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Compliance Officers Take Their Own Path

Position has become more visible and independent of GC's office.

BY JULIE GOLDBERG

THE compliance officer is becoming increasingly independent of the general counsel's office. Historically, compliance was addressed by the general counsel's office, because the function arose from adhering to laws and regulations. But chief compliance officers (CCOs) are now becoming more visible and detached from the general counsel's



office, in part, to establish the role's integrity with regulators. They are instead reporting to the chief executive office, audit committee or both.

Today, nearly 90 percent of compliance officers do not perform a dual role as general counsel, according to a 2006 survey by the Ethics and Compliance Officer Association (ECO) based in Waltham, Mass., and Salary.com, a Needham, Mass.-based provider of compensation data. However, smaller companies often combine the two roles as a cost-savings measure.

With this growing independence, many compliance officers in the post-Sarbanes-Oxley era have legal backgrounds. Compliance officers who are specifically trained to interpret and apply laws and regulations are becoming attractive corporate assets and an added measure toward preventing company wrongdoing. An integral function of CCOs is to develop strategies and processes to prevent corporate operations from running afoul of regulatory bodies, including the Securities and Exchange Commission and the Federal Reserve.

About half of the nation's top ethics and compliance officers have law degrees, according to Joseph Kilmartin, Jr., compensation director for Salary.com.

Evolution of a Thriving Field

Ethics and compliance officers today are more prominent than at any time in the history of the function, which dates back several decades. Compliance officers have always existed in regulated industries such as financial services, insurance and health care. However, their roles were back-office in



nature, usually part of an internal audit group that organized paper documentation. Compliance positions required only narrow technical expertise and contributed negligibly to strategy and revenue. The field was utterly divorced from the entrepreneurial impulse of business.

Compliance programs arose from government initiatives to protect the public and the mutual efforts of companies that wanted a more positive corporate image. The need for compliance first became more significant during the 1960s in the wake of several "boiler room" scandals, in which brokerage firms were accused of hawking securities via extensive cold-calling operations, but actually selling worthless investments or failing to deliver. "There were many abuses and a lack of internal procedures—a clear indication of an absence of controls," recalls Harvey Pitt, a former Securities and Exchange Commission chairman and now CEO of Kalorama Partners, a global strategic consulting firm based in Washington, D.C.

In the 1970s, the defense contracting industry struggled with allegations of overcharging the government and taxpayers. Jack Welch, who became chairman of General Electric in 1981, spearheaded efforts to reform the industry by developing codes

Julie Goldberg, an attorney, is leader of Korn/Ferry International's legal specialty group, based in Stamford, Conn. Korn/Ferry is an executive recruitment company.

of conduct and procedures for voluntary disclosure of wrongdoing. The Defense Industry Initiative on Business Ethics and Conduct (DII), established in 1986, united 32 major defense contractors that adopted an ethics code governing their business responsibilities with the Department of Defense and each other.

Businesses of almost every nature became serious about developing compliance initiatives when the Federal Sentencing Guidelines for Organizations became effective in 1991. Today, the metamorphosis from back-office function to compliance as a critical responsibility is virtually complete. The Sarbanes-Oxley Act of 2002 and the public demise of giants such as Enron, Arthur Andersen and WorldCom, have elevated compliance to a strategic function that is critical to a profitable business.

Best Practice

Companies will devote \$28 billion to compliance initiatives in 2007, according to a study by AMR Research. Costs will reach \$80 billion by 2010, according to the Boston-based research firm.

Mean total cash compensation for top global ethics and compliance executives was \$285,000 in 2006, a 12 percent increase from 2005, according to an ECOA and Salary.com survey. Top global ethics and compliance executives could earn more than \$700,000, including long-term incentives such as stock options, depending on the company's size and location, said Mr. Kilmartin of Salary.com.

The general counsel and CCO continue to share the ultimate goal of minimizing corporate risk, even as their roles become more distinct: the general counsel protects the company, while the CCO develops and implements programs to detect and prevent corporate wrongdoing, said Donna C. Boehme, principal of Compliance Strategists, a consulting firm in New Providence, N.J. "They're partners in protecting the company, but they apply different approaches and skills to discharge their accountabilities. Occasionally, they may have divergent views and methods on what is best for the company, and when this happens, it's important that both views receive equal consideration by senior management."

Compliance programs are now prevalent at financial services organizations, investment firms, insurance multinationals, pharmaceutical giants and technology companies. Local governments are also showing interest in developing compli-

ance programs, according to Joseph Murphy, a compliance expert, lawyer, and co-author of "Building a Career in Compliance and Ethics" (2007: SCCE). As hedge funds receive increased scrutiny, the presence of hedge fund compliance executives remains attractive to institutional investors. Although a federal appeals court invalidated an SEC rule that required hedge funds with assets of more than \$25 million to register and appoint a compliance executive, experts say the role continues to enhance the image of legitimacy. "Being well-run with integrity and strong ethical precepts are the first and foremost steps toward sustained profitability," said Mr. Pitt, who is also a lawyer.

Today, investors and regulatory agencies both view a strong compliance leader and function as an established "best practice" that is essential to a positive reputation and healthy profits. Multiple compliance programs are now often in place at a single company to minimize the risk of potential legal and regulatory breaches such as accounting fraud, workplace safety, document management, and environmental hazards. "When companies bring a product to market, they will have a better chance of succeeding. People will trust those companies more. Compliance brings legitimacy to an organization and is attractive to institutional investors," explains Roy Snell, CEO of the Society of Corporate Compliance and Ethics, a Minneapolis-based non-profit organization focused on improving compliance initiatives.

Benefits of Legal Background

A legal background enhances a CCO's awareness of facts and circumstances to examine in a corporate investigation and laws and regulations that apply to it, said Deborah House, vice president and deputy general counsel for the Association of Corporate Counsel in Washington, D.C.

Officers working within highly regulated areas, such as financial compliance, may interface directly with federal agencies, according to Ms. Boehme, of Compliance Strategists. "They're more in touch with views of the agency, how regulations are interpreted day to day, and maybe closer with the realities of financial compliance," she said.

Odell Guyton is the director of compliance for Microsoft. Prior to joining Microsoft he served as corporate compliance officer at the University of Pennsylvania and for the university's Health System.

Previously, Mr. Guyton was a prosecutor for 12 years, including six years as an assistant U.S. attorney with the Department of Justice.

"Becoming familiar with the U.S. Sentencing Guidelines for Organizations helped me appreciate that companies of all sizes benefit from a compliance program to establish responsible leadership and sound business practices," said Mr. Guyton. He said he also learned to develop proactive strategies to help his clients adhere to all laws and regulations affecting their business. "That's what compliance is all about," he said.

Patrick J. Gnazzo, chief compliance officer of CA, Inc. (formerly Computer Associates International, Inc.), was a chief trial attorney for the U.S. Department of the Navy and deputy general counsel at Pratt & Whitney before entering the compliance field. "A legal background is not absolutely necessary, but from a compliance perspective, it's certainly helpful," said Mr. Gnazzo, who was chief compliance officer at United Technologies for 10 years prior to joining CA, an Islandia, N.Y.-based management software developer. Mr. Gnazzo said he gained tremendous insight into potential corporate legal problems as a government contracts litigator. He devises compliance programs with those issues in mind, he said.

CA named Mr. Gnazzo to the post in 2004 in an effort to remediate its own legal troubles. A deferred prosecution agreement between the company and federal authorities earlier that year required appointing a compliance officer and developing a comprehensive compliance and ethics program. Mr. Gnazzo's responsibilities also include establishing a records and information management program.

Other prominent compliance executives with law degrees include Laura Kennedy of Honeywell International, Inc., and Arjun Rajaratnam of Glaxo-SmithKline, PLC.

"To have a compliance officer with a legal background very much facilitates establishing a good compliance program in the company. Compliance is all about complying with laws and regulations—and also doing the right thing," explained Ms. House.

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