Being a Good Partner to USAID: The Importance of an Effective Ethics and Compliance Program to Mitigate Risk of Disallowances, Investigations, and Debarment

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This White Paper—which is based on input provided by the United States Agency for International Development ("USAID") and several of its for-profit and not-for-profit Partners—is designed as a resource for USAID Partners to develop ethics and compliance programs tailored to the requirements and expectations of their primary funder.

As one of the world's largest funders of development and relief goods and services, USAID offers tremendous opportunities for its Partners and beneficiaries. The last decade, however, has demonstrated that USAID's Partners must also appreciate the unique compliance risks associated with accepting Federal funding and operating in some of the most volatile and unstable environments in the world. Partners have faced criminal and civil liabilities as a result of regulatory violations, and in some notable instances, faced suspension and debarment for failing to develop adequate internal controls to deal with the risk of fraud and non-compliance. Organizations have also fallen under greater scrutiny when it comes to counter-trafficking in persons ("C-TIP") and sexual exploitation and abuse ("SEA") failures. Perhaps more so than ever, USAID Partners should take the necessary steps to develop a ready and capable ethics and compliance program.

Complexity of USAID's Compliance Regime

U.S. Government spending on development and relief is wholly different from commercial contracting and private sector donations. From formation through administration, federal government acquisition and assistance are increasingly complicated, highly-regulated, and subject to more risks than virtually any other business or charitable endeavor. Implementation of these programs can be costly

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because the unique rules and risks associated with federal funding require great attention from management to develop a sound compliance infrastructure tailored to each Partner's particular risks and circumstances.

Unlike commercial contracting and private donations, USAID contracting and assistance are governed by a system of laws, regulations, and contract or agreement clauses – and a body of case law interpreting those rules – that govern the actions of USAID and its Partners. The most significant federal procurement regulations are contained in the Federal Acquisition Regulation ("FAR"). For assistance agreements such as grants and cooperative agreements, the regulations are contained in the Office of Management and Budget Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, more commonly known as the "Super Circular." USAID also issues supplemental regulations and policies in the Agency for International Development Acquisition Regulations ("AIDAR"), the Acquisition Directives System ("ADS"), and 22 Code of Federal Regulations ("CFR") Parts 226 and 228.

This maze of laws and regulations dictate, for example, what methods or processes the agency must use to bind USAID's Partners to any number of commitments and obligations. Any failure to comply can result in non-reimbursement of costs; and if this failure results from willfulness, "deliberate ignorance," or "reckless disregard," it can lead to criminal, civil, and administrative penalties and other sanctions, including debarment from receiving future federal contracts and assistance agreements. In addition, the FAR requires all recipients of federal contracts to disclose to it any "credible evidence" of crimes, false claims violations, and overpayments in connection with the award, performance or closeout of its grants and assistance agreements. Further, USAID expects that recipients of contracting and assistance funding alike have processes in place to be able to identify when fraud may be taking place and promptly report on it.

Unfortunately, USAID does not publish a comprehensive database of the laws, regulations, and requirements that govern its Partners. This results in Partners regularly being surprised by an agency audit that invokes a requirement that is not widely known in the community. Additionally, USAID occasionally interprets the requirements in ways that seem to be unpredictable and inequitable, resulting in disputes that can be costly. In short, the risks to the Partner, affiliated entities, and individuals, at all levels are real.

Importance of Robust Compliance & Ethics Programs

The good news is that undertaking the efforts to become a consciously-compliant USAID Partner can ensure a clearer path to greater financial opportunities with the agency. This raises an obvious question: what steps can a board of directors and C-suite executives take to effectively mitigate the varied compliance risks faced by their organization?

The most crucial step in mitigating the minefield of accountability and enforcement risks facing Partners is the development of a fully integrated approach to risk management. Nichols Liu attorneys addressed this imperative in the publication *Contractor Responsibility: Toward an Integrated Approach to Contractor Risk Management*.

The most effective corporate risk management programs ("Programs") include two components: (1) a code of ethics and compliance (and implementing program) that identifies and teaches the core obligations and values by which the Partner is defined, and (2) internal infrastructure and processes designed to ensure compliance with that code and those values.

To illustrate the importance of both compliance obligations and organizational values, consider the possible approaches to solving a commonplace problem: schoolyard bullying. From a compliance perspective, bullying may be addressed by the school's adoption of strict rules against fighting and name-calling. From a values-based perspective, however, bullying is more successfully prevented by cultivating a culture of respect among the broader student population, which makes clear to any would-be bully that such conduct will not to be tolerated by his or her peers. These two concepts are not mutually exclusive, and sophisticated organizations incorporate elements of each to manage risk effectively.

In terms of compliance, the first step in developing a stout compliance program is for a company to look inwards and, through some form of enterprise risk management system, identify the largest compliance risks it faces in light of the unique characteristics of its industry and business. This is essential and smart from a cost-benefit standpoint because, once the key risks to a company are known, it can tailor its compliance program accordingly. To guarantee the effectiveness of the program, however, the company also must make an effort to ensure that its employees are made aware of its key points of emphasis. To this end, a company is best served by incorporating the compliance program into its governance documents, employee handbooks, and codes of ethics, as well as ensuring that employees receive periodic training on the program requirements.

The other half of an effective program involves a genuine commitment to instilling a culture of ethical conduct within a company. Achieving this goal requires more than merely putting pen to paper. Corporate directors and other senior management must set an example by demonstrating the company's commitment to honesty and integrity in their own actions and by rewarding employees who demonstrate a commitment to *promoting* ethical values (as opposed to merely rewarding ethical behavior). Making such a commitment to a values-based standard of ethical behavior is important as it lessens the chance that an employee will commit wrongdoing that will put the company at risk. Prosecutors and judges, and many Government agencies including USAID, now expect these types of programs.

Most large Government contractors have already recognized the importance of corporate governance programs that effectively manage risk and have spent time and resources into developing them. Yet, newspaper headlines are rife with stories of noncompliance by - and enforcement actions - against these same contractors. Clearly, it is not enough to merely adopt a risk management program. Rather, organizations must continually monitor and retool their compliance and ethics programs to respond to changes in their company or organization, the industry, implementation environment, and the regulatory and legal landscape. Although easily stated, developing and maintaining an integrated risk management program requires both creativity and meticulous planning, including continuous process improvement through steps such as benchmarking the effectiveness of their program through periodic employee surveys, evaluating allegation-receipt mechanisms and reporting statistics, random compliance checks, and reviewing investigation files for thoroughness and timeliness.

Key Features of Effective Compliance and Ethics Programs

There is no single program that can be applied – cookie-cutter style – to every USAID Partner organization, or to any business in any other industry. The sizes and, more importantly, the cultures of organizations are too varied for a single approach to work. Certain general features have become accepted, however, as "best practices." How those features are applied to particular businesses is what makes the program effective.

The following list identifies the key features of generally accepted "best practices" programs. The examples that are provided are just that – examples of how some organizations with successful programs have chosen to implement their programs. Not every example would be effective for every organization.

1. Determine the Organization's Values and Culture

The first step in designing a Program is determining the organization's culture and values. Any Program that is generic or obtained "off the shelf" will fail. It is essential that the Program lead from the organization's strengths, address its weaknesses, and establish where it wants to go. There are a number of ways that culture and values can be determined.

Often, management conducts surveys of its employees, with questions addressed to cultural issues, such as how employees view the ethics of their leadership, whether they feel empowered to voice concerns, to what extent they fear retaliation for raising issues, and the extent of pressure they feel to cut corners. To augment the survey results, some organizations also conduct focus groups whereby employees can respond anonymously to questions.

Management must also ensure that its vendors, subcontractors and agents are aligned with the organization's ethics and values, as well as the code of conduct and ethics. Illustrating best practices in this regard, some organizations request annual certifications of vendors requiring their acknowledgment of the code of conduct/ethics, and whether they have any reportable violations of the codes.

An organization's values can also be gleaned from discussions with employees and management. Rather than addressing culture, these questions would be designed to determine the values that employees believe in, what the organizations stands for, the historical values of the organization, and how it measures up to others in the development space. Many organizations also feel that the values of key stakeholders also inform its values. This would be particularly significant for USAID Partners, as their mission itself is values-based and doing right by their stakeholders and aid beneficiaries is of utmost importance.

2. Organizational Assessment

After identifying its values and culture, and before beginning the process of designing a Program, many organizations feel that it is important to assess the processes and procedures by which they operate, and how those relate to risk. This assessment – typically done with separate focuses on compliance and ethics – provides a baseline for how the existing structure may be leveraged to mitigate overall risk.

Initially, management identifies the areas of greatest compliance risk to the company, and its existing Enterprise Risk Management ("ERM") system determines and quantifies those risks. Employees that are in job assignments most susceptible to violating laws and regulations within those risk areas are identified and then mitigation efforts are focused on addressing gaps and vulnerabilities around those job functions.

3. Code of Ethics and Conduct

The best Codes of Ethics and Conduct are those that succinctly state the organization's values that are shared by all employees, the regulatory and contractual obligations, and management's expectations, and explain the meaning of those elements either in a letter from the Chief Executive Officer ("CEO") or elsewhere in the Code. They encourage concepts such as transparency and integrity, and empower employees to raise concerns without fear of retaliation. Poor Codes tend to be limited to statements of the elements of regulations and laws that employees are prohibited from violating. While there is value to directing employees to obey the law, Codes that are limited to that create risks. How can management, using this approach, list all laws employees are expected to follow comprehensively? Further, regulators tend to suspect that overly detailed descriptions of laws in Codes are intended to encourage employees to be amateur lawyers, and to look for loopholes that they believe would allow them to violate the law.

The wording of even the best Codes, and how they are implemented, vary widely among organizations. Typically, the Code will be introduced by the CEO or President, often focusing on key high-risk compliance issues unique to the organization. Codes also generally explain the structure and role of the Ethics Organization; and encourage employees to raise issues of concern with their ethics advisor, supervisor and/or others.

4. Performance Evaluations

The most effective ethics and compliance programs are "owned" by executive leaders. In order to ensure managers' ownership of the programs, many organizations incorporate into managers' annual performance appraisals a requirement that they promote ethical business conduct. This should not be worded as a "pass/fail" of whether the manager acted ethically during the year; but, rather, as an incentive to actively promote ethics, by continually discussing the importance of having an ethical culture, including such concepts in speeches and published articles, and incorporating ethics considerations into business decisions. Some organizations include such an ethics element in "360 reviews," by which a manager's supervisor, direct reports and colleagues provide input into how well the manager has promoted ethics throughout the year.

5. Communication Plan

Business leaders seeking to improve and maintain a high ethical culture recognize that addressing such issues is a continuous process. A program that appears only once a year in the form of some employee training has little value, and is even counterproductive, since it sends a negative message to employees that management is merely "checking the box" that it has a program.

Effective ethics and compliance programs include a Communication Plan that identifies unique and varied ways to communicate the importance of ethical conduct to employees throughout the year. Examples often include regular articles in employee newsletters. These may generally address the importance of ethical business conduct. But the more effective articles identify and explain positive examples of named employees' ethical decision-making; and descriptions of disciplinary actions taken against employees (typically not named) for having made poor choices.

Other methods many organizations use to communicate the importance of having an ethical culture to employees include periodic email "pop-ups" with short, positive messages, and posters throughout the offices, encouraging employees to raise issues of concern. Routine communication on these issues with Board members is also recommended.

6. Training

Training is the most visible feature of programs that differentiate between compliance and ethics. Effective programs do not limit training to compliance with laws and regulations but, rather, focus also on encouraging and empowering employees to do "the right thing." Compliance training needs to address identified risks, and should be directed to all employees that face those risks. Training on the Foreign Corrupt Practices Act, for example, can be directed specifically to employees involved in implementation of international programs. On the other hand, training on the False Claims Act should be directed to employees across the board, ranging from finance personnel at the local and corporate level, program managers, timekeeping clerks, and subcontract overseers, because each has a hand in preventing the submission of false claims. Mechanisms should be implemented to track the employees that have been targeted for specific courses and to verify that they completed the required training.

Unlike many compliance courses, training in ethics should be directed to all employees. Ethics training encourages employees to do "the right thing," through discussion of situational scenarios, and ethical decision-making. Most importantly, to be done effectively, such training should be led by each employee's immediate supervisor, in a "cascaded" manner, starting from the CEO down throughout the organization.

Both compliance and ethics training are usually required to be taken by every employee upon hiring; and refresher training provided annually. Ideally the importance of ethics is instilled in prospective employees even before they are hired, by including discussion of the organization's values, and the importance of ethical conduct in the interview process.

7. Business Leaders' Ownership of the Program

Woven throughout the other features of effective ethics and compliance programs is the important concept that managers at all levels must lead by example and be accountable for the success of the programs. This is accomplished initially by including topics such as ethical role modeling in leadership courses. With tools such as performance evaluations, managers should be encouraged to promote ethical values, and should be held accountable for the success of their organization's ethics and compliance programs.

8. Risk Mitigation Process

Effective ethics and compliance programs contain processes for identifying and tracking allegations of misconduct; and incorporate mechanisms for identifying risks related to that misconduct, such as enterprise risk management-type systems. The identification and tracking is typically accomplished through a database that tracks complaints made to Hotlines, or to ethics advisors, the resolution of such complaints, and a process for determining whether to impose discipline and to disclose the allegations to the government or other customers.

ERM is then utilized to identify trends and key risk areas that should be addressed by management generally, and/or through revisions to the ethics and compliance program designed to mitigate the identified risks.

9. Ethics and Compliance Infrastructure

As discussed previously, business leaders should "own" the ethics and compliance program, and be held accountable for its success. A program infrastructure is necessary, however, to support the businesses. Ethics organizations manage the program elements described above, oversee the Hotline and most related investigations (in coordination with the legal or compliance officers), and assist managers in conducting employee training.

Depending upon the size of the organization, this can be led by a Chief Ethics and Compliance Officer ("CECO"), with direct reporting to the CEO (and access to the Board), or, in smaller organizations, by an attorney or HR official, with reporting through the General Counsel or VP for HR. Many believe that a structure whereby the CECO is independent of the General Counsel, Executive Officers, and other departments, provides a positive message to employees as to how management views the ethics and compliance program. But for smaller organizations, the costs of such a structure are not always justified by the benefits.

Ethics Officers are frequently assigned to each business unit and often to each facility to assist the local business leaders in the operation of the program in larger organizations. They perform the ethics functions on a part-time basis in all but the largest organizations and report to the business leaders and to the CECO, either on a dotted line, or hardline basis.

Compliance training (unlike ethics training) is usually conducted by the compliance and ethics department, the HR department or the law department, any of which also may conduct investigations into serious allegations. Third-party consultants are often retained to serve in these capacities.

10. Program Assessment

Good ethics and compliance programs are both effective and dynamic. Whether all important features have been implemented, and how well they are managed should be periodically evaluated through internal, and occasional external audits or benchmarking assessments.

Many organizations also employ mechanisms to determine whether the program should be revised to meet changing risks. One common approach is to include ethics-related questions in periodic employee surveys. If results indicate increasing fear of retaliation for reporting misconduct, for example, the program can be adjusted to increase its focus on that risk. Some organizations also occasionally engage outside ethics consultants to review, and to make recommendations for improvements to the program.

Conclusion

Government regulators can – and often do – impute non-compliance and a lack of integrity. This regularly results in cost disallowances and, in more egregious cases, in investigations, false claims damages, and suspension or debarment. At the same time, regulators are often more understanding where the organization has taken reasonable actions to mitigate the risk of employee misconduct and to properly handle any misconduct when it does occur. The key to effective risk mitigation and proper handling of violations is the effectiveness of the organization's compliance and ethics program. Leaders of organizations that understand this are in a much better position to protect themselves from negative consequences and to be a better partner to USAID.