CEP Magazine - March 2022

Our third rail: Compliance within the legal department

By Rebecca Walker and Jeffrey M. Kaplan

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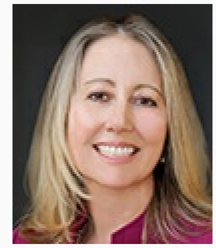

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The issue of whether the chief ethics and compliance officer (CECO) should report to the general counsel (GC) has been a hot-button issue in the compliance community for many years. Indeed, as far back as 2003, US Senator Charles Grassley famously said, "It doesn't take a pig farmer from Iowa to smell the stench of conflict in that arrangement."

But does this reporting relationship necessarily create conflicts of interest? Can CECO-to-GC reporting be effective? These questions are somewhat contentious, even in our very civil and civilized compliance and ethics (C&E) community. Indeed, if there is any "third rail" in the C&E field, it is this.

A CECO who reports directly to the CEO with a seat at the senior leadership table, a budget on par with the law department, a strong voice in strategic decision-making, and a close relationship with the chair of the audit committee certainly sounds ideal, but that structure is simply not feasible in many organizations. And—hold on to your hats—it is not, in our experience, typically necessary for the program to report directly to the CEO for it to be effective. We have seen numerous empowered, independent, effective compliance functions that exist inside the law department, reporting to the GC.

There can, of course, be disadvantages to the CECO-to-GC reporting relationship, and there are issues to consider in this—as in any—reporting relationship. In this article, we will explore the advantages and disadvantages of this reporting relationship and provide some practical suggestions for enhancing the independence and authority of the CECO, regardless of the reporting structure.

Which type of reporting?

One of the reasons that this issue can be challenging to explore is that there are two related but clearly distinct types of reporting relationships, and it is not always clear which is being discussed. One of these is informational reporting (e.g., providing information in written reports, oral presentations). There will generally be plenty of benefit and little downside to the CECO's reporting informationally to both the board of directors and the GC (and perhaps also the chief executive officer). Indeed, the reporting relationship between the CECO and the board or a board committee (often the audit committee) is the most important means of ensuring that a C&E program possesses sufficient independence and authority, as we discuss in more detail later.

The other type of reporting is administrative or, in other words, supervising the CECO on a day-to-day basis, including setting goals and compensation. It is this type of reporting that presents the more challenging issues when structuring a C&E program.

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