



Building and Maintaining an Effective Compliance Program

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ABSTRACT

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The ethics, corporate compliance and anti-fraud functions have faced a rapid growth in the last few years. Such a growth was explained as a kind of response to several high profile governance failures and subsequent regulatory reforms. Organizations throughout the whole world are now making huge investments in compliance, ethics and fraud prevention, launching their compliance programs, building risk management systems, rolling out comprehensive mandatory trainings and communication plans, designing and distributing compliance standards and procedures, and engaging their employees through so called tone from the top. This trend has touched companies from various industries and markets even from those that are traditionally receiving less regulatory attention. Nowadays, when most of the organizations have already established some basic level of compliance, anti-fraud, and ethics infrastructure, many of them begin to evaluate whether these are effective enough. This paper sets forth several ideas, tools, examples, and solutions tending to help and support the organizations in either building or preserving their effective compliance programs.

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In the aftermath of the worst financial crisis of the modern age, companies around the whole globe struggle to meet investors' expectations and remain competitive in the international level. Facing challenging financial conditions, companies have focused their efforts on significant cost-cutting measures; on the other hand, they still continue to explore various business opportunities in emerging markets and develop new products and services. As this attitude might be marked as challenging but necessary, companies must become more resilient and avoid possible fraud engagements of their employees. It can further be stated that regulators have, at the same time, increased their investigative and enforcement efforts to resist the

growth in corporate fraud. Following this, organizations are nowadays recommended and also expected to remain focused on building and maintaining a strong fraud prevention and compliance program. The best global companies of today and of the future must ensure that corporate integrity and ethics will be perceived as centerpieces of their culture. This perception of truly ethical corporate culture must permeate through every single corner of the organization - from the board of directors through its senior executives and leaders, down to entry-level employees in foreign subsidiaries. Focus should be placed not only on compliance with the law, but also on compliance with precepts of honesty, ethics, and integrity. Although it is not easy to create a culture where everyone does what is right and understands the importance of such behavior, it is nowadays a reality for any organization that wishes to successfully compete in the global market; a strong compliance program is therefore frequently seen as an essential business requirement. In addition, such a compliance program is also seen as a crucial aspect for regulators when determining various sanctions after problems appear. Compliance and ethical failures can be understood as significant indirect expenses (as there is a deliberate relationship between legal and reputation risks, *i.e.* legal issues give rise to reputation risks and reputation risks give rise to legal issues). However, building and maintaining a strong fraud prevention, ethics and compliance program should no longer be publicly seen as a matter of paying fines but rather as a matter of protecting the company itself, its shareholders, senior executives, leaders and managers, and the rest of its employees from significant harm and serious reputation and other compliance-based risks.

Although this paper intended to be a comprehensive overview of compliance and its interrelated measures, it cannot cover every possible aspect of this large and complex field. However, it is the author's intention to cover the underlying principles of effective compliance and it is also the author's hope that after reading this paper, the audience will get a greater understanding of not only how to establish and maintain an effective compliance and ethics program but also to comprehend the importance of creating that very special and lasting culture of compliance.

Why Business Ethics and Compliance Matter?

What is Compliance?

Compliance means knowing and following the relevant laws, rules, principles, and standards and procedures. It is making sure that the organizations adhere to all applicable legal and other requirements. Compliance must be seen and understood as a detailed and complex process. For any particular situation, one must be aware of all potentially applicable laws and regulations such as international and local laws and internal company-instituted rules. As this is not a possibility (*i.e.* something we would call "nice-to-have") but a strict obligation, a strong compliance and ethics program is necessary to protect the organization both internally and externally. Ignorance of the law is no excuse. A legal and/or natural person cannot escape a criminal charge or civil liability by claiming that he or she did not realize that the law was broken. The role of compliance is therefore to make sure that people know the rules beforehand and to ensure that they continuously follow them.

However, knowing the law and following it is only one side of compliance. It is obvious that businesses also have to know where and to what it applies. Once they have this

information, they must implement it into an effective compliance program. To get the word “effective” out of its theoretical meaning, it is highly recommended that the organizations hire experienced compliance professionals, issue detailed policies and guidance, institute and roll out respective training, and promote all other aspects of the compliance and ethics program. The aim of these compliance activities is to spread the knowledge to all who need it. It should be highlighted that the above described process must be continuous. The compliance program is the heart of compliance putting all of the elements above into effect. To sum up, true compliance should go beyond the borders of knowing and following the law, *i.e.* beyond the minimum requirements. In other words, simply following the law so as the organization’s representatives do not get into trouble will never be considered as full compliance. Effective compliance develops and sustains a culture based on values, integrity, and accountability; it ensures consistency of actions to eliminate or at least to lessen the opportunities for harm from criminal conduct or other compliance failures. It is therefore very important that true compliance involves the ongoing commitment from senior executives and leaders to promote ethical conduct and compliance with the law. Leading by example and establishing the tone at the top set the stage for every other element of compliance (Biegelman, 2008). Simply said, human beings mirror their leaders.

There are two significant obstacles that might occur in terms of compliance program’s implementation: The first one can be described as “using compliance as an excuse”. In practice, some executives, leaders, and other company representatives very often tend to use compliance as so called tool which helps them to mask their own negligence or even wrongdoing. It must be highlighted that this attitude is even more dangerous than having no compliance program at all. That is because it gives shareholders, employees, vendors, and also the public (or third parties) a false belief that the organization cares about following legal and other requirements when, in fact, all it wants is just to misguide others into believing it. Plenty of organizations that faced corporate scandals had, for example, implemented the code of conduct. In actual fact, in the end, these codes showed up to be nothing more than empty words. The second obstacle which might go in hand with compliance and ethics program’s implementation is when the program itself is not sufficiently supported by skilled personnel, meaningful awareness, management engagement, etc. This is not only risky from the perspective of all stakeholders involved, but also counterproductive. True compliance means that one believes in what he/she (or even the organization itself) is doing in every single aspect of the business concerned. The organizations cannot have effective compliance and ethics programs without that. If their management believes in compliance and supports and underlines this belief by its actions, people will feel more motivated and should easily follow its lead. An under-funded and unsupported program is predestined to fail. Without sufficient support from the organization and its management, a compliance and ethics program cannot fulfill its objectives of changing and influencing employees’ behavior. To sum up, true compliance requires direct input by company leadership and the key support of a qualified compliance officer running a reliable compliance department and providing the organization with an appropriate direction.

A Brief History of Compliance

Today's definition of corporate compliance function is nothing more than a simple result of many years of growth, evolution and experience. Various laws and rules covering businesses have been developed over the years into a more formal and complex structure. Such regulation started slowly in the 19th century as a response to several individual scandals. By the 1960s, with increasing complexity in both the business and regulatory areas, the foundations of modern compliance have been laid down and further developed. This trend continued in 1970s and 1980s until it reached a tipping point with the release of the USSC Organizational Guidelines. Although many compliance programs existed well before these guidelines came into force, they gave them a major push into the mainstream of business. The compliance framework has further developed with the passage of other well-known laws and regulations such as the U.S. Sarbanes-Oxley Act from 2002 or UK Bribery Act from 2010. The above-described evolution resulted into increased importance and role of compliance officers in the 21st century.

In many ways, the history and development of business and its regulation parallel the history of various publicly known scandals. This idea could be described as an ongoing tug of war between regulators who seek to reign in corporate excess and business that resists regulation to achieve greater flexibility and innovation. It is a matter of fact that regulators have always stepped in during the exposure of massive corporate scandals. As these scandals have usually been extremely devastating, they have simply forced lawmakers to step in. This pattern lies at the heart of the majority of related corporate governance regulations. Considering the American corporate regulation as an example, Skeel (2005) concluded that American corporate regulation has composed of periodic and dramatic regulatory interventions by federal lawmakers. It happened after a major scandal together with more nuanced ongoing regulation by the states. In the aftermath of these scandals, the public outrage and calls for justice change into broad support for evident reform that would otherwise be unbearable if the scandals had not occurred.

Compliance has always been around, in some form or another, since the establishment of organized business activities and commerce. Walsh and Pyrich (1995) propose that self-regulation of business stretches back to Middle Age merchant and craft guilds setting business standards for themselves. They further explain that businesses have acquired their own codes of conduct, often in the wake of other companies' scandals. To this end, these types of self-imposed regulations were voluntary, informal, and comparatively simple. As regulation grew in the middle of the 20th century, a few companies had to discover and realize new ways to make sure they observed and obeyed the law. They necessitated a more formal and structured way to encounter the complexity of modern regulation. Most authors then agree on the fact that modern compliance and ethics programs were first created after the electricity industry's antitrust scandal in the early 1960s. A widespread bid-rigging and price-fixing conspiracy involving electrical equipment manufacturers such as General Electric and Westinghouse resulted in dozens of individuals and corporations convicted of antitrust violation. The importance of the case and related publicity of the first prison sentences passed on in the 70-year history of the Sherman Antitrust Act stimulated the advancement of antitrust compliance and codes of conduct and programs. In this period, companies in the highly and massively

regulated industries began internal compliance efforts, especially including the above-mentioned antitrust issues. With additional scandal, these compliance attempts would start to reach other industries (Biegelman, 2008). It is therefore obvious that the public outrage combined with governmental pressure encouraged businesses to adopt much-needed reforms. Last but not least example underlining the above introduced idea is the enactment of U.S. Foreign Corrupt Practices Act (FCPA). The FCPA has been enacted shortly after the Watergate investigation (conducted in 1977) which discovered that companies were paying bribes to foreign and domestic officials using funds maintained “off the accounting books”. Therefore, the Foreign Corrupt Practices Act makes it crime for American companies as well as individuals and organizations acting on their behalf to bribe any foreign government official in return for assistance in obtaining, retaining, or directing business.

The United States Sentencing Commission issued several organizational guidelines recommending minimum requirements for an effective compliance and ethics program. As the Sentencing Guidelines for Organizations focus (among other measures) on prevention and deterrence of law violations that include self-reporting and acceptance of responsibility, they gave companies a strong incentive to establish and maintain a truly effective compliance program, either to receive a lessened sentence or mandated as part of probation. The original seven steps to achieve effective compliance introduced by USSC in 1991 have been significantly enhanced by 2004 FSGO Amendments.

Compliance Challenges and Objectives

Ideally, a compliance program should not only be industry-specific, but also organization-specific. It should be tailored to fit the requirements of the organization concerned, its specific needs and the overall compliance requirements of the particular industry, as well as to reflect the compliance requirements imposed on all organizations and the laws they must follow. Each organization must therefore ensure that its compliance and ethics program is getting the individualized attention it needs to enhance the corporate compliance culture. The focus on individuality rather than on image of the compliance program itself produces great benefits such as the better employee productivity and also morale, higher profits, and stronger reputation among customers, investors, and other third parties. Such a compliance and ethics program can also help to catch various regulatory and other problems before they reach the level where they can significantly hurt the company, its culture and also, its stock price. Last but not least, with a strong and effective compliance and ethics program, an organization can have a more beneficial position when dealing with state prosecutors.

Running an ethical organization that places its values on compliance and ethics is not simply a good idea, it also makes a good business sense. Over the past years, a lot has been written about the importance of business ethics, the damage that can be caused by compliance failures and scandals, and about related legal requirements and benefits. However, less has been published about how an ethical business with strong corporate governance outperforms organizations that do not focus on ethics. Senior executives can damage their business and its future if they do not properly value ethics. Copeland (2002) mentions that the majority of corporate executives consider an ethics program as an expense that adds nothing to a company’s bottom line. Even more disturbing, some executives afraid that placing an emphasis

on business ethics could put their company at a competitive disadvantage. They are uncertain that ethics and profits are adoptable. Enlightened business leaders, however, are aware that building an ethical business culture is an influential means of maximizing shareholder value and developing business profits. In the end, ethics increases the bottom line. A strong link between organization's public commitment to ethics and its financial performance has been confirmed by a number of studies. According to Verschoor (2004), well managed companies that accept their ethical, social, and environmental responsibilities in a serious manner have powerful long-term financial performance than the remaining companies in the S&P 500 Index.

The challenges to developing an ethical culture are therefore more than great. In the first place, cultural change takes time and it cannot happen overnight. The compliance and ethical values might be possibly written very quickly, but culture is not imbedded until everyone acts on those values. To achieve a successful and lasting compliance culture, the program has to be more than simply using a check-the-box and it-is-done approach. It is the management's responsibility to drive a culture of true compliance and build it element by element until all employees understand every single component of the compliance and ethics program.

Warning Signs of Compliance and Ethical Failures

An excellent overview of several major indicators of ethical collapse has been identified by Jennings (2006). These seven signs include the pressure to maintain the business numbers, a culture of fear and silence, a bigger than life CEO and awe-struck direct reports that will not go against their leader, a weak board of directors, a practice of conflicts of interest, a belief that the organization is above the law, and that goodness in some areas such as corporate giving stones for evil in others. Although these seven signs are not a guarantee of an ethical collapse, they can definitely be used as potential announcers or indicators of compliance and ethical challenges.

Ethical Culture, Integrity and Proper Business Conduct

The famous major compliance and ethical failures of recent years resulted in various positive changes to corporate lives and cultures. Nowadays, integrity and accountability are publicly considered as key elements for every single organization and its management. Senior executives and other business leaders are increasingly confronted with ordinary and daily realities of business ethics and compliance. They must ensure compliance with the organization's internal rules and policies. In addition, all organizations must follow respective local and sometimes international laws; and moreover, in most of the legal orders there is usually a stricter regulation being applied to publicly held businesses. Some of these regulations even mandate the creation of compliance programs, other constitute stern restrictions from anti-bribery rules to free trade provisions. A flagship among these requirements is the idea of ethics. Ethics should lie at the heart of every corporate governance requirement.

Ethics include integrity and proper business conduct. It refers to standards and values by which an individual or an organization behaves and interacts with others. Aristotle (1962) declared that moral behavior is obtained by habituation and that without question moral behavior is fine. This principle has not changed despite years. Ethics and compliance are

clearly on the minds of senior executives and leaders as well as investors, public, and government. Thanks to many corporate scandals of the past decades, business ethics has become a hot topic. However, despite the increased awareness given to ethics and compliance, the problem has not been solved yet. Ethics and ethical behavior cannot be created and attained only by corporate expenditure; they both require a much deeper commitment of everyone in the organization concerned that can only be achieved through victimization of time, effort, and expenditure. As in many other areas of life and business, quality matters here far more than quantity. A commitment to ethical conduct cannot be accomplished by simply initiating a compliance and ethics program and then just checking the box that the process is complete. Building an ethical culture takes time. Integrity and character bring out the best in people and are, therefore, critical components of ethics and compliance. Yet, human beings are not flawless creatures and tend to lose strength and purpose from time to time. The significance of ethical conduct needs to be nurtured, reinforced, and repeated for many times lest people forget and move away from the course (Biegelman, 2008). Therefore, building and maintaining an effective compliance and ethics program requires smart decisions, deep commitment, and organization's willingness and also some budget – these are all necessary to achieve true compliance over the long term.

Ethics can also bring benefits in other areas such as hiring and retaining top quality employees. Unethical behavior not only affects a company's bottom line, but it also impacts its workforce. Such a behavior and attitude affect current employees as well as the company's ability to attract qualified staff. A study conducted by the consulting company LRN provides for a clear evidence of a link between the company's ability to build and support an ethical corporate culture, and its ability to attract, retain, and ensure productivity among U.S. employees. This study, among other facts, concludes that 94 % of employees state it is demanding that they work for an ethical company. Moreover, more than one third of respondents accounted leaving their job for ethical reasons and 56 % of respondents say their employer accepts ethics and corporate values in everything it does. In addition, 30 % of employees say their company simply toes the line by pursuing the law and company policies. Finally, 5 % declare they work at a company where they do what they are asked for and they are not motivated to ask questions about what is right or wrong, or they often perceive management and peers performing in questionable ways. To sum up, employees are very sensitive to business ethics. They are intensely aware of their organization's culture and pay attention to the tone set from the top and around them. Unethical behavior has a strong effect on employee's morale and distracts them from the company's business. One in four employees reported seeing unethical or even illegal behavior in the organization they work with; of those who saw unethical behavior, 89% said it affected them.

Establishing an Effective Compliance Program

During the past years, a well-documented and reasonably functional compliance and ethics program was adequate and enough but, today, it is not. The compliance program would no longer be only well-documented and reasonably functional, but also effective. Such an effective program should, at a minimum, contain a qualified compliance officer, comprehensive employee-training program (ideally a combination of face-to-face sessions and

eLearning), appropriate and functional system of internal policies, procedures and controls, and an independent audit function to test whether these are functional enough. Such a program should be understood as living efforts that need to continually evolve with time and circumstances. To be effective, however, one needs to combine compliance with ethics. Employees need to know more than the “dos” and “don’ts” of compliance; they should believe in the organization’s values and judge their conduct and decisions according to them. Ethical conduct goes beyond the perception and definition of compliance and deciding between right or wrong. Ethical conduct means choosing the best and most ethical course of conduct by applying the organization’s values. Fortunately, such a conduct can be taught to most employees regardless of a lack of prior ethics training.

A commonly recommended best practice for public and private companies to establish a meaningful compliance and ethics program is to design it according to the seven requirements outlined in the FSGO. Following these FSGO recommendations, however, does not ensure a fully effective ethics, compliance, and anti-fraud program. Quite the opposite – we can say it only means that the organization has met the minimum required components and effective compliance requires more than that. The “seven steps plan” for establishing a compliance and ethics program as described in the FSGO, therefore, serves as a pure backbone which should further be developed. To be more specific, the plan itself requires the organizations to take primarily the following actions: It should establish standards of conduct, reasonably capable of reducing the likelihood of criminal behavior; also, it should assign overall responsibility for compliance to a specific high-level officer or senior executive; it should not delegate discretionary authority to individuals with a history of illegal conduct or any other conduct inconsistent with the requirements of your compliance and ethics program; following this, it should communicate standards and procedures to all employees, agents and other third parties; in addition, it should establish comprehensive monitoring, auditing, and reporting plans and systems; and, it should enforce organization’s standards with discipline and, where possible, also incentives; and finally, it should take reasonable steps to respond to discovered criminal conduct, *i.e.* do not leave such findings without reaction.

Compliance Standards and Procedures

Each organization must establish relevant standards and procedures to prevent and detect criminal conduct and other failures and ensure compliance with the law. The cornerstone of those standards and procedures is usually an ethics code called code of conduct. This code is an integral component of the compliance and ethics program pointing out on organization’s values. Following criteria, namely public availability, tone at the top, readability and tone of the code, non-retaliation, commitment to stakeholders, risk topics, learning aids, and presentation and style should be taken into account when assessing the code’s effectiveness. The corporate ethics code should always fit the organization. Therefore, it might be very advantageous to involve the organization’s employees into assessing it. The biggest mistake is to simply “copy-paste” another organization’s code and substitute its heading with the name of the organization.

Organizational Leadership and a Culture of Compliance

The respective governing authority of each organization concerned (usually represented by the CEO, CFO, and/or the Board of Directors) should be fully aware of the content and operations of their compliance, ethics, and anti-fraud program. In addition, such a governing authority should also exercise reasonable oversight with respect to the implementation and effectiveness of the whole program. Respective individual(s) from within the highest levels of the organization concerned, such as the organization's top managers or heads of should be assigned with overall responsibility for the compliance and ethics program. In such a case, other individual(s) – from within the organization such as the compliance specialists – might be delegated with day-to-day operational responsibility for the program and report periodically to respective high-level personnel. To carry out such responsibility, these individual(s) may be given adequate resources, appropriate authority, and access to the governing body.

Reasonable Efforts to Exclude Prohibited Persons

The next step of the FSGO plan has been simply but very energetically described by Biegelman (2008). He concluded that the organization might use acceptable and satisfactory attempts not to involve within the considerable authority personnel who the organization knew or should have known through the exercise of due diligence, have engaged in illegal enterprises or other conduct conflicting with an impressive compliance and ethics program.

Training and Communication

Each organization should take reasonable steps to communicate regularly and especially practically its standards, procedures, and other important elements of the compliance and ethics program such as controls, plans and remedial actions. Apart from that, an effective training preferably the face-to-face one should be conducted. These training sessions should not only be provided to all members of the governing authority and other high-level leaders, but, generally, to every single employee of the organization and also, to its agents and where applicable to other third parties.

Monitoring, Auditing, and Evaluating Program's Effectiveness

The organization should take rational steps to evaluate the program's effectiveness. Besides, it should take other steps that ensure having and publicizing a system which include mechanisms that allow for anonymity or confidentiality of those employees and agents who report or seek for guidance regarding any potential or even actual criminal conduct without any fear of retaliation such as ombudspersons or hotlines. As Biegelman (2008) highlights, compliance will always begin and end with people. That includes everyone from the CEO to the newest intern. His words emphasize that people who are willing to speak up and be heard, even when it is culturally not popular to do so, are extremely valuable and necessary in terms of an effective compliance and ethics program. Senior executives must therefore ensure a corporate culture where employees are not afraid to blow the whistle and report wrongdoing and other potential violations of business conduct they are aware of.

A common mistake that a compliance and ethics program can make is to focus too much on the "easy" things and too little on the "hard" ones. It might be easy to do the training, prepare

and roll out a code of conduct, institute an external hotline, talk up the culture and tone from the top; however, it is much harder to beat areas such as discipline, audits, monitoring, incentives and the fact that the organization needs so-called corporate cops.

Performance Incentives and Disciplinary Actions

The organization's compliance, ethics, and anti-fraud program should be promoted and enforced consistently. This might be achieved through appropriate incentives to perform in accordance with the program's ethical basics and also through suitable disciplinary measures used in case that someone fails to take reasonable steps to prevent or detect such a conduct.

Response to Criminal Conduct and Remedial Action Plan

After criminal conduct has been revealed, the organization should take all possible and reasonable steps to respond to it appropriately and timely and to prevent further similar behavior in the future. This might be the case of modifying the respective components of the compliance program. This should not be done on an ad hoc basis only, but also periodically. The organization should therefore regularly assess the risk of criminal conduct and take appropriate steps to design, implement, and modify each compliance component to reduce the risk of criminal conduct identified through the above mentioned risk assessment.

International Compliance

It should be highlighted that in today's corporate world compliance goes beyond the geographical borders. This must be understood as a side effect of globalization of business. International compliance is therefore a necessity. The global nature of doing business, where organizations have various abroad subsidiaries, affiliates and frequent international vendors provide great opportunity but also a great risk. Both U.S. and UK laws reach all around the world and cover the actions of "their" corporations and employees, no matter where they are. Illegal actions relating to the FCPA or the UK Bribery Act can have major implications; there are severe penalties for those who violate the anti-bribery provisions of those acts. In addition, third party liability is another major concern as organizations are, in many foreign jurisdictions, held liable for any unethical or illegal actions of people they hire by their direct employees or agents. An appropriate solution might be represented by a strong global compliance and ethics program that ensures everyone knows what the rules are, what is currently going on and that an appropriate audit trail about who is doing what (particularly on the local level) is being tracked.

Fraud Prevention

What is Fraud?

Before moving to fraud prevention and related measures, one should know what fraud is. Fraud is the knowing misrepresentation of the truth or concealment of material fact to induce another to act to his or her detriment and a misrepresentation made recklessly without belief in its truth to induce another to act. Simply said, fraud is about stealing, cheating, lying, and, generally, lack of integrity. Preventing fraud is often much harder than one would originally assume, because human nature and a kind of people's greed guarantee that the society will always face the issue of fraud. Trying to stop all fraud is impossible; however, much can be done to limit its

effects. The key step to preventing fraud is to realize that it actually exists and limit its potential for harm. Fraud theory and prevention are necessary parts of organization's compliance program. One can conclude that fraud prevention requires compliance and compliance requires fraud prevention.

The Rouge Employee

A rouge employee refers to any employee who strays from hired responsibilities and commits fraud by attacking the company from within, creating notable financial and reputational harm. The interests of rouge employees are not in the straight line with the interests of their employers. Actually, they should not be regarded as real employees. True employees are committed to the mission of company and are part of the team in assisting the company to develop to even greater heights and outcomes (Biegelman & Bartow). Rouge employees are not supporting the common good and betterment of the businesses concerned. They are stealing and defrauding. Following this, they line their pockets to the disadvantage and impairment of their employers. Such a rouge employee might be found at any level of the organization concerned. Media are typically portraying them as senior executives or leaders (very often even the CEO or CFO). It is obvious that these positions attract the most media attention, however, rouge employees can really be found anywhere in the company. Very often, a so-called long-time, loyal, lower level employee who stays below the radar screen will be the offender. Greater attention, management, and planning in terms of internal controls and fraud prevention are therefore essential in lessening or eliminating the damages caused by employee fraud and criminality.

Fraud Theory and Prevention

The Association of Certified Fraud Examiners (ACFE) reports that "*The average organization loses around 5 percent of its annual revenue to frauds.*" Such a statistic alone might be reasonable enough for organizations to implement a robust compliance, ethics, and fraud prevention program. Although this number might look – at the first sight – like a moderate one, the cumulative losses to businesses are astonishing. The logical question which goes in hand with such a fact is therefore "Why do people commit fraud?" There are many theories trying to explain this behavior. One centers solely on the elements of motive, opportunity, and rationalization. Lessening or removing opportunity might be seen as an effective way to fight fraud. This can be easily done by improved and strengthened system of internal controls and accountability. If employees know that they will be held responsible for their possible acts of fraud, the likelihood to commit it should logically come down. Understanding the importance of strong and effective fraud prevention program is critical for any organization that wishes to achieve a true culture of ethics and compliance.

A strong and effective fraud prevention program demands a system of rules that minimizes the likelihood of fraud occurring whilst maximizing the possibility of detecting any fraudulent activity. The potential of being caught most often outweighs the commitment of fraud itself. Mainly because of this principle, the existence of a thorough control system is essential to fraud prevention. In terms of fraud prevention, organizations must be proactive rather than reactive. Fraud prevention is much more than only a favorable business practice; it tends to be

a requirement today. Companies confront various risks, some of which are possibly damaging and destructive. Among these risks, the issue of vicarious liability is very noticeable. Corporations and other organizations can be regarded responsible for criminal acts committed as a matter of organizational policy. They may also be held liable for the criminal acts of their employees if those acts are executed in the course and in the scope of their employment for the goal of assisting and improving the corporation (Biegelman & Bartow, 2012). To sum up, the financial risks from fraud losses, risks to reputation, shareholders' lawsuits, federal prosecution, fines, and convictions for fraud are all good reasons to incorporate a strong fraud prevention program.

Although it is almost a common knowledge that people and organizations commit fraud, it is often not exactly understood why they do it. Therefore, understanding the motive behind fraudulent behavior is extremely important in preventing it. There are three critical elements coming together when fraud occurs including motive, opportunity, and rationalization. For an employee who commits fraud, any of those elements is necessary. The absence of any one of those will not allow him/her to do it. Hence, every corporate executive should get familiar with this "triangle relationship".

Financial pressure is the most often motive for people and organizations to commit fraud, the so-called driving force behind a person changing from a law-abiding citizen to corporate fraudster. It typically implies an emotion or desire. Most of the frauds committed under a financial pressure are greed related, *i.e.* they include an immediate financial need, debts, poor credit, a drug or gambling addiction, family pressure *etc.* Sometimes revenge and ego play a significant role. An employee may feel anger against the organization for some perceived wrong and may try to settle such emotion by defrauding the company. Sometimes the motive is "only" a simple desire to beat the system. Some people think they are smarter than anyone else in the organization concerned and believe that no one, not a single manager, specialist, or even a senior executive can stop them. Pressure to perform is another frequent motive for fraud – sometimes the offenders commit fraud just to help to improve the company's financial results, plans, or other numbers. Emotional instability might be considered as a motivating factor; however, this one is not that frequent.

Opportunity is the encouraging circumstance that allows fraud to occur. The level of opportunity that an employee has to commit fraud is usually determined by his or her position in the company and access to relevant systems. Poor internal controls enhance the opportunity for fraud. An employee who can both open a new vendor and process its invoices provides an example of weak internal controls and a high opportunity for fraud. Strong separation of duties and oversight lessen the opportunity to commit and also succeed at fraudulent activity.

Rationalization explains how the fraudster justifies his or her inappropriate actions. When the elements of need and opportunity come together, the fraudster might be convinced that what occurred can never be perceived as wrong. Fraudsters often think of themselves as clear and honest human beings, *i.e.* rather than considering themselves as criminals who defraud the company and its shareholders; they tend to feel like victims.

The element of capability also plays a significant role and might be added among the above-introduced elements of motive, opportunity, and rationalization. Capability includes the fraudster's personality including knowledge, creativity, ego, self-confidence, and ability to

handle stress. While opportunity focuses on the employee's role and access to commit fraud, this factor takes it one step further. The fraudster is ought to be intelligent enough to perceive and utilize internal control's weakness and to employ position, function, or authorized access to the greatest advantage (Dorminey, Fleming, Kranacher, & Riley, 2010).

Internal Controls and Anti-Fraud Programs

An effective way to ensure a culture of ethics and compliance is through a well-designed internal control and anti-fraud program. A principal element of any antifraud program tends to be an appropriate code of conduct (or other ethics policy) that can support an organization to arrange a tone of honesty and integrity. The code should be effectively and adequately communicated to all employees. Before fraud related risks can be mitigated, they must be recognized and properly quantified. These two steps guide to form a suitable method of risk mitigation. There are various methods in use to administer a risk assessment (Biegelman & Bartow, 2012).

In 2002, the American Institute of Certified Public Accountants (AICPA) accredited a study to provide guidance on preventing and detecting fraud. The result, *Management Antifraud Programs and Controls*, has already been released in November 2002. The overall message of this document is that organizations should take proactive steps to avoid and hinder fraud to protect their financial integrity, their reputation, and their future. The *Management Antifraud Programs and Controls* is an exceptional and remarkable 14-step program that any organization can implement to detect and prevent fraud. The study recommends that any organization that fights against fraud should particularly take the following three fundamental mitigation actions, namely creating a culture of honesty and high ethics, evaluating anti-fraud processes and controls, and developing an appropriate oversight process.

It is the organization's responsibility to create a culture of honesty and high ethics. The acceptable behavior and expectations for each employee must be clearly and precisely communicated throughout the entity. Creating a culture of honesty and high ethics should therefore include setting the tone at the top, creating a positive workplace environment, hiring and promoting appropriate employees, training, confirmation, and discipline. Organization's expectations about the consequences of committing fraud and actions that might be clearly and repeatedly communicated throughout all levels of the organization is concerned. If a violation occurs and an employee is disciplined, it can be very helpful to communicate this fact across the company, e.g. on a no-name basis.

In terms of evaluating anti-fraud processes and controls, the *Management Antifraud Programs and Controls* recommends that organizations should be proactive in reducing fraud opportunities mainly by identifying and measuring applicable fraud risks, taking appropriate steps to mitigate them, and implementing and monitoring respective internal controls (both preventive and also detective) as well as other effective deterrent anti-fraud measures.

Oversight can take many forms. It can also be performed by many individuals within and outside the entity under the overall oversight of the audit committee and/or the board of directors. The key steps under the third section ("Developing an Appropriate Oversight Process") of the *Management Antifraud Programs and Controls* are audit committee, management, internal auditors, independent auditors, and certified fraud examiners.

Ensuring Future Compliance

There are many reasons to establish an effective compliance and ethics program and one of the most beneficial one is to be able to monitor and positively influence internal behavior in order to achieve desired results. However, the practical experience and reality may differ in some cases, as not all employees will independently follow the rules and presence of bad employees can negatively influence others around them. Other reasons for effective compliance and ethics program's establishment reflect the legal framework in which companies must operate. The USSC Federal Sentencing Guidelines for Organizations explicitly mandate that prosecutors take into account the existence (or lack thereof) of an effective compliance program, providing opportunities for reduced sentences if such a program exists. In addition, other laws and regulations give companies strong incentives and reasons to put a compliance program in place and to ensure that an existing program is effective and runs as smoothly as reasonably possible. An organization should therefore confirm management's responsibility for establishing and maintaining adequate internal controls structure and procedures as well as evaluating the effectiveness thereof.

One of the key elements of ensuring future compliance is a correct response to identified violations of business practices. A professional and predictable process for responding to allegations of misconduct and conducting internal investigations should be in place in every organization that wishes to incorporate and maintain a truly effective compliance and ethics program. That is why the organizations should bring in experienced investigators to conduct and resolve issues of fraud and non-compliance. By doing that, they might gain credibility and required (not only compliance) effectiveness. The senior executives and other leaders must be able to answer their employees' questions on how they will ensure that the discovered violation or fraud will never occur again. The best assurance towards this is an open communication and a culture of raising and escalating concerns. Non-compliance can be lessened or even stopped by providing employees and others outside the organization an opportunity to break the chain if fraud or corruption exists. A well-communicated hotline together with a strong and independent audit committee and professionally staffed compliance and human resources might be considered as key elements for successful implementation and subsequent communication of applicable compliance measures. The best insurance that the culture of compliance will be effectively supported for the future is therefore open communication and resources to escalate issues.

Following this, Patrik J. Gnazzo, a Senior Vice President, Business Practices and Chief Compliance Officer at CA, Inc. provides for five practices for an excellent compliance program (Biegelman, 2008, p. 104). These practices indicate that the head of compliance needs to be seen at the table with other top executives; the Chief Compliance Officer (CCO) must be independent with a solid reporting line to the audit committee and a dotted line to the general counsel; an organization must have an open communication program where anyone can report an allegation or issue through many different channels; the organization must have a strong investigative response and process for allegations; and the organization should have so-called Business Practice Officers embedded in the offices worldwide.

To sum up, in terms of ensuring future compliance, it should be highlighted, that the measure of an organization's success is how it deals with trouble, not that it never had any trouble to begin with.

The Final Notes towards the Road to Compliance

Ethics, integrity, accountability, and a strong leadership are key elements of a culture of compliance. They can even be seen as constant for any successful organization. When a business talks about increasing shareholder value, return on investment and driving revenue, one of the best investments is to establish and maintain an effective compliance program. Best in class compliance program is a real competitive advantage. Compliance then is a solution.

A culture of reasonable ethics and true compliance certainly takes time to develop. It can be a super-long journey to reach the highest level of ethical standards as well as to fulfill all applicable compliance requirements. All the positive changes in legislation, regulation, initiatives, policies, and procedures have taken years to clarify the purpose of improving corporate governance. The legal and compliance requirements have significantly changed the way businesses operate. Today's senior executives and leaders, employees, and other stakeholders must be aware of these requirements and their impact on a culture of compliance.

In terms of building and maintaining an effective compliance program, the organizations meet a wide variety of different laws, regulations, and standards. Some of them provide the organizations with guidance on how to best construct a truly working program or establish the minimum requirements demanded by the law; others include industry standards or organizational certification requirements. As the topic of compliance is so broad, this paper cannot possibly cover every aspect of every law. For example, the areas of health and safety, information security, competition law compliance, trade controls, environmental impact, and privacy regulations have specific compliance and legal requirements. This paper tried to cover most of the key points but the world of compliance is so vast that even a book could not hope to be fully comprehensive in anything less than several volumes. However, understanding compliance from the concepts introduced in this paper provides the readers with the basics for effective implementation and maintenance of compliance and ethics programs no matter what particular law or regulation applies.

To underline the compliance principles presented in this paper, more impressive words than the ones said by W. C. Stone could hardly be found: "Have the courage to say no. Have the courage to face the truth. Do the right things because they are right. These are the magic keys to living your life with integrity."

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