

Compliance and ethics programs: competitive advantage through the law

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Abstract This paper aims to address whether deploying compliance and ethics programs will assist US organizations in implementing the internal mechanisms necessary to achieve a competitive advantage from the law. My focus will be on the US legal system, as the corporate compliance and ethics programs examined are based on mitigation provisions contained in the US Federal Sentencing Guidelines. In particular, I propose that organizations can attain a sustainable competitive advantage from the law by considering the following questions: Do compliance and ethics programs assist organizations in achieving a better understanding of the law? Are compliance and ethics programs a cost-effective approach for coping with an organization's legal issues? Can compliance and ethics programs aid organizations by preventing these legal issues from occurring in the future? Will compliance and ethics programs support organizations in reframing legal issues as business opportunities?

Keywords Business law · Competitive advantage · Compliance and ethics programs · Organizational strategy · Legal environment

1 Introduction

General anxiety regarding the complexity of the legal regulations affecting the American business environment has grown considerably in recent years. Due to scandals that have saturated all channels of the business media (Hays 2005; O'Hara 2005; Haughney 2008; Bowley and Lattman 2010; Lattman 2010), we have seen increased efforts by the US government to improve regulatory supervision over the business community (Thompson 2004). Evidence of the crackdown by government

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agencies and stricter regulations being sought in Congress is embodied in the revised version of Sarbanes–Oxley and its progeny (Schwartz 2007). Sarbanes–Oxley ushered in a new era of public accountability in response to outrages involving financial reporting misconduct, insider trading, breach of fiduciary duty, and other legal issues surrounding companies like Enron, WorldCom, and Tyco (Gabel et al. 2009). Legal experts believe this push is a response to public concerns that poorly conceived legal regulations and a lack of adequate government supervision failed to prevent these scandals (Fisch and Rosen 2003).

Scandals involving the breach of laws and regulations by American corporations regularly act as a catalyst for heightened US governmental regulation of the country's business environment (Cleek and Leonard 1998; Behr and Witt 2002). Not only has this amplified the influence of legal regulation on organizational success (Siedel 2000; Ring et al. 2005) and led to a growing interest in organizational responses to law (McKendall et al. 2002; Canary and Jennings 2007), but it has also produced a growing body of academic literature on law and the organization. With increasing numbers of in-house counsel now being classified as members of senior management (Nelson and Nielsen 2000), even shaping strategy formulation at the CEO level (Kim 2001; Beardslee 2002) at respected companies like Merck, Pfizer, and Home Depot, scholars have begun taking greater notice of the nexus between law and business strategy, concluding that law can be a source of competitive advantage (DiMatteo 2010; Orozco 2010; Siedel and Haapio 2010). However, as limited attention has been paid to the mechanisms that organizations can implement to actualize competitive advantage theories, a gap still remains in the academic literature.

Heeding the call for research, this paper aims to address whether deploying compliance and ethics programs will assist US organizations in implementing the internal mechanisms necessary to achieve a competitive advantage from the law. By applying the Manager's Legal Plan developed by Siedel and Haapio (2010) to corporate compliance and ethics programs, I aim to address the following questions: Do compliance and ethics programs assist organizations in achieving a better understanding of the law? Are compliance and ethics programs a cost-effective approach for coping with an organization's legal issues? Can compliance and ethics programs aid organizations by preventing these legal issues from occurring in the future? Will compliance and ethics programs support organizations in reframing legal issues as business opportunities? Thus, in this paper I attempt to contribute to the literature by examining the effectiveness of utilizing compliance and ethics programs as a tool in the creation of an overall business strategy focused on obtaining a competitive advantage from the law.

The global scale of modern business implicates laws from diverse jurisdictions around the world, each with their own unique form of legal interpretation, application, and administration. While the research questions I attempt to answer may be equally applicable to other countries with developed legal systems, this paper focuses on the US legal system, as the corporate compliance and ethics programs examined are fundamentally based on mitigation provisions contained in the US Federal Sentencing Guidelines.

I begin with an introduction to compliance and ethics, followed by a brief review of the literature on law and competitive advantage. Using the four-part framework for achieving competitive advantage developed by Siedel and Haapio (2010), I then discuss how compliance and ethics programs can assist organizations in achieving a competitive advantage. I conclude with specific suggestions for future research.

2 Literature review

2.1 Compliance and ethics

Violation of civil and criminal regulations in the US can result in a variety of penalties, ranging from light censure and warning letters to heavy monetary fines, lengthy prison sentences, and an irrevocable loss of business operating licenses. Consequently, organizations have generated internal measures as a means of complying with these diverse and convoluted obligations (Fuller et al. 2000; Mendelhoff and Gray 2005; Shimshack and Ward 2005). As noted by Short and Toffel (2010), scholars have analyzed the use of internal mechanisms by corporations attempting to comply with financial regulations (Krawiec 2004; Langevoort 2006; Gabel et al. 2009), environmental regulations (Lenox and Nash 2003; Shum and Yam 2011), workplace safety/labor regulations (Kolk and van Tulder 2002; Lobel 2005; Estlund 2010), and employment discrimination regulations (Edelman et al. 1991; Edelman 1992; Edelman and Suchman 1997). The extensive studies in these areas highlight an acknowledgment by the business community of the heavy penalties associated with violations of these laws. For example, the top ten most expensive settlements in 2008 for employment discrimination, wage discrepancy, and ERISA class action lawsuits cost corporate America over \$18 billion (Reuters 2009).

As a result of the pressures generated by contemporary business regulations, many US organizations have designed internal mechanisms to bring management standards and business practices in line with prevailing legal requirements (Fuller et al. 2000; King and Lenox 2000; Delmas and Toffel 2008), including corporate compliance and ethics programs (FitzSimon and McGreal 2005; McGreal 2010), codes of ethics (Schwartz 2001, Gaumnitz and Lere 2002; Kaptein 2004; Bartley 2007), and employee grievance procedures (Sutton et al. 1994). Organizations commonly employ a combination involving one or more of these measures. For instance, IBM's Trust and Compliance Office is tasked with overseeing the company's compliance program, business conduct guidelines, and grievance procedures. Led by IBM's Vice President, Assistant General Counsel, Chief Trust & Compliance Officer, Co-Lead Sales and Distribution Legal, one of the central goals of this office is to provide communication channels for employees, suppliers, and business partners to anonymously report concerns or suspected violations to the company (IBM 2010). In assessing the organizational application of these varied measures to the process of ethical goal achievement, scholars have recognized a distinction between compliance-based and integrity-based approaches. While a compliance-based approach focuses chiefly on the prevention of legal liability, an

integrity-based approach emphasizes a level of ethically responsible behavior above and beyond the evasion of legal liability. While some argue strongly for the integrity-based approach, noting that legal compliance is unlikely to yield significant moral imagination or commitment (Paine 1994), most companies employ a combination of both approaches (Paine 1994; Trevino et al. 1999).

Despite the increased attention paid to the diverse means of establishing ethical cultures in recent years, the mechanism that has seen the greatest rise, and the focal point of this paper, is the compliance and ethics program. A possible influential factor accounting for this rise is the US. Federal Organizational Sentencing Guidelines. Originally enacted in 1994 and recently amended, these guidelines facilitate the assessment of legal penalties for organizations found guilty of civil and criminal violations. Fines are based on a calculation that takes organizational size, extent of senior management involvement in criminal activity, existence of prior criminal violations, and prior obstructions of justice into account. However, a reduction in fines is permitted for companies that have effective compliance and ethics programs in place at the time of the legal violation (Oakes 1999; McKendall et al. 2002). Organizations that are able to design and implement such programs have the potential to drastically reduce their legal fines and penalties (Moeller 2004; Green 2005; Rezaee 2007). For instance, in 2006 BP Products North America was charged with violating the Commodity Exchange Act when accusations surfaced that it had manipulated the market price of physical propane from 2004 to 2006. As a result of having a compliance and ethics program in place, the civil monetary penalty against BP was significantly reduced to \$125,000,000, despite the program's failure to prevent the alleged unlawful conduct (U.S. Commodity Futures Trading Commission 2007). Due to the significant effect compliances and ethics programs can have on organizational legal costs, the overall role of compliance in the value creation process needs to be studied in greater detail.

2.2 Law and competitive advantage

In today's marketplace organizations must adapt to operating within a complex legal environment where the lines separating lawful from unlawful conduct are distorted and vague (Stohl et al. 2009). However, out of the uncertainty comes the opportunity for organizations to use legal knowledge and capabilities to achieve a competitive advantage in the marketplace (Siedel 2002; Bagley 2008; Bird 2008; DiMatteo 2010). As introduced by Porter (1985) in his legendary treatise, competitive advantage may be attained by reconfiguring the value chain to provide either lower cost or better differentiation. Primary activities in the value-chain include inbound logistics, operations, outbound logistics, marketing/sales, and service. Firm profits depend on performing these activities efficiently, so that the amount that the customer is willing to pay for the products exceeds the cost of the activities in the value-chain. Through these primary value-chain activities, organizations have the chance to create value. Applying Porter's definition to the legal context, Hasl-Kelchner (2006) notes that companies must perform these activities at a lower cost, or execute them in a manner that leads to differentiation and a premium price while reducing undesirable legal hazards.

The potential for competitive advantage inherent in legal resources is sustained by virtue of their imperfect imitability, causal ambiguity, social complexity, and high substitute costs (Bird 2008). Every activity in the value chain is affected by the legal environment (Bagley 2010). The federal government has enacted extensive trade regulations to monitor transactions between the US and foreign countries. Anti-trust laws prohibit business conduct or structures that tend to restrict fair competition, such as price fixing, price discrimination, and the formation of monopolies. Health and safety regulations prohibit false advertising and product mislabeling, regulate the quantity of goods produced, and establish purity standards for cosmetics, food, and pharmaceutical drugs. In addition, each of Porter's five determinants of industry attractiveness, from buyer/supplier bargaining power and substitute availability to the threats presented by rivals and new market entry, is shaped by the legal system (Bird 2008). For example, organizations wishing to enter the healthcare industry must take extensive measures under HIPPA and other laws to protect the integrity of sensitive personal information.

Consequently, law can be a substantial factor in value creation (DiMatteo 2010) through the protection of innovation, the enabling of free labor markets, and the efficient regulation of contracts (Bird 2008). Through the use of intellectual property law, organizations can protect and leverage the value of their resources by copyrighting original works, increasing revenue through licensing agreements, patenting inventions to erect barriers to entry, and protecting proprietary trade secrets (Bagley 2008). For example, Microsoft recently took legal action against Barnes & Noble, Inc., Foxconn International Holdings Ltd., and Inventec Corporation, based on allegations of patent infringement by the Nook e-reader and the Nook Color tablet, which rely on the Android operating system. Use of an industry-wide licensing program supported by proactive use of patent infringement remedies, in instances such as this one, was one substantial factor that allowed Microsoft to achieve revenues of \$60.42 billion in 2008 (Gutierrez 2011; Microsoft 2008). Taken together, this growing area of research suggests that the law plays an increasingly important role in contributing to organizational success.

2.3 The Manager's Legal Plan

Traditionally, organizations have viewed legal concerns as problems demanding resolution as quickly as possible. However, this attitude overlooks the fundamental point that even if legal matters are viewed as problems, they directly affect the business goals of an organization and its competition. Recognizing that avoiding this line of thinking creates the opportunity to seize competitive advantage, Siedel and Haapio (2010) developed the Manager's Legal Plan to assist organizations in converting competitive advantage concepts and theories into tangible action plans. Comprised of four steps, the it allows organizations to proactively use law to uncover and develop new forms of competitive advantage by reframing legal concerns as business opportunities.

Step one focuses on understanding the legal dimensions of business and learning how to work alongside legal professionals. Specifically, it involves appreciating the legal characteristics of business, describing the law in business terms, and knowing

when outside legal assistance is necessary. While the level of legal knowledge can vary between industries, a solid understanding of key legal principles provides organizations with the necessary foundation for conducting the legal-business analysis outlined in the remaining steps.

Step two examines knowing how to cope with legal issues by managing their costs and learning from the difficulties they present. It requires organizations to recognize the drawbacks of the traditional flight or fight responses to law. Flight responses refer to actions that allow organizations to avoid legal confrontations, such as settling cases or moving operations to a different country to escape the dominion of various laws. However, this type of response can have unintended consequences. For instance, settling certain cases can prompt future litigation if an organization develops a reputation as an easy target for litigation. On the other hand, the fight response, where an organization chooses to contest an individual legal matter in court, can be costly, time consuming, with no guarantee of success. As such, organizations should consider the limitations of these responses with an eye towards examining how to avoid similar legal issues in the future.

Step three concentrates on the development of business strategies and solutions to prevent future legal problems. The root of this step is to help organizations take action that moves beyond flight or fight. When addressing any legal issue, organizations must avoid focusing only on the legal aspects of the situation. By considering the business aspects of legal issues, organizations can exercise sound business judgment when faced with legal decisions. In order to avoid the limitations of flight or fight responses, organizations can utilize three preemptive strategies: prevent the legal issue from arising, prevent the legal issue from doing harm, and limit the damage of legal issues that do arise and inflict harm. The limitation of step 3 is that these strategies only focus on compliance with existing regulations. Focusing on these regulations may lead organizations to overlook significant opportunities to move ahead of the competition.

Finally, step four involves seeing the big picture and reframing legal problems as business opportunities, thereby allowing organizations to create new options for discovering value and gaining a competitive advantage. It starts with changing the belief that the law relates only to legal problems, assisting organizations with transitioning from a reactive to proactive legal posture. It is through this transition that organizations are able to create value. In order to assist with this step, Siedel and Haapio (2010) outlined four linked approaches that can guide organizations in the reframing process: make a commitment to looking at the law as a strategic asset, select an appropriate framework for guiding that commitment, outline specific actions for meeting that commitment, and implement the chosen actions.

Siedel and Haapio (2010) recognized that by concentrating too narrowly on law and ethics, organizations run the risk of overlooking the role these elements play in overall profit attainment. However, their limited analysis only skimmed the surface of this issue and failed to address internal mechanisms that organizations can use to incorporate concepts from the Manager's Legal Plan into organizational processes and procedures. Building upon their research, I examine how organizations can apply the lens of the Manager's Legal Plan to compliance and ethics programs, in order to create value and obtain a competitive advantage from the law. In the next

section, I will use their model to examine how implementing compliance and ethics programs within organizations can lead to value creation and competitive advantage.

3 Compliance programs as a valuable capability

Viewing compliance and ethics programs through the lens of the Manager's Legal Plan can assist organizations in achieving a competitive advantage from the law by answering the following questions: Do compliance and ethics programs assist organizations in achieving a better understanding of the law? Are compliance and ethics programs a cost-effective approach for coping with an organization's legal issues? Can compliance and ethics programs aid organizations by preventing these legal issues from occurring in the future? Will compliance and ethics programs support organizations in reframing legal issues as business opportunities?

3.1 Organizational understanding of the law

A well-rounded, practical understanding of the law provides a decisive foundation for using the law to achieve competitive advantage, as organizations that discount the strategic potential inherent in legal perception will be hard pressed to minimize legal risk and create value (Siedel and Haapio 2010). Past research in this area has focused on developing a fundamental knowledge of legal statutes, doctrines, and concepts (Siedel 2002), grasping the public policy objectives of law (Bagley 2005), addressing management criticisms on the importance of law (Hasl-Kelchner 2006), and viewing the law with a strategic mindset (Bird 2008).

Building on this research, I propose that compliance and ethics programs support organizations in recognizing and reinforcing two key realities about the legal system. First, they highlight the large measure of uncertainty inherent in the law. Despite the heavy influence of the legal environment on organizational structure, policies, and culture (Edelman 1992), legal interpretation is a function of best guess (Langevoort and Rasmussen 1997) as companies attempt to keep pace with the changes wrought by dynamic legal trends (Edelman and Suchman 1997; Bagley 2008). The vague language contained in many laws leads to difficulties in assessing their application to a given legal situation (Altman 2001; Arthur and Shaw 2006) and determining what actions are most appropriate for their fulfillment. For instance, Title VII of the Civil Rights Act prohibits discrimination in the "terms, conditions or privileges of employment." Past cases have tasked the courts with the tricky assessment of whether transfer from a bright office to a dimly lit cubicle, exclusion from meetings and seminars, or denial of challenging tasks can legitimately constitute a violation of such terms, conditions or privileges of employment.

Compliance programs allow organizations to address such uncertainty by reminding management that much of the law is a grey area. The knowledge of the legal system delivered through compliance programs can shift organizational culture by helping the organization move away from viewing legal issues as speed

bumps that distract focus from more important business issues (Oder 2009) towards viewing the law as an element of business environment that needs to be examined alongside every major business decision. In addition to being comprised of laws with amorphous language, the legal landscape is dynamic in nature. The state of constant change forces organizations to continuously examine and address new developments in the law. Instead of resting on their laurels, organizations can harness the concerns generated from this uncertainty to instigate preventive measures, measures designed to make the dynamics of such a system easier to handle by mitigating the concerns, fears, and costs associated with legal violations.

Second, compliance programs suggest that violations of the law are inevitable, as even companies that have compliance measures in place do not have fewer legal violations (McKendall et al. 2002). For instance, Enron's self-celebrated code of ethics, which repeatedly emphasized the importance of legal obedience, had little effect in preventing the corporate scandal that made the company a household name. Similarly, despite having a distinguished compliance and ethics program in place, complete with an annual Corporate Compliance and Ethics Week (Consonery 2008, Home Depot continues to be sued by plaintiffs alleging misrepresentation, employment discrimination, and improper wage compensation. Compliance programs act as a constant reminder that no amount of training, support, and oversight can completely eliminate all legal violations. KPMG, recognizing that its compliance and ethics program does not guarantee success in preventing illegality, conducts constant supervision and modifications, requests employee feedback, and solicits outside support to make its policies more efficient. As a result, the company's program has been highly effective (KPMG 2010).

Notice of pending litigation or government investigation can dramatically affect the day-to-day operations of unsuspecting companies by causing a significant amount of extra work, anxiety, and disruption. Organizations that understand litigation is an inevitable part of doing business stand a higher chance of responding more appropriately and effectively to legal situations. Compliance programs provide a plan of attack in the event of a legal crisis by outlining suitable organizational responses. The knowledge that legal violations are inevitable, coupled with a knowledge that a response plan is in place, will mitigate the level of disruption to daily operations. In addition, such knowledge may reduce the temptation to devote excessive company resources to resolving any one legal issue. In the next section, I will examine in greater detail how this knowledge factors into the costs of coping with legal issues.

3.2 Coping with legal issues

Given the understanding of the law afforded by compliance and ethics programs, the question becomes whether compliance and ethics programs are a cost-effective approach for coping with an organization's legal issues? As noted by Harvard Professor Lynn Paine (1994), "the economic case for corporate ethics has both a negative and a positive aspect...The negative case for ethics focuses on risk management and cost avoidance, and the positive case emphasizes innovation, productivity gains, and revenue enhancement." Focusing on the negative aspect of

Professor Paine's argument, while existing legal regulations have altered nearly every aspect of business strategy and operations (Siedel 2000), organizations in diverse industries routinely view legal fees as costs to be minimized (Kaplan 2007). Legal consultants frequently advise that companies can reduce litigation costs without sacrificing litigation quality through budgetary planning, efficient use of technology, quality controlled legal billing, and restrictions on legal research, discovery tools, and court appearances (Drumm 2009; Meiselman and Carton 2009). Thus, scholars have argued that the array of costs associated with supporting such programs, which can include technology investment, public relations, increased training and certification, incident management, audits and assessments, and vendor management, are unnecessary expenses that can place organizations in precarious financial positions by requiring them to improperly allocate limited resources to the compliance process (Pelliccioni 2002; Bowman 2004; FitzSimon and McGreal 2005; Langevoort 2006).

The danger in this approach is that organizations choosing to focus primarily on these short-term costs tend to miscalculate the enormity of potential long-term costs like decreased sales, tarnished reputation, and increased capital costs (Baucus and Baucus 1997). In addition, studies have also shown that while the difference between non-compliance and compliance costs varies by industry, the costs of non-compliance clearly outweigh the cost of compliance. Non-compliance costs result when organizations fail to comply with rules, regulations, policies, contracts and other legal obligations, and can include direct costs like fines and legal fees associated with criminal, civil, and administrative statutes. Indirect costs can include reputation damage, decreased sales, jail time for high-level executives, damaged supplier relationships, productivity losses and massive public disapproval (Hasl-Kelchner 2006; Bagley 2008). For example, a 2011 study by the Ponemon Institute found that on average, the cost of non-compliance is 2.65 times greater than the cost of compliance. The extrapolated average cost for compliance in the organizations examined was only \$3.5 million, compared to an extrapolated average cost of non-compliance of nearly \$9.4 million. Adjusting total cost by organizational size yielded a per capita compliance cost of \$222 per employee, compared to a per capita non-compliance cost of \$820 per employee (Ponemon 2011).

Responding to legal regulations by creating compliance and ethics programs represents a means of moving beyond fighting legal issues individually to addressing them on a collective basis. By using compliance programs in this way, organizations put measures into place that allow a more cost effective response. While consideration of such programs requires a thorough cost-benefit analysis of strategies for coping with legal issues, the costs of a program outweigh the costs of having no program and attempting to fight every issue on an individual case by case basis.

3.3 Preventing future legal violations

While the establishment of compliance programs assists in the reduction of legal costs, the prevention of future legal violations and the realization of a competitive advantage calls for the integration of overall legal and business strategy. The legal

compliance process entails more than simply ensuring legal observance; it also involves careful management of day to day business affairs (Laufer 1999; Copeland 2000). For instance, compliance programs often involve the formation of standards and procedures to prevent illegal conduct, typically codified in the company's code of ethics, along with training sessions to disseminate and reinforce those standards, and management oversight and supervision of program implementation, monitoring, and evaluation (McKendall et al. 2002). Organizations that put such measures into practice experience a heightened level of integration between their legal and business arms. For instance, Baker Hughes, a top-tier supplier to the world's oil and gas industry operating in over 90 countries with more than 50,000 employees, proclaims that collaboration is the cornerstone of its business (Deaton 2010). Corporate governance at Baker Hughes encompasses a comprehensive set of policies, processes and guidelines in order to facilitate valuable interaction with key stakeholders. Highlights of the company's compliance program include a compliance council, special compliance committee, and centralization of human resources (Baker Hughes 2011). Based on such examples, compliance and ethics programs provide a catalyst for using the law to achieve a competitive advantage.

However, in order for a competitive advantage to be achieved, it is necessary to integrate the compliance and ethics program with overall business strategy. Legal strategy and business strategy are necessary complements that must be tied together (Bagley 2010; DiMatteo 2010), as most business decisions involve legal and non-legal factors, requiring simultaneous examination by an organization's legal and business risk management teams (Sharer et al. 2007; D'Aversa 2008). Given the competitive advantage that can result through well-organized and resourceful management of the legal process, organizations are beginning to regularly incorporate compliance programs and other legal considerations into the strategic planning process (Oliver and Holzinger 2008; Ostas 2009). For example, the Centers for Medicare and Medicaid Services (CMS), which oversees the enrollment, reimbursement, monitoring and enforcement policies applicable to health care providers under Medicare, Medicaid, and CHIP, requires its own providers to have compliance and ethics programs in place (Halabi 2010).

Implementing a compliance and ethics program links legal strategy to overall business strategy by acting as the mechanism to integrate those functions into organizational life, organizations can more effectively execute the preemptive strategies that can help avoid future legal violations. First, compliance programs assist in preventing the causes of legal issues from arising by creating an environment that encourages ethical behavior and tying it to business decision making processes. Utilizing law in the strategic sense necessitates proactive incorporation of legal resources into the preliminary decision-making process, in order to mitigate the incidence of problems that will arise in the future (DiMatteo 2010). In order to have an effective program, reasonable steps must be taken to ensure the program's observance, periodically evaluate program efficacy, and establish a means through which guidance on criminal activity can be sought. To assist with this, program standards must be consistently enforced using suitable incentives and appropriate disciplinary measures. By requiring employees at all hierarchical levels to actively participate in the legal compliance process,

organizations have key feedback from the ground up that can be used to facilitate more effective decision making (Hasl-Kelchner 2006).

Second, compliance programs assist in preventing legal issues from doing harm, but if harm does occur, they assist in limiting the resulting damages. A compliance and ethics program provides a means of responding to discovered unlawful conduct within the organization, which translates into quicker resolution and reduced damages (McKendall et al. 2002). The program gives the benefit of having a response plan, reducing the negative effects that can accompany a legal crisis, such as panic and indecision. Compliance programs allow organizational response to be faster and more organized, leaving less time for the legal problem to cause substantial damage. Swift and focused responses can assist organizations by encouraging them to bring legal issues to the attention of appropriate governmental agencies, assist with governmental investigations, and provide compensation to affected individuals and business entities. Not only can such actions reduce the impact and severity of the harm on the environment, general public, or shareholders as the case may be, but they can also aid in the reduction of governmental fines and penalties.

3.4 Reframing legal issues as business opportunities

While the actions described above provide ample benefits to an organization, the greatest benefit of the Manager's Legal Plan lies in reframing legal issues as business opportunities. Reframing legal issues as business opportunities is a crucial factor in achieving a competitive advantage from the law. As noted above, there are four linked approaches that can assist organizations in reframing legal issues as business opportunities: make a commitment to looking at the law as a strategic asset, select an appropriate framework for guiding that commitment, outline specific actions for meeting that commitment, and implement the chosen actions.

3.4.1 *Make a commitment*

The first approach focuses on making a commitment to linking law and business in order to create more ethical culture. Given the challenges inherent in putting effective compliance mechanisms into practice (McKendall et al. 2002), few organizations have the requisite mindset necessary for reaping the full benefits of compliance programs. Despite evidence that internal structures can align organizational behavior with law and social expectations (Hess 2007), scholars have argued against the effectiveness of compliance mechanisms, stating that organizations have strong incentives to adopt "ceremonial" compliance measures, procedures adequate to indicate "legal legitimacy while simultaneously limiting law's impact on managerial power," thereby preventing any interference with central company structures (Anderson 2000; Cunningham 2004; Porter and Kramer 2006; Talesh 2009; Bamberger 2010).

However, by applying the Manager's Legal Plan, organizations can develop a mindset that embraces legal opportunities and recognizes the importance of the legal side of business. This is vital, as there is an assortment of legal concerns that

are closely linked to business concerns and opportunities. For example, wrongful discharge, which can start as a legal concern, can be transformed into a broad business opportunity by helping organizations secure key access to talent. Similarly, risk allocation through contracts can, in turn, support using contracts to build successful relationships in business networks. Product liability lawsuits over safety malfunctions can assist in the development of newer and safer products that more fully satisfy customer needs.

Reframing legal issues as business opportunities permits organizations to leverage their positions and generate differential advantages in the marketplace (Dyson 2004; Hasl-Kelchner 2006; Bagley 2008) through the use of compliance and ethics programs. By requiring the supervision and oversight of high-level executives, compliance programs have allowed organizations to reap the benefits of including lawyers at the strategic planning table (Bagley 2008). Learning valuable lessons from the \$4.85 billion Vioxx settlement, Merck announced attorney Kenneth Frazier would take over as CEO in 2010, a move that has served the company well in ensuing quarters. Serving as general counsel and then head of company's biggest unit, human health, Frazier possessed the legal and business knowledge necessary for navigating the obstacles and avoiding the pitfalls that dominate the heavily regulated pharmaceutical industry (Troise 2010).

In addition, compliance programs allow organizations to reframe legal issues as business opportunities by reducing the divide between lawyers and businesspeople (DiMatteo 2010), which creates more efficient working relationships that translate into higher profits. For example, The Hartford Financial Services Group was named to Ethisphere Institute's Second Annual World's Most Ethical Companies List in response to its efforts to build a stronger, more cohesive ethics and compliance program for its 31,000 employees. Alexander Brigham, executive director of the Institute, noted by its actions, the company forces its competitors to follow suit or lag behind, personifying the notion that ethical business practices are more profitable in the long run (The Hartford Financial Services Group, Inc. 2008). Perhaps he is right, as the Hartford has seen steady revenues in recent years, reaching nearly \$22.4 billion in 2010.

3.4.2 *Select a framework*

Once an organization makes a commitment to reframing legal issues as business opportunities, it must select an appropriate framework that will guide that commitment. In the case of law and ethics, a code of ethics provides a suitable means of articulating the ideas and concepts behind the new commitment. Ethical codes and compliance programs cannot function effectively standing alone; each requires the support of the other. Compliance programs require the organizational commitment established by a code of ethics, while a code of ethics require an organizational infrastructure capable of supporting the mechanisms and strategies needed to make the codes come to life (Driscoll et al. 1999). By creating and enforcing a code of ethics and making it part of company culture, organizations add vision and purpose to their compliance programs.

The corporate code of ethics lays out a company's ethical vision in order to guide the behavior of its employees and representatives (Schwartz 2001). Although the content and language within a code may fluctuate from organization to organization (Newberg 2005), a closer examination reveals a number of commonalities and ethical themes that transcend firm and industry boundaries (Gaumnitz and Lere 2002). For example, codes routinely describe a company's responsibilities towards its stakeholders, stress adherence to federal and state legal regulations, and encourage honesty, fairness, and teamwork (Kaptein 2004). Ethical codes have the dual role of enforcing appropriate conduct by employees as a worthy pursuit and key success factor for organizational success (Valentine and Barnett 2002) while working to assure the general public and various government agencies that business is undertaken in an ethical manner (Sethi 1999).

Notwithstanding this dual role, the legal regulatory environment has a heavy tendency to pressure and shape code content, language, and management (Newberg 2005; Webley and Werner (2008). As a result, several studies have concluded that codes of ethics are little more than legal self-defense measures; mechanisms more concerned with preventing employee misconduct (Emmelhainz and Adams 1999; van Tulder and Kolk 2001), such as conflicts of interest and insider trading (Snell et al. 1999), than with articulating values, beliefs, and guidelines to influence organizational culture (Stevens 2004; Singh 2006). However, Schwartz (2001) noted that despite varied studies as to the relationship between codes and behavior, codes offer the most value in situations residing in the grey area between right and wrong that are riddled with uncertainty. Codes of ethics have the ability to positively influence how employees view and respond to articulated organizational values, thus achieving their intended goals of encouraging ethical and legal behavior (Valentine and Barnett 2002). Thus, a code of ethics can act as a framework for outlining the core ideals behind the organization's commitment, providing a foundation for creating action plans described in the next approach.

3.4.3 *Select specific actions*

The third approach involves outlining specific actions to meet the organization's new commitment to looking at the law as a strategic asset. Compliance and ethics programs sketch suitable action steps for implementing this strategy, as they establish guidelines for establishing organizational processes and procedures. Organizations are provided a fair measure of latitude in program creation that allows them to create compliance processes without substantially disrupting managerial prerogatives and organizational needs (Edelman 1992; Krawiec 2004; McGreal 2010). Thus, compliance and ethics programs can assist organizations to facilitate compliance without sacrificing business needs (McKendall et al. 2002).

There are a number of specific action steps that organizations can take in order to achieve the commitment set out above. First, compliance and ethics programs should require organizations to establish standards and procedures designed to prevent and detect illegal conduct by company employees (McKendall et al. 2002). In order for these standards and procedures to be effective, an ongoing risk assessment should be conducted that identifies and prioritizes legal risks. Through

this risk assessment, are better able to articulate organizational commitment to law and ethics, identify what behavior is prohibited, list punishment for violation of that behavior, set forth procedures for asking questions and reporting violations, and establish procedures for investigating complaints and imposing discipline.

Second, top management must be knowledgeable about program content, undertake reasonable supervision of program implementation, and designate high-level individuals with responsibility for program management. The organization's board or controlling body should initiate and exercise oversight over the program (McKendall et al. 2002). This involves authorizing resources and personnel to undertake the compliance effort, as well as establishing a timetable and measurable goals. The key is to demonstrate the organization takes compliance seriously. Overall responsibility for the program should reside with chief compliance officer. While such individual may delegate responsibility to subordinates, reasonable efforts must be used to ensure discretionary authority over the program is not given to anyone that has engaged in illegal activities or other conduct inconsistent with the program's goals.

Third, reasonable measures must be employed to periodically publicize program requirements, reinforce program standards, and ensure program observance (McKendall et al. 2002). Organizations can publicize compliance program procedures through training sessions and broadcasting of appropriate information. For the compliance program to work, organizations must ensure employees understand and follow the policies. There is no substitute for formal training, leaving organizations to consider the most effective approach, which customarily includes a combination of live presentations, videos, and computer-based modules. Once training is completed, program standards may be reinforced using suitable incentives and appropriate disciplinary measures. Companies may choose to add compliance criteria to performance evaluations and commend individuals who work to improve the program functions. Similarly, reasonable steps must be taken to ensure the program's observance, periodically evaluate program efficacy, and establish a means through which guidance on criminal activity can be sought. Organizations should establish clear lines where individuals can seek guidance about program procedures, as well as lines to generate periodic feedback. If this ongoing monitoring reveals possible legal violations, internal investigations should be carefully conducted so as to prevent retaliation against the individual who discovered the violation and protect the privacy of the accused.

3.4.4 Implement the actions

The final approach focuses on implementing the specific actions for meeting commitment to strategy of compliance and ethics. Although the mere presence of compliance and ethics programs alone may lack the level of influence and absorption necessary to influence organizational behavior (Marnburg 2000; Schwartz 2004; Webley and Werner 2008), an emerging body of research maintains that appropriately designed programs can successfully promote desired behaviors if effective implementation measures are taken (Kolk and van Tulder 2002; McKendall et al. 2002; Lere and Gaumnitz 2007). Compliance and ethics programs

that are communicated to all levels within the organization (Adam and Rachman-Moore 2004; Stevens 2004) and assimilated into organizational culture (Stevens 2008) are more likely to channel decision making in the desired direction (Trevino and Weaver 2003; Webley and Werner 2008). In addition, successful cultural assimilation necessitates reinforcement of compliance program procedures alongside the continuous support of senior management and employee training (Schwartz 2004; Stevens 2008). By encouraging appropriate behavior, effectively implemented compliance programs can be effective at reducing the likelihood of legal violations and dealing with violations when they do occur. As a result, less money will need to be allocated to the payment of legal fines and penalties, contributing to an overall competitive advantage.

4 Conclusions and further research

The business scandals of recent years in the United States have led the country's organizations, lawmakers, and general public to reexamine their respective stances on the success of legal regulations policing the business environment. While the increased complexity and severity of legal regulation has led some companies to establish compliance programs as legal response measures, little focus has gone into examining whether these legal mechanisms can be used as strategic tools to achieve competitive advantage. By applying the Manager's Legal Plan, I have demonstrated that by facilitating a more advanced understanding of the legal environment, inspiring more efficient means to address and prevent legal violations, and encouraging the perception of legal issues as business opportunities, compliance and ethics programs assist in the development of action plans for achieving a competitive advantage from the law.

Scholars in a variety of disciplines have posed questions about the complex relationship between the legal world and the business world. Previous research provides some insight into the nature of legal response measures within the larger scheme of organizational life. Specifically, this paper builds on previous research by analyzing compliance programs as a means for achieving competitive advantage. Conclusions in this paper may be used by scholars in management and law to further explore the relationship among law, compliance, and business strategy. Organizational strategists can look to compliance programs as benchmarks for analyzing their own views on integrating legal and business strategy.

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