
The Federal Sentencing Guidelines for Organizations—A Blueprint for an Effective Internal Control System

SCCE Utilities and Energy Compliance and
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Presentation Overview

- Evolution of the Federal Sentencing Guidelines for Organizations (FSGO) from Punishment Mitigation Device to Compliance and Ethics Internal Control System.
 - How the Guidelines themselves have Changed
 - Principal External Contributing Factors
- Examination of Important FSGO Compliance and Ethics Components
 - Guidance from the Sentencing Commission (USSC)
 - Implementation and Practice Points
- Case Studies—Lessons Learned

Initial Development of the FSGO

- Derivation—The Sentencing Reform Act of 1984
 - Principal purposes to reduce sentencing disparity, deter crime
 - U S Sentencing Commission to develop sentencing guidelines for individuals and organizations
- Initial FSGO of 1991 pioneered concept of Sentencing Punishment Mitigation for Effective Compliance Program and Cooperation
 - Seven Key Features

Principles of an Effective Compliance Program—Seven Key Features

- 1. Establish Standards and Procedures to achieve and maintain Compliance with the law.**
- 2. Ensure High Level Responsibility for implementation.**
- 3. Avoid delegating responsibility to known problem persons.**
- 4. Communicate/train effectively all personnel and agents.**
- 5. Monitor/audit effectively; establish Internal Reporting System/Hotline.**
- 6. Discipline violators appropriately but effectively.**
- 7. Respond promptly to problems, Remedy appropriately, Strengthen program.**

Key Objectives of the FSGO Approach

- Immediate Goal– Reduce sentencing punishment.
- Intermediate societal objective– Incentivize businesses to develop Internal Control Systems to achieve and maintain Compliance.
- Long term societal objective—Reduce, prevent crime; promote Good Corporate Citizenship and more Ethical Business Cultures.

Subsequent FSGO Amendments

- 2004 Updating and Strengthening Amendments
 - Created more visible, stand alone Guideline: **Section 8B2.1**, describing more detailed elements of an Effective Compliance and Ethics Program.
 - Expressly joined Ethics and Compliance functions, emphasizing importance of Organizational Culture.
 - Emphasized importance of Risk Assessments.
 - Established express Governing Authority Responsibilities.
 - Strengthened all program elements.

Subsequent FSGO Amendments (cont.)

- 2010 Amendments
 - Clarified expected responsive and remedial actions when violations occur.
 1. Restitution, remediation
 2. Voluntary disclosure
 3. Compliance program review, possible outside expertise
 - Emphasized importance of CCO Direct Reporting, Independence
 1. Direct reporting to governing authority re: criminal conduct occurrences and at least yearly re: compliance program operation.
 2. Policy expressed in context of judging program as effective even if high level person involved in wrongdoing.
 - Fact of Whistleblower Report does not render program per se ineffective.

External Forces Reinforce Importance of FSGO Compliance Programs

- The Courts
- The U S Congress
- Federal Regulatory Agencies
- The Securities and Exchange Commission
- The U S Department of Justice

The Courts as an External Contributing Force

- ***In Re Caremark Int'l. Inc. Derivative Litig.***, 698 A.2d 959 (Del. Chancery, 1996)
 - Shareholders sued Board (unsuccessfully) for failure to prevent and confront unlawful conduct by health care company.
 - Chancellor Allen admonished governing authorities to heed FSGO compliance program features.
- ***Burlington Industries v. Ellerth***, 524 U. S. 742 (1998)
 - U.S. Supreme Ct recognized value of effective compliance programs and prompt corrective action as part of affirmative company defense to sexual harassment suit under Title VII of Civil Rights Act of 1964.
- ***United States v. Booker***, 543 U. S. 220 (2005), and its progeny
 - Changing sentencing guidelines from presumptively mandatory to advisory has not diminished their importance as internal control system template.

United States Congress as a Contributing Force—Laws Furthering Compliance

- **Foreign Corrupt Practices Act of 1977.**
 - Lead to Corporate Codes of Conduct prohibiting overseas bribery.
 - Enforcement priority today for SEC, DOJ.
- **Sarbanes Oxley Act of 2002.**
 - Public companies must report re: ethics codes for financial, accounting officers.
 - U. S. Sentencing Commission directed to review, strengthen FSGO.
- **Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.**
 - 2000+ pages of law; approx. 50% implementing regulations issued to date.
 - No direct mention of compliance programs.
 - Strengthened hand of whistleblowers, providing indirect impetus to bolster compliance program internal reporting and investigation systems.

Program and Regulatory Agencies as Contributing Forces

- **Environmental Protection Agency**– recognizes value of effective compliance programs and cooperation as bases to refrain from DOJ Criminal or Civil Enforcement.
- **Equal Employment Opportunity Commission** – similar.
- **Nuclear Regulatory Commission; Federal Energy Regulatory Commission; North American Electric Reliability Corporation; 8 Regional Utility Regulatory Agencies.**

Utility and Energy Regulators (NRC, FERC,NERC, Regionals)

- Employ concepts, approaches similar to FSGO compliance model steps in their efforts to ensure compliance w/ applicable standards and to promote safe and reliable operation.
- These include:
 1. Identifying risks.
 2. Sharing best practices.
 3. Compliance education.
 4. Hotlines for licensees.
 5. Encouraging licensees to internally audit and self-report violations.
 6. Prompt remedial actions, cooperation w/ enforcement offices.

The Securities and Exchange Commission as a Contributing Force

- Outlined value of effective compliance and ethics program and cooperation in the *Seaboard* case.
- Principles recently applied in foreign bribery and financial fraud enforcement actions/settlements.

U.S. Department of Justice Enforcement as Contributing Force

- Principles of Federal Prosecution of Business Organizations (Thompson/McNulty, etc. Memoranda).
 - Prosecution decisions based significantly on compliance program effectiveness, cooperation (including voluntary disclosure).
 - DOJ evaluation of Compliance Programs

U.S. DOJ Compliance Program Evaluation Considerations

1. Program designed for maximum effectiveness, most likely risks?
2. Applied earnestly and in good faith? Does it work?
3. Supported with adequate staff and resources?
4. Employee awareness of program; effectiveness of training.
5. Effective internal reporting system for employees and to governing authority.
6. Sufficient internal audits; accurate results.
7. Violators effectively disciplined.
8. Violations promptly investigated, disclosed.
9. Program deficiencies promptly remedied.
10. Compliance program functions sufficiently independent.

U.S. DOJ Compliance Program Evaluation Considerations (Cont.)

Favorable DOJ consideration can lead to:

- Decision not to prosecute, or to only prosecute individuals.
- Negotiation of non-prosecution or deferred prosecution agreement.
- Civil fine only, or leave matter to regulatory agency.

Recent DOJ Enforcement Priorities, Attitudes Toward Compliance

- Priorities include foreign bribery (FCPA), antitrust, large-scale white collar frauds (including financial fraud and health care fraud).
- Increased DOJ recognition that strong compliance programs have value.
 - Help prevent crime.
 - Ensure misconduct more quickly uncovered, handled responsibly.
- Increased emphasis on independence of compliance function, CCO direct reporting to Board.

Key FSGO Components

1. Ethics and Culture
2. Risk Assessments
3. Training
4. Remedial Actions
5. Compliance Program Independence

Key FSGO Components—1. Ethics and Culture

- Since 2004, FSGO state 2 Overarching Requirements for an Effective C&E Program:
 1. Due Diligence to Prevent and Detect Violations.
 2. Promotion of an organizational culture that encourages ethical conduct and commitment to compliance with the law.
Section 8B2.1(a).
- Practice Points: Ethical conduct derives from organization's Core Values
 - Nominally expressed in Code of Conduct, Mission Statement, Board and Management statements.
 - Practically embodied in how the organization operates daily.
 - “Tone” –What matters most are not words but actions so that tone becomes Ethical Culture and Standard Operating Procedure.

Key FSGO Components—2. Risk Assessments

- Since 2004 FSGO require Periodic Risk Assessments with findings used to design, implement, or modify each C&E program element. **Section 8B2.1(c), App. n. 7.**
- Practice Points—Periodic risk assessments should cover:
 - Nature and seriousness of likely misconduct.
 - Particular risks associated w/ nature of business.
 - Particular risks associated w/ prior org. history.
 - Risks should be prioritized.
 - Ongoing, effective risk assessments are of heightened importance in heavily regulated U&E companies to protect public health and safety.

Key FSGO Components—3. Training

- Since 1991, FSGO require ongoing, effective training to communicate org. standards and procedures to all personnel and agents. **8B2.1(b)(4)(A).**
- Training, appropriate for org. roles, responsibilities must include Boards, senior management. **8B2.1(b)(4)(B).** 2004 amend.
- Practice Points:
 - Org. should document education (whether conducted on-line or in person), employee completion, test for understanding, audit for performance, remedy deficiencies.
 - Maintain records.

Key FSGO Components—4. Remedial Actions

- FSGO require reasonably prompt steps to investigate detected misconduct, respond appropriately, prevent reoccurrence (including necessary modifications to strengthen C&E Program). **Section 8B2.1(b)(7), App. n. 6.**
- Remedial actions generally will include restitution or appropriate harm remediation.
- Practice Points: Self reporting and cooperation are organization's call but get heavy emphasis from regulatory agencies, DOJ.
- Preventive actions generally include assessing, modifying C&E Program, discipline of individual violators, outside professional assistance (often necessary to satisfy regulators, DOJ).

Key FSGO Components—5.Compliance Program Independence

- As amended in 2004 and 2010, FSGO emphasize strength and independence of C&E function.
Section 8B2.1(b)(2), App. n. 3.
 - High level responsibility for C&E Program.
 - Periodic (at least yearly) reporting to management and Board.
 - Adequate resources, authority, access to governing authority.
- FSGO strongly suggest direct reporting for CCO to governing authority or subgroup charged w/ compliance oversight.
Section 8B2.5(f)(C)(i), App. n. 11.
 - Prompt reporting to Board re: criminal conduct.
 - At least yearly reporting on implementation, effectiveness of C&E Program.
- Practice Point: Compliance independence increasingly important to DOJ, others.

Case Study 1—Griffiths Energy International, Inc.

- Small, privately held Canadian oil and gas company.
- Plead guilty to bribery: Agreed to \$10.35 M penalty; largest fine RCMP has collected under Canada's Corruption of Foreign Public Officials Act.
- High-level co. official paid bribe to a company owned by wife of Chad's ambassador to Canada. (Co. Counsel had advised against paying off the ambassador.) Purpose to get production deals in Chad.
- No evidence of compliance program. Griffith's new management team uncovered the bribes, created special investigative committee, self-reported.

Source: Calgary Globe and Mail, 1/22/2013

Case Study 2—Parker Drilling

- Houston, TX-based oil and drilling company.
- SEC, DOJ investigations in 2008 alleged FCPA violations re: company business in Kazakhstan, Nigeria.
- Office of Foreign Assets Control reviewed case, recently decided not to punish the company. Why not?
- Company hired Dan Chapman, currently CCO and Counsel, to conduct internal investigation and establish integrated, robust C&E program.
- Program features new policies, Code, training, reporting systems, and separate, independent compliance department (instead of under finance and legal).

Source: Ethikos, 1/30/2013

Case Study 3—Morgan Stanley

- Large, Wall Street Investment Co., operating internationally.
- Managing director Garth Peterson charged with bribery of Chinese official in effort to secure real estate business in Shanghai.
- Peterson agreed to punitive settlement w/ SEC; Plead guilty to DOJ criminal charge.
- SEC, DOJ both decided not to prosecute Morgan Stanley. Why not?
- Company compliance officer multiple times warned Peterson of FCPA violations. He circumvented. Company had in place a comprehensive internal control system and subsequently strengthened it.
 - Thorough internal investigation.
 - Full cooperation w/ SEC, DOJ.
 - Changes in C&E program included new CCO, move reporting from Legal to Operational Heads.

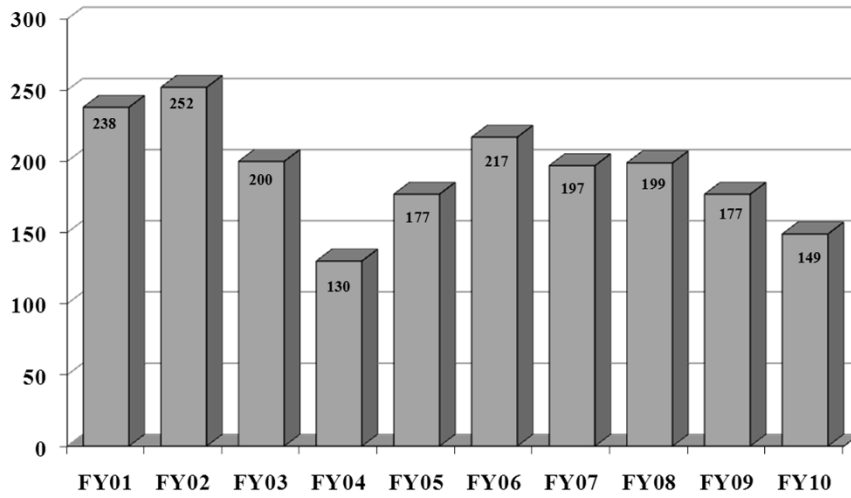
Multiple Sources

Summary

- FSGO have evolved over 2+ decades from punishment mitigation at sentencing to a template for all forms of compliance programs (criminal, civil, ethical misconduct).
- Elements of an effective C&E Program are applicable to all risk areas and types of violations.
- The FSGO continue to represent the **best fundamental model to achieve Compliance and Ethical behavior**-one that is industry flexible and internationally recognized.

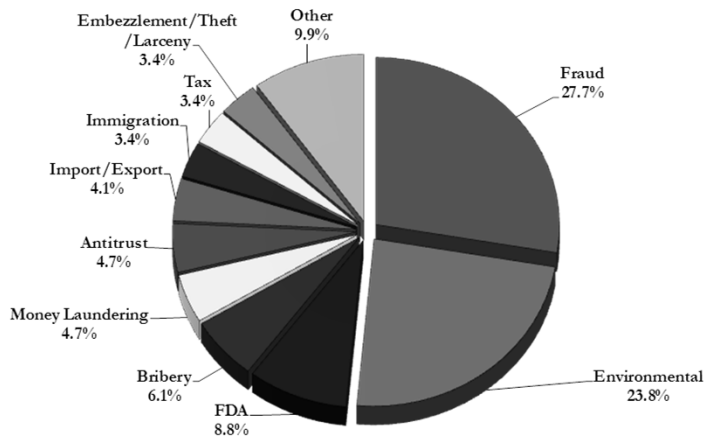
Organizational Sentencing Data

Number of Organizational Cases FY01-FY10



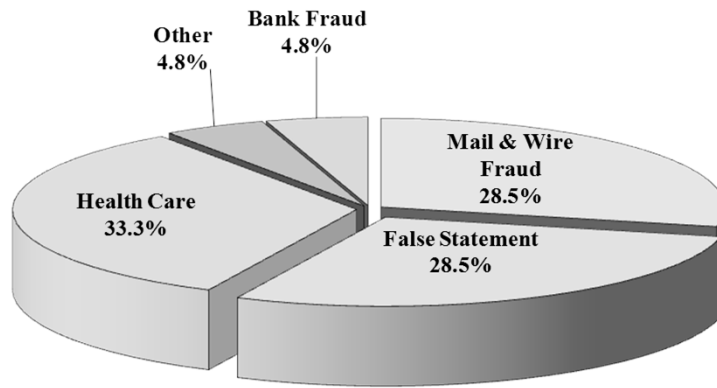
SOURCE: United States Sentencing Commission, 2001-2010 Sourcebook of Federal Sentencing Statistics.

Primary Offenses of Organizational Cases FY10



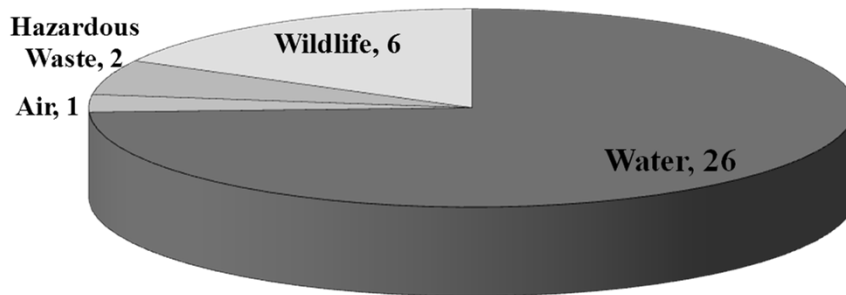
SOURCE: United States Sentencing Commission, 2010 Sourcebook of Federal Sentencing Statistics. The Environmental category includes the following offense types: Environmental-Water Pollution, Environmental-Air Pollution, Environmental-Hazardous/Toxic Pollutants, and Environmental-Wildlife.

Fraud Offenses in Organizational Cases FY10



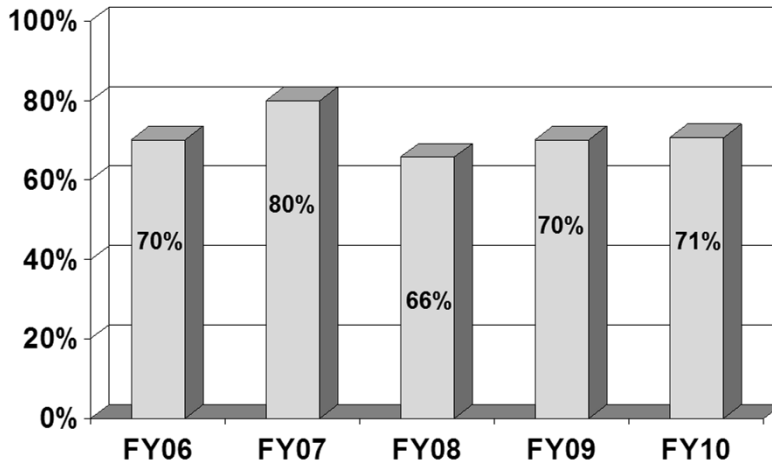
SOURCE: United States Sentencing Commission, 2009 Datafile.

Number of Environmental Organizational Cases FY10



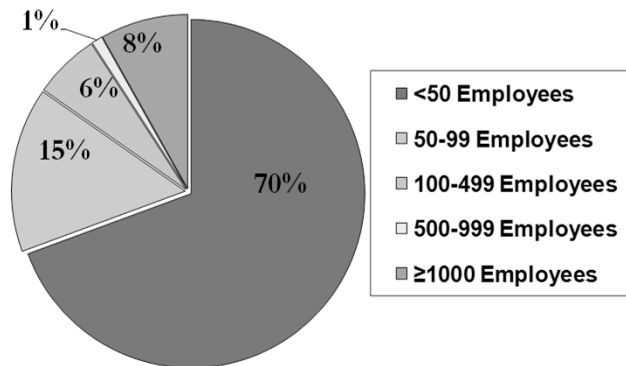
SOURCE: United States Sentencing Commission, 2010 Sourcebook of Federal Sentencing Statistics

Percentage of Organizational Cases Receiving Probation Fiscal Year 2006-2010



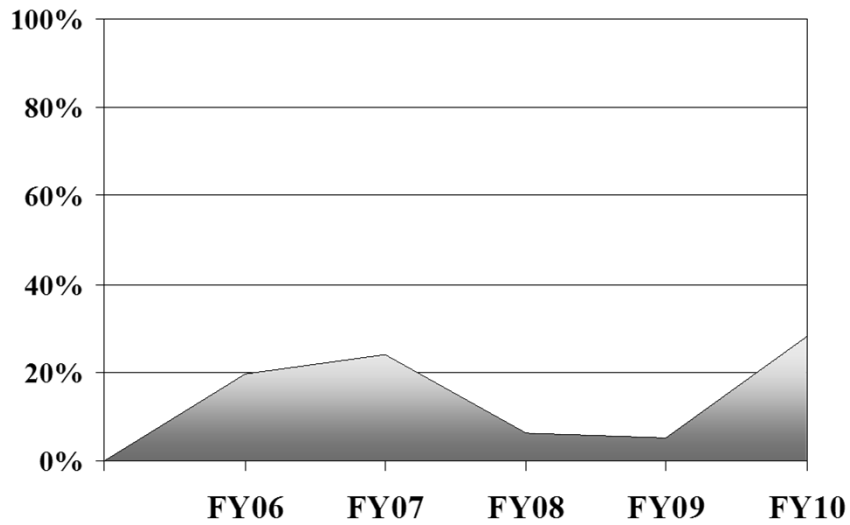
SOURCE: United States Sentencing Commission, 2006-2010 Sourcebook of Federal Sentencing Statistics.

Size of Organizations Sentenced By Number of Employees in Fiscal Year 2010



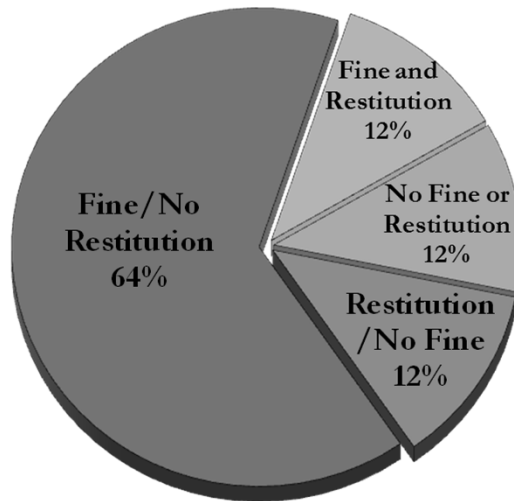
SOURCE: United States Sentencing Commission, 2010 Datafile

**Percentage of Organizational Cases With Court Ordered Compliance / Ethics as Component of Sentence Fiscal Year
2006 - 2010**



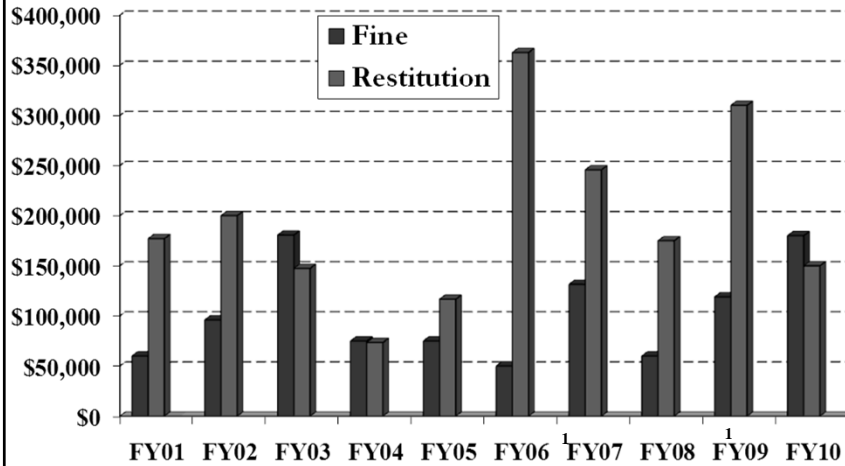
SOURCE: United States Sentencing Commission, 2006-2010 Sourcebook of Federal Sentencing Statistics.

Types of Monetary Sentences FY10



SOURCE: United States Sentencing Commission, 2010 Sourcebook of Federal Sentencing Statistics.

Median Fine and Restitution for Organizations FY01-FY10



FY04 data consists of only pre-Blakeley data from October 1, 2003 through June 24, 2004. FY05 data consists of only post-Booker data from January 12, 2005 through September 30, 2005. SOURCE: United States Sentencing Commission, 2001-2010 Sourcebook of Federal Sentencing Statistics.

Top Ten Organizational Fines and Restitution Orders by Offense Type (Millions of Dollars) - Fiscal Year 2010

Fines		Restitution	
Food & Drug	\$1,195.0	Fraud	\$200.0
Bribery	\$400.0	Fraud	\$200.0
Antitrust	\$38.0	Fraud	\$200.0
Antitrust	\$30.0	Fraud	\$16.2
Bribery	\$29.1	Money Launder	\$1.5
Racketeering	\$28.2	Bribery	\$.8
Bribery	\$27.4	Fraud	\$.8
Bribery	\$17.1	Fraud	\$.7
Bribery	\$14.1	Fraud	\$.7
Antitrust	\$9.0	Fraud	\$.6

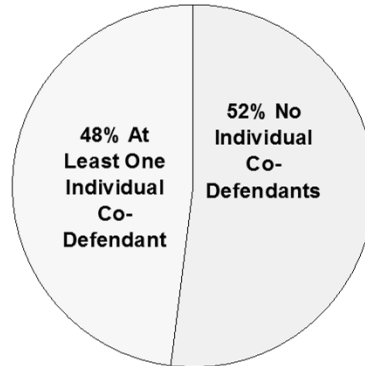
SOURCE: United States Sentencing Commission, 2010 Datafile.

Relationship of Individual Offender Cases to Organizational Cases in Fiscal Year 2009 & 2010

FY09



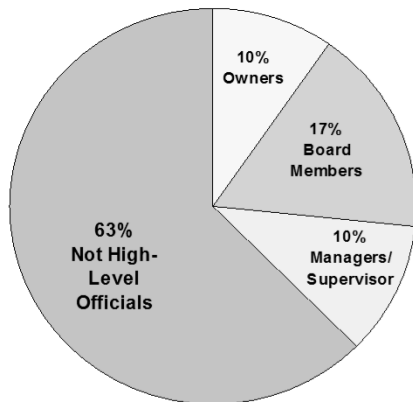
FY10



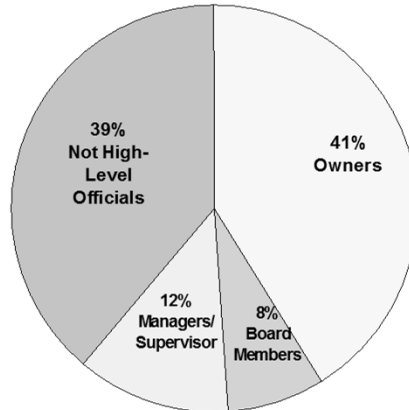
SOURCE: United States Sentencing Commission, 2009 and 2010 Datafile.

Percentage of Individual Offenders Who Were “High-Level” Officials of Co-Defendant Organizations Fiscal Year 2009 & 2010

FY09

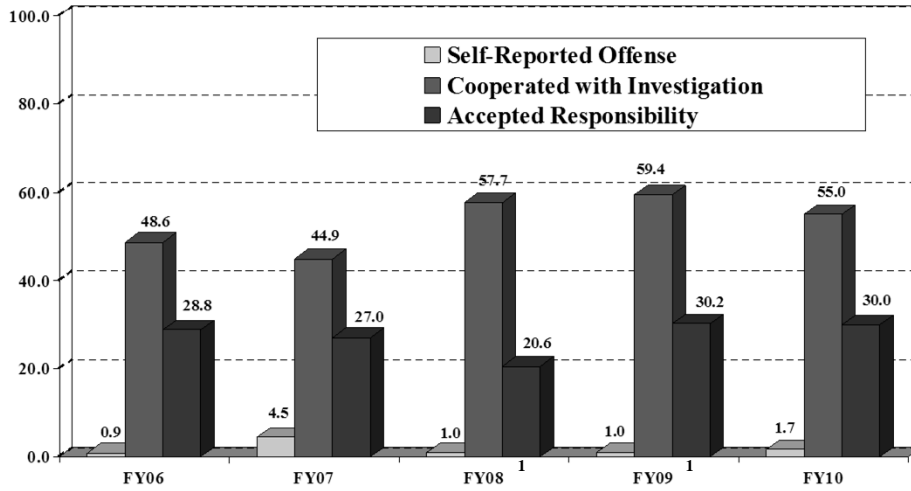


FY10



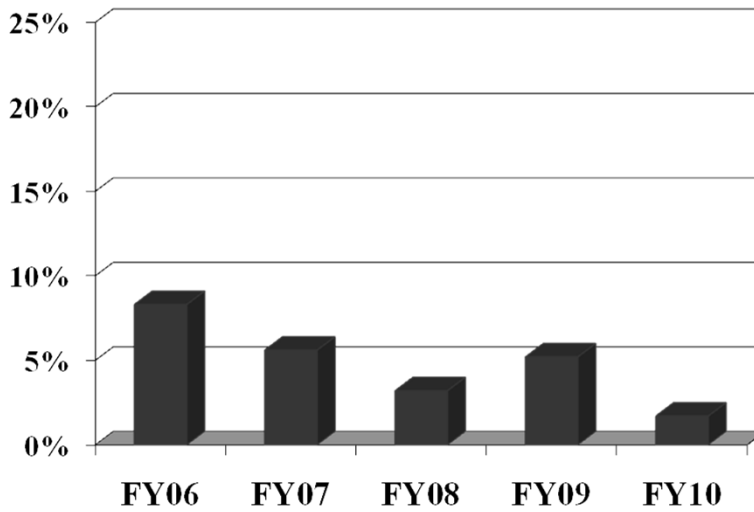
SOURCE: United States Sentencing Commission, 2009 and 2010 Datafile.

Percentage of Organizational Cases Receiving Reduction in Culpability Score Under § 8C2.5(g) Fiscal Year 2006 - 2010



SOURCE: United States Sentencing Commission, 2006-2010 Sourcebook of Federal Sentencing Statistics.

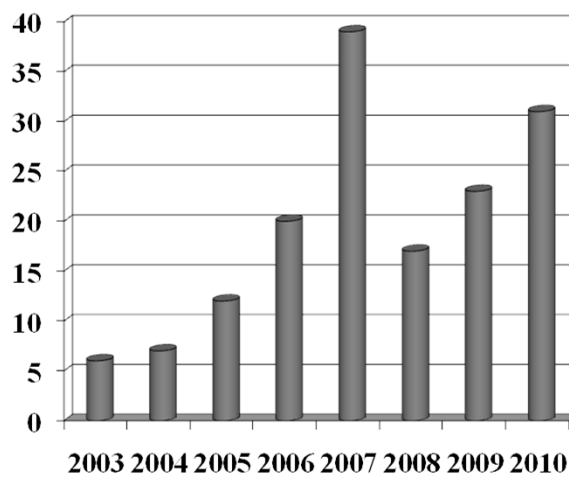
Percentage of Organizations Sentenced that Obstructed Justice (§ 8C2.5(e)) Fiscal Year 2006 - 2010



SOURCE: United States Sentencing Commission, 2006-2010 Sourcebook of Federal Sentencing Statistics.

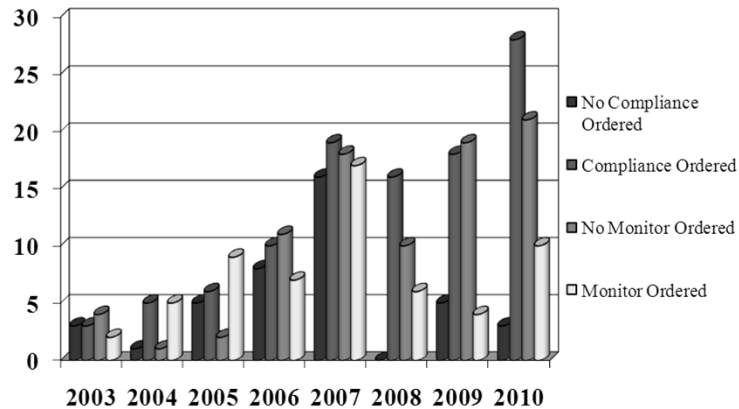
Deferred Prosecution and Non-Prosecution Agreements

Deferred Prosecution and Non-Prosecution Agreements for Organizations FY03- FY10



Source: Submission and Letter from Principal Deputy Assistant Attorney General Brian Benzckowski to Chairman John Conyers, Committee on the Judiciary, U.S. House of Representatives, May 15, 2007; Lawrence D. FINDER and Ryan D. McConnell, Annual Corporate Pre-Trial Agreement Update 2007 (2008); Lawrence D. FINDER, Ryan D. McConnell, and Scott L. Mitchell, Betting the Corporation: Compliance Programs in the Context of Deferred and Non-Prosecution Agreements (2009); Jay Martin, Ryan D. McConnell & Charlotte A. Simon, Plan Now or Pay Later: The Role of Compliance in Criminal Cases (Spring 2011).

Deferred Prosecution and Non-Prosecution Agreements for Organizations FY03- FY10



Source: Submission and Letter from Principal Deputy Assistant Attorney General Brian Benczkowski to Chairman John Conyers, Committee on the Judiciary, U.S. House of Representatives, May 15, 2007; Lawrence D. Funder and Ryan D. McConnell, Annual Corporate Pre-Trial Agreement Update 2007 (2008); Jay Martin, Ryan D. McConnell & Charlotte A. Simon, Plan Now or Pay Later: The Role of Compliance in Criminal Cases (Spring 2011).

U.S. Sentencing Commission

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