Compliance-oriented regulation should be understood as a holistic approach to regulatory design, implementation, monitoring, and enforcement in which the guiding principle is the achievement of regulatory outcomes. Compliance-oriented regulation is therefore distinctively concerned with the effects of public regulation in preexistent regulatory space where it must compete with private normative orderings. This article sets out the principles of compliance-oriented regulatory innovation together with evidence on their effectiveness. The widespread implementation of in-house corporate compliance systems in recent years means that compliance-oriented regulators need to be particularly concerned with nurturing compliance capacity among regulatees, fostering regulatory community through compliance professionalism, and developing standards for corporate compliance functions.

REINVENTING REGULATION WITHIN THE CORPORATION
Compliance-Oriented Regulatory Innovation

CHRISTINE PARKER
University of New South Wales

“Compliance”-oriented regulation is now recognized as a major strand of regulatory strategy and policy. Empirical studies have focused on individual tax, environmental, financial, and occupational health and safety officials’ reliance on education, persuasion, and cooperation rather than deterrence to persuade businesses to preventively comply with regulatory goals (e.g., J. Braithwaite, 1985; Hawkins, 1984; Hutter, 1997). Regulatory
agencies are experimenting with programs that provide incentives for voluntary implementation of sophisticated compliance systems by business and sanctions for lack of a program (e.g., Feitshans, 1997). The global deregulatory movement is maturing in some countries into a regulatory reform movement that moves beyond the cost-benefit analysis of regulatory impact assessment to principles for "better regulation" (e.g., Better Regulation Taskforce, n.d.; see Organization for Economic Cooperation and Development [OECD], 1997a). In the United States, for example, the "re-inventing regulation" program (Geltman & Skroback, 1998; Nesterczuk, 1996) aims to control "regulatory inflation" by ensuring that the design of regulation and regulatory enforcement strategy meets its goals in an effective and efficient way that maximizes voluntary compliance by business from the beginning. Some governments have even produced comprehensive approaches to encouraging compliance-oriented regulation, and the OECD has produced a report on the issue (see Parker, 1999c). These developments are all consistent with the broader style of the "new regulatory state," which uses enforced self-regulation and incentives for voluntary compliance to steer corporate conduct toward public goals without interfering too greatly with corporate autonomy and profit (Baldwin, 1997; J. Braithwaite, 2000; Grabosky, 1995; Manning, 1987; Parker, 1999a, 1999b).
IN-HOUSE COMPLIANCE SYSTEMS
AND REGULATORY INNOVATION

IN-HOUSE COMPLIANCE SYSTEMS

Compliance-oriented regulation is aimed as much at reinventing regulation within private regulatory space, such as corporations, as at reforming external regulatory agencies. Compliance-oriented regulatory strategies attempt to penetrate right inside businesses to transform and harness management systems, operational processes, and organizational cultures to regulatory goals. Each of the compliance-oriented regulatory innovations described above will tend to encourage the proliferation of in-house corporate compliance systems as a means of companies taking responsibility for in-house self-regulation to meet regulated outcome standards, implement codes of conduct and management standards, respond to rewards and incentives, or fulfill undertakings to implement a compliance assurance system after a breach has occurred. Internal corporate compliance systems, then, will be one of the important formal functions where the interaction between external regulation and internal management systems occurs. Because of its monopoly on legitimate coercion (i.e., legal and regulatory sanctions), the state can have a great impact in the regulatory space inside companies. But the precise nature of the impact is not controllable because of the complex ways in which state regulation interacts with preexisting orderings. To understand compliance-oriented regulation, it is important to look not just at strategies used by external regulators but at the internal workings of the company, the ethics and professionalism of internal compliance constituencies, and the way they interact with management as well as external regulators.

Organizational actors are already voluntarily implementing compliance programs as a response to perceived risks of legal liability, major ethical breaches, and other adverse publicity outcomes. For example, in the United States, a 1996 Price Waterhouse survey of corporate compliance practices in 262 large companies found that 86% had a formal compliance policy, 9% were developing a policy, and only 5% had no policy (Ward, 1997). In Canada, a 1998 KPMG survey of corporate compliance practices found that 65% of Canada’s largest companies had explicit compliance standards and procedures in place. A total of 63% had produced publications that communicated these standards and procedures to staff and management, and 58% had assigned responsibility to high-level personnel to oversee compliance (Schwartz, 1998). Table 1 summarizes the quan-
tative evidence available on the implementation of corporate compliance programs. The evidence suggests that corporate compliance programs are strongest in the areas of environmental, occupational health and safety, and financial services regulation (see, e.g., Aalders & Wilthagen, 1997, p. 421; Andersen, 1996; Genn, 1993). EEO and affirmative action compliance policies are also widely implemented but to a lesser extent. The evidence also shows that corporate compliance systems are much more likely to be implemented by large enterprises than small and medium-sized enterprises (SMEs).

The implementation of corporate compliance programs does not of itself necessarily represent an increase in compliance or in optimal regulatory outcomes. Indeed, it is possible that corporate compliance systems are a response to unnecessarily complex laws and high risks of private liability and bad publicity. But on the whole, the growth in adoption of corporate compliance programs illustrates a widespread acceptance among big business of the need to be seen to be responsive to, and ensure compliance with, reasonable regulatory requirements and social pressures. From the regulator’s point of view, at least three factors will affect the success of these regulatory interactions within the organization: regulators’ ability to nurture compliance capacity in business, the emergence of compliance professionals to act as mediators between regulators and organizations, and the development of meta-standards for internal corporate controls that help ensure the effectiveness of compliance constituencies within the organization. (Clearly, research from the point of view of corporate managers and employees will also be helpful in understanding the impact of compliance-oriented regulation; see Parker, 1999a, 1999b.)

ABILITY TO NURTURE COMPLIANCE CAPACITY

Strategic compliance-oriented regulatory design and enforcement does not necessarily reach an audience equipped to understand or effectively respond with compliance to regulatory objectives. Innovative regulatory strategies for encouraging compliance are not likely to be effective if organizations have no capacity or expertise in how to comply with regulation. Indeed, Heimer’s (1996) study of the impact of law inside neonatal intensive care units shows that

many organisations are organized anarchies, functioning much like garbage cans into which a variety of elements are tossed. . . . Rather than decisions being made in the “rational” way that organisation charts would suggest they are. . . . decisions instead result from the episodic coupling of key
elements that co-exist semi-autonomously in organisations. Which decisions get made depends on what participants happen to be there at the time, what is identified as a problem needing a solution, what solutions are available in the organization, and consensus that a choice point has arrived and it is time to make a decision. (p. 44)

Indeed, one of the main advantages of implementation of a compliance system from a corporate management point of view is that it will improve controls, efficiency, and the rationality of certain processes within the organization. Studies of organizational decision making and ethics have shown that organizational processes often tend to result in decisions in which the group decides on action that is more risky and unethical than any one of them individually would have chosen and that people often remain committed to group policies even when they are obviously working badly and have unintended consequences (Sims, 1994, p. 50; also see Gioia, 1992). Compliance-oriented regulatory strategy should foster “ethical intelligence” within organizational processes. Therefore, one of the more strategic things regulators can do to increase compliance is to nurture organizational capacity to comply through education, assistance, offering consultancy services, and encouraging the growth of compliance professionals with specialist expertise in the area.

SMEs are often particularly low in compliance often because they lack capacity (such as specialized staff) to comply. Assistance targeted at SMEs may therefore bear fruit. For example, OSHA’s Consultation program is a broad network of occupational safety and health services that provide a free source of information and technical assistance targeted at SME employers (those with no more than 250 employees) who request help in establishing and maintaining a safe and healthful workplace. The comprehensive assistance available includes an appraisal of all mechanical systems, physical work practices, and environmental hazards of workplaces and all aspects of employer’s present job safety and health programs. According to OSHA, the consultation program has helped identify and control more than 500,000 workplace safety and health hazards. The program is popular with SMEs because of the government’s willingness to pay for expert services that would otherwise cost thousands of dollars. The consultation program is also completely separate from OSHA’s inspection program, and the consultant pledges confidentiality provided the employer agrees to correct in a timely manner any serious hazards uncovered during the consultation visit. In an independent survey conducted for OSHA in 1995, employers who had received onsite consul-
tation visits indicated very high levels of satisfaction with the service provided (Weinberg, 1996).

**REGULATORY COMMUNITY AND COMPLIANCE PROFESSIONALISM**

For targeted monitoring and enforcement, incentives for voluntary compliance, and voluntary agreements to be effective, there must be a meaningful avenue of engagement between regulator and regulatee; there must be some medium through which information can flow and dialogue can occur. Regulators must receive information about whether compliance programs put in place to stave off more harsh sanctions are effective and in line with legal standards. Regulatees must understand what regulators and communities require and why regulators have taken particular strategic enforcement decisions. They must have enough in common to understand when escalation up the pyramid will fit regulatory goals and when escalation is not necessary. Indeed, compliance-oriented regulation generally relies on the assumption that regulatory messages are communicated into a world of shared bonds and shared understandings in which companies can effectively respond to regulatory signals, and the parties deliberate effectively about their responses to them, which, in turn, creates shared commitments to regulatory goals. Regulators and regulatees need to be part of the same “community” to have continuing relationships and the same basic understanding of the meanings and goals of regulatory action (see Ayres & Braithwaite, 1992; Black, 1997, pp. 30-38; Meidinger, 1987, p. 365).

An emerging compliance profession can act as a medium of regulatory community if regulators are willing to engage with them and can also act as a pool of compliance expertise that can be translated into corporate compliance capacity. The expansion of compliance and risk management programs in corporations has opened a new professional jurisdiction in which practitioners who identify themselves as “compliance professionals” is emerging. The new occupation spans nonlawyers including human resource managers, auditors, ex-lawyers who now see themselves as compliance managers, and lawyers who specialize in compliance issues. . . .
Some empirical evidence shows that flexible compliance-oriented programs are more likely to succeed where the regulated community includes compliance professionals who can act as a go-between for regulator and business so that business understands how to comply with regulatory goals and can communicate ideas for more innovative and flexible regulatory mechanisms back to regulators. Rees’s (1988) evaluation of the Californian branch of OSHA experiment with the Cooperative Compliance Program between 1979 and 1984 found that the growth of safety management professionalism was crucial to compliance with regulatory goals. The program authorized labor-management safety committees on seven large construction sites to assume many of OSHA’s regulatory responsibilities (such as conducting inspections and investigating complaints),
whereas OSHA ceased routine compliance inspections and pursued a more cooperative relationship with these companies. During the program, accident rates ranged from one third lower to five times lower than comparable company projects, and the satisfaction of workers, management, and government participants with the program was high. The evaluation found that this approach succeeded mainly because it strengthened the preexistent job-site safety programs in ways that traditional regulatory strategies could not. The voluntary job-site safety programs in turn had been promoted and implemented by safety management professionals, a professional specialization promoted by the American Society of Safety Engineers. The existence of safety management professionals within the companies also allowed the labor-management and regulator-management communication necessary for the program to succeed. . . .

McCaffrey and Faerman (1994) conclude from their study of self-regulation in the U.S. securities industry that the institutionalization of regulatory occupations within industry (in this case, financial compliance officers) is one of the main conditions in which self or “shared” regulation is most likely to be effective so long as the law strengthens the position of the compliance staff. In a completely different situation involving hospital neonatal intensive care units, Heimer (1996 p. 37) concludes that the law’s shadow is likely to be “densest” within organizations when “the law’s shadow largely coincides with the shadow cast by professional bodies.” She goes on to argue that “professions are simultaneously the organisational participants responsible for altering the scripts or routines of organisations and the carriers of legitimacy.” They legitimize organizations by acting as “sentinels” tracking the organization’s external environment, including legal and regulatory messages, and adapting organizational systems to respond to those messages appropriately.
STANDARDS FOR COMPLIANCE PROGRAMS AND CORPORATE STRUCTURES

Finally, regulators and regulatees must share some common standards for voluntary compliance. Edelman’s work on corporate EEO polices suggests that many companies will be highly motivated to preserve legitimacy by responding to external norms and setting up compliance programs, but these will not necessarily reflect legal norms in substance (Edelman et al., 1993). Regulators therefore need to develop some standards for compliance systems and internal corporate structures and monitor the compliance programs and functions that are being put in place; otherwise, compliance will be a sham.

One of the most significant factors influencing the effectiveness of a compliance program is whether the officer responsible for its implementation holds sufficient formal or informal clout within the organization to ensure that compliance policies are followed and ferret out breaches (J. Braithwaite & Murphy, 1993). For example, one study of the internal compliance systems of the five American coal-mining companies with the lowest accident rates for the industry showed that one of the factors they had in common was that they gave a lot of informal clout and top management backing to their safety inspectors (J. Braithwaite, 1985, p. 65). At the most basic level, this means being appointed at a senior enough level to earn respect within the hierarchical structure of the corporation. But even where formal clout is lacking or is not sufficient, savvy compliance officers find ways to appropriate clout. Clearly, the best way to achieve clout is through the direct support of the senior management, preferably the managing director himself or herself. As McCaffrey and Hart (1998) conclude from their study of internal compliance systems on Wall Street,

anyone who looks at broker-dealer firms in any detail will be struck by how internal politics and managerial styles produce regulatory differences across them. Those working in legal and compliance offices have professional and personal stakes in being taken seriously within the firm. How successful they are in this depends on how three issues are handled. First, how well do they convince enough powerful actors in the firm that legal and compliance “adds value” to it? Second, do they establish a reputation as competent, reasonable, and respectable “insiders”? Third, how strongly does upper management support them and internal controls generally? (p. 157)

In leading corporate compliance systems, the chief compliance manager reports directly to the board or a board audit or compliance committee.
In at least one Australian company, the chief compliance manager shares the same protection in employment as the chief financial officer: The compliance manager cannot be fired or even resign voluntarily without the matter going to a meeting of the board in which directors can satisfy themselves that the firing or resignation is not occurring for the wrong reasons. Similarly, in that company the chief compliance manager must report to the board the circumstances in which any of his or her staff resign or are fired from their compliance positions.5

If the effectiveness of compliance officers depends on certain structural conditions within the corporation such as seniority, independence, and appropriate reporting relationships, then for compliance-oriented regulation, issues of corporate constitutionalism will be fundamental. Ensuring that a variety of different constituencies within the corporation have a voice should be an important priority because the new regulation has to rely on the ability of internal constituencies to reform corporate cultures from within. Just as various conventions have grown up to protect the independence of auditors and general counsel, so should the place of other constituencies within the corporation that might hold it to important public values be protected. This means that it is important to institutionalize, indeed constitutionalize, the compliance function through the role of general counsel, the Board Audit Committee, compliance committees, and other checks and balances. For example, in Australia the 1998 Managed Investments Act requires Australian funds managers to implement a compliance program and a compliance committee that is responsible for it. Compliance scholars could therefore connect with progressive corporate law scholarship on the democratic reform of corporate structures beyond the shareholders (see, e.g., Bottomley, 1997, 1999; Chayes, 1960).

CONCLUSION

I have argued here that compliance-oriented regulation is concerned with an outcome defined by regulatory objectives. “Compliance” has been taken to mean compliance with a regulatory goal, not compliance with a set of technical rules. As Shearing (1993) writes, “policy makers should be very wary of an approach that regards compliance with rules whether achieved through cooperation or coercion as hallmarks of sound regulatory practices. Regulatory policy should be goal rather than rule oriented” (p. 75). The paradox for business is that in one sense, compliance with a broad regulatory objective is much harder than even the toughest set of
rules imposing the greatest paperwork burden because it requires thorough internalized commitment to showing regulatory responsibility in changing circumstances, not just ticking off a set of boxes. Similarly, for the regulator there is a paradox. Compliance-oriented regulation can seem weaker, perhaps less expensive, and certainly less aggressive than other styles of regulation. In fact, a truly compliance-oriented approach to regulation would include defining objectives, tailored rule design and implementation, targeted monitoring, and restoration and enforcement of compliance. It intrudes into private normative orderings in all its phases and requires understanding of and engagement with the intimate details of regulatees’ characteristics, attitudes, and operations. Such a holistic-tailored approach is likely to be neither easy, cheap, nor, if effectively implemented, weak.

For both regulator and regulatee, however, there is a particular danger that compliance rhetoric will be used merely to “manage appearances.” As Shearing (1993) writes,

Therefore regulatory space is a marketplace of assurances in which multiple guarantors often compete with each other for the confidence of persons who are faced with decisions as to where and how to act. Also regulators face temptation to be content with creating appearances that will promote confidence and to be less concerned with ensuring that this confidence is actually warranted. . . . Policy should be sensitive to the danger of permitting appearance management to “capture” the regulatory process. (pp. 75-76)

Even at their best, corporate compliance systems are frequently an attempt to manage appearances and preserve legitimacy (Edelman et al., 1993) in response to public and government concerns while making as little real change as possible. The critics are correct in their analyses of the shortcomings of compliance-oriented policy and scholarship that focus on only one type of strategy among the whole of regulatory design and implementation. The evidence outlined here for a holistic approach to compliance is designed to provide a more robust basis for further research and debate.
2. Nevertheless, when the Occupational Safety and Health Administration tried to expand the program, it met resistance from some employers (see Parker, 1999c).
3. See also Harrison (1995), who found that the purely cooperative Canadian approach to environmental regulation in the pulp-and-paper industry resulted in much lower compliance rates than the more adversarial regulation of the same industry in the United States.
4. Measurements of a number of other dimensions of restorative justice were made in other papers from the same study (Makkai & Braithwaite, 1993, 1994a).
5. This information is based on my own research on leading compliance systems in Australia.

REFERENCES


Christine Parker is a senior lecturer in the Law Faculty at the University of New South Wales. Her current research is on best practice corporate regulatory compliance functions and the emergence of compliance professionals. She has also acted as a consultant to the Public Management Service of the OECD on regulatory compliance and regulatory reform. She has published a book, *Just Lawyers: Regulation and Access to Justice* (Oxford University Press, Socio-Legal Studies Series, 1999) and numerous articles in the areas of legal ethics, the sociology of the legal profession, regulatory theory and policy, and corporate compliance in journals including the Journal of Law and Society, International Journal of the Sociology of Law, and Law and Policy.