

Federal Sentencing Guidelines- Requirements for Corporate Compliance and Ethics Programs

By Mary Lee Brown

The U.S. Sentencing Commission (USSC) on Friday April 30, 2004 sent to Congress significant changes to the federal sentencing guidelines (FSG). The changes will take effect November 1, 2004 unless Congress disapproves them during the six-month review period. The changes of interest to audit and compliance professionals are the amendments to Chapter 8, which address sentencing guidelines for organizations. The amendment elevates the seven required elements or criteria for an effective program, previously set forth in commentary, into a separate guideline. The revision also expands and strengthens the criteria, introducing additional rigor generally and imposing significantly greater responsibilities on the organization's governing authority (e.g., Board of Directors) and executive leadership.¹ The FSG have a broad reach, in that "organizations" are defined to include, among others, non-profits. This category encompasses colleges and universities. The amendment is in the Sarbanes-Oxley Act, Section 805, which response directed the USSC to review and amend the organization guidelines and related policy statements to ensure they are sufficient to deter and punish organizational misconduct.

Background

The USSC, an independent agency in the judicial branch the federal government, was organized in 1985 to develop a national sentencing policy for the federal courts. The resulting sentencing guidelines structure the courts' sentencing discretion to ensure that similar offenders who commit similar offenses receive similar sentences. In

November 1991 sentencing guidelines went into effect for organizations. A fundamental component of those guidelines is a compliance program that meets the seven minimal requirements that have become the hallmarks of an effective program.

Changes

Most of the amendment is an expansion of previous guidelines. The definition of an effective compliance and ethics program has been expanded to require, in addition to the exercise of due diligence to prevent and detect criminal conduct, that the entity must promote an organizational culture that encourages a commitment to compliance with the law. Expansions and changes to each of the original seven minimum requirements for due diligence are summarized below:

1. Standards and procedures to prevent and detect criminal conduct: There is no substantial change to this requirement except to note that "Standards and procedures" encompass standards of conduct and internal controls that are reasonably capable of reducing the likelihood of criminal conduct.

2. Overall Responsibility to Oversee Compliance: This part is expanded to include a requirement that the governing authority (i.e., Board of Directors) shall be knowledgeable about the content and operations and assume responsibility for oversight with respect to implementation and effectiveness of the compliance and ethics program. The individual(s) with day-to-day responsibility for the program must "be given adequate resources, appropriate

authority and direct access to the governing authority or an appropriate subgroup of the governing authority.”

3. Due Care in Delegation of Authority: This replaces the previous provision that personnel with substantial authority be screened for their “propensity to engage in violations of law” with the requirement that an organization “use reasonable efforts not to include within substantial authority personnel of the organization any individual whom the organization knew, or should have known through the exercise of due diligence, has engaged in illegal activities or other conduct inconsistent with an effective compliance and ethics program.”

4. Communication, Training and Education: It extends the training requirement to upper levels in the organization, including the governing authority and high-level personnel, in addition to all employees and agents. Furthermore, the communication and training must be ongoing with periodic updates.

5. Monitoring, Auditing and Reporting Systems: This section expands the existing requirement regarding reasonable steps to achieve compliance. The guideline mandates the use of auditing and monitoring systems designed to detect criminal conduct, adds the requirement to periodically evaluate the effectiveness of compliance and ethics programs and, more specifically, expands the focus of internal reporting to either “report or seek guidance regarding potential or actual criminal conduct.” It also replaces the existing reference to “reporting systems with out fear of retribution” with the more specific requirement that the organization must have “a system which may include mechanisms that allow for anonymity or confidentiality.”

6. Enforcement and Discipline: This par broadens the exiting criterion by adding that standards also be encouraged through “appropriate incentives to perform in accordance with the compliance and ethics program.” In essence this requirement encompasses both a duty to promote proper conduct as well as a duty to sanction improper conduct.

7. Appropriate, Consistent Response: There is no change to this requirement. The guideline retains the obligation to take reasonable steps, after an offense had been detected, to respond to and prevent further similar criminal conduct, including making any necessary modifications to the program. A new guideline added by the amendment requires an organization to periodically assess the risk of occurrence of criminal conduct and take appropriate step to design, implement or modify the requirements of its program to reduce the risk identified. In summary, the changes in these guidelines reflect a developing trend toward more explicit recognition of compliance programs as an enterprise-wide operational responsibility. Further information and a reference to the guidelines may be found at: <http://www.uscc.gov/guidelin.htm>

Note:

¹Desio, Paula. “An Overview of the Organizational Guidelines,” United States Sentencing Commission [Online], May 27, 2004, Available: <http://www.uscc.gov/guidelin.htm>

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