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United States Sentencing Commission
One Columbus Circle, N.E., Suite 2-500
Washington, D.C. 20002-8002
Attention: Public Affairs

Dear Honorable Members of the Sentencing Commission:

Kaplan & Walker LLP is grateful for this opportunity to comment on the Sentencing Commission's 2010 Proposed Amendments to the Sentencing Guidelines, Policy Statements and Official Commentary. Our comments are focused on certain of the proposed amendments to Chapter 8, and are based on our experience with respect to corporate compliance and ethics ("C&E") programs generally and our understanding of the ways in which many business organizations have interpreted the current Guidelines' C&E provisions in particular.[1]

Proposed Risk Assessment Amendment

We agree with the Commission that the Guidelines[2] risk assessment provisions should be amended. However, we do not believe that the proposed amendment is advisable because the proposed language[3] would likely not be well understood by C&E practitioners. In this connection, please note that we have discussed the proposed language with many of our colleagues in the C&E field and none were able to voice any degree of certainty as to the intent or practical impact of this contemplated amendment. Nor can we – despite our many years of experience with risk assessments – do so, either.

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[1] We briefly summarize our C&E-related experience in an appendix to this letter.
[2] In this letter, we sometimes describe not only the actual Guidelines but also Policy Statements and Official Commentary as "Guidelines," because in our experience C&E practitioners (meaning C&E officers and their advisors) generally do not distinguish among these three types of "content."
[3] By this we mean the "nature and operations of the organization with regard to particular ethics and compliance functions."

However, since the C&E provisions of Chapter 8 are being revisited, the Commission does have an opportunity to improve to a substantial degree the quality of companies' C&E risk assessment activities – and hence of the C&E programs for which those risk assessments serve as foundations. In that connection, based on our work in and general knowledge of C&E risk assessment practices, as well as our understanding of the intent of the existing risk assessment provisions in the Guidelines,[4] we respectfully make three observations about risk assessments, and couple each with a proposed recommendation.

1) Current risk assessment practices tend to focus largely (and sometimes exclusively) on the quantitative dimension of C&E risk and not enough on the qualitative dimension, rendering some C&E programs less effective than they should be. In the 2004 amendments to the Guidelines, the Commission essentially identified three risk assessment dimensions: the potential seriousness of a risk (which is often described as risk "impact"), the likelihood of a risk, and the nature of the risk. The first two of these are necessary to prioritizing risk; the third is important to determining how best to mitigate a given risk using the various parts (sometimes called "elements") of a C&E program. While prioritization is, of course, essential to program effectiveness, so is determining the best mitigation strategy once risk priorities have been set. Yet many organizations do not do nearly enough in regard to the latter.

To address this shortfall we recommend revising the current Application Note concerning risk assessment by adding the underscored language immediately below:

Application of Subsection (c).—To meet the requirements of subsection (c), an organization shall:

(A) Assess periodically the risk that criminal conduct will occur, including assessing the following:

(i) The nature and seriousness of such criminal conduct. <u>In assessing the nature of particular types of criminal conduct, organizations should consider which aspects of the compliance and ethics program are best suited to preventing the offense. For instance, if the offense is likely to be committed due to employees' misunderstanding or failing to appreciate the seriousness of an applicable law, the organization should generally consider training and other communications. On the other hand, where the wrongfulness and seriousness of an offense are well understood by employees but significant risks of a violation still exist, the organization should generally consider focusing on auditing, monitoring and other internal controls. Of course, for some types of criminal law risks, multiple compliance program elements should be utilized.</u>

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[4] In that connection, we note that the three suggestions made in this section of our submission are consistent with the only risk assessment methodological discussion cited in the October 7, 2003 <u>Report of the Ad Hoc Advisory Committee on the Organizational Sentencing Guidelines</u> (at page 91, fn 280: "For a thorough discussion of important considerations in risk assessments, see Jeffrey M. Kaplan, *Liability Inventory* in Compliance Programs and the Corporate Sentencing Guidelines ch. 6 (Jeffrey M. Kaplan, Joseph E. Murphy and Winthrop M. Swenson eds. 2002).")

2) Too many organizations fail to assess the "local" nature of C&E risks to a meaningful degree. Of course, some risks exist on an enterprise-wide level, but many others – such as in the corruption, fraud and antitrust areas – often exist to a significant degree and in distinct ways in a given business line, function or geography, or an even smaller "unit" of an organization. Yet too many risk assessments "paint with a broad brush" and fail to take account of the latter, sometimes with harmful consequences.

To address this shortfall we recommend the following revision in the underscored language immediately below to the same Application Note:

(D) Larger organizations or those that otherwise have relatively complex risks should consider conducting a risk assessment not only on an enterprise wide but also a "local" basis – meaning that the nature, seriousness and likelihood of specific criminal risks should generally be assessed by geographies, business units and/or functions.

3) Third-party related risks continue to be a "blind spot" in many C&E risk assessments. From the defense industry procurement scandals of the 1980's to the insurance industry scandals of the 1990s to more recent scandals concerning Foreign Corrupt Practice Act violations (among others), business organizations have often failed to take sufficient account of the risks of criminal conduct that can arise by virtue of dealings with independent agents and other third parties. We believe that this "blind spot" exists today in many companies.

To address this shortfall, we recommend the following revision to the same Application Note in the underscored language immediately below:

(E) Organizations should assess not only the risks of criminal conduct perpetrated by employees but also by independent agents and other third parties acting on their behalf.

Issue for Comment

The Commission has requested comments on whether the Commission should amend §8C2.5(f)(3) (Culpability Score) to allow an organization to receive the three level mitigation for an effective C&E program "even when high-level personnel are involved in the offense if (A) the individual(s) with operational responsibility for compliance in the organization have direct reporting authority to the board level (e.g. an audit committee of the board); (B) the [C&E] program was successful in detecting the offense prior to discovery or reasonable likelihood of discovery outside of the organization; and (C) the organization promptly reported the violation to the appropriate authorities."

We commend the Commission for suggesting this amendment, and believe that the Commission should amend §8C2.5(f)(3) generally as set forth above. Encouraging the person with operational responsibility to report to the board or a committee thereof should help empower and create a greater level of independence for this individual, which, as a general matter, should further empower C&E programs within organizations.

In addition, this provision should also help to enhance board oversight of C&E programs, which can benefit programs in a variety of ways, including increasing the clout and independence of the program.

However, we recommend that the language regarding reporting to the board (subsection (A)) be modified slightly, as follows:

(A) the individual(s) with operational responsibility for compliance in the organization periodically provide reports ~~have direct reporting authority~~ to the board level (e.g. an audit committee of the board) regarding the compliance and ethics program and have unfettered access to report to the board level regarding compliance and ethics issues or concerns;

We offer this suggestion because the term "direct reporting authority" could be interpreted to mean merely a dotted line reporting relationship that permits the person with operational responsibility to report to the board under certain circumstances, as opposed to that person's being required to provide periodic reports to the board or a board committee. We respectfully suggest that the Commission instead consider making clear that the individual with operational responsibility should, as a matter of an organization's policies, periodically provide reports to the board or a committee thereof regarding the C&E program and should have unfettered access to the board level in order to report C&E issues or concerns.

We also commend the Commission's inclusion of the requirement that the C&E program be successful in detecting the offense prior to discovery or reasonable likelihood of discovery outside of the organization. This provision should help encourage companies to enhance their focus on and boards of directors to enhance oversight of compliance by senior officers, who, historically, have represented the greatest risk to many organizations.

Other Proposed Amendments

Proposed revision to Application Note 3. We urge the Commission not to put forward the proposed revision to Application Note 3 concerning document retention compliance.[5] The proposed revision would, if implemented, elevate document retention to a category of criminal risk above all others, notwithstanding the fact that by any measure other areas (such as fraud, corruption and antitrust) are more frequently the subject of prosecution and are clearly of greater concern to C&E officers.[6] Given the fact that no company has unlimited time or resources to devote to its C&E program, elevating document retention

[5] We are referring to the proposal that would add the following to the Application Note: "Both high-level personnel and substantial authority personnel should be aware of the organization's document retention policies and conform any such policy to meet the goals of an effective compliance program under the guidelines and to reduce the risk of liability under the law."

[6] We base this observation not only on our combined thirty years of advising companies on C&E matters but also on our together having attended or chaired more than a hundred C&E conferences and other industry events and having read and published extensively in the field.

in this way could in fact skew C&E efforts away from more significant risk areas, and thereby weaken some companies' programs. For the same reason, we urge the Commission to omit the proposed language regarding document retention policies from Application Note 6, although, as discussed above, we recommend that the Commission omit the entirety of the proposed language from this section in favor of the language suggested above.

Proposed new Application Note 6. Our only comment with respect to this proposal is that the use of "independent monitor" could be a source of confusion. That is, as a matter of practice, what makes a monitor independent is a reporting relationship to a court or government agency; however, the context being described here is one in which there is presumably no court or government agency yet involved in the matter at issue. If the word "monitor" is replaced by "consultant," then there should be no basis for confusion, because independence *vis a vis* consultants is typically assessed with respect to criteria which would not be problematic in this context.[7]

Once again, we are grateful for the opportunity to submit these comments, and of course would welcome an opportunity to respond to any questions the Commission has about them.

Respectfully submitted,

Jeffrey M. Kaplan and Rebecca Walker

[7] These criteria are a) subject matter independence and b) relational independence, neither of which require a reporting relationship to a court or government agency.

Appendix

Jeffrey M. Kaplan has practiced compliance and ethics ("C&E") law since 1991, designing, implementing and assessing C&E programs for boards and managers of companies in nearly every major industry and assessing programs for both federal and state agencies. He is also the co-editor (with Joseph Murphy and Winthrop Swenson) of *Compliance Programs and the Corporate Sentencing Guidelines* (Thomson); co-author (with Ronald E. Berenbeim) of *Ethics and Compliance Enforcement Decisions—the Information Gap* (the Conference Board); the former Counsel to the Ethics and Compliance Officer Association; the former co-publisher of *ethikos* magazine; and an Adjunct Professor of Business Ethics at New York University's Stern School of Business. He is a graduate of the Harvard Law School.

Rebecca Walker's practice has been devoted exclusively to the C&E field since 1999, and she has also advised organizations on C&E program matters in nearly every major industry. She is, as well, the long-time co-chair of the Practising Law Institute's Corporate Compliance and Ethics Institute and of that organization's Advanced Compliance Workshop; author of *Conflicts of Interest in Business and the Professions: Law and Compliance* (Thomson); a member of the Advisory Board of the Society of Corporate Compliance and Ethics and a frequent contributor to that organization's bi-monthly magazine, *Compliance and Ethics Professional*; and an advisory board member of Corporate Compliance Center at the South Texas College of Law. She is a graduate of the Harvard Law School.