Maximum Impact: E&C Program Effectiveness Beyond Design and Implementation

Program Effectiveness: Who Cares, and Why?

In 2012 corporations spent, on average, $54 per employee on ethics and compliance (E&C) programs ($76 per employee in highly regulated industries.)[1] By any reasonable standard, that should be seen as a bargain.[2] Still, the average spend keeps rising—by as much as 10% annually in recent years—and the number of programs and employees covered by them continues to grow.

Growing, too, are the roles and responsibilities associated with the typical ethics and compliance program, which now range from mundane necessities, such as collecting annual code of conduct certifications or maintaining gift registries, to essential missions, such as inspiring cultural transformations.

For all of the money being spent, all of the roles being filled, and all of the increased focus on E&C as a key corporate function, we have not determined with any degree of confidence whether anything we are doing actually works or actually elevates or inspires employee behavior. Are our programs "effective"? What works and what doesn't? Which metrics can best supply answers? How do we improve?

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Program Effectiveness as Defined by the Regulators

The Federal Sentencing Guidelines for Organizations do not require a company to have a compliance and ethics program. They explicitly require, from the chapter's title to its footnotes, that companies have an "effective compliance and ethics program." So it should come as no surprise that "program effectiveness" is a matter of utmost concern for ethics and compliance professionals. While most also want to know that their company's investment and effort are paying off, those subject to U.S. jurisdiction or compliance requirements are at least as likely to be focused on judicial and regulatory mandates and expectations of their programs. Our 2013 Ethics & Compliance Leadership Survey ("Leadership Survey") makes clear that for the vast majority (76%) of E&C leaders, the most important program priority is to "meet all regulatory requirements for effective E&C programs and best practices."[3]

Section 8B2.1 of the Guidelines (and the commentary to it) includes the word "effective" or "effectiveness" 18 times and specifically requires that an organization "evaluate periodically the effectiveness of the organization's compliance and ethics program" (§8B2.1. (b)(5)(B)).[4]

What does it mean to have an effective program? On this point, the guidelines are somewhat less clear. In the space of just a few lines, two different concepts surface. The first seems to lay out a broad mandate involving the exercise of due diligence and the promotion of ethical culture through efforts "designed, implemented, and enforced so that the program is generally effective in preventing and detecting criminal conduct" (§8B2.1. (a), emphasis added). This approach would seem to be focused on outcomes: Has the program generally succeeded in preventing and detecting criminal conduct? Subsection (b), on the other hand, goes on to clarify that "[d]ue diligence and the promotion of an organizational culture...minimally require" each of the elements of the now familiar seven-point standard.[5] This language certainly suggests that the structure of the program is critical to a finding of "effectiveness" for the various purposes of the Guidelines.

Subsection (c) prescribes periodic risk assessment and mandates that the organization "take appropriate steps to design, implement, or modify" each of the seven elements set forth in subsection (b) based on those assessments. Here again, the focus on the design and implementation of the program seems to point to structure rather than outcome or impact as the measure of effectiveness.

The DOJ and SEC's Resource Guide to the U.S. Foreign Corrupt Practices Act again addresses, but does not resolve, the issue. Taking the gist of its approach from the U.S. Attorneys' Manual,[6] the Resource Guide makes explicit the defensive utility of our E&C efforts: "An assessment of a company's compliance program, including its design and good faith implementation and enforcement, is an important part of the government's assessment of whether a violation occurred and, if so, what action should be taken" (page 56). The Guide goes on to discuss a series of "Hallmarks of Effective Compliance Programs."[7] In addition to examining program design and implementation in light of these hallmarks, prosecutors are also meant to ask of a program, "Does it work?" (ibid.). Regrettably, the Guide says little more on this central subject.

Do design and implementation measured against the seven requirements of the Sentencing Guidelines or the nine hallmarks of the Resource Guide (or the 12 "good practices" of the OECD, for that matter[8]) equal true program effectiveness? Is that how we answer the regulators' simple "does it work" inquiry?

No experienced practitioner would—and none should—ignore the guidance explicitly and intentionally given to us by our regulators. The defensive aspect of our programs—their salutary impact on charging, penalty, and settlement decisions—is a critical element of the potential ROI in ethics and compliance and is certainly among the expectations of our C-suites and boards. If and when the time comes, each E&C

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leader should be ready to demonstrate that her or his program has been designed and implemented to ensure the hallmarks or elements are present.

Our requisite collective focus on program design and implementation is warranted, useful, and just about mandatory, if not law. A close reading of all the available guidance will provide the practitioner with a good deal of actionable intelligence, roughly summarized as: (1) take risk-based steps to mitigate non-compliance appropriate to the enterprise; (2) monitor for effectiveness; and (3) rinse and repeat. But which steps work? How do we focus? How do we go from "hitting the marks" to elevating employee behavior?
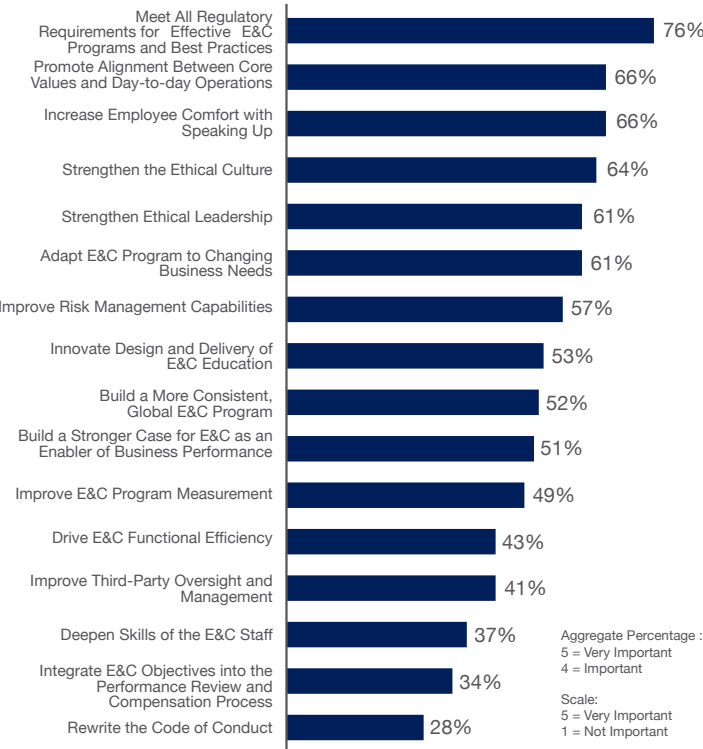
Ultimately, the success of the program—its true effectiveness—can't just be measured by how it was built or is being run. It has to be measured by the impact that program is having.

When You Can't Measure What You Value, You Tend to Value What You Can Measure

The first step to understanding what highly effective programs do is to identify which programs they are. While the fact or prevalence of misconduct seems as if it might be a useful starting point, two problems present themselves. First, misconduct has many causes, and an E&C program—no matter how effective—can no more take overall credit for an absence of misconduct than it can be blamed for an instance of it.[9] Second, relatively few instances of misconduct are made known outside of the organizations in which they occur.

Even those metrics that organizations use internally are insufficient for this purpose. As the table below makes clear,[10] those who manage E&C programs generally collect and report to the board of directors and others whatever is immediately measurable: numbers of helpline calls, code violations, disciplinary actions, and education completion rates.

Critical 2013 E&C Program Goals
Ranked by Percentage of Respondents

Goal	Percentage
Meet All Regulatory Requirements for Effective E&C Programs and Best Practices	76%
Promote Alignment Between Core Values and Day-to-day Operations	66%
Increase Employee Comfort with Speaking Up	66%
Strengthen the Ethical Culture	64%
Strengthen Ethical Leadership	61%
Adapt E&C Program to Changing Business Needs	61%
Improve Risk Management Capabilities	57%
Innovate Design and Delivery of E&C Education	53%
Build a More Consistent, Global E&C Program	52%
Build a Stronger Case for E&C as an Enabler of Business Performance	51%
Improve E&C Program Measurement	49%
Drive E&C Functional Efficiency	43%
Improve Third-Party Oversight and Management	41%
Deepen Skills of the E&C Staff	37%
Integrate E&C Objectives into the Performance Review and Compensation Process	34%
Rewrite the Code of Conduct	28%

Aggregate Percentage :
5 = Very Important
4 = Important

Scale:
5 = Very Important
1 = Not Important

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These lagging indicators can be useful, particularly when geographic or organizational differences are mapped and trends over time are included in the results. But even in instances where these indicators are focused on E&C-related outcomes, such as code of conduct violations, none specifically speaks to the question of program effectiveness. We cannot know what works and what doesn't. We cannot determine from any of these measures whether a given program is particularly effective or what effective programs have in common.

The Program Effectiveness Index (PEI) that LRN introduced in the Leadership Survey is an attempt to address this issue.

Building the Program Effectiveness Index

In the course of conducting the Leadership Survey, we collected data pertaining to more than 200 programs from a wide range of industries.[11] We examined the effectiveness of these programs in terms of the three major roles that E&C programs play:

- As a significant part of a network of corporate controls (the legislative and "police" function, including policies and procedures, investigations, etc.)
- As a facilitator of business operations in regulated contexts
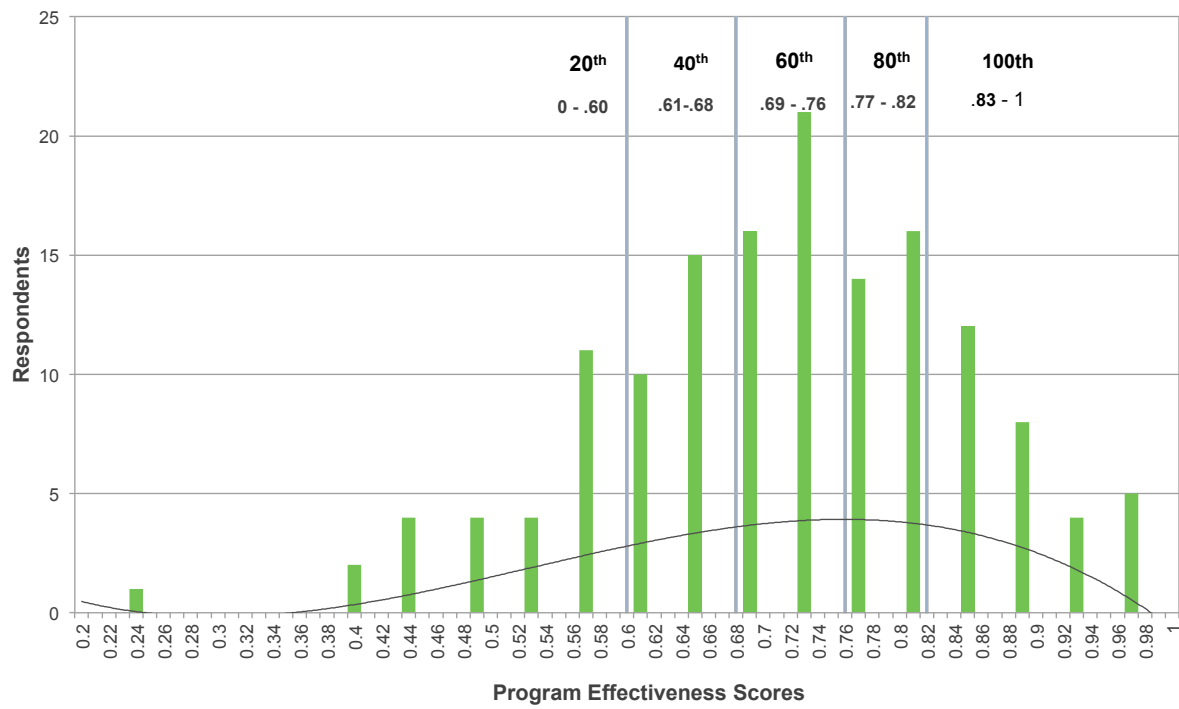- As the promoter of ethical conduct and culture

Because in most organizations the code of conduct synthesizes the expectations of the E&C program in each of the above three areas, the question of employee application of the code to business operations became another of the factors in our analysis. Because some form of education is the principal method for communicating expectations to employees, we also considered the impact of E&C education on employee behavior and decision making.

Mining the data collected for the survey, we used the questions addressing these issues as proxies for program effectiveness and combined the data collected from all respondents to create the PEI.[12] Utilizing respondents' self-evaluation on each aspect of program effectiveness is, of course, inherently subjective; however, if there is a self-evaluation bias, it should hold largely true across the spectrum of responses, and the point was not to create an absolute measure but to rank programs on a relative scale.

Programs were ranked from least to most effective on a scale of 0 to 1. The average PEI score was 0.71, and the distribution of Program Effectiveness Index scores appear as statisticians would expect. (See the table below.) Our respondents were fairly hard on themselves and the outcomes they achieved. No respondent scored its program "highly effective" across the board or entirely ineffective.

Program behaviors and attributes for which we had survey data (training, cost, staffing, reporting structures, and so on) were mapped against the index in search of possible correlation with program effectiveness.[13] The results address association, not causation. They demonstrate that certain behaviors and attributes are more prevalent in more effective programs while others are more prevalent in less effective ones. And some have no meaningful difference in association at all.

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Distribution of Program Effectiveness Scores

Chart: Distribution of Program Effectiveness Scores

Y-axis: Respondents (0 to 25)

X-axis: Program Effectiveness Scores (0.2 to 1)

Percentile bands:
- 20th: 0 - .60
- 40th: .61-.68
- 60th: .69 - .76
- 80th: .77 - .82
- 100th: .83 - 1

Key Program Effectiveness Index Findings

Correlations of particular interest are noted below.

Spending, Staffing, and Company Size Do Not Appear to Matter

The most basic program attributes—how many people are employed in the E&C effort, how much they spend, and the number of employees to whom they devote their efforts—do not appear to be associated with any greater or lesser degree of program effectiveness, as appears on the scatter plots below. Other attributes of note with no identified correlation to PEI scores include whether or not the company is highly regulated, to whom the chief compliance officer reports, and the average number of hours of computer-based training assigned.

E&C Budget per Thousand Employees
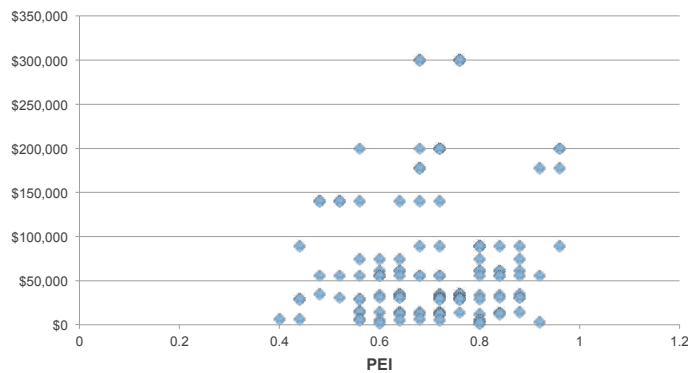
Dedicated E&C Headcount per Thousand Employees
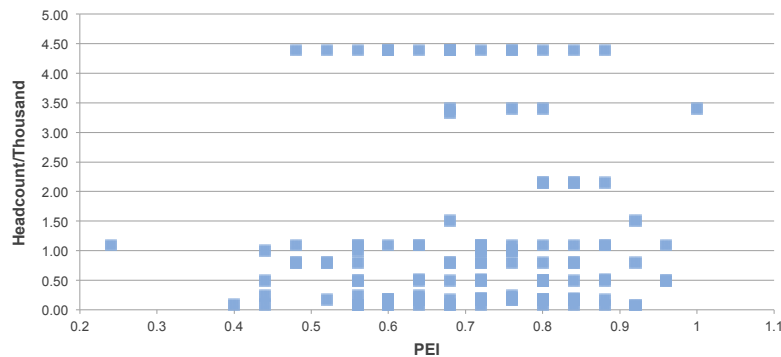
Company Size
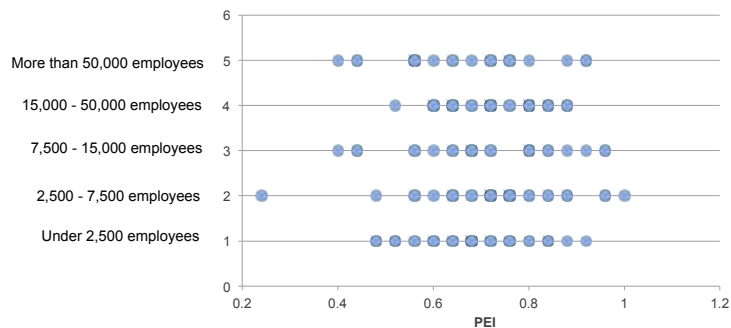
What Does Matter?

Goals matter. Overall, two-thirds of E&C programs have as their primary mandate "ensuring ethical behavior and alignment of decision-making and conduct with core values." These programs have an average PEI score of 0.74. In marked contrast, the one-third of E&C programs that have as their primary mandate "ensuring compliance with rules and regulations" have an average PEI score of 0.63, well below the mean.

Values matter. Whether in connection with weighting behaviors versus outcomes in performance reviews, or the relative importance of values and rules in forming the company's code, a balanced approach seems best. More effective programs communicate to their people that "how" matters as much as "what" or "how much" by saying it in their codes of conduct and "making it real" in their performance evaluations.

The PEI scores of programs taking blended approaches— incorporating multiple learning modalities— are considerably higher than those that do not.

Code of Conduct Orientation

Orientation	PEI	Percentage
Values only	0.71	4%
Values, supported by rules	0.71	44%
Values and rules equally	0.72	24%
Rules, supported by values	0.69	24%
Rules only	0.56	4%

### Emphasis in Performance Evaluations
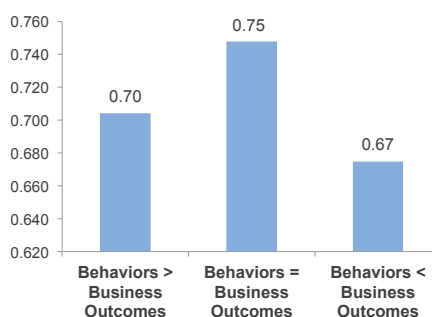
Education matters. Overall, PEI scores are relatively steady across the respondents' reported number of annual mandatory computer-based training (CBT) hours, with no noticeable impact differential in the entirety of the range from two hours to nine hours per year. In marked contrast, however, the 25 percent of programs assigning an hour or less of CBT per year have PEI scores more than 10 percent lower than the rest.

There is more to training—and more to effectiveness—than computer-based training, but it remains the steady tool of choice for E&C training, with more than 95 percent of all respondents using it to some degree, and three-quarters of respondents relying on it to deliver all or most of their E&C instruction. The PEI scores of programs taking blended approaches—incorporating multiple learning modalities—are considerably higher than those that do not. And the PEI scores of the 14 percent of programs delivering ethics and compliance messaging to employees' mobile devices are higher still. It is likely that these results reflect not the greater efficacy of any one method, but the impact of using multiple platforms.

Certain actions have significant impact. Repeating and reinforcing messages as well as putting those messages in contexts in which employees are meant to put them to use are examples. Programs that implement theme-based campaigns at least quarterly sport average PEI scores of .76, while those that do not roll out theme-based campaigns at all average PEI scores of .59—one of the most notable differences in average scores identified across the spectrum of behaviors

Methods of Learning
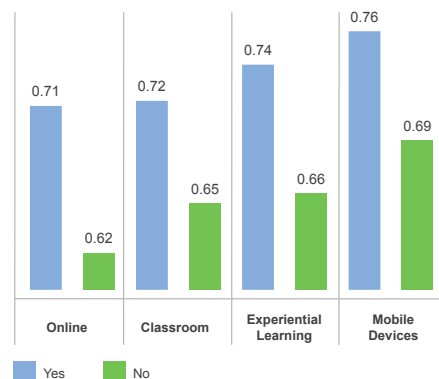
Theme-based Campaign Rollout
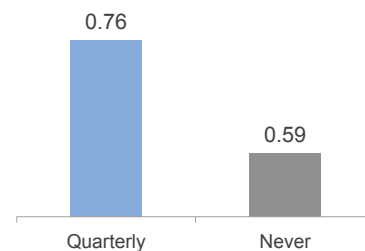
Average PEI Scores of Programs Based on Education Metrics Used

	Employee Feedback	Employee Behaviors	Organizational Impact
Yes	0.73	0.73	.75
No	0.67	0.69	0.69

■ Yes ■ No

The most effective programs, it appears, are those most deeply embedded within the fabric and structure of their organizations.

Metrics matter. Most programs measure completion rates, test results, and employee feedback. Without more, they hover around average PEI scores, though programs not tracking employee feedback seem to underperform (PEI score of .67). Excellent programs also track employee behaviors (PEI score of .73) and organizational impact (PEI score of .75).

Comparing Quintiles—Highly Effective Programs Versus Less Effective Programs

A comparison of the attributes and behaviors of the most and least effective programs—defined as those with scores in the top and bottom quintiles of the PEI range—highlights a few key principles, none of which will surprise the experienced E&C practitioner. The most effective programs, it appears, are those most deeply embedded within the fabric and structure of their organizations.

We examined the most effective programs against all others, the least effective against all others, and—finally—the most effective against the least.

The most effective against all others

Compared to all the rest, the most effective 20 percent of programs are much more likely to:

- Celebrate employees' acts of ethical leadership, both in team meetings and other company communications vehicles
- Have the following as key program goals:
  - Innovate design and delivery of E&C education
  - Drive E&C functional efficiency
  - Adapt E&C programs to changing business needs
- Focus on the validity and improvement of program metrics
- Focus on people (use HR data) as a key element of risk assessment
- Include social responsibility in their codes of conduct
- Have their officers be consulted by their CEO on senior management performance and promotions

The least effective against all others

Compared to all the rest, the least effective 20 percent of programs are much less likely to:

- Publicly celebrate employee acts of ethical leadership at all
- Have the following as key program goals:
  - Promote alignment between core values and day-to-day operations
  - Adapt E&C programs to changing business needs
  - Strengthen the ethical culture
- Focus on people (use HR data) as a key element of risk assessment
- Capture data on program effectiveness or report on it to the board
- Have the sponsorship of senior management (or have the CEO refer to the code of conduct without prodding)
- Provide risk information to executives to enable decision making
- Be responsible for driving culture in their organizations
- Have adequate resources

**The top quintile against the bottom**

These attributes most clearly distinguish the most effective ethics and compliance programs from the least:

• The celebration of acts of ethical leadership

• The effort to adapt E&C programs to changing business needs

• The focus on employees as a key element of risk assessment

• Access to and support of senior management

• Management's use of risk data in decision making

Highly effective E&C programs have shifted the focus of their budgets away from external consultants and toward education initiatives. On average, highly effective programs allocate about 29 percent of their budgets to education and 8 percent to consultants, while less effective programs allocate nearly twice as much to consultants (14%) and one fifth less (24%) to education.[14]

**Allocation of E&C Budget
(Top Versus Bottom Score Quintile)**
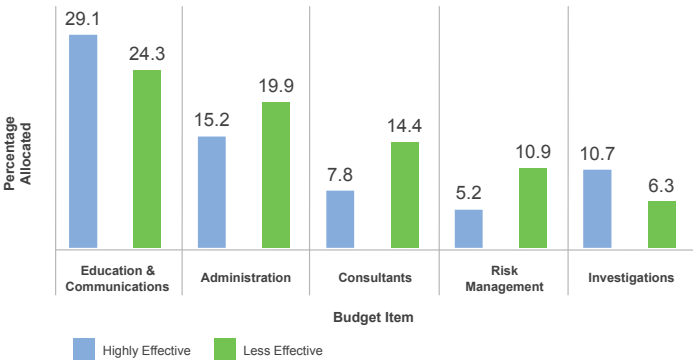
Embedding the E&C program by making sure it evolves with the business it serves is clearly characteristic of truly effective programs, with four out of five programs in the top quintile having it as a goal, compared to one out of three among the programs in the lowest quintile.

Innovation may well be its own reward, likely as a tool for grappling with online (and other forms of) education fatigue. The vast majority of very highly effective programs have innovation among their E&C goals, while very few low-impact programs seem to focus on it.

Most companies (58 percent) do not celebrate acts of ethical leadership in any recognized way, a lapse even more pronounced among those companies in the lowest quintile (84 percent). The fact that 80 percent of the companies with programs in the top quintile do celebrate acts of ethical leadership in one way or another speaks for itself.

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Conclusion

As noted above, an examination of the attributes and behaviors of effective programs does not establish causation. But it is clear that there are differences between more effective and less effective E&C programs, and that those differences cannot be understood only in terms of program design and implementation with reference to regulatory guidance. Fostering an ethical culture requires a focus not just on structure, but on a program's actual impact on actual behaviors. Increased compliance is likely to follow as just one of the important outcomes of that focus.

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Footnotes

1 All data, unless otherwise noted, from the LRN 2013 Ethics & Compliance Leadership Survey Report (http://www.lrn.com/operational-guidance-whitepapers/2013-ethics-compliance-leadership-survey-report).

2 Consider, for example, that Weatherford International's recent $253 million bribery fine works out to more than $3,600 per employee, while JP Morgan's $13 billion mortgage-related settlement comes to more than $52,000 a head.

3 Leadership Survey, p. 21.

4 The Guidelines are, of course, precatory, but not only is an "effective" program necessary to qualify for substantial mitigation in a sentencing calculation (or its far more common analog, the settlement negotiation), but the absence of such a program in an organization which by law should have one is, in the view of the Sentencing Commission, enough to justify an upward departure from the full, unmitigated sentence as calculated under the guidelines. See the policy statement at §8C4.10, "Mandatory Programs to Prevent and Detect Violations of Law."

5 The required elements are: (1) standards and procedures to prevent and detect criminal conduct; (2) a board knowledgeable about the program and exercising reasonable oversight with respect to its implementation and effectiveness; (3) assigned, appropriate, and responsible high-level personnel ensuring an effective program; (4) periodic communication of standards and procedures through effective training programs; (5) monitoring and auditing to detect criminal conduct, periodic evaluation of program effectiveness, and a confidential reporting system; (6) consistent program promotion and enforcement through appropriate incentives and disciplinary measures; and (7) appropriate responses to criminal conduct when detected, including making any necessary modifications to the program.

6 See United States Attorneys' Manual (USAM), 9-28.800.B: "While the Department recognizes that no compliance program can ever prevent all criminal activity by a corporation's employees, the critical factors in evaluating any program are whether the program is adequately designed for maximum effectiveness in preventing and detecting wrongdoing by employees and whether corporate management is enforcing the program or is tacitly encouraging or pressuring employees to engage in misconduct to achieve business objectives. The Department has no formulaic requirements regarding corporate compliance programs. The fundamental questions any prosecutor should ask are: Is the corporation's compliance program well designed? Is the program being applied earnestly and in good faith? Does the corporation's compliance program work? ...Prosecutors should therefore attempt to determine whether a corporation's compliance program is merely a 'paper program' or whether it was designed, implemented, reviewed, and revised, as appropriate, in an effective manner."

7 The hallmarks identified in the DOJ and SEC's Resource Guide to the U.S. Foreign Corrupt Practices Act are: 1) commitment from senior management and a clearly articulated policy; 2) clear, concise, and accessible code of conduct and compliance policies and procedures; 3) sufficient oversight, autonomy, and resources; 4) periodic risk assessment; 5) training and continuing advice; 6) incentives and disciplinary measures; 7) due diligence on third parties and payments; 8) confidential reporting and internal investigation; 8) continuous improvement (periodic testing and review); and 9) due diligence in M&A.

8 OECD Good Practice Guidance on Internal Controls, Ethics, and Compliance, adopted 18 February 2010. See also https://www.justice.gov.uk/downloads/legislation/bribery-act-2010-guidance.pdf for the "six principles" underlying "adequate procedures" for preventing bribery under the UK Bribery Act.

9 As noted in the Sentencing Guidelines (at 8.B2.(a)), the USAM (at 9-28.800.B), and the Joint Guidance (at p. 56), the failure to prevent a given violation does not mean that a company's compliance program is not generally effective.

10 Unless otherwise noted, all tables are from LRN's 2013 Ethics & Compliance Leadership Survey Report. See footnote 1, above.

11 Energy and utility, manufacturing, insurance, and financial services were the most significantly represented industries. Four out of five of the programs were headquartered in North America, with most of the remainder in Europe. Forty percent of participating companies had more than 15,000 employees (with 16% of those employing more than 50,000 workers).

12 The survey questions upon which we built the index were:

- How do you perceive the effectiveness of the E&C program as an Overseer (e.g., focusing on controls, risk management, and investigations)?

- How do you perceive the effectiveness of the E&C program as a Business Enabler (e.g., providing advice/counsel, enabling better decision making)?

- How do you perceive the effectiveness of the E&C program as a Corporate Conscience (e.g., promoting an ethical culture through education and addressing employee concerns)?

- To what extent do you believe your employees apply their understanding of the Code of Conduct on the job?

- What impact does your current E&C education have on employee behavior and decision making?

13 Survey responses on Likert items were scatter plotted against the PEI; survey responses on binary or "all that apply" items were compared based on the delta between the average PEI scores in each response category.

14 This finding may speak to program maturity, since it appears likely that programs in the early stages of development would spend a larger percentage of their budgets on outside consultants.