

National Government Ethics Conference

Organizational Integrity: A View from the Private Sector

September 14, 2011

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When bubbles burst...



Post-Tech Bubble

- Enron
 - Tyco
 - Adelphia
 - Xerox
 - Rite-Aid
 - Martha Stewart
 - ImClone
 - Aurora Foods
 - Computer Associates
 - WorldCom
 - Accounting
 - Wall St.
 - Mutual Funds
 - Insurance
 - Hospitals
 - Pharmaceuticals
 - Brokers
 - Fannie Mae
 - Freddie Mac
- 

Not Uniquely American

- Mannesmann
 - ELF
 - Royal Dutch Shell
 - VW
 - ABB
 - France Telecom
 - ABN-Ambro
 - Heidelberg Cement
 - Royal Ahold
 - Bank of Italy
 - Parmalat
 - Samsung
 - Bank of China
 - Livedoor
 - Hyundai
 - Nikko Cordial
 - United Nations
- 

Settlements

(DPAs and Federal Monitors)

- HCA (\$1.7B)
 - AIG (\$1.6B)
 - Royal Ahold (\$1.1B)
 - Fannie Mae (\$400M)
 - Time Warner-AOL (\$510M)
 - KPMG (\$465M)
 - Adelphia (\$715M)
 - Tyco (\$750M)
 - Prudential (\$600M)
 - CA (\$225M)
 - Marsh McLennan (\$850M)
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Lessons Learned

1. Irrational exuberance + uninhibited self-interest
 2. Arrogance
 3. Fraud
 4. Conflicts-of-interest
 5. Preferential treatment
 6. Accounting arbitrage
 7. Failure of independent auditors
 8. Failure of analysts
 9. Failure of rating agencies
 10. Failure of regulators
 11. Failure of board oversight
 - 12. *Culture of greed***
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In Response?

- Sarbanes-Oxley Act (“SOX” - 2002)
- Thompson (2003) + McNulty (2006)
- Revisions to Federal Sentencing Guidelines
-ethics and corporate culture (2004)
- NYSE + Nasdaq

Sarbanes-Oxley Act

- CEO/CFO financial certifications
- Loan prohibitions
- Bonus forfeiture
- Blackout trading restrictions
- Internal control certifications
- Codes of ethics
- Whistleblower provisions

Audit committee

(Section 301) - Must establish procedures for:

- receipt, retention + treatment of accounting issues;
- confidential + anonymous tips regarding questionable accounting.

(Section 406) – Must:

- adopt code for financial officers, or explain why not

Thompson + McNulty

Thompson Memo (2003)

- Seriousness of the offense
- Pervasiveness of wrongdoing
- History of serious misconduct
- Timely and voluntary disclosure
- Existence and adequacy of compliance
- Corporate remedial actions
- Collateral consequences of conviction
- Adequacy of non-criminal remedies

McNulty Memo (2006)

- Adequacy of board oversight
- Did the board perform independent oversight, or merely “unquestioningly ratify officers’ recommendations?”

Federal Sentencing Guidelines

November 1, 1991

-Periodic risk assessments.

-There must be standards and procedures to prevent and detect criminal conduct.

-The board must be knowledgeable about and reasonably oversee the program.

-There must be a high-level person charged with oversight.

-That person must have appropriate authority and adequate resources and unfiltered access to the board.

-The firm must take reasonable steps to communicate and train...including the governing authority.

-Evaluate the effectiveness of the program.

Federal Sentencing Guidelines

Revised November 1, 2004

Precondition to an effective program:

“...promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.”

“A good corporate citizen must first and foremost operate ethically.”

Judge Reuben Castillo, Vice Chairman

Federal Sentencing Guidelines

Revised November 1, 2010

7th element - When criminal conduct is detected, a company must take “reasonable steps to respond...”

Now “reasonable steps” may include:

- restitution to identifiable victims;
- self reporting, and/or;
- cooperation with authorities.

Also, to prevent similar misconduct;

- undertake periodic program evaluations, and;
- periodic risk assessments, which may include “use of an outside professional advisor to ensure adequate assessment and implementation.”

Federal Sentencing Guidelines

Revised November 1, 2010

The Commission has recommended sentencing reduction when high-level personnel are involved if these conditions are met:

-if the person with “operational responsibility” for the program has direct reporting obligations to the board.***

-the C&E program detected the offense before discovery outside the organization.

-the offense was promptly reported to government authorities.

-no one managing the C&E program participated in, condoned or was willfully ignorant of the offense.

The Bubble Burst (again)

The Great Recession



Post 9-11

2001-2006

- Extraordinary growth in mortgages
- Accommodating conditions
- CDO's
- AAA Rating

2007

- Teaser rates begin to expire
- Delinquencies rise
- Foreclosures rise

The Meltdown

- 3/16/08 Bear Stearns sold to JPM Chase
- 7/11/08 IndyMac Bank (bankrupt)
- 9/7/08 Fannie Mae & Freddie Mac (gov't ownership)
- 9/15/08 Lehman Brothers (bankrupt)
- 9/16/08 Merrill Lynch sold to BofA
- 9/16/08 AIG (77.9% gov't ownership)
- 9/18/09 Money market fund "breaks the buck"

The Meltdown

“We need the equivalent of war time powers.”

-Hank Paulson

“If you (congress) don’t act today there will be no economy tomorrow.”

-Ben Bernanke

9/19/08 - Treasury Secretary asks congress for \$700 billion (TARP)

Headlines

- 9/24/08 WAMU (bankrupt), to JPMorgan Chase
- 9/29/08 ***TARP bill voted down by congress***
Fortis Bank nationalized
HYPO Real estate bailed out
Bradford & Bingley nationalized
Glitner Bank nationalized
Ireland guarantees all deposits
Italy guarantees all deposits
- 10/1/08 Senate passes TARP
- 10/4/08 Germany guarantees all deposits
Russia discusses bail out of Iceland

Headlines

- 10/6/08 UK buys 70% RBS, 43% Lloyds Bank
- 10/7/08 UK announces \$500B stimulus
- 10/17/08 Germany approves \$750B stimulus
- 11/10/08 China announces \$600B stimulus


When the tide goes out...?

- Mark Deier, \$400 million
- Marcus Schrencker, \$100 million
- Arthur Nadel, \$300 million
- Joseph Forte, \$100 million
- Nicholas Cosmo, \$300 million
- Paul Greenwood, \$900 million
- Danny Pang, \$100 million
- Milowe Brost, \$400 million
- Bernard Madoff, \$65 billion**

“Am I a sociopath?”

B. Madoff to his therapist
New York Magazine 3/7/11

When the tide goes out...?

- ❑ Satyam Computer - \$1 Billion
 - ❑ Siemens - \$1.6 billion settlement
 - ❑ Halliburton - \$599 million
 - ❑ Stanford Financial Group - \$8B
 - ❑ Galleon Group - \$1B
 - ❑ BAE - \$400+ million
 - ❑ Daimler - \$185 million
- 

When the tide goes out...?

- ❑ “Operation Broken Trust” (>500 prosecutions)
- ❑ “Deutsche Bank pays \$554m to NYS for Tax Evasion”
- ❑ “BofA Pays \$150 million Re Muni Bid Rigging”
- ❑ “UBS Fined \$780 million in Tax Evasion”
- ❑ “Schwab Pays \$119 million to Settle”
- ❑ “FDIC Seeks \$2.5 Billion in Clawbacks”
- ❑ “BofA Pays \$150 Million to Settle Merrill Lynch”
- ❑ “SAC Ex-Manager Set to Plead Guilty”
- ❑ “European Regulators Investigate Banks for Credit Swaps”
- ❑ “HSBC Accused of Helping Mubarak Regime Land Deals”

When the tide goes out...?

- Pfizer - \$2.3 billion
- GSK - \$750 million
- Novartis - \$422.5 million
- Eli Lilly - \$1.4 billion



Other Issues - Culture

“Secretive Culture Led Toyota Astray”

The Wall Street Journal
February 8, 2010

“The *Toyota Way* Was Lost on Road to Phenomenal Growth.”

The Washington Post
February 13, 2010

Other Issues - Fraud & Culture

“Goldman Sachs Charged with Fraud”

Financial Times

April 17, 2010

“The whole building is about to collapse anytime now...Only potential survivor, the fabulous Fab...standing in the middle of all these complex, highly-leveraged, exotic trades he created.”

“Anyway, not feeling too guilty about this, the real purpose of my job is to make capital markets more efficient and ultimately provide the U.S. consumer with more efficient ways to leverage and finance himself, so there is a humble, noble and ethical reason for my job; ***amazing how good I am at convincing myself.***”

Other Issues - Fraud & Culture

“Goldman Blasted for Conflicts of Interest”

cnbc

April 14, 2011

“A case study of recklessness and greed”

Other Issues – Risk & Culture

“BP’s Tony Hayward and the Failure of Leadership Accountability”

Harvard Business Review
June 7, 2010

“Culture of Complacency at BP Set Stage for Oil Spill, Commission Says”

The Washington Post
November 9, 2010



**“Cables Show US Concern on
Japan’s Disaster Readiness”**

The New York Times
May 3, 2011

“Compartmentalization and risk aversion....”

Behind the Headlines - Corruption

- “Four Sama Dubai Employees Are Held In Corruption Probe”
- “Ex-Head of Bank of Italy to Go on Trial”
- “Bahrain Kickback Investigation Widens”
- “Siemens Excluded from World Bank Contracts for Two Years”
- “Control Components Admits to Violating FCPA in 36 Countries”
- “Ex-Sinopec Corporate Chairman Sentenced to Death for Bribery”
- “China Executes 2 For Role in Tainted Milk Scandal”
- “Chevron Offers Evidence of Bribery Scheme in Ecuador Lawsuit”
- “Maybey & Johnson To Be Sentenced in Bribery Case”
- “Postmaster General in India Held for Corruption”
- “UN Cuts Back on Investigating Fraud”
- “Rio Tinto Employees Admits to Taking Bribes in China”
- “Nine British Companies in US Bribe Inquiry”
- “Alstom UK Directors Arrested in SFO Bribery Investigation”

Corruption

- “Greece Condemned for Falsifying Data”
- “Nortel Will Liquidate Assets”
- “Italian Notables Feel Heat in Corruption Scandal”
- “Ex-Gome Head is Sentenced”
- “How German Companies Bribed Their Way to Greek deals”
- “Avon Bribery Probe”
- “BHP Billiton in US Anti-Corruption probe”
- “Alcatel Agrees to Pay \$137 Million to Avoid U.S. Prosecution”
- “Russia’s Two Top IKEA Execs Sacked Over Suspected Bribery”
- “Nexus Technologies and Three Employees Plead Guilty to Paying Bribes to Vietnamese Officials”
- “Bribe Case Focuses on Negotiator for Alcoa”
- “Total Indicted for Alleged Corruption in Iraq”
- “Johnson & Johnson Settles Bribery Case”

Corruption

- ❑ “Russia Leads the World in Economic Crime, Report Says”
- ❑ “Russian Corruption May Force Western Firms to Quit”
- ❑ “Half of Russians Believe Bribery Solves Problems”

“There is actually no success so far”
(Russian President Dimitry Medvedev on his government’s attempts to fight corruption).

Anti-Corruption

- ❑ “Brazil’s Lula Sends Anti-Fraud Bill to Congress”
- ❑ “Peru Government Announces Creation of Anti Corruption Commission”
- ❑ “Australia Introduces New Laws to Fight Cartels and Corporate Corruption”
- ❑ “Anti-Corruption Candidate Wins Croatia Election”
- ❑ “Italian Cabinet Approves Corruption Crackdown
- ❑ “China Premier Calls for Intensified Fight Against Corruption”

Anti-Corruption

- ❑ Foreign Corrupt Practices Act
 - ❑ UN Convention Against Corruption
 - ❑ UN Global Compact
 - ❑ OECD Working Group – “Good Practice Guidance”
 - ❑ UK Bribery Bill
 - ❑ G-20
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In Response – U.S.

DOJ -Fraud task forces
-Anti-trust

SEC

- FCPA, insider trading
- Risk and BOD governance
- Dodd-Frank - 922 & 748 whistleblower bounty
- Compensation

**“A Whole New Ballgame:
Dodd-Frank Whistleblower Provisions”**

Forbes 11/2/10

New Risks for the 21st Century

WikiLeaks

Whistleblowing

Social Media

Hacking/Cyber crime

Transparency



“I intend to take down an American Bank and expose an ecosystem of corruption”

Julian Assange
November 29, 2010



News Corp

“News of the World Hacking Scandal Exposed”

“Australian PM: Murdoch Has Questions to Answer”

“Wall Street Journal Head Resigns”

“Piers Morgan Denies Phone Hacking”

“Head of Scotland Yard Resigns”

“DOJ Preparing Subpoenas”

“PM Cameron Grilled by Parliament”

Cyber Threats

- “FBI Directors Warns of Growing Cyber Threat”
- “Internal Sabotage Security Risks Rising”
- “Mass Leak of Client Data Rattles Swiss Banking”
- “Social Media Use Puts Companies At Risk”
- “Unseen Security Risks Lurk in the Copy Room”
- “Data Breaches Are Heaviest At Hotels”
- “White House Focus on Nuclear Terrorism Gets Scrutiny”
- “Senators Seek Documents on Fort Hood Suspect”
- “Terror Attack on US Flight to Detroit Investigated”
- “Deloitte Poll: respondents Lack Confidence in Ability of Private Enterprises to Reduce the Occurrence of Cyber Crimes”

“China Launches Whistleblower Websites”

Sify.com India Ltd.
February 15, 2011



**“Mexico Offers Reward for Reporting
Money Laundering, Promising to
Share Loot with Informants”**


AP

April 5, 2011

Government Issues

- ❑ ***“OIG at Interior Finds A Culture of Ethical Failure at MMS”***
- ❑ “Army Employee Sentenced for Bribery and Supplementation of Salary Violations”
- ❑ “VA Official Abused Position, Misused Official Time and Travel”
- ❑ “Hatch Act Cases Lead to Significant Disciplinary Actions”
- ❑ “NASA-OIG Report Finds Director Violated the Ethics Pledge”
- ❑ “SEC Adopts New Supplemental Ethics Standards for Employees”
- ❑ “Ethical Problems Found Between MMS Employees and Regulated Companies”
- ❑ “MSHA Found Negligent in Training and Safety”
- ❑ “SEC-OIG Find Misuse of Government Resources”
- ❑ “DOD Employee Sentenced for Post-Employment Violation”
- ❑ “SEC Accused of Destroying Files”

Lessons of the Great Recession

1. Arrogance
 2. Fraud
 3. ***Conflicts-of-interest***
 4. ***Preferential treatment***
 5. Conspicuous consumption
 6. Failure of all the gatekeepers
 7. Culture of greed
- 

Lessons of the Great Recession

In most cases the culprits believe:

1. They'll never get caught.
2. They're smart enough to get out of trouble.

Generation Y

- They're plugged in and networked:
 - iPhones, iPods, iPads, iTunes, downloads, blogging, texting, tweeting, FaceBook, LinkedIn, etc.
- Politically savvy
- Socially responsible
- Crave team culture
- Want constant communication
- Driven by a sense of purpose
- Not afraid to challenge the status quo

Josephson Institute

30,000 H.S. students surveyed in 2008

- 64% admitted cheating on a test in the previous year (up from 60% the year before)
- 38% cheated more than once
- 36% admitted plagiarizing from the Internet
- 33% said they stole something from a store
- 25% admitted stealing something from a parent or relative.

Surprisingly, 93% said they were satisfied with their personal ethics, while 26% admitted lying on one or two questions in the survey.

Deloitte & Touche with Junior Achievement

750 students 12-17 surveyed in 2008

- 21% indicated cheating was acceptable
- 13% believed plagiarizing was acceptable
- 28% indicated that illegally downloading music and not paying for it was acceptable

Regarding cheating:

- 54% indicated that did it to succeed in school
- 35% said it was pressure from parents
- 18% justified it as “everybody else does it”

On plagiarizing, 49% said they did it because they didn't have enough time to finish assignments

McCabe, Trevino, Butterfield

2006 survey

- MBA students cheat more than other graduate students (56% MBA v. 54% engineering, 45% law students)
- McCabe earlier discovered:
 - 74% of undergraduates admit relying on the Internet, crib notes, or peeking at classmates' tests to gain a competitive advantage.

The Chicken or the Egg?

- Pressure to get ahead
 - Pressure from supervisory authorities (parents, etc.)
 - A desire to succeed
 - *Everybody else does it*
-

- Enron, Tyco, WorldCom
- Skilling, Lay, Koslowski, Ebbers
- Satyam, Siemens
- Goldman Sachs
- Bernie Madoff
- Barry Bonds, Alex Rodriguez, Manny Ramirez, Mark Maguire
- Marion Jones
- Bill Belichick
- Rod Blagojevich

There has been a profound loss of trust in every part of society, including our:

- markets
 - financial institutions
 - organizations
 - government
 - leaders
- 

You can't legislate trust.



What is trust?



How do you build trust?




Culture

“A system of shared values”

“The underlying assumptions, beliefs, attitudes and expectations shared by an organization.”

“It’s the way things really get done around here.”

Central Concepts of Corporate Culture

1. They're collective.
 2. It's what members agree about.
 3. They're emotionally charged
 4. They're historically based
 5. They're inherently symbolic
 6. They're dynamic
 7. They're vague, at times contradictory
 8. They're paradoxical
- 

Corporate Culture

Strong cultures have two primary characteristics:

- High level of agreement on what's valued.
 - High level of intensity about these values.
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Corporate Culture and Performance



Ikea

Starbucks

Dannon

Michelin

FedEx

Southwest Airlines

Google

Culture trumps compliance!




Strong cultures self-regulate



OGE Mission

In partnership with executive branch agencies and departments, OGE fosters high ethical standards for employees and strengthens the public's confidence that the Government's business is conducted with impartiality and integrity.



OGE Mission

The underlying principle of public service is that
“public office is a public trust.”



This is a defining moment!

The image features a solid blue background. On the right side, there is a faint, stylized graphic of a globe with latitude and longitude lines. On the left side, there is a vertical band consisting of many thin, closely spaced horizontal lines. The text "This is a defining moment!" is centered in the upper half of the image in a white, serif font.