

EBEF Paper **One**

The Evolving Responsibilities & Liabilities of Ethics Representatives: **A practical guide**

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The Evolving Responsibilities & Liabilities of Ethics Representatives: A practical guide

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About the European Business Ethics Forum

The European Business Ethics Forum (EBEF) provides an opportunity for learning and sharing among those responsible for the ethics, compliance or business conduct programmes within their organisations. The organising committee for EBEF is a collaboration of the Institute of Business Ethics (IBE) of the United Kingdom, the Cercle d'Éthique des Affaires (CEA) of France, the Ethics and Compliance Officer Association (ECO) of the United States and the European Business Ethics Network (EBEN) (see p39). For more information on EBEF visit: www.ebef.eu.

Note: The material in this report is for general information only and is not intended to provide legal advice.

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Part 1: Introduction

Recent years have seen ethics and compliance programmes become the norm in large businesses. The trend has been driven in part by the high profile ethical and compliance failures within global organisations. These have led to more intensive public scrutiny of business behaviour and a strengthened regulatory and legal framework around ethics and compliance programmes, including the Sarbanes-Oxley Act 2002 (US), the Bribery Act 2010 (UK) and the amended Sentencing Guidelines 2010 (US). In some cases these have extraterritorial application and include provisions for personal liability.

There is more emphasis on boards overseeing the design, implementation and monitoring of effective programmes to embed ethical values and reduce misconduct. Such programmes are usually led by a Chief Ethics and Compliance Officer, a Head of Ethics or equivalent, who in some organisations will report directly to a board member. They are supported by 'Ethics Representatives'. Ethics Representatives (ERs)

“Within our organisation, it’s being seen as a more serious position – we’ve moved from generally having part time Ambassadors who do this in addition to their day job to full-time dedicated employees”³

refers here to those with an explicit ethics role - either working directly from the ethics/compliance office, or as full-time or part-time 'ethics ambassadors' within other functions, sometimes on a voluntary basis in addition to their 'day job' (e.g. as ethics champions).¹ These varied roles could include managing the different elements of the programme, monitoring, providing advice to employees, carrying out investigations into misconduct and advising the ethics/compliance office on local issues.² In

some cases, duties may be subject to regulatory or statutory standards.

The visibility of both the ethics function⁴ and these ERs has evolved at all levels of a company which, along with the increasing profile of ethics matters in business generally, has created new opportunities and responsibilities for ERs. For some, this will include a greater emphasis on fiduciary duties (being entrusted to put company interests above all others) depending on their specific duties, seniority and the regulatory environment. Consequently, ERs may find themselves facing a new exposure to personal risk and, in some

¹ The term Ethics Representative is used throughout to include such analogous roles as ethics officer, compliance officer, and certain types of ombudsmen.

² See IBE (2010) *Good Practice Guide to Ethics Ambassadors*.

³ Quotes in boxes throughout this report are based on the responses of business ethics professionals to an email survey by the authors in 2012.

⁴ In some organisations, ethics is managed from the compliance office or from other functions, including legal and audit.

cases, legal liabilities. Liability may arise where an ER either knowingly or unknowingly, for whatever reason:

- fails to prevent or detect misconduct,
- fails to report misconduct or to escalate it sufficiently,
- fails to act professionally or in accordance with her/his contracted or assumed duties, or
- fails to act with integrity.

“The expectations placed on ERs have increased, and although this is not universal throughout the entire organisation, increasingly it’s seen as a core management role – especially in those markets with heightened compliance risk.”

Conversely, the authors are also aware of claims that ERs have been dismissed because they did act with integrity but contrary to the interests or wishes of their superiors. We recognise that, as well as the liability that arises due to a failure to act, ERs will be concerned with liabilities and other consequences arising because of acting - including being ostracised or dismissed for stepping into sensitive areas and finding something that seems wrong while fulfilling their duties.

1.1 Background

In 2008, the Head of Internal Audit and Legal at a public cleaning service company, ‘Berliner Stadtreinigung’ (owned by the State of Berlin), was convicted for failing to act on evidence of customer overcharging. When he became aware of the systematic overcharging, in the region of some €23 million, he informed a member of the company’s board, who instructed him not to correct the error. The German Bundesgerichtshof (Federal Supreme Court) convicted and imprisoned the Head of Internal Audit and Legal on the basis that he had assisted fraud by failing to act, i.e. to take his concerns to a higher level.⁵

In another case in November 2011, the UK’s Financial Services Authority (FSA) imposed a fine of £14,000 on a compliance officer at a hedge fund management company (Dynamic Decisions Capital Management). She had failed ‘to challenge a colleague, [and] investigate and act on the information she received’ following concerns raised by investors around the sale of a bond. The FSA concluded that she ‘did not engage with her responsibilities...and therefore failed to act with due skill and care’ and neglected ‘to understand the importance of her role and the wider regulatory obligations it brings’.⁶

⁵ ‘Germany: The Compliance Officer’s Function within a Company – The Federal Supreme Court decides on compliance officers’ criminal liability regarding violation of their duties and challenges the compliance organisations within the companies’. 2nd January 2010. See: www.mondaq.com/article.asp?articleid=91716

⁶ ‘FSA fines and bans hedge fund Compliance Officer £14,000 for failing to act with due skill, care and diligence’. 22nd November, 2011. See: www.fsa.gov.uk/pages/Library/Communication/PR/2011/099.shtml

Such legal cases are rare and alone do not suggest a trend regarding all ERs. Exposure to such personal risk will not apply to all ERs and is very dependent upon sector, seniority and professional duties (a trend to increased liability is perhaps evident for senior roles). The cases do however, suggest that ERs need clarity around their responsibilities and liabilities, and to understand how to protect themselves while also upholding and fulfilling their designated duties to the organisation. They also suggest that employers of ERs would be advised to provide the right support to increase employee confidence, to emphasise the opportunities the role brings and to avoid employees feeling inclined to opt out of their voluntary ER roles.

1.2 Challenges of the role and influences on liability

In many cases, the role of ERs within organisations is still being defined. There is no standard, one-size-fits-all job description as responsibilities will depend on the context and the needs of the organisation. The

“Our ethics ambassadors are getting more approaches from other staff for advice.”

position could involve policy owning responsibilities, such as ensuring that controls are in place, managed appropriately and complied with, or the ER may be a voluntary, supportive part-time role with the employee simply acting as a local point of contact.

Many factors influence an ER’s exposure to personal liability. Since, of itself, it is an unrecognised and unregulated profession in any official sense, there is little formal protection or guidance directed at ERs with respect to this. While all employees have a responsibility to abide by the law and the terms and conditions of their employment contract (whether that be written or not), it is not always the case that employees understand their responsibilities (documented or assumed), nor their potential exposure to personal risk and liability. This is particularly so where ERs are operating without a formal job description covering their ethics role and responsibilities. Evidence suggests that this is a common state of affairs for ERs – particularly in the US.⁷

Furthermore, the spectrum of employees carrying out the ER role is likely to include those with specified professional duties, e.g. accountants and lawyers, and/or varying seniority. The obligations imposed by their professional body or their ‘officer status’ in the company will influence the liability context within which these ERs work. Also, some job titles are significant. For example, ombudsman, auditor and ethics officer can be defined in some jurisdictions as technically and legally specific roles and this will determine their legal responsibilities and privileges etc.

⁷ Research by the Society of Corporate Compliance and Ethics found that only 30% of compliance and ethics officers surveyed had an employment contract. See SCCE (2009) Compliance and ethics officer positioning: A benchmarking survey www.corporatecompliance.org/Resources/View/ArticleId/262/Compliance-and-ethics-officer-positioning-A-benchmarking-survey.aspx

Finally, liability can be prescribed because of particular duties assigned specifically to the ER role. For example, in the US, ERs in the securities industry are more exposed to the risk of personal liability if they have supervisory duties rather than solely a monitoring role. In some jurisdictions, legal liability may be formally 'delegated' to senior employees in their employment contract. In practice employment contracts are not always updated to reflect a new role or evolving responsibilities and the accompanying changes in liabilities.

In some jurisdictions (for example France and Germany), the Board or a senior officer of the company may, in a separate written document, formally set out a senior employee's delegated duties and authorities with accompanying legal and criminal liabilities. The delegee can further delegate his/her powers, but not the associated liabilities.

Formal delegations are likely to be relevant only to senior ERs, such as the Chief Ethics and Compliance Officer. Where delegations of authority and duties have been formally made, and an employee is acting within the scope of their duties, the employer would generally be expected to be vicariously liable for a wrongdoing, together with the employee. Even if personal liability does arise, the employer should bear the brunt of any claim and be covered by insurance.

For voluntary and part-time ERs, it is unlikely that legal and personal liabilities arising due to particular responsibilities will have been identified or set out formally, nor that cover will exist.

In any case, as we explore in this report, ERs are unlikely to be exposed if they operate diligently and within the scope of their duties. If ERs do inadvertently fail to act according to their assigned duties, or act outside the scope of those duties, then personal liabilities without cover from the employer might arise (see Part 3). However, there is little case history to indicate that this need be a concern for the majority of ERs, and such risks may be mitigated (see Part 4).

Ultimately, the relevance and efficacy of an ER role – on paper and in practice – will be determined within a particular company by the expectations of the board, as well as by the synergies or lack of synergies with line management and other functions such as human resources. However, there are particular challenges associated with the role that potentially make exposure to risk for ERs more likely than for other employees. Box 1 lists some challenges associated with the ER role.

Box 1: Common challenges faced in the Ethics Representative role

Stakeholder trust

The nature of the ER role usually implies heightened duties to different stakeholder groups and a position of trust including the trust of management around protecting the company and the trust of employees who confide/speak to them about their concerns. This can increase their risk of being in the line of fire, of their decisions and conduct being scrutinised, and perhaps of being a target for litigation or harassment following a case of misconduct, and in turn posing a significant risk to an ER's career and reputation.

Split loyalties

There can be a tension for ERs between building trust with colleagues and the obligation to act on information given to them. Maintaining independence can be difficult where an ER also fulfils a full-time operational role. Where an ER is an in-house lawyer, she/he may be unable to advise an employee because, formally, she/he represents the company's interests and not the employee's (explaining this point appropriately to an employee is known in the US as an 'Upjohn warning').

Challenging senior executives

For those involved in investigations, challenging senior executives can be difficult. Executives are likely to be sensitive to suggestions of omissions or misconduct made against them and, when the misconduct is substantiated, they may use their power to demand no or minimal enforcement against them. In some instances, ERs have lost their jobs when trying to hold executives accountable to ethics standards.

Inadequate mandate

Insufficient sponsorship of or buy-in to the ethics programme at executive level can result in a lack of drive and support throughout the rest of the organisation. This can mean ERs have a lack of mandate. This may be a particular challenge where companies are in joint ventures or have minority participation.

Inadequate resources

Inadequate resources make the discharge of an ER's duties difficult. Lack of resources might include a lack of training, support or guidance for ERs. This is a prominent challenge for volunteer ERs.

Lack of follow through

Concerns or issues raised by ERs may not be followed through adequately by the company. In the USA for example, as with all employees, ERs working in publicly reporting companies now face the personal decision of either attempting to report through the company, or reporting externally to the Securities and Exchange Commission (SEC). SEC and Commodities Futures Trading Commission (CFTC) rules disallow the ER from seeking a bounty when she/he learned about the misconduct from another employee, but they may report to either of these agencies if they have new information and suspect that the company will not act expeditiously. In these instances, they may file a claim not only to pursue the monetary reward as a buffer against economic retaliation but to benefit from the anti-retaliatory provisions of the Dodd-Frank Act (2010).

Lack of an independent reporting line

Some ERs may not have access to the board, the executive management team or have the ability to go 'outside the chain of command' with their concerns (e.g. to a non-executive or independent director).

Conflicts with professional obligations

Some ERs hold dual roles in their organisation. Where the ER holds a role such as Legal Counsel or Head of Internal Audit or is a qualified or chartered professional such as an attorney or accountant, there is the possibility that a clash will occur between her/his professional obligations and duties to the company as an ER. For example, such employees will have a heightened fiduciary responsibility to raise concerns and uphold a public interest requirement.

Ombudsman privilege

Where the ER is an 'ombudsman', she/he may in some jurisdictions have special professional privilege obligations around non-disclosure (which does not extend to other ERs). The challenge for these individuals is not to be compromised by what they are told and their need to react.

Scrutiny

ERs may be held to higher standards than other employees. They are expected to 'walk the talk' and demonstrate exemplary conduct with their behaviour scrutinised more so than other employees.

Exposure

There is a risk of exposure in relation to taking part in investigations into misconduct (which may be subject to external legal scrutiny) because of the growing need to follow appropriate or even strict protocols, and to demonstrate that they were followed.

Unclear scope of responsibility

Where the ER's remit with regards to integrity risks posed by third parties such as suppliers, customers, joint ventures have not been made sufficiently clear, the ER may be exposed where they handle incidents incorrectly.

Variations in local law

Where an ER represents or acts across more than one national jurisdiction, being sufficiently familiar with differences in local laws and regulations may pose a challenge. For example, in France, the law around data protection and promoting speak up procedures may be limiting on some ER responsibilities.⁸ Another example is Works Councils in Europe. Their role and function will need to be taken in to account when handling ethical issues and this will vary in practice across Europe.

Also ERs may have to promote or challenge behaviours which are in accordance with local laws but which represent a lower ethical standard than the company demands.

1.3 About this report

The aim of this report is to prompt ERs, and their employers, to consider whether their evolving responsibilities are likely to pose any increase in personal liability. It aims to provide practical guidance in order to reassure those in an ER role and their employers that exposure to risk can generally be avoided and mitigated.

Its main focus is on employees in roles supporting the Chief Ethics Officer or similar, rather than those with responsibilities at or just below executive or board level who may be exposed to liability arising mainly from their directorship. The focus is also on anticipated or inadvertent exposure to personal liability, rather than that arising from incompetence or intentional misconduct.

Below, **Part 2** will explore the nature of the evolving responsibilities, risks and developments outlined above through the perspectives of a senior Ethics Officer from a global aircraft manufacturer based in Europe, a UK based international law firm and a Chief Operating Officer of a membership association in the US for individuals responsible for ethics and compliance in their organisation.

⁸ See www.cnil.fr

Part 3 will briefly outline sources of legal risk including some recent legal developments in Europe and the United States, and will suggest developments on the horizon likely to impact on the risk climate.

Example cases will illustrate where ERs may face personal consequences and liabilities in the context of corporate practice, laws and regulations in those jurisdictions.

Part 4 provides guidance to ERs on how to manage and avoid risks and so protect themselves from personal liability. It also suggests how senior executives might fulfil their duties to ERs in their organisation, thereby enabling them to perform their role confidently and effectively.

“I am aware of ERs who have left their organisations because management did not support their decisions, or had asked them to engage in unethical behaviour that conflicted with either the organisation’s or their personal values.”