and Office of Foreign Asset Control*, in RISK MANAGEMENT MANUAL OF EXAMINATION POLICIES 8.1-1, 8.1-8, <https://www.fdic.gov/regulations/safety/manual/section8-1.pdf> [https://perma.cc/FTE2-MTEA] (last updated Apr. 2005).

to the specific firm implementing a compliance program because the compliance needs of each organization will be different.⁵²

Thus, there are a variety of rules, standards, and mandates in place that amount to requirements that organizations develop compliance programs to address potential misconduct. In addition to these measures, prosecutors and regulators engage in a variety of efforts to incentivize firms to create effective ethics and compliance programs.

B. Enforcement Incentives

Despite the existence of rules, standards, and mandates that require organizations to engage in efforts to adopt effective ethics and compliance programs, compliance failures have continued to occur. As a result, governmental actors also utilize a variety of enforcement incentives to encourage firms to curb misconduct within their ranks.⁵³ Indeed, it has long been understood and well documented throughout law and economics literature that “governments that want to effectively deter corporate crime should provide firms with strong incentives to undertake corporate policing.”⁵⁴ This is key because governmental actors have a very limited ability to detect misconduct within private organizations and must rely on organizations to police their own members. Thus, regulators and prosecutors have adopted a range of policies and enforcement norms that serve as incentives for organizations to monitor their members in an effort to deter and prevent corporate misconduct.

One example of a strong set of incentives utilized by regulators and prosecutors comes from the Federal Sentencing Guidelines, which contains a section entitled “Effective Compliance and Ethics Program.” That section requires organizations to “exercise due diligence to prevent and detect criminal conduct.”⁵⁵ This provision is part of what has become known as the Organizational Guidelines, which provide mechanisms for sanctioning corporations for criminal misconduct.⁵⁶ Specifically, the Organizational Guidelines allow organizations to be “fined, sentenced to

52. See, e.g., *OFAC FAQs: Sanctions Compliance*, U.S. DEP’T TREASURY, https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_compliance.aspx [<https://perma.cc/GF7A-MSGP>] (last updated July 17, 2018) (“There is no single compliance program suitable for every financial institution.”).

53. One reason incentives from governmental actors remain quite important is that corporate law jurisprudence has “essentially removed personal liability of directors and officers from the range of remedies used to shape corporate conduct.” Lisa M. Fairfax, *On the Sufficiency of Corporate Regulation as an Alternative to Corporate Criminal Liability*, 41 STETSON L. REV. 117, 117 (2011).

54. Jennifer Arlen, *Corporate Criminal Enforcement in the United States: Using Negotiated Settlements to Turn Potential Corporate Criminals into Corporate Cops* 1, 9 (N.Y. Univ. Sch. of Law, Pub. Law & Legal Theory Research Paper Series, Working Paper No. 17-12; Law & Econs. Research Paper Series, Working Paper No. 17-09, 2018) (citations omitted), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2951972 [<https://perma.cc/2WUT-C7TH>].

55. U.S. SENTENCING GUIDELINES MANUAL § 8B2.1 (U.S. SENTENCING COMM’N 2016).

56. PAULA DESIO, U.S. SENTENCING COMM’N, AN OVERVIEW OF THE ORGANIZATIONAL GUIDELINES, <https://www.ussc.gov/sites/default/files/pdf/training/organizational-guidelines/ORGOVERVIEW.pdf> [<https://perma.cc/TJ9G-RR9H>].

probation . . . ordered to make restitution . . . [required to] issue public notices of conviction . . . and exposed to applicable forfeiture statutes.”⁵⁷

Interestingly, the Organizational Guidelines, while technically applicable only to criminal enforcement actions, have become an important tool that prosecutors and regulators utilize to encourage corporations engaged in misconduct to settle claims through the use of civil enforcement actions.⁵⁸ The threat of criminal sanction under the Organizational Guidelines has proven an effective mechanism for governmental enforcement authorities to incentivize corporations to address and remediate misconduct.

For example, when General Motors’s ignition switch scandal came to light, it became clear that the company’s decision to ignore the faulty ignition switches resulted in the injury and, in some cases, death of dozens of individuals.⁵⁹ Despite the company’s decision to ignore the problem for several years, the government allowed General Motors to enter into a deferred prosecution agreement, a civil agreement, to resolve the corporate misconduct.⁶⁰ The agreement established that the government would defer bringing criminal charges for three years if General Motors agreed to undertake certain remediation efforts.⁶¹ Additionally, General Motors agreed to have an independent monitor “review and assess policies, practices, and procedures relating to [General Motors’s] safety-related public statements, sharing of engineering data, and recall processes.”⁶² General Motors also agreed to forfeit \$900 million. At the conclusion of the three-year period, if General Motors performs as expected under the deferred prosecution agreement, then the criminal charges against it will be dismissed in their entirety.⁶³

As demonstrated by this example, the government is able to utilize a variety of enforcement incentives to motivate private firms to engage in specific behavior.⁶⁴

57. *Id.*

58. Root, *supra* note 35, at 1014–16.

59. Brent Snavelly, *Court: GM Gets No Shield from Old Ignition-Switch Cases*, USA TODAY (Apr. 24, 2017, 12:07 PM), <https://www.usatoday.com/story/money/cars/2017/04/24/court-gm-gets-no-shield-old-ignition-switch-cases/100842980> [<https://perma.cc/THS9-YSF7>] (“[A] defect that killed at least 124 people and injured 275 in small cars made by the old GM.”).

60. Press Release, U.S. Attorney’s Office, S. Dist. N.Y., U.S. Dep’t of Justice, Manhattan U.S. Attorney Announces Criminal Charges Against General Motors and Deferred Prosecution Agreement with \$900 Million Forfeiture (Sept. 17, 2015), <https://www.justice.gov/usao-sdny/pr/manhattan-us-attorney-announces-criminal-charges-against-general-motors-and-deferred> [<https://perma.cc/JT6K-UPE4>] [hereinafter GM Press Release].

61. *Id.*

62. *Id.*

63. *Id.*

64. In previous work, I have argued that the government could utilize enforcement incentives more aggressively and efficiently to incentivize organizations to implement robust ethics and compliance programs if they would be more willing to utilize formal criminal sanctions. *See generally* Root, *supra* note 35. Other enforcement incentives that governmental actors might utilize would include things like debarment or withdrawal of a bank’s status as a well-known, seasoned issuer. *See Frequently Asked Questions: Suspension & Debarment*, GSA, <https://www.gsa.gov/portal/content/192903> [<https://perma.cc/XY3H-SMSZ>] (last updated Aug. 13, 2017); *see also* Joe Mont, *New Guidance on SEC Waivers, Exemptions in*

When the government's enforcement incentives are viewed in tandem with the pre-existing rules, standards, and mandates that require organizations to adopt ethics and compliance programs, one might think that organizations would engage in a robust effort to ensure perfect compliance with legal and regulatory requirements. In actuality, however, some compliance failures are not only expected, they are accepted as necessary realities.

C. Imperfect Compliance

Despite the focus by regulators and prosecutors on the importance of developing an effective compliance program, it is commonly understood that it would be inefficient for firms to strive to obtain "perfect" compliance.⁶⁵ Much of this understanding comes from law and economics scholarship, which two decades ago outlined the argument against a mandate for firms to achieve perfect compliance with legal and regulatory demands.⁶⁶

Organizations are sanctioned for misconduct, but the actual offenders are an organization's agents—the organization's employees or members.⁶⁷ Thus, organizations are sanctioned not because they themselves commit crime, but because they are held vicariously liable for the actions of their agents.⁶⁸ The question debated at the time was whether organizations should be held to a strict vicarious liability standard, or something more malleable:

[Vicarious liability] is not only the most familiar regime of corporate liability, but also is the most plausible one whenever agents only act in the best interests of their principals—either because they share these interests or because they do as they are told. In this situation, the firm's agents are logically compelled to avoid misbehavior if the firm must internalize its costs. But when this condition does not hold—when the firm has different interests from its agents and cannot control them costlessly—then simple vicarious liability may no longer be the preferred corporate incentive regime. In that case, the state cannot deter misconduct simply by setting liability high enough to ensure that firms cannot profit from it.

the Works, COMPLIANCE WEEK (Feb. 23, 2015), <https://www.complianceweek.com/blogs/the-filing-cabinet/new-guidance-on-sec-waivers-exemptions-in-the-works#.WZdBwIT3bCQ> [<https://perma.cc/TRW6-BSC3>].

65. Root, *supra* note 35, at 1033–36.

66. See Jennifer Arlen & Reinier Kraakman, *Controlling Corporate Misconduct: An Analysis of Corporate Liability Regimes*, 72 N.Y.U. L. REV. 687 (1997).

67. See *id.* at 690.

68. There are scholars who have advocated for a different method of attributing liability to organizations for the conduct of their agents. For example, one might limit a finding of organizational misconduct to circumstances where the organization's agent acted "primarily with the intent to benefit the firm." Samuel W. Buell, *The Blaming Function of Entity Criminal Liability*, 81 IND. L.J. 473, 473–75 (2006) ("[C]ommon law courts . . . imported respondeat superior liability from tort law into the criminal law . . . without serious theoretical analysis").

Instead, the firm must be induced to take direct action to deter agents from committing wrongs, including measures to prevent misconduct and policing measures to detect and sanction it.⁶⁹

The latter path was chosen, which resulted in prosecutors and enforcement agents tolerating certain amounts of noncompliance with legal and regulatory requirements. In part, this is because “strict liability enforcement, while the best regime for ‘inducing firms to sanction culpable agents,’ ‘may actually deter firms from monitoring, investigating, or reporting’ corporate misconduct.”⁷⁰

Recognizing this, in 2016 the DOJ Fraud Section (“DOJ Fraud”) initiated a pilot program that allows corporations to reduce the sanction they would otherwise face for violations under the Foreign Corrupt Practices Act (FCPA), which prohibits bribery of foreign officials.⁷¹ To receive the lesser sanction, companies must “voluntarily disclose misconduct, fully cooperate [with the DOJ], and timely and appropriately remediate” the misconduct surrounding the FCPA violation.⁷² As a result of the program, DOJ Fraud has issued several “declinations” to prosecute.⁷³ One such declination was entered into between DOJ Fraud and Linde North America Inc. and Linde Gas North America LLC (collectively, “Linde”).⁷⁴ From November 2006 to December 2009, Linde “made corrupt payments to high-level officials at the National High Technology Center (‘NHTC’) of the Republic of Georgia (‘Georgia’), a 100% state-owned and -controlled entity” in an effort to receive the officials’ assistance in obtaining certain contracts related to the production of boron gas.⁷⁵

Sanctions for FCPA violations vary, but previous empirical research suggests “the sanction imposed in an FCPA action increases with the size of bribe, the profit related

69. Arlen & Kraakman, *supra* note 66, at 690–91; *see also* V.S. Khanna, *Corporate Liability Standards: When Should Corporations Be Held Criminally Liable*, 37 AM. CRIM. L. REV. 1239 (2000) (arguing in favor of a composite regime for sanctioning corporate misconduct).

70. Root, *supra* note 35, at 1034 (quoting Arlen & Kraakman, *supra* note 66, at 701, 717).

71. Memorandum from Andrew Weissmann, Chief, Fraud Section, Criminal Div., U.S. Dep’t of Justice, The Fraud Section’s Foreign Corrupt Practices Act Enforcement Plan and Guidance 1–2 (Apr. 5, 2016), <https://www.justice.gov/archives/opa/blog-entry/file/838386/download> [https://perma.cc/6F5Z-FE4V] [hereinafter FCPA Program Memo]. The program was initially a one-year pilot program, but it was temporarily extended for an indeterminate amount of time. Sack, *supra* note 38; *see also* Marc Alain Bohn & James G. Tillen, *Evaluating FCPA Pilot Program: Declinations on the Rise*, LAW360 (Apr. 10, 2017, 5:10 PM), <https://www.law360.com/articles/905127/evaluating-fcpa-pilot-program-declinations-on-the-rise> [https://perma.cc/QQ87-X6JR].

72. FCPA Program Memo, *supra* note 71, at 3.

73. *Declinations*, U.S. DEP’T JUST., <https://www.justice.gov/criminal-fraud/pilot-program/declinations> [https://perma.cc/FCP9-2PCA] (last updated Aug. 23, 2018).

74. Letter from Jacob T. Elberg, Chief, Health Care & Gov’t Fraud Unit, U.S. Attorney’s Office, Dist. of N.J. & Laura N. Perkins, Assistant Chief, U.S. Dep’t of Justice, Criminal Div., Fraud Section, to Lucinda Low & Thomas Best, Steptoe & Johnson LLP (June 16, 2017), <https://www.justice.gov/criminal-fraud/file/974516/download> [https://perma.cc/DVE7-7KK8] [hereinafter Linde Declination].

75. *Id.* at 1.

to the bribe, [and] the amount of business affected by the bribe.⁷⁶ This possible emphasis on correlating the seriousness of the offense with the sanction might be consistent with attempting to adopt a near strict liability standard for corporations engaged in FCPA violations. In contrast, granting a declination in the face of multiyear, widespread bribery of multiple foreign officials would seem inapposite with the goal of incentivizing firms to prevent misconduct within their ranks. The government, however, has recognized that there are benefits to allowing for imperfect compliance. In the case of Linde, the declination letter explained that leniency was warranted because of:

(1) Linde's timely, voluntary self-disclosure of the matter; (2) the thorough, comprehensive and proactive investigation undertaken by Linde; (3) Linde's full cooperation in this matter (including its provision of all known relevant facts about the individuals involved in or responsible for the misconduct) and its agreement to continue to cooperate in any ongoing investigations of individuals; (4) Linde's agreement to disgorge the profits . . . and forfeit to the United States the corrupt proceeds . . . ; (5) the steps Linde has taken and continues to take to enhance its compliance program and its internal accounting controls; and (6) Linde's full remediation (including terminating and/or taking disciplinary action against the employees involved in the misconduct . . .).⁷⁷

DOJ Fraud's declination program and policy is just one of many ways in which the government acknowledges that there are practical reasons to provide strong incentives for firms to prevent and detect misconduct, while also acknowledging that perfect compliance is an imprudent goal.

Thus, the admonition to enact an effective compliance program is not an effort aimed at achieving perfect compliance. Instead, firms are tasked with engaging in good faith efforts at ensuring that their members and employees engage in activity that is in accordance with legal and regulatory requirements.

* * * *

As highlighted by this Part, prudent organizations will implement ethics and compliance programs in areas where they are subject to certain legal or regulatory requirements or strong sets of mandates or potential sanctions. They are not, however, expected to achieve perfect compliance because such a requirement might have the unintended consequence of actually diminishing firms' efforts to pursue effective compliance programs. As a result, the quest for an effective compliance

76. Stephen J. Choi & Kevin E. Davis, *Foreign Affairs and Enforcement of the Foreign Corrupt Practices Act*, 11 J. EMPIRICAL LEGAL STUD. 409, 440 (2014). *But see* F. Joseph Warin, Michael S. Diamant & Veronica S. Root, *Somebody's Watching Me: FCPA Monitorships and How They Can Work Better*, 13 U. PA. J. BUS. L. 321, 337 (2011) (explaining that certain sanctions for violating FCPA violations, in particular the imposition of a corporate monitor, are difficult to predict because no precise set of factors appears dispositive as part of the government's decision-making).

77. Linde Declination, *supra* note 74, at 2.

program is something of a moving target and a seemingly elusive goal. Organizations know they must implement a compliance program, but failure within these programs is persistent. These failures have led firms to question continuously how they can craft a more effective compliance program that is more likely to deter misconduct.

II. THE COMPLIANCE PROCESS

*“Process” “a series of actions or operations conducing to an end.”*⁷⁸

As explained in Part I, governmental actors have long emphasized the importance for firms to design effective ethics and compliance programs. Industry officials have responded in kind by creating compliance programs within their organizations that are often headed by chief compliance officers⁷⁹ and sometimes include hundreds, if not thousands, of compliance personnel.⁸⁰ Yet, these same industry leaders and enforcement authorities are asked each and every day to evaluate the cause of compliance failures. To date, when organizations have undertaken these sorts of inquiries, they have focused almost entirely on why the compliance program failed. The presumption behind that inquiry, however, fails to prompt decision-makers within firms to look beyond the surface cause or causes of the identified corporate misconduct.

This Article suggests a new method of evaluating compliance failures by asking at what stage in the compliance process did the failure or failures occur. Reframing the inquiry when compliance failures occur from a generalized discussion about a firm’s compliance program to a more specific discussion that references particular stages within the compliance process may assist in creating, implementing, and modifying compliance programs in a more effective manner.⁸¹ This Part discusses

78. *Process*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/process> [<https://perma.cc/ZZ3R-T75D>] (last updated Sept. 20, 2018).

79. See Deloitte, *How Chief Compliance Officers Can Make an Immediate Impact*, WALL ST. J.: RISK & COMPLIANCE J. (May 15, 2017, 12:01 AM), <http://deloitte.wsj.com/riskandcompliance/2017/05/15/how-chief-compliance-officers-can-make-an-immediate-impact-2> [<https://perma.cc/PV39-RP26>].

80. Jill Treanor, *JP Morgan Chase Hires 3,000 New Staff in Its Compliance Department*, GUARDIAN (Sept. 17, 2013, 4:36 PM), <https://www.theguardian.com/business/2013/sep/17/jpmorgan-banking> [<https://perma.cc/Z3JC-MBQ8>].

81. For example, in 2007 the chief executive officer of BP stated: “Our operations failed to meet our own standards and the requirements of the law.” RICHARD M. STEINBERG, GOVERNANCE, RISK MANAGEMENT, AND COMPLIANCE: IT CAN’T HAPPEN TO US—AVOIDING CORPORATE DISASTER WHILE DRIVING SUCCESS 93 (2011). He pledged to improve the company’s risk management processes. This was a relatively general statement that led to a broad inquiry that did not have effective results. “Federal officials and industry experts say BP continued to lag other oil companies on safety.” *Id.* Similarly, governmental actors often set up relatively broad inquiries when drafting requirements for firms that enter into settlement agreements, which routinely focus on activities that would fall under the categories of prevention and detection with no mention of a need to establish policies related to investigation or remediation. See, e.g., Deferred Prosecution Agreement at C-1–C-8, United States v. Keppel Offshore & Marine Ltd., No. 17-CR-697 (KAM) (E.D.N.Y. Dec. 22, 2017), <https://www.justice.gov/criminal-fraud/file/1021786/download> [<https://perma.cc/7DSC>].

each stage undertaken within the compliance process—prevention, detection, investigation, and remediation—in turn.⁸²

Before turning to these stages, however, it is important to remember that misconduct within organizations occurs in a variety of ways and in many different contexts. And some contexts suggest that the organization has no desire to adopt policies or programs that are compliant with legal and regulatory requirements. There are many examples of significant organizational misconduct where this Article's framework will not be of significant use because the organization is not committed or interested in improving its compliance program.⁸³ As such, this Article's framework will be most helpful for (i) organizations that are committed to ferreting out compliance failures and (ii) regulators or prosecutors engaged in robust investigations of corporate misconduct.

Additionally, in many instances the compliance process is effectively and routinely performed in its entirety by one person, department, or external consultant. This Article is not suggesting that compliance officers should start evaluating each and every decision as a stage in a compliance process. For relatively simple compliance failures, it may not be necessary for the firm to pay careful attention to what compliance stage it is in. When, however, the compliance failure is more significant, it becomes more important that the compliance stage is carefully considered when engaging in compliance activities.

A. Prevention

The stage of prevention involves actions undertaken to prevent compliance failures from occurring within a firm. In some instances, that prevention happens by refusing to endorse certain information—like when an auditor refuses to certify certain financial statements because they fail to meet regulatory or industry standards.⁸⁴ In other instances, prevention involves setting up systems and policies that will stop conduct from occurring within the firm that would violate legal mandates.⁸⁵

-B88N] (outlining the need to adopt new policies, new training procedures, and new methods for detecting and monitoring misconduct within the firm).

82. In previous work, I briefly flagged the concept that there are multiple stages in the compliance effort. See Veronica Root, *Modern-Day Monitorships*, 33 YALE J. ON REG. 109, 157 (2016). In that work, I framed the inquiry slightly differently than I do here because I combined prevention and detection into one stage. Further time and contemplation have convinced me that prevention and detection are distinct stages within compliance efforts.

83. For example, Volkswagen's purposeful use of an emissions-compliance "defeat device," as well as a variety of other examples of corporate misconduct would have occurred regardless of whether this Article's process frame was utilized by the organization because the commitment to corrupt activities was stronger than a commitment to compliance. See Russell Hotten, *Volkswagen: The Scandal Explained*, BBC NEWS (Dec. 10, 2015), <http://www.bbc.com/news/business-34324772> [<https://perma.cc/3GEU-AKCW>].

84. See John C. Coffee, Jr., *Gatekeeper Failure and Reform: The Challenge of Fashioning Relevant Reforms*, 84 B.U. L. REV. 301, 308 (2004).

85. See, e.g., Root, *supra* note 35, at 1013–16 (discussing enforcement actions that required firms to set up systems reasonably designed to prevent certain types of misconduct within a firm).

To clarify, prevention does not mean perfection, as it is commonly accepted by scholars, regulators, and industry officials that “perfect” compliance is not the ultimate goal of the compliance program.⁸⁶ Instead, what is expected is that firms take reasonable efforts to create systems and policies that will prevent the types of risks that the firm might reasonably be contemplated to confront. It is certainly true that all compliance failures have some element of a “prevention” failure, because if a compliance failure occurred within a firm, it was not prevented. For purposes of this Section, however, the prevention stage is concerned with instances of corporate misconduct where the primary compliance failure appears to have been one of prevention. In other words, the firm failed to appropriately conceive of its responsibilities associated with prevention and as a result, wrongdoing occurred.

For example, the Enron scandal appears, at core, to be a failure of prevention. Enron Corporation (“Enron”) “was almost universally considered one of the country’s most innovative companies” in the late 1990s.⁸⁷ Enron bought and sold “gas and electricity futures,” but it also “created whole new markets for such oddball ‘commodities’ as broadcast time for advertisers, weather futures, and Internet bandwidth.”⁸⁸ At its most successful, Enron was worth approximately \$70 billion, but the value of the firm diminished significantly when it admitted to misstating its income and “that its equity value was a couple of billion dollars less than its balance sheet said.”⁸⁹ The prevention failure was twofold. First, the external actor meant to withhold its certification or approval of certain activities—Arthur Andersen LLP—failed to do so.⁹⁰ Arthur Andersen’s failure resulted in Enron engaging in accounting practices that improperly misstated the true value of the firm and ultimately led to Enron’s total collapse. Second, Enron’s board of directors approved a series of transactions fraught with serious, atypical conflicts of interest, which enriched Enron officials, including its chief financial officer.⁹¹ The results of Enron’s misconduct were devastating and vast, but at its core, the compliance failure was one of a lack of prevention.

The importance of preventing misconduct within firms is not a new phenomenon. Indeed, one of the seminal cases on fiduciary duties and arguably one of the founding cases in modern compliance law—*Caremark*—began with a prevention failure.⁹² In *Caremark*, the board of directors explicitly sought the guidance of lawyers and accountants regarding the propriety of making certain payments to physicians, but it was given poor advice from both sets of gatekeepers, which resulted in the

86. See *supra* Section I.C.

87. *The Fall of Enron*, NPR, <http://www.npr.org/news/specials/enron> [<https://perma.cc/N9D7-BZSP>].

88. *Id.*

89. *Id.*

90. See WILLIAM C. POWERS, JR., RAYMOND S. TROUBH & HERBERT S. WINOKUR, JR., REPORT OF INVESTIGATION BY THE SPECIAL INVESTIGATIVE COMMITTEE OF THE BOARD OF DIRECTORS OF ENRON CORP. 1–17 (2002).

91. See *id.* at 8–9.

92. *In re Caremark Int’l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996). In *Caremark*, the Delaware Chancery Court outlined the obligation that board of directors and other corporate managers have “under the duty of care to maintain adequate internal controls and compliance programs.” Chaffee, *supra* note 32, at 430.

company's indictment as well as other significant sanctions levied by the Department of Health & Human Services and DOJ.⁹³

Thus, the idea that compliance officials are responsible for preventing misconduct within their respective organizations is not at all new. Yet when organizations are given an admonition to construct or fix their internal compliance programs, the importance of considering the particular stage of prevention might get lost within broader discussions about the more general compliance program. By honing in on the various stages within the compliance process, officials charged with assessing compliance failures may be more likely to assess prevention activities in a more direct and complete manner.

B. Detection

The stage of detection involves an organization's policies aimed at detecting misconduct, risks, or errors within its ranks. Detection is particularly complex because the organization must detect when an agent acts outside the parameters of internal policies set up as part of the company's preventive efforts,⁹⁴ but it must also detect potential risks that might result in harm to third parties or itself.⁹⁵

For example, the primary cause of the General Motors ignition switch scandal appears to have been a detection failure. General Motors is a global automotive company headquartered in Detroit, Michigan.⁹⁶ It currently has over 180,000 employees on five continents and is a storied American corporation.⁹⁷ In 2014, news of a potentially deadly defect in the functioning of ignition switches of certain General Motors's vehicles came to light.⁹⁸ An investigation ensued, which determined that while engineers had identified problems with the ignition switch as early as 2002, the full scope of the defect was not detected. Indeed:

[S]ophisticated engineers with responsibility to provide customers with safe and reliable automobiles – did not understand one of the most fundamental consequences of the switch failing and the car stalling: the airbags would not deploy. The failure of the switch meant that drivers were without airbag protection at the time they needed it most. This failure, combined with others . . . led to devastating consequences.⁹⁹

93. *Caremark*, 698 A.2d at 960–62.

94. For example, the Bank Secrecy Act requires firms to implement specific policies aimed at stopping money-laundering activity. See 31 U.S.C. § 5318(h) (2012) (explaining that the purpose of the statute is to “guard against money laundering”).

95. See MODEL RULES OF PROF'L CONDUCT r. 8.4(c) (AM. BAR ASS'N 2016).

96. *About*, GEN. MOTORS, <https://www.gm.com/company/about-gm.html> [<https://perma.cc/K54B-2YBT>].

97. *Id.*

98. Peter Valdes-Dapena & Tal Yellin, *GM: Steps to a Recall Nightmare*, CNN MONEY, <http://money.cnn.com/infographic/pf/autos/gm-recall-timeline/index.html> [<https://perma.cc/U4T3-MGZV>].

99. ANTON R. VALUKAS, REPORT TO BOARD OF DIRECTORS OF GENERAL MOTORS COMPANY REGARDING IGNITION SWITCH RECALLS 1 (2014).

As a result of the failure to understand the full ramifications of the defect, General Motors improperly classified the ignition switch defect as one of “customer convenience” instead of as a “safety” issue.¹⁰⁰ This misclassification resulted in the belief that fixing the ignition switch defect was a low-priority concern, which resulted in General Motors’s failure to comply with regulatory requirements, as well as related industry practice, regarding the recall of unsafe automobile components.¹⁰¹ Additionally, subsequent committees charged with considering the implementation of a fix for the ignition switch also failed to reclassify the problem as a safety issue.¹⁰² Indeed, a group “charged with identifying and remedying safety issues, made the same mistake; it opened and closed an investigation in 2005 in the span of a month, finding no safety issue to be remedied.”¹⁰³ Yet in 2007, both a Wisconsin Safety Patrol trooper and an Indiana University research team correctly detected the connection between the faulty ignition switch and the nondeployment of airbags.¹⁰⁴ Finally, a group of internal lawyers at General Motors who were charged with using settlement data to generate settlement forecasts and detect trends indicating safety issues abdicated this responsibility.¹⁰⁵

Like prevention, the importance of detecting potential misconduct, risks, or errors is well-settled within corporate law jurisprudence. For example, in *Stone v. Ritter*,¹⁰⁶ the bank adopted an anti-money laundering program, but the U.S. Department of the Treasury, Financial Crimes Enforcement Network determined that the program was deficient because the bank had “a fragmented program in which areas of the Bank had information on suspicious activity that was never communicated to those responsible for Bank Secrecy Act compliance.”¹⁰⁷ As such, while the bank formally detected the potential misconduct, it failed to structure the program in a manner that allowed the people responsible for evaluating the behavior to detect it.

Again, the idea that compliance officials are responsible for detecting compliance failures within their respective organizations is not novel. Indeed, the Organizational Guidelines specifically instruct organizations on the importance of detecting misconduct within their ranks.¹⁰⁸ But it is not clear that organizations make a concerted effort to specifically evaluate the role a detection failure may have contributed to the general failure within its compliance program.

100. *Id.* at 2–3.

101. *See id.* at 3–5; *see also* Bill Vlasic & Hilary Stout, *Auto Industry Galvanized After Record Recall Year*, N.Y. TIMES (Dec. 30, 2014), <https://www.nytimes.com/2014/12/31/business/a-year-of-record-recalls-galvanizes-auto-industry-into-action.html> [<https://perma.cc/4L8B-GQTZ>] (discussing how the General Motors scandal has impacted industry standards regarding vehicle recalls).

102. VALUKAS, *supra* note 99, at 2–5.

103. *Id.* at 3.

104. *Id.*

105. *See id.* at 107–15.

106. No. Civ.A. 1570-N, 2006 WL 302558, at *2 (Del. Ch. Jan. 26, 2006) (“This case is not about a board’s failure to carefully consider a material corporate decision that was presented to the board. This is a case where information was not reaching the board because of ineffective internal controls.”).

107. *Id.* at *1.

108. *See* U.S. SENTENCING GUIDELINES MANUAL § 8B2.1 (U.S. SENTENCING COMM’N 2016).

C. Investigation

The stage of investigation involves a firm's policies and practices targeted at determining the existence of and, if relevant, scope of the compliance failure. Investigation requires discovering the facts surrounding the failure, so that decision-makers at the firm are equipped with a sufficient amount of knowledge to make informed decisions about the appropriate next steps.¹⁰⁹ The investigative stage is particularly tricky because it inevitably starts with the detection stage and often continues on after the firm has begun its remediation efforts. The importance of the investigation stage, however, cannot be overstated, and even if completed in conjunction with detection or remediation, it is its own discrete stage within compliance efforts.¹¹⁰ And failures at the investigatory stage, just as with prevention and detection, can be devastating for firms.

For example, the Wells Fargo fake account scandal appears to have been exacerbated in large part due to deliberate actions taken by bank officials to block a thorough and proper investigation of the inappropriate conduct within the firm.¹¹¹ Wells Fargo provides "diversified financial services," which include a community bank division that provides traditional banking services to consumers and small businesses.¹¹² "From 2011 to mid-2016 – but possibly going back to 2009 or before – Wells [Community Bank] employees created more than 1.5 million unauthorized deposit accounts and issued more than 500,000 unauthorized credit card applications. These accounts racked up \$2.6 million in fees for the bank."¹¹³ A subsequent investigation by the board of directors for the bank identified failures with the bank's investigative function. First, it determined that "Community Bank leadership resisted and impeded outside scrutiny or oversight and, when forced to report, minimized the scale and nature of the problem."¹¹⁴ Second, it determined that the former chief executive officer "was too slow to investigate or critically challenge sales practices in the Community Bank."¹¹⁵ In addition to these findings in the board's report, reporting indicates that Wells Fargo employees were fired after reporting to their supervisors regarding the fraudulent behavior within the Community Bank.¹¹⁶ If

109. AM. COLL. OF TRIAL LAWYERS, RECOMMENDED PRACTICES FOR COMPANIES AND THEIR COUNSEL IN CONDUCTING INTERNAL INVESTIGATIONS 2 (2008).

110. *See id.* at 22 (discussing the use of internal investigation work product to assist in remediation needs and efforts).

111. INDEPENDENT DIRECTORS OF THE BOARD OF WELLS FARGO & COMPANY, SALES PRACTICES INVESTIGATION REPORT (2017) [hereinafter WELLS FARGO REPORT].

112. *History of Wells Fargo*, WELLS FARGO, <https://www.wellsfargo.com/about/corporate/history> [<https://perma.cc/LK7R-RFAT>]; *see also* Wayne Thompson, *Wells Fargo Unveils Organizational Changes in Its Community Bank*, WELLS FARGO (Mar. 7, 2017), <https://stories.wf.com/wells-fargo-unveils-organizational-changes-community-bank> [<https://perma.cc/ZCX8-K2WC>].

113. *The Wells Fargo Fake Account Scandal: A Timeline*, FORBES, <https://www.forbes.com/pictures/ejhj45fjj/two-million-phony-account/#4f1d8e7a6f24> [<https://perma.cc/8JSY-TSYE>].

114. WELLS FARGO REPORT, *supra* note 111, at Overview.

115. *Id.*

116. *See* Stacy Cowley, *Wells Fargo Whistle-Blower Wins \$5.4 Million and His Job Back*, N.Y. TIMES (Apr. 3, 2017), <https://www.nytimes.com/2017/04/03/business/04-wells-fargo>

Wells Fargo had acted on the misconduct that was detected within its ranks and properly investigated the allegations, it could have, at a minimum, stopped the misconduct at an earlier date. Instead, officials at the firm disregarded the information they received and failed to trigger the investigative stage within the compliance process.

Again, like prevention and detection, the importance of utilizing appropriate investigative methods when confronting potential firm misconduct is commonly accepted. For example, in *Auerbach v. Bennett*,¹¹⁷ the court evaluated whether a board engaged in an appropriate investigation of misconduct within a corporation. The court explained that “[a]s to the methodologies and procedures best suited to the conduct of an investigation of facts and the determination of legal liability, the courts are well equipped by long and continuing experience and practice to make determinations.”¹¹⁸ It ultimately determined that the board’s actions were proper and noted that “[t]he selection of appropriate investigative methods must always turn on the nature and characteristics of the particular subject being investigated.”¹¹⁹

The importance of a robust investigation in the face of a compliance failure has long been an important component of organizational compliance efforts. There are numerous documents outlining the best industry practices for conducting internal investigations.¹²⁰ The idea, however, that the investigation itself might fail or be deficient in some manner is not typically considered. The assumption is that the investigation will present a solution, not serve as the impetus of the compliance failure. Yet by purposefully considering whether the investigation itself contributed to the compliance challenges faced by the organization, compliance officials may develop a better understanding regarding the root cause of the compliance failures facing their organizations.

D. Remediation

The stage of remediation involves a firm’s strategies for responding to and recovering from the misconduct uncovered at the detection and investigation stages.

-whistleblower-fired-osha.html [https://perma.cc/9E6G-JGA6]. *But see* WELLS FARGO REPORT, *supra* note 111, at 87–88 n.26 (indicating that the board and counsel were still reviewing allegations of retaliation against potential whistleblowers).

117. 393 N.E.2d 994 (N.Y. 1979).

118. *Id.* at 1002.

119. *Id.* at 1003.

120. *See, e.g.*, Daniel P. Elms, *Documents from Internal Investigation Protected by Privilege*, ABA: LITIG. NEWS (Dec. 30, 2015), <https://www.americanbar.org/groups/litigation/publications/litigation-news/top-stories/2015/documents-from-internal-investigation-protected-by-privilege.html> [https://perma.cc/LXW2-5E7M]; Barry F. McNeil & Brad D. Brian, *Overview: Initialing an Internal Investigation and Assembling the Investigative Team*, in INTERNAL CORPORATE INVESTIGATIONS (Brad D. Brian, Barry F. McNeil & Lisa J. Demsky eds., 4th ed. 2017), https://www.americanbar.org/content/dam/aba/administrative/litigation/materials/2017_sac/written_materials/1_chapter_1_overview_initialing_an_internal_investigation.authcheckdam.pdf [https://perma.cc/MVZ7-NGKZ]; Sidley Austin, *Conducting Internal Investigations: A Primer*, ABA (2015), https://www.americanbar.org/content/dam/aba/administrative/litigation/materials/2015_corporate_counselcseminar/Materials/3b1_12_conducting_internal_investigations.authcheckdam.pdf [https://perma.cc/XPH2-UCHW].

The remediation stage provides firms an opportunity to expressly confront the misconduct that occurred in a manner targeted at addressing the compliance failure completely and thoroughly. In some instances a remediation effort may involve compensating victims for a harm caused as part of a mandate from a government regulator,¹²¹ and in other instances it may require developing a robust set of policies and procedures targeted to prevent similar misconduct in the future in an effort to comply with the Organizational Guidelines.¹²² Regardless of the particular tasks that are required for the remediation effort, it is an important last step in a firm's effort to address misconduct in its ranks.

For example, Credit Suisse Securities (USA) LLC ("Credit Suisse") failed to address deficiencies in its anti-money laundering compliance program and, as a result, was fined \$16.5 million by the Financial Industry Regulatory Authority (FINRA) in December 2016.¹²³ While a number of factors ultimately led to the fine, one of the concerns was Credit Suisse's failure to properly remediate misconduct. Specifically, the Accept, Waiver, and Consent settlement between Credit Suisse and FINRA explained that in December 2013, a "consulting firm issued a detailed report identifying numerous inadequacies in the firm's implementation" of an anti-money laundering automated system.¹²⁴ Credit Suisse "developed a plan to fully remediate the issues identified by the consultant, and in 2015 retained additional consultants to help improve the system, [but] it initially failed to devote adequate resources and funding to resolve the issues identified by the consulting firm[s] in an adequately timely fashion."¹²⁵

The importance of remediation efforts, like prevention, detection, and investigation, continues to be emphasized by enforcement authorities. For example, in 2016, then DOJ Fraud Section Chief Andrew Weissmann commented that "companies are not focused enough on the remediation that should follow findings

121. For example, one component of the Independent Foreclosure Review was that banks were required to "remediate all financial injury to borrowers caused by any errors, misrepresentations, or other deficiencies." Press Release, Office of the Comptroller of the Currency, U.S. Dep't of the Treasury, OCC Takes Enforcement Action Against Eight Servicers for Unsafe and Unsound Foreclosure Practices (Apr. 13, 2011), <http://www.occ.treas.gov/news-issuances/news-releases/2011/nr-occ-2011-47.html> [<https://perma.cc/VNT4-DUMC>].

122. Root, *supra* note 82, at 128 (discussing corporate compliance monitorships, which require a remediation effort that "involves an overhaul of the organization's corporate compliance program with respect to the area of misconduct").

123. Press Release, Fin. Indus. Regulatory Auth., FINRA Fines Credit Suisse Securities (USA) LLC \$16.5 Million for Significant Deficiencies in Its Anti-Money Laundering Program (Dec. 5, 2016), <http://www.finra.org/newsroom/2016/finra-fines-credit-suisse-165-million-significant-deficiencies-its-aml-program> [<https://perma.cc/SY68-JAPW>]; see also *FINRA Fines Firm for Deficient AML Monitoring—Are Your Policies Up to Par?*, VENABLE LLP (Dec. 12, 2016), <https://www.venable.com/finra-fines-firm-for-deficient-aml-monitoring-are-your-policies-up-to-par-12-12-2016> [<https://perma.cc/53JA-4LCY>].

124. Letter from Jeffrey P. Bloom, Senior Special Counsel, Fin. Indus. Regulatory Auth., to Dep't of Enforcement, Fin. Indus. Regulatory Auth. 6 (Dec. 5, 2016), https://www.finra.org/sites/default/files/CreditSuisse_AWC_120516.pdf [<https://perma.cc/UJX7-S2HN>] [hereinafter Credit Suisse AWC].

125. *Id.*

of misconduct.¹²⁶ Indeed, he stressed that based on the comparative falloff in attention given to matters of remediation, he expects for the government to use formal tools to encourage more systematic regulation like the use of corporate monitors—independent, private outsiders—to oversee remediation efforts within firms.¹²⁷

A failure of a remediation effort is particularly susceptible to being overlooked as a root cause of an organization's compliance failures. A firm cannot have a remediation effort unless there was a failure at one of the three preceding stages within compliance efforts. As such, it may be easy for organizations to focus their attention on issues of prevention, detection, and investigation at the expense of a robust analysis regarding the organization's efforts to remediate misconduct. Yet examples like Credit Suisse and Fox News demonstrate the importance of evaluating the relative success or failure of an organization's remediation effort when attempting to ascertain the full scope and breadth of a compliance failure within the organization.

* * * *

Thus, the effective compliance program may be broken up into the four distinct stages of prevention, detection, investigation, and remediation.

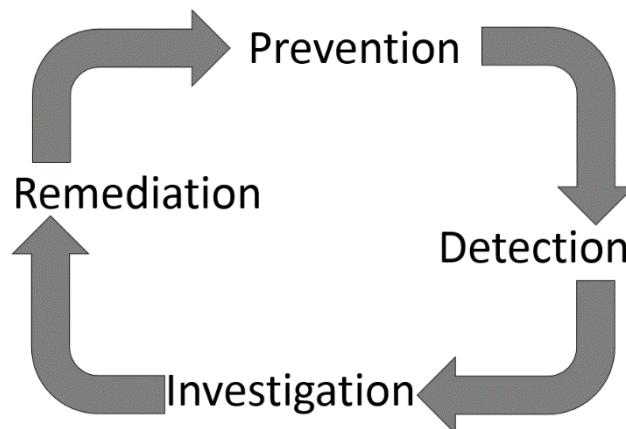


Figure 1: Stages of the Compliance Process

This Article is not arguing that these stages are always completed at a separate point of time. A competent compliance officer may engage in the detection and investigative processes at the same time and then go on to institute a remediation process that bleeds into the creation of prevention policies. This Article also is not arguing that misconduct typically only occurs within one stage or, as evidenced by the Fox News example, a compliance failure might encompass deficiencies within

126. *2016 Year-End FCPA Update*, GIBSON DUNN (Jan. 3, 2017), <https://www.gibsondunn.com/2016-year-end-fcpa-update> [<https://perma.cc/V6PR-PE34>].

127. *Id.*

all four stages of the compliance process. This Article argues that these are distinct tasks, and when these stages are considered discretely and independently, the root cause of compliance failures may be easier to identify and rectify.

Thus, the upshot of this Article is that there is a class of compliance failures where utilizing the evaluative framework proposed above may be helpful in identifying the root cause of the failure and developing a plan for the future that will avoid similar misconduct. For firms engaged in a rather intense struggle to implement an effective compliance program in the midst of multiple compliance deficiencies, it may be helpful to conceive of the compliance challenge as having multiple, discrete components.

III. REFRAMING THROUGH THE COMPLIANCE PROCESS

As demonstrated above, scholars, regulators, and industry leaders have long considered strategies for addressing compliance failures. In doing so, they have mentioned the importance of certain aspects within the compliance process like prevention and remediation. They have not, however, suggested using these aspects as a method of framing the analytical assessment of compliance failures in a more systematic way. This Article—relying on insights from cognitive psychology, behavioral economics, and behavioral ethics—argues that changing the frame by which compliance failures are assessed may help to better determine the root cause of the breakdown within an organization’s compliance system.¹²⁸

Framing, as explained by cognitive psychologists and applied to decision-making models by scholars within the field of behavioral economics, can drastically change the manner in which people process information.¹²⁹ This change can occur because “choices depend, in part, on the way in which problems are stated.”¹³⁰ Thus, by restating the problem from “how or why did this compliance failure occur” to “at what stages within the compliance process did breakdowns occur,” those responsible for analyzing compliance failures within organizations might focus their inquiries in a more precise way.

Root-cause analysis is a tool often employed by business professionals to determine why certain actions or phenomenon occurred within an organization or industry.¹³¹ In particular, root-cause analysis is meant to:

128. Business and legal scholars have previously identified the benefits of utilizing insights from cognitive psychology, behavioral economics, or behavioral ethics to assess compliance challenges. See, e.g., Todd Haugh, *The Ethics of Intracorporate Behavioral Ethics*, 8 CALIF. L. REV. ONLINE 1 (2017); Langevoort, *supra* note 34, at 936, 946, 950.

129. See RICHARD H. THALER & CASS R. SUNSTEIN, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* 39–40 (Penguin Books 2009). Richard H. Thaler has been awarded the 2017 Nobel Prize in Economics for his work in the field of behavioral economics, including the insights provided in *Nudge*. Frank Armstrong III, *Richard Thaler, A Giant in Economics, Awarded the Nobel Prize*, FORBES (Oct. 13, 2017, 12:04 PM), <https://www.forbes.com/sites/frankarmstrong/2017/10/13/richard-thaler-a-giant-in-economics-awarded-the-nobel-prize/#280b50933a10> [<https://perma.cc/D6VH-G3VJ>].

130. THALER & SUNSTEIN, *supra* note 129, at 40.

131. Root-cause analysis is distinct from Enterprise Risk Management. Enterprise Risk Management is “a process, effected by an entity’s board of directors, management and other

[A]nswer the following questions: (1) What happened? (What, exactly, was the ultimate outcome?); (2) Why did it happen? (What causal factors contributed to the outcome?); and (3) What can you do to prevent it from happening again? (What system changes can be put in place to anticipate and intervene in the errors that inevitably occur in human activities?).¹³²

Properly ascertaining the root cause of a compliance failure is important for those charged with creating, implementing, maintaining, and enforcing compliance norms and mandates. If the root cause of a compliance failure is mis- or only partially-identified, the ability to prevent similar failures in the future is severely limited.

This Part demonstrates how reframing the assessment of compliance failures through the four stages of compliance outlined in Part II—prevention, detection, investigation, and remediation—might assist industry leaders and policymakers in evaluating and identifying the root cause of certain compliance failures. To demonstrate the potential of utilizing the proposed process frame, this Part discusses four compliance efforts that were plagued by significant missteps. When these compliance activities are assessed under a process frame, new considerations are revealed.

The first example comes from the Apple monitorship and suggests that part of what caused the difficult remediation effort was confusion regarding the proper role of the monitor and the appropriate scope of duties. The second example comes from a bank's engagement of the Promontory Financial Group, LLC ("Promontory") to assist it with a series of compliance failures, which resulted in a failure to apprehend when Promontory's role with the company converted in a manner that required more independence. The third example demonstrates how the Office of the Comptroller of the Currency (OCC) misunderstood the expansive nature of its own consent order's demands, which wasted millions of dollars and stalled remediation payments to homeowners. And the fourth example demonstrates how Baylor University lacked a true commitment to compliance with regulatory guidance, despite its statements to the contrary.

A. Example 1: Role Confusion

In 2013, a district court judge, in a civil action brought by DOJ Antitrust, found Apple to have engaged in improper collusive activity in the sale of e-books.¹³³ The

personnel, applied in strategy-setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives." Office of the President, Univ. of Cal., *What is ERM?*, U.C., <http://www.ucop.edu/enterprise-risk-management/procedures/what-is-erm.html> [<https://perma.cc/V32K-XMYR>]. Enterprise Risk Management is made up of four primary objectives, which have eight additional interrelated components. *Id.* The goal of Enterprise Risk Management is to understand what sort of future risks an organization may encounter. *Id.* Root-cause analysis is an attempt to understand why an event occurred. Root-cause analysis could be used to assist in efforts to develop an Enterprise Risk Management process, but the two efforts are distinct.

132. Charles M. Key, *Toward a Safer Health System: Medical Injury Compensation and Medical Quality*, 37 U. MEM. L. REV. 459, 464 (2007).

133. Nate Raymond, *Apple Cannot Escape U.S. States' E-Book Antitrust Cases: Judge,*

court appointed a monitor to oversee Apple's remediation efforts with respect to its antitrust compliance program.¹³⁴ The Apple monitorship was, however, plagued with a variety of problems, which have been attributed to potential cronyism in the monitorship appointment,¹³⁵ a lack of appropriate limitations regarding the appointment of monitors,¹³⁶ and my own suggestion that the evolution and prevalence of modern-day monitors had muddied the understandings of the appropriate limitations for court-appointed monitors.¹³⁷ There does, however, appear to be another account that reveals itself when one considers the difficulties surrounding the Apple monitorship utilizing a compliance process frame: instead of taking on the role of overseeing the remediation of Apple's antitrust compliance program, the monitor attempted to take on a broader preventative task that included undertaking activities unrelated to Apple's antitrust program.

1. Difficulties with the Apple Monitorship

The district court's order requiring Apple to submit to a monitorship stated that the monitor was to "review and evaluate Apple's existing internal antitrust compliance policies and procedures" and "to recommend to Apple changes to address any perceived deficiencies in those policies, procedures, and training."¹³⁸ Apple was not pleased about the imposition of the monitor but upon reviewing the district court's order did not initially file objections. This changed, however, when the monitor began to engage in activities broader than what Apple originally contemplated as appropriate under the court order.¹³⁹ For example, the monitor sought to interview "Apple's entire executive team and its entire board of directors," even though many of these individuals had not been involved in antitrust matters.¹⁴⁰ The district court did not attempt to restrain the monitor's behavior and instead seemed to approve of the monitor's view that he needed to "crawl inside the company," so as to ascertain Apple's tone and culture at a very broad level.¹⁴¹

REUTERS (Apr. 15, 2014, 5:35 PM), <http://www.reuters.com/article/us-apple-ebooks/apple-cannot-escape-u-s-states-e-book-antitrust-cases-judge-idUSBREA3E1Y520140415> [<https://perma.cc/KXW4-KLYB>].

134. For a more detailed account of the Apple monitorship, see Root, *supra* note 82.

135. See John Dean, *Michael Bromwich's Apple Monitoring Continues: Chapter Two*, VERDICT (Feb. 21, 2014), <https://verdict.justia.com/2014/02/21/michael-bromwichs-apple-monitoring-continues-chapter-two> [<https://perma.cc/PS3N-67WW>].

136. See Roger Parloff, *Rocky Term of Apple's Ebooks Antitrust Monitor Will Expire Friday*, FORTUNE (Oct. 13, 2015), <http://fortune.com/2015/10/13/apple-antitrust-monitor-term-expiring> [<https://perma.cc/B5DX-AQQH>] (noting a dissenting opinion from a Second Circuit ruling that determined that "the manner in which Judge Cote had structured Bromwich's appointment . . . 'warp[ed] the role of a neutral, court-appointed referee into that of an adversary party'").

137. See Root, *supra* note 82, at 132–38.

138. *United States v. Apple, Inc.*, Nos. 1:12-CV-2826, 1:12-CV-3394, 2013 WL 4774755, at *6 (S.D.N.Y. Sept. 5, 2013).

139. Root, *supra* note 82, at 134.

140. *Id.*

141. *Id.* at 135 (alteration omitted).

Eventually the Second Circuit reigned in the scope of the monitorship, but the damage was done.¹⁴²

As a result of the dispute regarding the appropriate scope of the monitor's duties, a variety of consequences occurred. The monitorship and the district court were highly criticized.¹⁴³ The relationship between the monitor and Apple became contentious and plagued with various rounds of litigation.¹⁴⁴ Ultimately, the Second Circuit went so far as to criticize the monitor's actions in a written opinion.¹⁴⁵ As such, a rather typical, at least at the outset, remediation effort ended up being far from successful on a number of objective measures.

2. The Apple Monitorship Under the Compliance Process Frame

It is relatively simple—and correct—to look at the Apple monitorship and classify it as a remediation effort gone wrong. But the goal of the process frame is to utilize the stages to determine the root cause of why it went wrong. Determining the root cause requires an inquiry into the actions of the monitor, judge, government, and Apple to determine why the remediation effort was plagued by so many challenges.

The facts demonstrate that the initial moment of tension between the monitor and Apple occurred when the monitor attempted to interview Apple's entire executive team and board of directors, which included individuals who had no responsibility or interaction with antitrust policies or procedures.¹⁴⁶ This initial dispute turned into a much larger battle regarding the appropriate scope of the monitor's authority, with the monitor, government, and court taking a rather broad interpretation of the monitor's authority and Apple insisting that the monitor was overstepping.¹⁴⁷

The activities the monitor engaged in that Apple complained about, however, did look unusual for a typical remediation effort. As explained in Part II:

The stage of remediation involves a firm's strategies for responding to and recovering from the misconduct uncovered at the detection and investigation stages. The remediation stage provides firms an opportunity to expressly confront the misconduct that occurred in a manner targeted at addressing the compliance failure completely and thoroughly.¹⁴⁸

142. *Id.* at 136–37.

143. *Apple's Star Chamber: An Abusive Judge and Her Prosecutor Friend Besiege the Tech Maker*, WALL ST. J. (Dec. 5, 2013, 7:09 PM), <https://www.wsj.com/articles/apple8217s-star-chamber-1386288543?tesla=y> [<https://perma.cc/7AT5-FXNJ>].

144. Nate Raymond, *U.S. Judge Says Apple E-Books Antitrust Monitor's Term to End*, REUTERS (Oct. 13, 2015, 7:07 AM), <http://www.reuters.com/article/us-apple-ebooks-monitor/u-s-judge-says-apple-e-books-antitrust-monitors-term-to-end-idUSKCN0S719G20151013> [<https://perma.cc/A9AU-7ZV9>].

145. Jeff John Roberts, *Appeals Court Scolds Apple Monitor, but Does Not Remove Him*, FORTUNE (May 28, 2015), <http://fortune.com/2015/05/28/appeals-court-scolds-apple-monitor-but-does-not-remove-him> [<https://perma.cc/385P-4ABY>].

146. *See supra* Section III.A.1.

147. *See supra* Section III.A.1.

148. *See supra* Section II.D.

The Apple monitor, however, went beyond activity that was tied to remedying Apple's antitrust misconduct and sought to address a much broader scope of conduct. Indeed, careful reflection suggests the monitor attempted to take on more of a prevention role. Instead of directly tying his activities to addressing the antitrust misconduct at Apple, the monitor engaged in activities that looked similar to what one might do if he or she were creating a compliance program from scratch. But the original court order had not contemplated the creation of a compliance program; it required modifications to the existing program—a much narrower task.

This leads one to wonder why the monitor, with support from the district court judge and government attorneys, engaged in activities that were broader than what would be found in a typical remediation effort. In part, this might have been a result of what behavioral economics terms cognitive conservatism. “Once an impression is gained, it is insufficiently revised to reflect new information. There is a bias to the status quo. Especially in noisy information environments where observers have little time to think reflectively, the strong inclination is to construe data as normal rather than abnormal.”¹⁴⁹ Once the monitor interpreted his role broadly, his view may have become entrenched despite the protestations of Apple. Indeed, Apple's protests created a particularly “noisy” environment that resulted in multiple appeals to the Second Circuit and significant, critical news reports toward the monitor and district court. Thus, Apple's objections may have inadvertently served to entrench further the view of the monitor, court, and government about the appropriateness of the monitor's actions, allowing the tendency of cognitive conservatism to take hold.

Therefore, the breakdowns associated with the Apple monitorship might properly be characterized as, at least in part, being caused by the monitor, court, and government's failure to consider whether the monitor's initial impression regarding his scope of authority was correct. Instead of reflecting on the appropriate boundaries and norms that should restrain a compliance actor engaged in a remediation effort, the monitor's initial impression became the status quo view. The confusion is understandable in that remediation efforts may often bleed into prevention efforts, but the failure to recognize that they are discrete and distinct stages may have contributed to the conflicts between the parties in this case.

If, however, Apple had framed its objections utilizing the process frame outlined in this Article or if the monitor, court, or government had been mindful that the monitorship was meant to be part of a remediation effort, the conflicts created by the monitor's more expansive view of the appropriate boundaries for the monitorship may have been more apparent. Instead of viewing Apple's objections as the protests of a recalcitrant bad actor, they may have been viewed as legitimate concerns regarding the appropriate scope of authority for an individual engaged in a remediation, as opposed to a prevention, effort. And instead of viewing his role expansively, the monitor may have been more likely to restrict his actions to those appropriate for a narrowly tailored remediation effort.

149. Donald C. Langevoort, *Monitoring: The Behavioral Economics of Corporate Compliance with Law*, 2002 COLUM. BUS. L. REV. 71, 87–88 (2002).

B. Example 2: Unidentified Role Conversion

Promontory is “a leading strategy, risk management, and regulatory-compliance consulting firm focusing on the financial services industry.”¹⁵⁰ It “help[s] entities understand and implement global and national financial services regulation.”¹⁵¹ Ironically, Promontory, a firm charged with assisting firms facing compliance challenges, experienced its own compliance failure that resulted in significant sanctions, including a \$15 million penalty.¹⁵² As described by the New York State Department of Financial Services, Promontory exercised “a lack of independent judgment in the preparation and submission of certain reports.”¹⁵³ When one considers Promontory’s conduct under a compliance process frame, however, it looks as if the failure was more complicated. The root cause of Promontory’s lack of independent judgment appears related to its failure to identify a need to change the parameters of its relationship when it went from assisting a bank with detection efforts to assisting the bank and the regulator with a related investigation.

1. Promontory’s Misconduct

In 2009, Standard Chartered, a bank, hired Promontory to serve in what appeared to be a role meant to assist the bank in detecting certain types of misconduct.¹⁵⁴ Specifically, “Promontory contracted with the Bank’s counsel to provide ‘consulting services in connection with the identification and collection of historical transaction records relating to cross-border financial transactions.’”¹⁵⁵ After Promontory completed its review, Standard Chartered “reported to various regulators, including the New York [Department of Financial Services] . . . that it had engaged in conduct related to the evasion of U.S. sanctions.”¹⁵⁶ It appears, therefore, that Promontory properly assisted the bank in detecting instances of misconduct and the bank then, again properly, reported the detected misconduct to the appropriate regulator.

In April 2010, Standard Chartered again engaged Promontory “to identify, collect and review historical transaction records ‘with certain countries or certain Specially Designated Nationals (“SDNs”) subject to sanctions’ administered by” the Office of Foreign Assets Control of the U.S. Department of the Treasury.¹⁵⁷ “As part of the engagement, Promontory produced a number of reports and made various presentations to the Bank and government authorities These reports included

150. *About Promontory*, PROMONTORY, <http://www.promontory.com/OurFirm.aspx> [<https://perma.cc/3VD7-F55R>].

151. *Id.*

152. Ben Protes & Jessica Silver-Greenberg, *Promontory Financial Settles with New York Regulator*, N.Y. TIMES: DEALBOOK (Aug. 18, 2015), <https://www.nytimes.com/2015/08/19/business/dealbook/promontory-financial-settles-with-new-york-regulator.html> [<https://perma.cc/58XR-9GLR>].

153. N.Y. STATE DEP’T OF FIN. SERVS., REPORT ON INVESTIGATION OF PROMONTORY FINANCIAL GROUP, LLC 1, 15 (2015) [hereinafter PROMONTORY REPORT].

154. *Id.* at 2.

155. *Id.*

156. *Id.*

157. *Id.* at 2–3.

interim reports throughout 2010, final reports in January and March of 2011, and updates to those final reports in October 2011.¹⁵⁸ This second engagement, known as “Project Green,” involved efforts to investigate the full scope of the bank’s misconduct and is where problems with Promontory’s conduct occurred.¹⁵⁹

When Promontory took on the Project Green engagement, it held itself out to be independent from Standard Chartered, and as part of the engagement, it provided formal and regular reports to the New York Department of Financial Services. The regulator, in turn, relied “upon the work conducted and presented by Promontory to identify the scope of the Bank’s improper conduct and to determine an appropriate resolution of the investigation.”¹⁶⁰ Utilizing information from Promontory’s investigation, the New York Department of Financial Services required Standard Chartered to “pay a penalty of \$340 million and to install an independent on-site monitor, for a period of two years.”¹⁶¹ The newly engaged monitor, however, uncovered additional misconduct at the bank, which (i) resulted in additional sanctions for the bank and (ii) prompted an investigation into Promontory’s actions.¹⁶²

The investigation of Promontory’s conduct revealed that it did not, in fact, maintain its independence from Standard Chartered.¹⁶³ For example, Promontory removed a portion of an interim report at the request of the bank after the bank expressed concerns that the section “referred to conduct that regulators were not yet aware of and might ‘draw questions which we’re not yet prepared to answer.’”¹⁶⁴ Additionally, Promontory changed language in its reports at the request of Standard Chartered in an effort to make the bank’s misconduct look less significant.¹⁶⁵ These facts, among others, led the New York Department of Financial Services to determine that “Promontory exhibited a lack of independent judgment in the preparation and submission of certain reports.”¹⁶⁶ Ultimately, Promontory agreed to voluntarily “abstain from certain consulting arrangements in New York for six months” and to pay a \$15 million penalty.¹⁶⁷

2. Promontory’s Activities Under the Compliance Process Frame

While it certainly seems reasonable for the New York regulator to determine that Promontory failed to exercise an appropriate level of independent judgment, that determination does not attempt to uncover the root cause of Promontory’s misconduct. When, however, Promontory’s conduct is evaluated against the process frame outlined in Part II, a possible reason for its failure becomes apparent.

158. *Id.* at 3.

159. *Id.*

160. *Id.*

161. *Id.*

162. *Id.* at 3–4.

163. *Id.* at 6–7.

164. Protess & Silver-Greenberg, *supra* note 152.

165. PROMONTORY REPORT, *supra* note 153, at 6.

166. *Id.* at 1, 15.

167. Protess & Silver-Greenberg, *supra* note 152.

When Promontory took on the 2009 engagement, it was charged with assisting Standard Chartered in its efforts to detect potential misconduct. The 2010 engagement, Project Green, while distinct, likely looked to be a very similar set of tasks. Even the descriptions of the two engagements appear quite similar. The difference, however, is that when Promontory was engaged to assist in Standard Chartered's detection efforts, Promontory reported solely to the bank, but when it shifted into an investigatory role, Promontory had a responsibility to provide information to both Standard Chartered and the New York Department of Financial Services. This shift changed Promontory's ethical obligations.

The field of behavioral ethics, in part, addresses the "predictable situational and social forces that can lead people to engage in unethical behavior."¹⁶⁸ In particular, behavioral ethics research explains that an actor may know that a particular behavior is wrong, but may be "unaware of the forces that are leading [him or her] to cross ethical boundaries (intentional unethical behavior)."¹⁶⁹ In the case of Promontory, the individuals working on Project Green most likely "knew" that it was unethical or, at the very least, a conflict of interest to take significant instruction from Standard Chartered about what to include in independent reports to the New York regulator. Yet they assented to making changes to their independent reports and thereby failed to include relevant information to the regulator. The decision to take instruction from Standard Chartered during the 2009 engagement would have been acceptable, but the shift in its role as part of the 2010 Project Green engagement changed the calculus by which Promontory employees should have evaluated their ethical duties and responsibilities. Thus, Promontory employees and management may have failed to identify the conversion of its role, which may have been a root cause of Promontory's failure to exercise appropriate independent judgment.

C. Example 3: Regulatory Design Failure

In November 2011, in response to the mortgage foreclosure crisis, the Board of Governors of the Federal Reserve System ("Federal Reserve") and the Office of the Comptroller of the Currency (OCC) began what came to be known as the Independent Foreclosure Review.¹⁷⁰ The Independent Foreclosure Review "require[ed] a review by

168. Max H. Bazerman & Francesca Gino, *Behavioral Ethics: Toward a Deeper Understanding of Moral Judgment and Dishonesty*, 8 ANN. REV. L. & SOC. SCI. 85, 91 (2012). The field of behavioral ethics is rooted in behavioral decision theory and is related to many concepts found in the field of behavioral economics. For example, behavioral economists often discuss the idea of "bounded rationality" while a behavioral ethicist focuses on "bounded ethicality." See Dolly Chugh, Max H. Bazerman & Mahzarin R. Banaji, *Bounded Ethicality as a Psychological Barrier to Recognizing Conflicts of Interest*, in CONFLICTS OF INTEREST: CHALLENGES AND SOLUTIONS IN BUSINESS, LAW, MEDICINE, AND PUBLIC POLICY 74, 75-77 (Don A. Moore et al. eds., 2005).

169. Bazerman & Gino, *supra* note 168, at 91.

170. Press Release, Office of the Comptroller of the Currency, U.S. Dep't of the Treasury, Independent Foreclosure Review Underway (Nov. 1, 2011), <https://www.occ.gov/news-issuances/news-releases/2011/nr-occ-2011-133.html> [<https://perma.cc/T6VG-36XG>] [hereinafter OCC Press Release]; Anna Cuevas, *Independent Foreclosure Review: Is It the Real Deal?*, HUFFPOST (Nov. 22, 2011, 10:37 AM), <http://www.huffingtonpost.com/anna>

an independent consultant to determine if errors or misrepresentations made by banks might have caused financial harm to homeowners.¹⁷¹ In particular, the reviews were targeted at identifying improper foreclosure practices with a goal of providing financial compensation to those harmed. The Independent Foreclosure Review, however, failed in stunning fashion. Two common rationales for the failure of the review are (i) that conflicts of interest existed among the independent consultants engaged to complete the review and (ii) that the Federal Reserve and OCC failed to properly supervise the reviews. But, yet again, when one utilizes this Article's process frame to evaluate the compliance failure, it looks as if the root cause may be more complicated and related to the expansive nature of the review, which required consultants to engage in an unprecedented effort of detection, investigation, and remediation.

1. The Failed Independent Foreclosure Review

In April 2011, in response to the mortgage foreclosure crisis, enforcement actions were brought by the OCC, the Federal Reserve, and the Office of Thrift Supervision against fourteen mortgage servicers, which required them "to correct deficiencies in their servicing and foreclosure processes."¹⁷² Specifically, each of the mortgage servicers was required to engage independent consultants "to conduct a multi-faceted independent review of foreclosure actions that occurred in 2009 and 2010."¹⁷³

To effectuate this review, each of the independent consultants developed a set of questions utilized to evaluate conduct at the specific bank whose policies the consultant was charged with overseeing.¹⁷⁴ The questions allowed the independent consultants to "evaluat[e] whether borrowers suffered financial injury through errors, misrepresentations, or other deficiencies in foreclosure practices and determin[e] appropriate remediation for those customers."¹⁷⁵ Additionally, the independent consultants were charged with "review[ing] a variety of sample cases from each servicer."¹⁷⁶ In the event an issue was identified, the independent consultant was required to "conduct additional secondary reviews to identify as many affected borrowers as possible."¹⁷⁷ In instances where a "borrower suffered financial injury as a result of" a mortgage servicer's conduct, "the consent orders require[d] remediation to be provided."¹⁷⁸

When the reviews commenced in November 2011, the acting head of the OCC said that the reviews would "take several months to complete, considering the large

-cuevas/foreclosure-review_b_1098840.html [https://perma.cc/9ANM-AT8L].

171. Cuevas, *supra* note 170.

172. OCC Press Release, *supra* note 170.

173. *Id.*

174. See, e.g., Ben Hallman & Eleazar David Melendez, *Foreclosure Review Insiders Portray Massive Failure, Doomed from the Start*, HUFFPOST (Jan. 14, 2013, 9:23 AM), http://www.huffingtonpost.com/2013/01/14/foreclosure-review-failure-start_n_2468988.html [https://perma.cc/W8HN-JUPF].

175. OCC Press Release, *supra* note 170.

176. *Id.*

177. *Id.*

178. *Id.*

pool of borrowers that could be part of the review.¹⁷⁹ Over a year later, however, the review ended in an abrupt fashion once it became clear that it was “doomed.”¹⁸⁰ The individual file reviews for various homeowners were halted in favor of a new deal, which allowed any homeowner who received a foreclosure notice in 2009 or 2010—over four million people—to receive some share of a fixed, multibillion amount of money ranging from \$250 to \$125,000.¹⁸¹ At the time the reviews ceased, over \$1.5 billion had been paid to the independent consultants and their employees or agents for the failed review.¹⁸²

The failure of the Independent Foreclosure Review, unsurprisingly, sparked criticism from the public at large¹⁸³ and drew the ire of congressional members.¹⁸⁴ It also resulted in multiple investigations by the Government Accountability Office, which determined that the OCC and Federal Reserve (i) needed to enhance borrower outreach efforts,¹⁸⁵ (ii) should have improved oversight of the reviews,¹⁸⁶ and (iii) should have done more to define testing activities aimed at overseeing the foreclosure reviews.¹⁸⁷ In the weeks and months that followed, multiple accounts emerged blaming the review’s failure on a variety of causes, including flawed guidance from the regulators¹⁸⁸ and inherent conflicts of interest by the independent consultants.¹⁸⁹

179. *Id.*

180. Hallman & Melendez, *supra* note 174.

181. *Id.*

182. *Id.*

183. *See id.*

184. *See Independent Foreclosure Review*, U.S. HOUSE COMM. ON FIN. SERVS. DEMOCRATS, <https://democrats-financialservices.house.gov/news/documentquery.aspx?IssueID=126815> [<https://perma.cc/7H8V-BQ9Y>].

185. U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-12-776, FORECLOSURE REVIEW: OPPORTUNITIES EXIST TO FURTHER ENHANCE BORROWER OUTREACH EFFORTS (2012), <http://www.gao.gov/assets/600/592059.pdf> [<https://perma.cc/J7L8-UQA3>].

186. U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-13-277, FORECLOSURE REVIEW: LESSONS LEARNED COULD ENHANCE CONTINUING REVIEWS AND ACTIVITIES UNDER AMENDED CONSENT ORDERS (2013), <http://www.gao.gov/assets/660/653327.pdf> [<https://perma.cc/Q3HN-UF5D>].

187. U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-14-376, FORECLOSURE REVIEW: REGULATORS COULD STRENGTHEN OVERSIGHT AND IMPROVE TRANSPARENCY OF THE PROCESS (2014), <http://www.gao.gov/assets/670/662791.pdf> [<https://perma.cc/8TWX-EWMC>].

188. Hallman & Melendez, *supra* note 174; *see also* Alexis Golstein, *Foreclosure Review Report Shows that the OCC Continues to Bury Wall Street’s Bodies*, NATION (Apr. 10, 2013), <https://www.thenation.com/article/foreclosure-review-report-shows-occ-continues-bury-wall-streets-bodies> [<https://perma.cc/R83Z-HRCL>]; Francine McKenna, *GAO Blames Regulators for Faulty Foreclosure Reviews but That’s Not the Whole Story*, FORBES (Apr. 4, 2013, 8:13 AM), <https://www.forbes.com/sites/francinemckenna/2013/04/04/gao-blames-regulators-for-faulty-foreclosure-reviews-but-thats-not-the-whole-story/#6bb50fac5407> [<https://perma.cc/2JC7-G8JA>].

189. Francine McKenna, *Another Conflicted Foreclosure Review: PricewaterhouseCoopers and Ally/Res Cap*, FORBES (June 25, 2013, 2:40 PM), <https://www.forbes.com/sites/francinemckenna/2013/06/25/another-conflicted-foreclosure-review-pricewaterhousecoopers-and-allyrescap/#657380eb4907> [<https://perma.cc/BL9U-QQWB>]; John E. Miller, *There’s a Big Conflict of Interest in the National Foreclosure Review Process*, BUS. INSIDER (Mar. 6, 2012, 8:23 AM), <http://static5.businessinsider.com/more-info-revealed-about-the-foreclosure-review-process--and-some-dont-like-it-2012-3> [<https://perma.cc>

And yet, when considered under the compliance process frame, another potential root cause comes to light.

2. The Independent Foreclosure Review Under the Compliance Process Frame

A variety of missteps led to the ineffectiveness of the Independent Foreclosure Review, but when one engages in root-cause analysis while utilizing the compliance process frame, a pragmatic limitation is revealed. The independent consultants were expected to conduct individualized reviews for over four million homeowners in an effort to detect, investigate, and remediate claims of improper foreclosure practices.¹⁹⁰ The detection and investigation mechanisms required by the various consent orders prompted independent consultants to draft an extraordinarily large—in one case 2,000—set of questions for the independent consultant reviewers to utilize in determining whether the banks followed their own internal policies and practices for each individual homeowner.¹⁹¹ When one considers the sheer magnitude of the project, particularly in light of the responsibility of the independent consultants to engage in three stages of the compliance process for over four million homeowners, one begins to question whether the expectations at the outset of the review were realistic. Regulators were concerned with ensuring that the monetary remediation received by homeowners was accurate, but in the process, they crafted a highly burdensome review that required the consultants to do much more than simply oversee the monetary remediation efforts. Therefore, it may be that a root cause of the Independent Foreclosure Review's failure was a result of a failed regulatory design at the outset of the engagement.

D. Example 4: Lack of Commitment to Compliance

Baylor University (“Baylor”), a private Christian university located in Waco, Texas, is “a [n]ationally [r]anked [r]esearch [i]nstitution” that “provides a vibrant campus community for more than 16,000 students.”¹⁹² Baylor describes itself as “a place where the Lordship of Jesus Christ is embraced, studied, and celebrated . . . [that is] compelled to care for one another and to address the challenges of [a] hurting world.”¹⁹³ Baylor, however, failed to address allegations and incidents of sexual assault within its student body for several years.¹⁹⁴ Baylor's failure to live up to its

/8BZK-BBWP].

190. Hallman & Melendez, *supra* note 174.

191. *Id.*

192. *About Baylor*, BAYLOR U., http://www.baylor.edu/about/?_buref=1172-91940 [<https://perma.cc/24EZ-CF9Z>].

193. *Pro Futuris: A Strategic Vision for Baylor University*, BAYLOR U., <http://www.baylor.edu/profuturis> [<https://perma.cc/XG5K-RJF8>].

194. See Paula Lavigne, *Baylor Faces Accusations of Ignoring Sex Assault Victims*, ESPN (July 13, 2017), http://www.espn.com/espn/otl/story/_/id/14675790/baylor-officials-accused-failing-investigate-sexual-assaults-fully-adequately-providing-support-alleged-victims [<https://perma.cc/HFQ5-ZXHB>]; *The 8 Biggest Recent Revelations in Baylor's Sexual Assault Scandal*, SPORTSDAY (May 2017), <https://sportsday.dallasnews.com/college-sports/college>

own stated values and those required of it by the Department of Education has a variety of causes. One of the primary causes pointed to is the deficiencies within Baylor's Title IX compliance program.¹⁹⁵ While it is correct that a failure by Baylor to implement an effective Title IX compliance program was a significant cause of its sexual assault scandal, careful study demonstrates that the compliance process at Baylor was deficient at each and every step. Thus, Baylor's sexual assault scandal was not just a result of an ineffective compliance program. Instead, it appears to reflect a lack of commitment by Baylor to create, implement, or prioritize a Title IX compliance program.

1. Baylor's Failed Compliance Process

Baylor's failure to *prevent* Title IX violations was significant. First, Baylor did not develop a formal Title IX program,¹⁹⁶ despite guidance provided to schools by the Department of Education in 2011.¹⁹⁷ Second, “[p]rior to the 2014-2015 academic year, Baylor failed to provide training and education to students [and] failed to identify and train responsible employees under Title IX.”¹⁹⁸

Baylor also neglected to properly *detect* Title IX violations. For example, Baylor did not “provide clear information about reporting options and resources on

sports/2017/05/24/5-biggest-recent-revelations-baylors-sexual-assault-scandal [https://perma.cc/WZ8F-6L9L].

195. Title IX prohibits sex discrimination in education programs and activities and, among other things, dictates how educational institutions that receive federal funding must respond to allegations of sexual assault. Title IX of the Education Amendments of 1972, 34 C.F.R. § 106.8(a) (2014); *see also* Letter from Russlynn Ali, Assistant Sec’y for Civil Rights, Office for Civil Rights, U.S. Dep’t of Educ., to Colleagues (Apr. 4, 2011), <http://www2.ed.gov/about/offices/list/ocr/letters/colleague-201104.pdf> [https://perma.cc/9WWY-RASR] [hereinafter Sexual Assault Dear Colleague Letter]; Letter from Catherine E. Lhamon, Assistant Sec’y for Civil Rights, Office for Civil Rights, U.S. Dep’t of Educ., to Colleagues (Apr. 24, 2015), <https://www2.ed.gov/about/offices/list/ocr/letters/colleague-201504-title-ix-coordinators.pdf> [https://perma.cc/69EV-EM9P]. The Department of Education provides colleges and universities with guidance regarding their regulatory and legal requirements, which for many schools provides the basis for their Title IX compliance programs. Much of the reporting regarding Baylor's sexual assault scandal has focused on its failure to adhere to the Department of Education's guidance regarding the creation and implementation of an effective Title IX compliance program. *See, e.g.*, Nancy Armour, *Former Title IX Officer Accuses Baylor of Discrimination, Intimidation*, USA TODAY (Jan. 19, 2017, 1:55 PM), <https://www.usatoday.com/story/sports/ncaaf/big12/2017/01/19/former-title-9-officer-gabrielle-lyons-accuses-baylor-discrimination-intimidation/96779182> [https://perma.cc/U67Y-TBCS]. Indeed, an independent and external review conducted by an outside law firm, Pepper Hamilton LLP, “reflect[ed] a fundamental failure by Baylor to implement Title IX.” BAYLOR UNIVERSITY BOARD OF REGENTS: FINDINGS OF FACT, BAYLOR U. 1 (2016), <https://www.baylor.edu/thefacts/doc.php/266596.pdf> [https://perma.cc/HFE7-SQNN] [hereinafter PH FINDINGS]. Specifically, “Baylor’s efforts to implement Title IX were slow, ad hoc, and hindered by a lack of institutional support and engagement by senior leadership.” *Id.*

196. PH FINDINGS, *supra* note 195, at 4.

197. Sexual Assault Dear Colleague Letter, *supra* note 195.

198. PH FINDINGS, *supra* note 195, at 4.

campus.”¹⁹⁹ Additionally, Baylor “failed to have a centralized process for ensuring that all reports reached the Title IX Coordinator.”²⁰⁰ As a result, some reporting went directly to athletic department staff, who were not trained in Title IX compliance and failed to refer several Title IX violations to appropriate individuals within the university.²⁰¹

The claims of sexual assault that were referred to the appropriate office at the time, the university’s judicial affairs office, were not properly *investigated* by Baylor staff. For example, Baylor “failed to appropriately evaluate and balance institutional safety and Title IX obligations against a complainant’s request for anonymity or that no action/investigation be pursued.”²⁰² Additionally, Baylor “failed to conduct prompt, equitable, adequate, and reliable investigations.”²⁰³ Moreover, Baylor administrators charged with investigating claims of sexual assault “were not adequately trained in the dynamics of sexual and gender-based harassment and violence, dating violence, domestic violence, stalking, [and] the neurobiological impacts of trauma.”²⁰⁴

Baylor’s failures to prevent, detect, and properly investigate claims of sexual misconduct became a high-profile scandal in January 2014, when a former football player was found guilty of sexually assaulting a former Baylor student and sentenced to twenty years in prison.²⁰⁵

Baylor did eventually engage in what appeared to be a sincere attempt to address its past compliance failures. In November 2014, it hired its first full-time Title IX coordinator who was charged with building and strengthening the Title IX office.²⁰⁶ In August 2015, it conducted an internal inquiry into how it handled sexual assault allegations.²⁰⁷ And in September 2015, it hired external counsel to conduct an “investigation into how the university handle[d] cases of alleged sexual violence,” which resulted in 105 recommendations for the university to implement.²⁰⁸ In June 2016, the university’s interim president expressed Baylor’s commitment to implement the recommendations, explaining that he “consider[ed] them to be mandates” that must be adopted “so this will not happen again.”²⁰⁹

And yet, Baylor’s initial *remediation* efforts appear unsuccessful. The individual hired in October 2014 to run its new Title IX office eventually resigned in October

199. *Id.*

200. *Id.*

201. Mark Schlabach, *Art Briles, Ian McCaw Failed to Report Allegations of 2012 Sexual Assault*, ESPN (Nov. 14, 2016), http://www.espn.com/college-football/story/_/id/18029536/baylor-ex-coach-art-briles-ad-ian-mccaw-failed-report-allegations-2012-sexual-assault [<https://perma.cc/PT7V-KA98>].

202. PH FINDINGS, *supra* note 195, at 5.

203. *Id.*

204. *Id.* at 7.

205. *Timeline: Baylor Sexual Assault Controversy*, WACO TRIB.-HERALD (Jan. 1, 2017), http://www.wacotrib.com/news/higher_education/timeline-baylor-sexual-assault-controversy/article_abf21ab8-2267-51bf-84d8-6268f4222af0.html [<https://perma.cc/ZHG9-GALP>] [hereinafter *Timeline*].

206. *Id.*

207. *Id.*

208. *Id.*

209. *Id.*

2016, citing an inability to perform her job due to “resistance . . . from senior leadership.”²¹⁰ In particular, she claimed to have “never had the authority, resources or independence to do her job.”²¹¹ She went so far as to file a formal complaint with the U.S. Department of Education’s Office for Civil Rights, as did another staff member of the Title IX office.²¹² Baylor’s efforts to address the misconduct that occurred within its organization and improve its Title IX compliance are ongoing, and only time will tell their relative success or failure.

2. The Baylor Scandal Under the Compliance Process Frame

Thus, Baylor engaged in long-term resistance to creating and implementing a Title IX compliance program despite clear regulatory guidance from the Department of Education and signals from its community about the need for an effective Title IX compliance program. This insight may have been helpful for those responsible for implementing a compliance program at Baylor, and it may also have important takeaways for organizations responsible for regulating Baylor’s conduct.

It is possible that Baylor employees, students, and other members were suffering from what cognitive psychologists refer to as the “halo effect.” The halo effect is a cognitive bias “in which one’s judgment of a person’s character can be influenced by one’s overall (and usually first) impression of him or her, with little actual knowledge of the individual.”²¹³ While initially a tool used for individuals, the halo effect has been documented to influence how businesses are viewed. For example, recent economics scholarship determined that when a business is perceived as socially responsible, the company received an average of \$2 million less in fines after being found to have committed an FCPA violation, even though social responsibility and foreign bribery are uncorrelated.²¹⁴

As relevant to Baylor, it may be that individuals’ positive impressions of the school made it difficult for them to recognize that it was failing in a profound way to develop and maintain an effective Title IX compliance program. Indeed, the halo effect may have impacted the ability of individuals to conceive of Baylor having a problem with sexual assault on its campus at all. If, however, individuals at Baylor had utilized a process frame to evaluate its missteps prior to engaging in its initial remediation effort, they may have realized the depth of the institutional deficiencies in the Title IX space and been more receptive to the requests of the initial Title IX director.

Additionally, the compliance frame may be helpful for regulators tasked with assessing the progress a regulated entity is making toward meeting certain compliance requirements. For example, a regulator assessing Baylor’s commitment to Title IX may have initially believed it could take a relatively hands-off approach and allow Baylor to initiate a compliance program without robust oversight. When,

210. *Id.*

211. *Id.*

212. *Id.*

213. Harrison Hong & Inessa Liskovich, *Crime, Punishment and the Halo Effect of Corporate Social Responsibility* 1–2 (Nat’l Bureau of Econ. Research, Working Paper No. 21215, 2015), <http://www.nber.org/papers/w21215.pdf> [<https://perma.cc/2HFK-AGCH>].

214. *See id.* at 16–20.

however, one utilizes a process frame and determines the extent of Baylor's shortcomings in the Title IX area, it may prompt the regulator to engage in more aggressive actions in an effort to ensure Baylor implements the reforms necessary to create and maintain a compliance program that is likely to be successful.

Thus, the root cause of Baylor's compliance failure—a lack of commitment to a Title IX compliance program—might more readily be identified when a compliance frame is utilized. A lack of commitment is an extremely high hurdle to clear for those charged with implementing a compliance program, but recognizing the lack of commitment may be the key insight needed to develop a strategy that can begin to overcome the related cultural resistance to long-term organizational change.

* * * *

To be sure, the predictive value of these examples is necessarily limited. The benefit of full and complete information about the compliance outcomes outlined in this Part was not available to those charged with constructing these efforts, which means an element of hindsight bias is likely present in these accounts. The potential power of the process frame suggested by this Article will need to be utilized before any final determinations can be made with regard to its usefulness. Despite this limitation, the process frame does provide a new tool of assessment that leads to an alternative, or additional, determination regarding the root cause of some relatively significant compliance failures. As such, at a minimum the compliance frame presented in Part II of this Article may assist in more fully understanding the nature and scope of certain compliance failures.

IV. BENEFITS & POTENTIAL CONCERNS

This Article seeks to provide a new method for evaluating compliance failures. This Part addresses some, although certainly not all, of the potential benefits of this Article's proposed framework. The Part then addresses some potential concerns raised by the arguments herein.

A. Benefits

If those charged with creating and modifying compliance programs were to utilize the compliance process outlined in this Article when attempting to determine the root cause of the failure before them, a variety of benefits would follow. This Part addresses a few such benefits. It begins by discussing how the process frame may assist in narrowing the potential cause or causes of systematic compliance failures. The Part goes on to explain how the process frame can be utilized for institutional design efforts. It then explains how the process frame—an intervention made primarily for the benefit of those within organizations responsible for developing and assessing compliance failures—might also be useful for governmental actors charged with incentivizing effective ethics and compliance programs within organizations. The Part next explains how the process frame helps to support the establishment of compliance as a discrete field of study. It continues by identifying the ways in which the Article's proposal might improve assessments of conflicts of interest. It

concludes by discussing how a process frame may bolster notions of procedural fairness within firms engaged in creating and modifying their compliance programs.

1. Assist in Narrowing the Cause of Systemic Compliance Failures

In an earlier article, I criticized the government's current enforcement strategy, because it focuses on particular compliance areas, like Title IX or the FCPA, instead of considering whether there is a larger, more sophisticated failure within a firm's compliance program.²¹⁵ My previous study, for example, demonstrated that Hewlett-Packard entities engaged in improper bribery that violated the laws of three different statutory regimes.²¹⁶ One problem with a segmented enforcement strategy is that it fails to incentivize firms to systematically assess the effectiveness of their compliance efforts. This Article's proposed framework, however, might be helpful to firms that would like to undertake more holistic assessments of their compliance programs. A firm may be able to utilize the Article's proposed framework to engage in its own independent assessment of whether similar types of misconduct within the firm should prompt changes within its broader compliance efforts. Specifically, the framework may assist firms in their efforts to determine whether multiple compliance failures occurred in the same stage of the compliance process. If all of the failures occurred in one stage, like the prevention stage, it might serve as evidence of a need for the company to revamp its policies and procedures surrounding prevention in a broad and systematic manner.

2. Utilized in Institutional Design Efforts

The process frame outlined in this Article is primarily put forth to assist compliance actors in their attempts to determine the root cause of compliance failures. The process frame can also, however, be utilized in institutional design efforts. Once compliance actors have used the process frame to determine the root cause or causes of a compliance failure, they can then use the information gleaned to make tangible changes to the organization's compliance program. For instance, a company could determine how it should best allocate resources among the four stages. It may be that a firm decides it is overspending on the prevention stage and should allocate more resources toward detection. Currently, the Organizational Guidelines emphasize prevention and detection, so one often sees firms spend a great deal of time on those two stages within the compliance process, but an assessment that relies upon the compliance process frame may reveal deficiencies with a firm's investigative function. Additionally, utilizing a process frame may make it easier to break out tasks in manageable components and determine what work has and has not been completed. Because firms often employ both in-house and external actors to assist them in their compliance programs, it may be helpful to definitively assign responsibility for different stages within the compliance process to particular departments or external attorneys, auditors, or consultants. To the extent that both in-house and external actors engaged in duplicative work, using the process frame may

215. See Root, *supra* note 35, at 1029–36.

216. *Id.*

also assist in efforts to compare and evaluate what was and was not done by the internal and external actors and identify where the two sets of actors' results diverged.

3. Provide Regulators with an Additional Tool for Evaluating Compliance Failures

The primary purpose of this Article is to provide those charged with creating and implementing compliance programs with another tool for assessing compliance failures. Internal compliance officers are often in the best position to determine the root cause of compliance failures and challenges within their particular organization because they are aware of the most significant risks their organizations face.

This Article's proposed compliance process frame might be equally useful to regulators and prosecutors engaged in investigations of organizational misconduct. Government enforcement agents are charged with determining appropriate sanctions and remedial actions for organizations that fail to comply with legal and regulatory mandates, which require an assessment regarding the nature and scope of the wrongdoing. For misconduct that looks pervasive, a government enforcement agent may be more likely to issue a significant sanction. For misconduct that looks like an aberration, the government enforcement agent may want to decline to impose a penalty altogether. When making these sorts of distinctions, it may be helpful for regulators and prosecutors to assess whether the compliance failure at an organization involved one or multiple stages within the compliance process. Additionally, knowing what stage in the compliance process misconduct occurred might assist them in crafting certain remedial actions and consequences.

The upshot is that regulators and prosecutors, not just industry leaders and compliance personnel, might also benefit from utilizing the compliance process frame to assess compliance failures.

4. Identifies Compliance as a Discrete Field of Study

The examples used in this Article encompass a diverse set of regulatory and legal requirements and include organizations of differing corporate forms when discussing compliance failures. The field of compliance is an emerging one within legal scholarship, but the diversity of issues raised by compliance may make some wonder whether it truly is its own field. One additional benefit of this Article's proposed framework is that it assists in the effort to identify common concepts and characteristics that are found throughout the field of compliance. Whether the compliance program is targeted toward bribery, sexual assault, product liability, or consumer protection, all compliance programs must consider how they can prevent misconduct, detect when wrongdoing occurs, investigate the scope of the misconduct, and determine the best steps for remediating the malfeasance within the organization. The stability of the compliance process helps identify seemingly divergent areas into a cognizable field of study.

5. Improved Ability to Assess Potential Conflicts of Interest Within the Compliance Process

One common concern presented by compliance failures is the role that conflicts of interest play in the underlying misconduct. Two of the four examples outlined in Part III of this Article have what appear to be conflict of interest stories.

For example, Promontory was allowed to assist Standard Chartered in its investigation after already being engaged in a detection effort. Promontory may have developed a strong sense of loyalty to Standard Chartered, or it may have been suffering from capture²¹⁷ as a result of its prior relationship. Additionally, Promontory may have hoped to continue its relationship with Standard Chartered at the conclusion of Project Green, the investigative engagement, particularly given the highly lucrative nature of the project to Promontory, which earned \$54.5 million in total revenue from its work on Project Green.²¹⁸ Similarly, multiple conflicts of interest were detected as part of the Independent Foreclosure Review, as many of the independent consultants had prior auditing relationships with the mortgage servicers they were assigned to oversee.²¹⁹

Interestingly, these conflicts of interest should have been apparent to the relevant regulators in each of these examples. The conflicts were not secret and the prior relationships were subject to public reporting. And yet, the regulators failed to (i) appreciate the existence of the conflict of interest or (ii) properly assess the potential importance of the conflict.

The existence of a conflict of interest does not necessarily mean that a person or entity should be barred from assisting a firm or organization in future compliance efforts. Indeed, prior familiarity with a certain company or industry might actually result in certain efficiencies, improved working relationships, or more optimal compliance recommendations. But potential conflicts of interest should be evaluated fully and completely, and one potential benefit to this Article's proposed framework is that it might assist in those efforts by making certain distinctions—like a conversion of an external compliance consultant's role in a manner that creates conflicts of interest—more apparent.

6. Bolster Notions of Procedural Fairness

One challenge for individuals charged with creating, implementing, and maintaining compliance programs is finding ways to get employees and other members within the organization to comply with the actual compliance program. Research from the field of social psychology has determined an essential component

217. “‘Capture refers to an extremely close relationship between regulators and industry.’ And while not all scholars believe that capture is problematic, it is accepted that capture could lead to ‘sympathy to industry (implying excessive sympathy), identification with industry’s interest, and (unduly) lax enforcement.’” Veronica Root, *The Monitor-“Client” Relationship*, 100 VA. L. REV. 523, 579 (2014) (footnotes omitted).

218. PROMONTORY REPORT, *supra* note 153, at 3 n.1.

219. McKenna, *supra* note 189.

of shaping the behavior of individuals lies in the perceived fairness of the processes authorities use.²²⁰

For example, “[p]eople think that decisions are being more fairly made when authorities are neutral and unbiased and make their decisions using objective indicators, not their personal views.”²²¹ By purposefully and publicly utilizing the compliance process frame when assessing compliance failures, individuals charged with making changes to compliance programs may more readily demonstrate that they have engaged in an unbiased, deliberative process. Using the compliance frame as a tool may encourage organizational employees and members to perceive the resulting changes in policies and procedures as the legitimate conclusion of a fair assessment process. And if the modifications to the compliance program are perceived as fair, it is more likely that the organization’s members and employees will adhere to the parameters of the program.

B. Potential Concerns

Despite the many benefits to this Article’s proposed framework, there are some potential concerns raised by this Article and the proposed framework. This Section begins by discussing whether this Article’s proposal will potentially create “paper” compliance programs instead of encouraging “cultures of compliance.” The Section next discusses whether the process frame suggested by this Article is a genuinely new idea within compliance scholarship. It then addresses whether the Article’s proposal would be equally applicable to internal and external compliance actors. The Section goes on to assess whether there is an appreciable distinction between the Article’s use of “prevention” and more classic discussions regarding the role of gatekeepers. Finally, the Section discusses the roles of information disclosure and adjudication within the four stages of the compliance process.

1. Paper Programs Versus Cultures of Compliance

One common refrain within compliance circles is a concern that organizations will engage in so-called “paper compliance.” Paper compliance refers to the development of a compliance program on paper that is ineffectual in practice.²²² The concerns about paper compliance often dovetail into discussions about how an organization can create a culture of compliance. Recent legal scholarship has recognized that “[c]ulture becomes especially important . . . when . . . the structural aspects of compliance and supervision cannot or do not otherwise influence

220. Tom R. Tyler, *Procedural Justice, Legitimacy, and the Effective Rule of Law*, 30 CRIME & JUST. 283, 284–85 (2003). The research conducted by Tyler and the scenarios presented in this Article do not track perfectly. He is focused on formal adjudication, which is not the focus of the compliance process. That said, the notion of procedural fairness does analogize well to this situation where significant consequences are levied when misconduct occurs—whether the consequences are imposed by internal or external firm actors.

221. *Id.* at 298.

222. Tom Fox, *What Is a Paper Compliance Program?*, COMPLIANCE WEEK (Dec. 29, 2016), <https://www.complianceweek.com/blogs/the-man-from-fcpa/what-is-a-paper-compliance-program#.WniEWudG13g> [https://perma.cc/6A7D-4WX3].

behavior.”²²³ Thus, one major question raised by this Article’s proposed framework is whether it is likely to (i) contribute to the undesirable creation of paper compliance programs or (ii) promote more effective cultures of compliance.

In regard to the first question, the Article’s proposed framework is meant to combat “paper compliance” programs by providing a new tool for assessing the root cause of compliance failures. By changing the inquiry from the broad question of “why did the compliance program fail” to the more precise inquiry of “where within the compliance process did misconduct occur,” this Article’s proposal is aimed at improving assessments of corporate misconduct. When assessments more clearly identify the root causes of organizational malfeasance, it will make it more difficult for firms to employ ineffective remediation efforts. That is not to say that it would be impossible for a firm to attempt to utilize the process frame in a surface way, but essentially all methods of reform are vulnerable to manipulation by sufficiently motivated bad actors. That possibility is not a reason to abandon the intervention.

In regard to the second question, it appears unlikely that the compliance process frame on its own would encourage a firm committed to noncompliance to make meaningful change toward a more compliant culture. “Culture of compliance refers to the shared beliefs—‘sense-making’—inside any given organization about the importance or legitimacy of legal compliance vis-à-vis other pressures and goals.”²²⁴ The compliance process frame will not, on its own, change the shared beliefs within a firm with a defunct compliance culture. It may, however, serve to expose the extent of the deficiencies within an organization’s culture. And that exposure may create a set of incentives—whether from regulatory action or public pressure—to change the culture within the organization.

2. The Four Stages of the Compliance Process Are Already Recognized as Important to Compliance Efforts

As outlined in Part II, each stage of the proposed compliance process frame has been recognized as important by previous scholarship, courts, or regulatory mechanisms. Thus, a question may exist as to whether this Article’s attempted intervention is providing a genuinely new framework for assessing compliance failures. For example, a recent article explained:

The common structural framework for compliance includes (1) a commitment from senior leadership to the task, setting a right “tone at the top;” (2) delegation of authority to officials with distinct compliance responsibilities and the resources to do their task; (3) firm-wide education and training about both the substance and process of compliance; (4) informational mechanisms to alert as to suspicious activity (e.g., whistleblowing procedures); (5) audit and surveillance tactics to detect compliance failures or risks; and (6) internal investigation, response, discipline and remediation so as to learn and adjust when failures occur. The right mix of these is firm-specific, a

223. Langevoort, *supra* note 34, at 944.

224. *Id.* (footnote omitted).

customization that recognizes the great range of motives, opportunities, and types of violations most likely to be a problem at a given firm.²²⁵

The concepts of prevention, detection, investigation, and remediation are present in this description, which means individuals charged with assessing compliance failures are likely aware of the importance of these concepts.

This Article is not arguing that it is inventing new methods for assessing compliance failures. Instead, it has (i) evaluated compliance failures across a wide variety of legal and regulatory areas, (ii) determined that within that diversity there are four stages that those charged with overseeing compliance efforts must consider or address, and (iii) suggested that these four common aspects within the compliance process can be utilized to frame inquiries surrounding the root cause of compliance failures.

Because the method by which one frames a question can affect the answers one is able to identify, this Article's suggestion to purposefully utilize these four components of the compliance process when undergoing and assessing compliance efforts does allow these previously recognized concepts to serve a new purpose. The current approach to addressing compliance failures has tended to focus on why or how compliance failures occurred, which allowed for concrete answers. The question did not, however, prompt or force institutions to consider the full complexity of their compliance breakdowns. The hope is that this Article's proposal will encourage a more robust inquiry and corresponding root-cause analysis into the causes of corporate misconduct and potential avenues for corrective action.

3. Internal Compliance Assessments

The first three examples given in Part III involved external individuals charged with addressing compliance challenges or failures within a separate organization or firm, and the fourth involved a very public compliance failure. This may prompt one to wonder about the salience of this Article's proposed framework when dealing with purely internal compliance assessments.

Because the proposal outlined in this Article will need to be utilized and tested before its potential effectiveness can be fully and properly assessed, it is difficult to say definitively how the proposal may function when utilized by internal compliance personnel to engage in confidential assessments. The use of external and public examples in Part III was motivated by an attempt to utilize well-known examples that had been heavily reported on in public spaces, so that the Article's claims would remain accessible to a wide audience of readers. Internal compliance failures and challenges often remain just that, internal, which makes it more challenging to garner examples that can be shared in a public forum. That said, the hope is that this Article's proposal will be considered for use by those within industry.

225. *Id.* at 939–40 (footnotes omitted).

4. The Propriety of Utilizing the Same Framework for Public Firms and Nonprofit Organizations

The examples in this Article include both public firms, like Apple, and nonprofit organizations, like Baylor.²²⁶ It is often the case in legal scholarship that the public/nonprofit divide is inappropriate to cross, and a question remains about the propriety of utilizing the same process frame for evaluating misconduct in different types of organizations.

While it is certainly true that different organizations often face distinct challenges and difficulties, at its core the task of identifying the root cause of misconduct within firms and organizations remains the same, or basically the same, inquiry. This Article's proposed framework is aimed at assisting industry leaders, policymakers, and academics in determining why misconduct occurred, but the strategies implemented for resolving the misconduct might differ widely based on the type of organization where the wrongdoing occurred. For example, in another article, I proposed a more aggressive enforcement regime for corporate repeat offenders, but the proposed solutions were only applicable for public companies.²²⁷ More research is certainly needed regarding the different compliance challenges facing public firms and nonprofit organizations, but as of now it does appear that conducting a root-cause analysis may be a similar task regardless of corporate form.

5. Whether There Is a Relevant Distinction Between This Article's Use of "Prevention" and the Classic "Gatekeeper"

This Article suggests that the first stage in the compliance process is one of prevention. Gatekeepers are often characterized as actors who are charged with preventing misconduct within firms. The tie between the concepts of gatekeeping and prevention is strong, which raises a question as to whether this Article's use of "prevention" is meant to include the role of gatekeepers or is a purposeful attempt to exclude gatekeepers from its typology.

For example, in discussing misconduct committed by senior officers of a firm, legal scholarship explains that "preventive measure[s] establish[] an internal gate and gatekeeper that can bar misconduct, either literally or figuratively, unless the would-be wrongdoer invests resources and skill in circumventing it."²²⁸ Similarly, when discussing the proper role of the corporate attorney, one potential role is known as "the gatekeeper model," which "may require the attorney to take affirmative steps to prevent or limit client wrongdoing."²²⁹ Thus, the ideas of prevention and gatekeeping often appear together. Moreover, discussions of compliance often talk about the role of the gatekeeper, which makes its omission from this Article's framework potentially concerning. For example, the leading compliance casebook describes a gatekeeper as "someone who guards a gate. The 'gate' in this metaphor separates the organization from some objective that the organization seeks to achieve. The

226. See *supra* Sections III.A and III.D.

227. Root, *supra* note 35.

228. Arlen & Kraakman, *supra* note 66, at 702.

229. Jill E. Fisch & Kenneth M. Rosen, *Is There a Role for Lawyers in Preventing Future Enrons?*, 48 VILL. L. REV. 1097, 1102 (2003).

gatekeeper has control over the gate, and accordingly can prevent or impede the organization from achieving its objective.”²³⁰

It is certainly true that gatekeepers are quite important to compliance efforts. This Article’s dependence on the word prevention, however, is done to ensure clarity of meaning and thought. As has been noted, “[t]he term ‘gatekeeper’ is widely used in compliance circles, but the specific meaning is not always precise.”²³¹ There are competing definitions of gatekeepers throughout legal scholarship, with some emphasizing service providers²³² and others focusing on a type of liability.²³³ Because of the ongoing debate about what is and is not a gatekeeper, this Article’s framework has deliberately avoided the term.

6. The Role of Information Disclosure

Recent scholarship has explained that “the compliance function attends to the flow of information within [an] organization.”²³⁴ As such, one may wonder why this Article’s proposed framework does not discuss the role of information disclosure. Across all four stages of the compliance process, there are a variety of functions that individuals engaged in compliance efforts undertake. One of those functions is to provide information from one part of the organization to another. For example, the compliance department may be responsible for training lower-level employees while also responsible for reporting misconduct to senior management. The information disclosure function is present and necessary at each stage of the compliance process. Because information disclosure is a function of compliance efforts and not a distinct stage within the compliance process, a robust discussion of information disclosure is not necessary for understanding this Article’s proposed framework. It is, however, an essential component of an effective compliance program.

7. The Role of Adjudication Within the Process Frame

As outlined, this Article does not address formal and informal adjudicative decisions and where they would fit within the compliance process framework. Formal adjudication may consist of a decision from a court, regulatory body, or self-regulatory organization, while informal adjudication may include a decision by an organization that one of its employees or agents engaged in misconduct. Adjudicative decisions—both formal and informal—are important because they allow a firm to understand that misconduct did in fact occur. They can occur, however, at the detection, investigation, and remediation stages. It may be that a company detects misconduct and immediately understands and interprets the relevant actions as misconduct. In other instances, a firm may detect potential misconduct, but the formal finding of misconduct is not confirmed until after an investigative period.

230. GEOFFREY PARSONS MILLER, *THE LAW OF GOVERNANCE, RISK MANAGEMENT, AND COMPLIANCE* 371 (2d ed., 2017).

231. *Id.*

232. Coffee, *supra* note 84, at 308.

233. Reinier H. Kraakman, *Corporate Liability Strategies and the Costs of Legal Controls*, 93 *YALE L.J.* 857, 868 (1984).

234. Griffith, *supra* note 31, at 2095.

This is important because it is possible to initiate an investigation and determine that a compliance failure did not in fact occur. Finally, a remediation effort into corporate misconduct will sometimes uncover other instances of wrongdoing within the organization. This insight cements the importance of firms fully engaging and investing in each stage of the compliance process, so that informal and formal adjudicative decisions are made properly.

CONCLUSION

As is detailed above, there are a number of reasons and incentives for firms and organizations to comply with legal and regulatory requirements, but compliance failures persist. This Article is the second in a series of articles aimed at improving compliance programs, and this particular Article makes three primary contributions to legal scholarship.

First, it demonstrates that compliance failures can be analyzed using a process frame based on the four stages of prevention, detection, investigation, and remediation. Currently, academics, regulators, industry professionals, and the public often focus broadly on the “compliance failure,” but this Article shifts the framing of the inquiry presented in a manner that forces compliance actors to be more deliberative and focused when making assessments.

Second, the Article argues that utilizing a process frame may in many instances lead to a new or additional root-cause determination when evaluating compliance failures. Currently, when compliance failures occur, compliance actors often focus on the immediate misconduct or wrongdoing without systematically assessing whether there might have been multiple failures or contributing causes. As a result, those charged with overseeing remediation efforts at firms may not fully appreciate the scope of work that needs to be undertaken. This Article’s framework will assist in efforts to hone in on the root cause of compliance failures. This assistance holds even when an organization is not fully committed to creating an effective compliance program.

Third, it provides yet another tool for those charged with improving compliance within firms and organizations. For example, the Article’s framework will improve the ability to assess potential conflicts of interest within the compliance process. Additionally, it will provide regulators with another tool for evaluating compliance failures. The Article’s framework will also assist compliance actors in pinpointing systemic compliance failures. Finally, utilizing a process frame may increase notions of procedural fairness and encourage organizations’ members and employees to comply with newly implemented policies and procedures.

Compliance failures are often quite complex, but this Article’s proposal allows complex compliance failures to be assessed in components that are more manageable. As such, it will hopefully assist in the greater effort to improve compliance programs at firms and organizations more generally.